

Blue Line Capital

How Duration Risk Wiped Out Silicon Valley Bank

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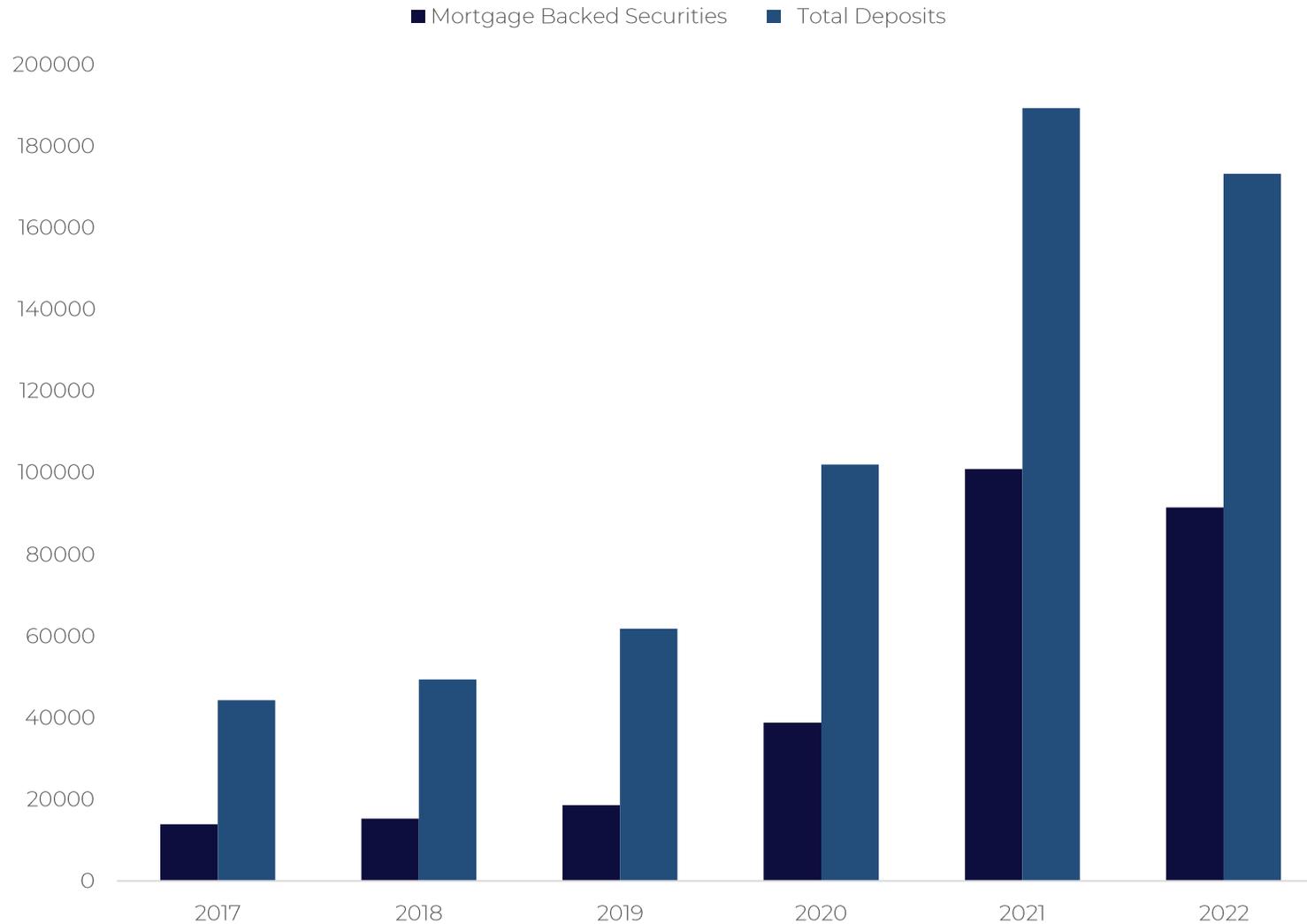


