HFG WEALTH MANAGEMENT

INSIGHT

PERSPECTIVES FOR THE GOAL-BASED INVESTOR

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A Different Type of Contagion

The closure of Silicon Valley Bank (SVB) has raised concerns about potential contagion risks to the financial system. The bank, which specializes in serving the technology and innovation sector, has been a key player in the venture capital ecosystem, providing financing to early-stage startups and helping them grow. Its sudden closure has left many wondering about the impact on the broader financial ecosystem.

The first potential contagion risk is the loss of confidence in the financial system. When a bank fails, it can create a ripple effect that can lead to a loss of confidence in the overall financial system. This can lead to a run on other banks as depositors seek to withdraw their funds, creating a liquidity crisis. While SVB is a relatively small bank, its closure could still have a negative impact on market sentiment and investor confidence. The quick and decisive action by the Fed to guarantee liquidity went a long way in helping to restore confidence that this would not be a repeat of 2008.

The second potential contagion risk is the impact on the broader technology and innovation sector. SVB has been a major player in this space, providing financing to some of the most promising startups in the industry. Its closure could lead to a reduction in the availability of financing for these companies, which could in turn lead to a slowdown in innovation and growth. This could have broader economic implications, as the technology sector has been a key driver of growth in recent years.

The third potential contagion risk is the impact on other banks and financial institutions. SVB is not the only bank that serves the technology and innovation sector, and its closure could create a domino effect that could lead to the failure of other banks and financial institutions that have exposure to this sector. This could create a systemic risk to the financial system as a whole.

To mitigate these risks, it is important for regulators and policymakers to closely monitor the situation and take appropriate action. This may include providing liquidity support to affected banks, implementing measures to prevent runs on other banks, and taking steps to ensure that the technology and innovation sector continues to have access to financing.

In addition, it is important for investors and market participants to remain calm and avoid panic. While the closure of SVB is certainly a significant event, it is not necessarily an indication of broader problems in the financial system. By maintaining a level head and taking a measured approach, investors can help to mitigate the potential contagion risks and ensure that the financial system remains stable and resilient.

Protecting Your Financial Information

As our lives continue to move online, the threat of cybercrime continues to grow, and investors must be cautious when dealing in financial matters online. Investment firms are also increasingly becoming targets of cyber-attacks, making it important for investors to understand how their advisory firm and custodians prioritize cybersecurity to help protect their investments.

Recent examples of cyber-attacks in the financial industry include the 2019 attack on Capital One and the 2020 attack on the hedge fund, Grubman Shire Meiselas & Sacks. In the Capital One breach, hackers gained access to over 100 million customers' personal information through a vulnerability in the company's firewall. The Grubman Shire Meiselas & Sacks attack involved the theft of sensitive information belonging to some of the firm's high-profile clients, including celebrities and politicians. While there was no theft of financial assets in either case, the information that was obtained could have been used to gain access to other financial assets.

Investment firms that take cybersecurity seriously will have robust measures in place to help safeguard your assets and information. These measures may include using advanced encryption methods, implementing strong password policies and two-factor authentication, and regularly monitoring accounts for any suspicious activity. While these are essential for providing security outside of your control, the level of security is only as good as the weakest link. In many cases, that link resides with personal security habits.

Here are some additional steps you can take to help protect your finances from cyber-attacks:

- Use strong passwords: Use complex passwords with a combination of upper and lowercase letters, numbers, and symbols. Avoid using the same password for multiple accounts.
- Enable two-factor authentication: Two-factor authentication adds an extra layer of security by requiring a second form of identification, such as a fingerprint or a code sent to your phone.
- Keep your software up to date: Regularly update your computer's operating system, antivirus software, and any other programs to ensure you have the latest security patches.
- Be wary of suspicious emails and phone calls: Scammers may try to trick you into giving them access to your accounts by sending phishing emails or making fraudulent phone calls. Be cautious and never give out personal information over the phone or via email.
- Review your account activity regularly: Check your account activity regularly and report any suspicious transactions or activity to your investment firm immediately.

It is important to understand the risks that investment firms face and prioritize cybersecurity to protect clients' investments. We use the most advanced encryption methods to protect your data, and we have implemented robust password policies and two-factor authentication to help prevent unauthorized access to your accounts. We also regularly monitor your accounts for any suspicious activity and have measures in place to alert you immediately if we detect any unauthorized transactions or changes.

By choosing a firm that takes cybersecurity seriously and following these steps, investors can help safeguard their assets and information against the growing threat of cyber-attacks. We are committed to providing our clients with the highest level of security and peace of mind, knowing that their investments are protected. With our state-of-the-art security measures and your vigilance, you can manage your finances with confidence, knowing that your information is safe and secure.

Plan Ahead For Possible Shutdown

We have seen some troubling signals that the upcoming debate regarding the U.S. debt ceiling will be contentious. As an investor, it's important to consider the potential impact of a government shutdown on your portfolio. In the event of a government shutdown, markets can become volatile and unpredictable, causing losses for investors. While these types of situations are usually not long-lasting, they can have a significant impact in the short-term. However, there are steps that investors can take to protect their portfolio during a government shutdown. Here are five specific ways to do so:

Diversify Your Portfolio

Diversifying your portfolio is one way to protect it during a government shutdown. By investing in a variety of different assets across different sectors of the economy, you reduce your exposure to any one particular market or asset. This can help you better weather the storm of a government shutdown. Including assets like commodities and other alternatives lessens the reliance on equity performance.