Macro Dynamics

Regional Banks & Silicon Valley Bank Wipeout

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Silicon Valley Bank Duration Mismatch



- Silicon Valley Bank increased MBS holdings by ~6.5x while the company's deposit base grew by ~4.4x from 2017 to peak levels in 2021.
- SVB served cash-needy customers like start-ups and VC firms, who ultimately caused a bank run after becoming aware of ~\$15bn of unmarked losses on security holdings.
 - Comparing against equity of ~\$12bn

Sources: Silicon Valley Bank IR, Blue Line Capital, Blue Line Futures

3/13/2023

Joint Press Release – Depositors Are Safe

Joint Press Release

March 12, 2023

Joint Statement by Treasury, Federal Reserve, and FDIC

Department of the Treasury

Board of Governors of the Federal Reserve System

Federal Deposit Insurance Corporation

For release at 6:15 p.m. EDT

Share 

Washington, DC -- The following statement was released by Secretary of the Treasury Janet L. Yellen, Federal Reserve Board Chair Jerome H. Powell, and FDIC Chairman Martin J. Gruenberg:

Today we are taking decisive actions to protect the U.S. economy by strengthening public confidence in our banking system. This step will ensure that the U.S. banking system continues to perform its vital roles of protecting deposits and providing access to credit to households and businesses in a manner that promotes strong and sustainable economic growth.

After receiving a recommendation from the boards of the FDIC and the Federal Reserve, and consulting with the President, Secretary Yellen approved actions enabling the FDIC to complete its resolution of Silicon Valley Bank, Santa Clara, California, in a manner that fully protects all depositors. Depositors will have access to all of their money starting Monday, March 13. No losses associated with the resolution of Silicon Valley Bank will be borne by the taxpayer.

We are also announcing a similar systemic risk exception for Signature Bank, New York, New York, which was closed today by its state chartering authority. All depositors of this institution will be made whole. As with the resolution of Silicon Valley Bank, no losses will be borne by the taxpayer.

Sources: Federal Reserve, Blue Line Capital, Blue Line Futures

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- All Deposits, irrespective of whether they're uninsured by the FDIC's 250k standard will be returned to customers.
- No losses carried by the taxpayer.
- Avoiding 1930 type bank runs.
- No bailout for equity or bondholders.
- Depositors trust in the banking system restored.
- Banks may continue to fail.

The Regulators' Response – Funding Facility (BTFP)

Bank Term Funding Program

Program: To provide liquidity to U.S. depository institutions, each Federal Reserve Bank would make advances to eligible borrowers, taking as collateral certain types of securities.

Borrower Eligibility: Any U.S. federally insured depository institution (including a bank, savings association, or credit union) or U.S. branch or agency of a foreign bank that is eligible for primary credit (see 12 CFR 201.4(a)) is eligible to borrow under the Program.

Eligible Collateral: Eligible collateral includes any collateral eligible for purchase by the Federal Reserve Banks in open market operations (see 12 CFR 201.108(b)), provided that such collateral was owned by the borrower as of March 12, 2023.

Advance Size: Advances will be limited to the value of eligible collateral pledged by the eligible borrower.

Rate: The rate for term advances will be the one-year overnight index swap rate plus 10 basis points; the rate will be fixed for the term of the advance on the day the advance is made.

Collateral Valuation: The collateral valuation will be par value. Margin will be 100% of par value.

Prepayment: Borrowers may prepay advances (including for purposes of refinancing) at any time without penalty.

Advance Term: Advances will be made available to eligible borrowers for a term of up to one year.

Fees: There are no fees associated with the Program.

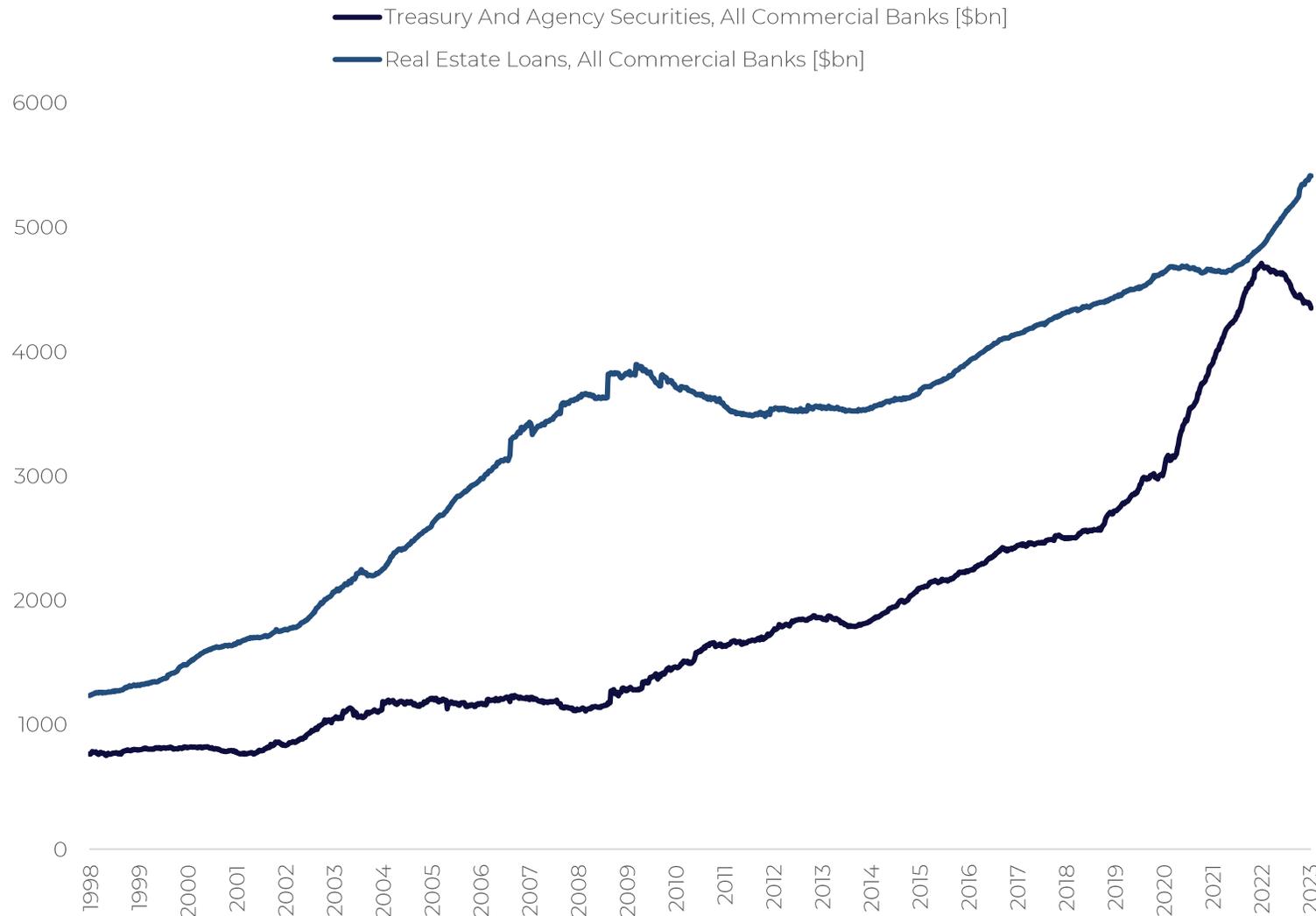
Credit Protection by the Department of the Treasury: The Department of the Treasury, using the Exchange Stabilization Fund, would provide \$25 billion as credit protection to the Federal Reserve Banks in connection with the Program.