Invest Defensively

Investing defensively is another way to protect your portfolio during a government shutdown. Defensive stocks are companies that are less sensitive to economic cycles and tend to perform better during market downturns. Examples include companies that produce consumer staples, such as food, household goods, and pharmaceuticals. These types of companies tend to be less affected by economic uncertainty and may provide a buffer to your portfolio in the event of a government shutdown.

Keep Cash on Hand

Keeping some cash on hand is important during a government shutdown. A government shutdown can cause significant market volatility, and having cash available to take advantage of buying opportunities can be advantageous. Additionally, keeping some cash on hand can provide a sense of security and help you avoid selling investments at a loss due to panic or fear.

Invest in Gold and Other Precious Metals

Investing in gold and other precious metals is another way to protect your portfolio during a government shutdown. During a government shutdown, the value of the US dollar may decline due to the uncertainty and economic impact of the shutdown. In such a scenario, investing in gold and other precious metals can provide a hedge against inflation and a stable store of value.

Consider Short-term Fixed Income

Investing in short-term bonds is another way to protect your portfolio during a government shutdown. These bonds tend to be less volatile and provide a more stable return during periods of uncertainty. During a government shutdown, the interest rates on these bonds may increase due to the uncertainty in the markets, providing investors with a stable and predictable return on their investment.

A government shutdown can have a significant impact on the markets and cause losses for investors. However, by diversifying your portfolio, investing in defensive stocks, keeping cash on hand, investing in gold and other precious metals, and considering short-term Treasury bonds, investors can protect their portfolios and mitigate potential risks during a government shutdown. By taking these steps, investors can ensure that their portfolios remain stable and profitable over the long run.

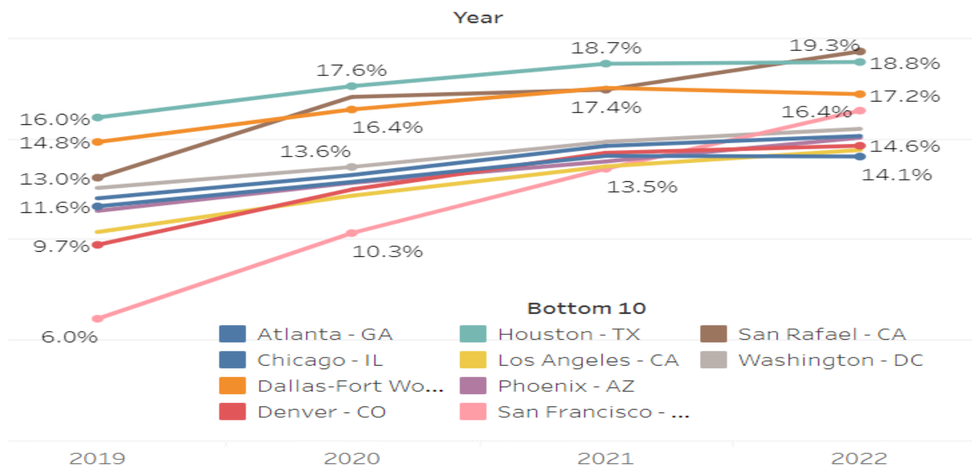
Real Estate Financial Crisis 2.0?

The sharp rise in interest rates last year has prompted concerns about a collapse in the commercial real estate market. There is about $1.35 TRILLION of commercial loans coming due in 2023 and 2024, with about 45% owned by banks and 20% owned by insurers. The concern is that with falling occupancy rates (current nationwide vacancy is about 14%), higher costs and a potential recession on the horizon, owners may simply elect to walk away from failing properties if there is not a viable refinance option available to them.

The issue is most dire in the retail/office space, which comprises about 35% of the loans coming due. As companies move back from the effects of COVID restrictions, many are finding that the full workforce has not returned and that remote workers are going to part of the future landscape. This has a direct impact on the amount of space that will ultimately be needed by the individual companies and the total rentable space that will be utilized in office complexes. Specifically, the top 10 worst-performing areas generally continue to be tech hubs that had high office vacancy rates even before COVID-19. It's just that now these areas are experiencing a further increase in vacant square footage.

So what could happen in the event that the worst case scenario develops – where property owners simply walk away from their obligations in the office and retail space? Based on analysis done by industry experts, if banks were forced to liquidate the assets at the prevailing rate, the estimate would be loan losses of $60-$70 billion for banks and $20-$30 billion for insurers. While this is not a pretty picture, it falls within the category of being painful but manageable and not likely to start a repeat of the conditions that led to the Financial Crisis of 2008.

Alternatively, it is estimated that if banks choose to "extend and pretend" to avoid liquidation, and all property owners were allowed to refinance their properties, banks and insurers wouldn't see any losses. But in that second scenario, property owners would have to add value somewhere in order to keep the loan to value ratio manageable for the banks.



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