Recourse: Advances made under the Program are made with recourse beyond the pledged collateral to the eligible borrower.

Program Duration: Advances can be requested under the Program until at least March 11, 2024.

- Banks can post collateral at par, irrespective of market price.
- Borrowing happens at the overnight swap rate (SOFR trades at ~4.55%)

Commercial Banks – Securities & RE Loans Holdings

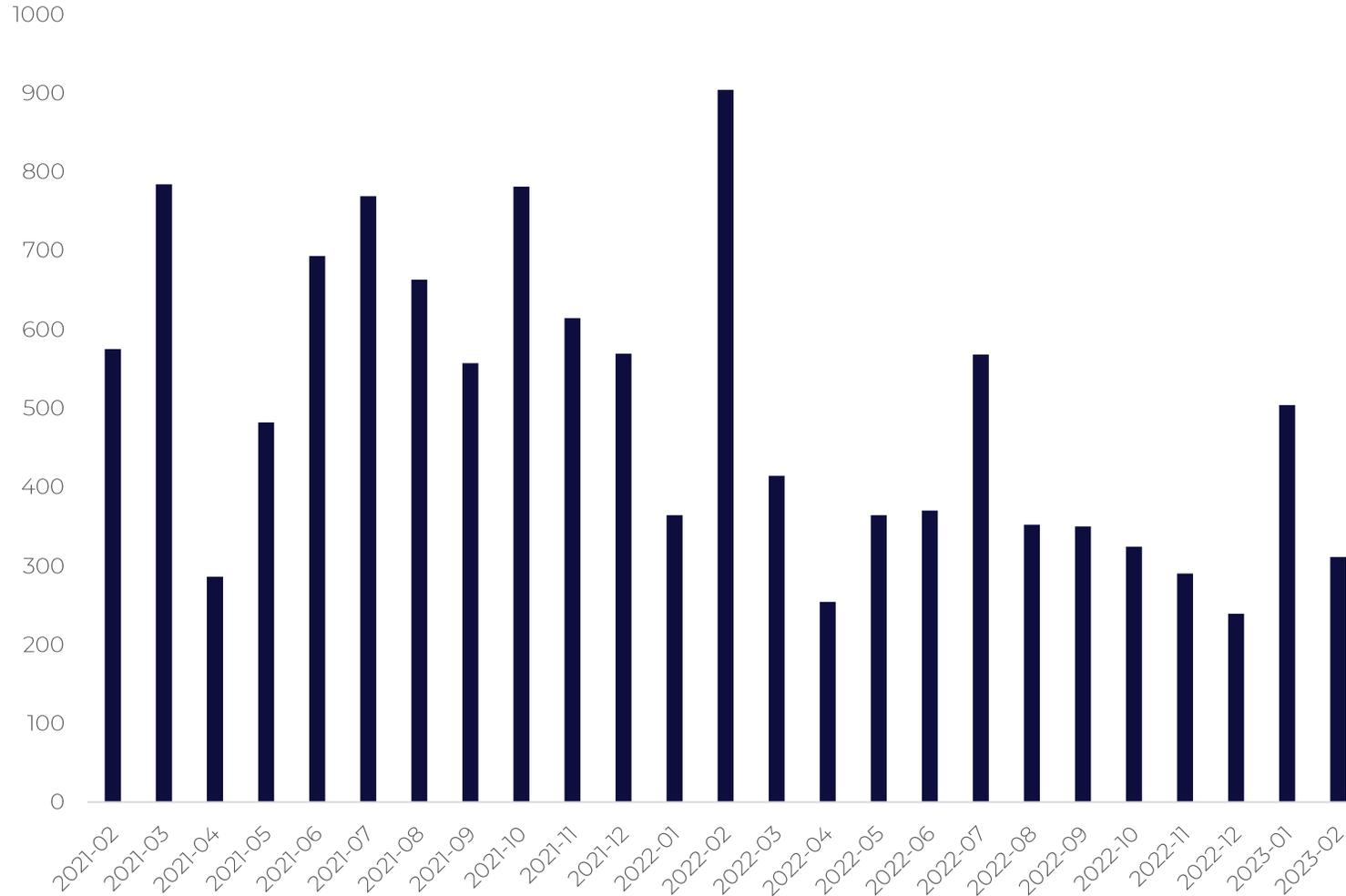


- Since the start of 2019, banks have increased their holdings of treasury and agency securities (treasuries & MBS) by more than 60% while increasing their real estate loan base by 22.5%.
- According to the Fed's H.8 report, treasury and agency securities holdings value is down from \$4.56trn in Feb. 2022 to \$4.25trn as of Feb. 2023., indicating banks might be some \$300bn under water on a mark-to-market basis.
- The value of real estate loans has increased from \$4.75trn to \$5.30trn, indicating that more loans have been handed out. Where are the marks?

Sources: Federal Reserve, FRED, [Alexander Campbell](#), Blue Line Capital, Blue Line Futures

Total Nonfarm Payrolls

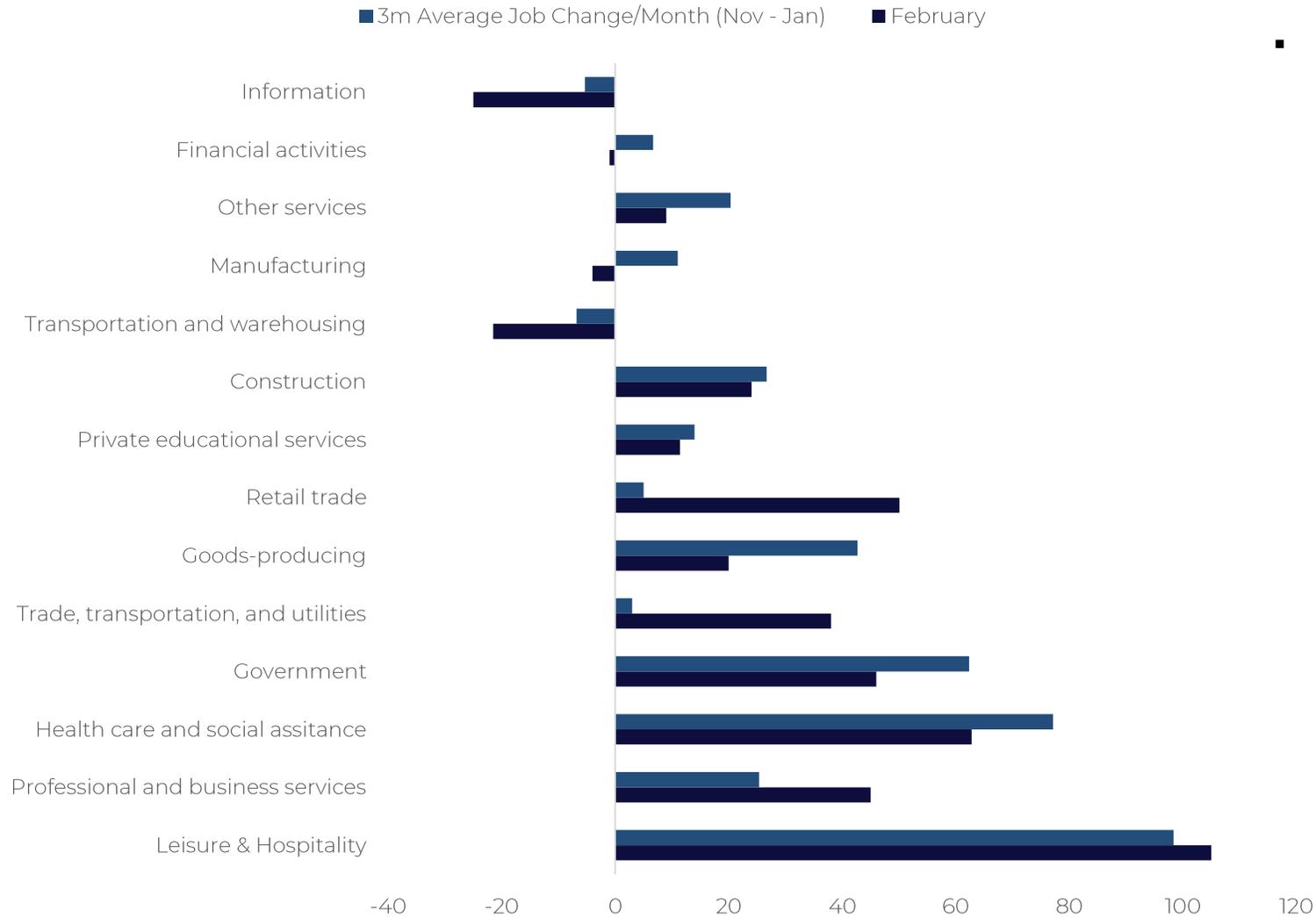
■ Total Nonfarm Payrolls [Thousands of Persons, Monthly]



- Employers added 311k jobs in February, below January's 504k (revision down from 517k)
- The unemployment rate ticked up to 3.6%, from a 50-year low at 3.4% the month prior.
- Labor Force Participation ticked up to 62.5%, the highest level since 62.6%.
- Prime age labor force participation (25-54 yrs) ticked up to 83.1% (vs. 82.7% in Jan.), back to where it was in January 2020.

Sources: BLS, FRED, Blue Line Capital, Blue Line Futures

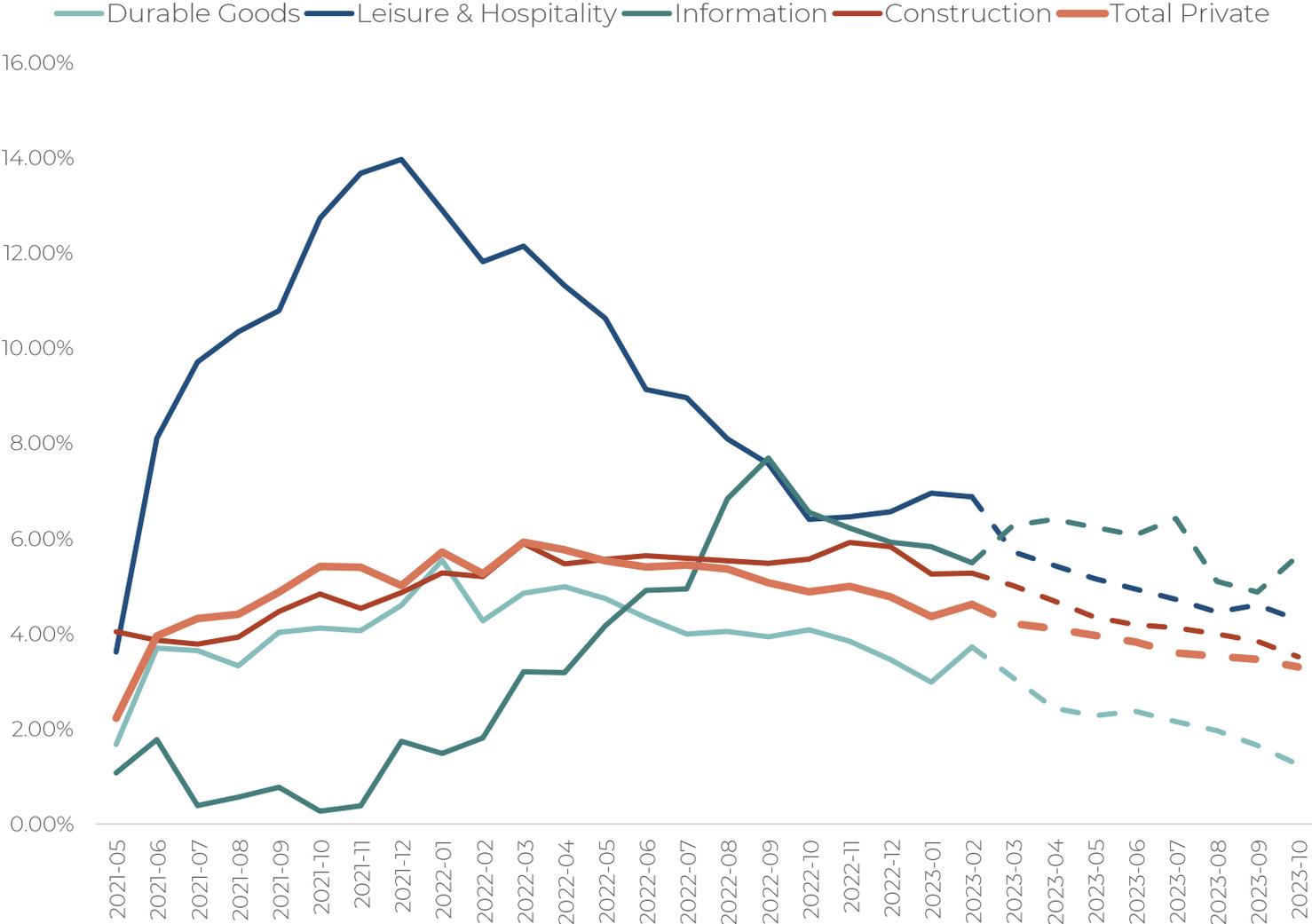
Monthly Job Adds By Industry



- February Monthly Jobs Change [3m Average from Nov. – Jan.] by Industry:
 - Leisure & Hospitality: 105k [98k]
 - Professional & Business Services: 45k [25k]
 - Health Care & Social Assistance: 62.8k [77k]
 - Government: 46k [62k]
 - Trade, Transportation & Utilities: 38k [3k]
 - Goods-producing: 20k [43k]
 - Retail Trade: 50.1k [5k]
 - Private Education Services: 11.4k [14k]
 - Construction: 24k [27k]
 - Transportation & Warehousing: -21.5k [-7k]
 - Manufacturing: -4k [11k]
 - Other Services: 9k [20k]
 - Financial Activities: -1k [7k]
 - Information: -25k [-5k]

Sources: BLS, Moody's Talks, Blue Line Capital, Blue Line Futures

February Wage Trends Extrapolation

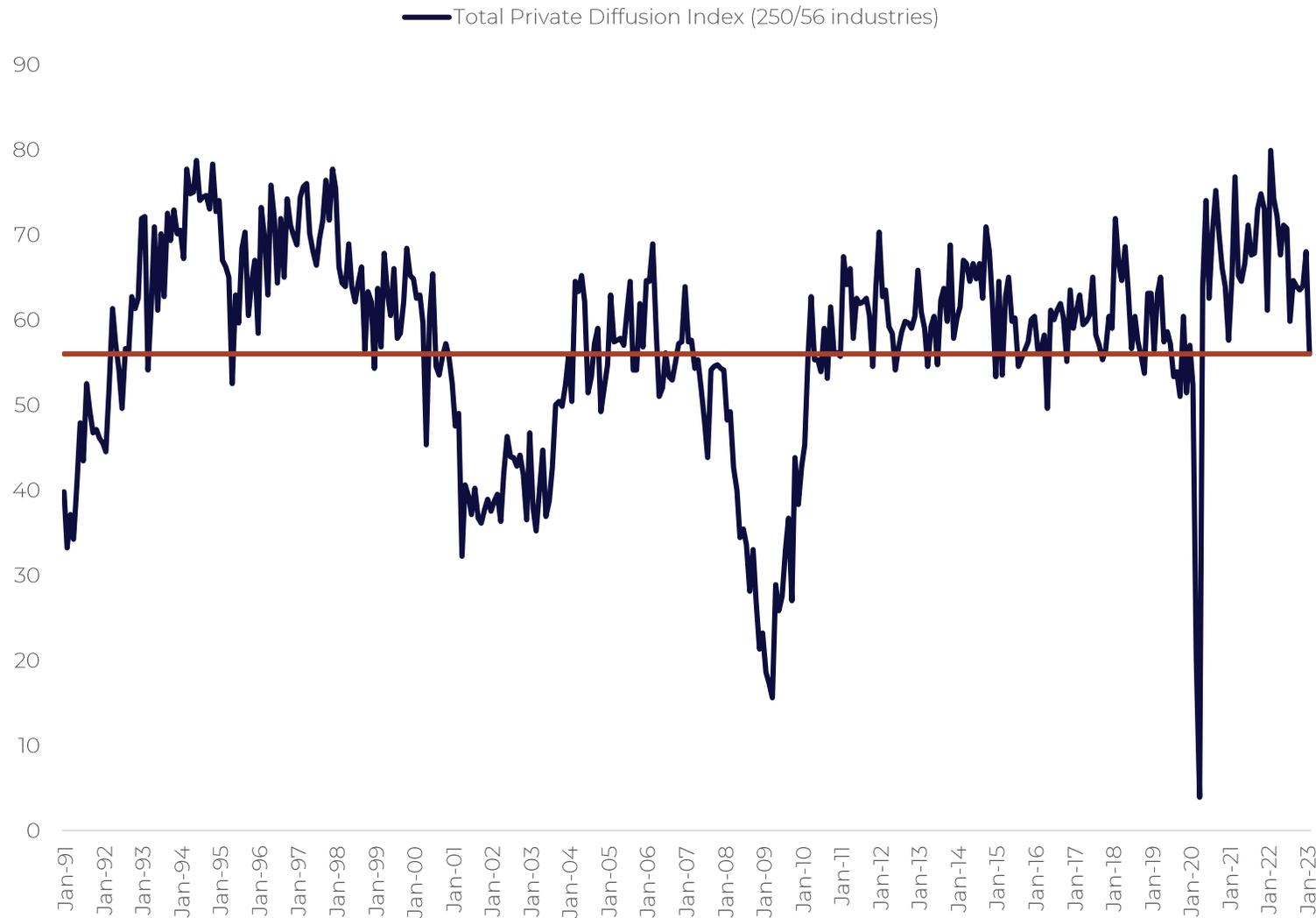


- M/M [Y/Y] February Wage Data:
 - Total Private: 0.24% [4.62%]
 - Construction: 0.25% [5.27%]
 - Information: 0.59% [5.49%]
 - Leisure & Hospitality: 0.29% [6.88%]
 - Durable Goods: 0.06% [3.72%]

- October 2023 Projections Based on Feb. Monthly Trend:
 - Total Private: 3.30%
 - Construction: 3.51%
 - Information: 5.64%
 - Leisure & Hospitality: 4.29%
 - Durable Goods: 1.25%

Sources: BLS, FRED, Blue Line Capital, Blue Line Futures

Percentage Of Industries Adding Jobs



- **Definition:** The Total Private Diffusion Index reflects the % of total surveyed industries adding jobs (250 of them)
- The index declined to 56 in February's NFP print, the lowest it's been since April 2020.
 - Some loosening of labor markets comes after record high of industries indicating they're adding jobs (79.9% in February 2022)

Sources: BLS, Moody's Talks, Blue Line Capital, Blue Line Futures

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Equity Trends Research

Morgan Stanley

United Health

Adobe

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Morgan Stanley

The Implications Of Silicon Valley
Bank & Financial Stability

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Morgan Stanley Earnings Highlights & Stock Performance

Management Commentary From Q4 2022 Earnings Call

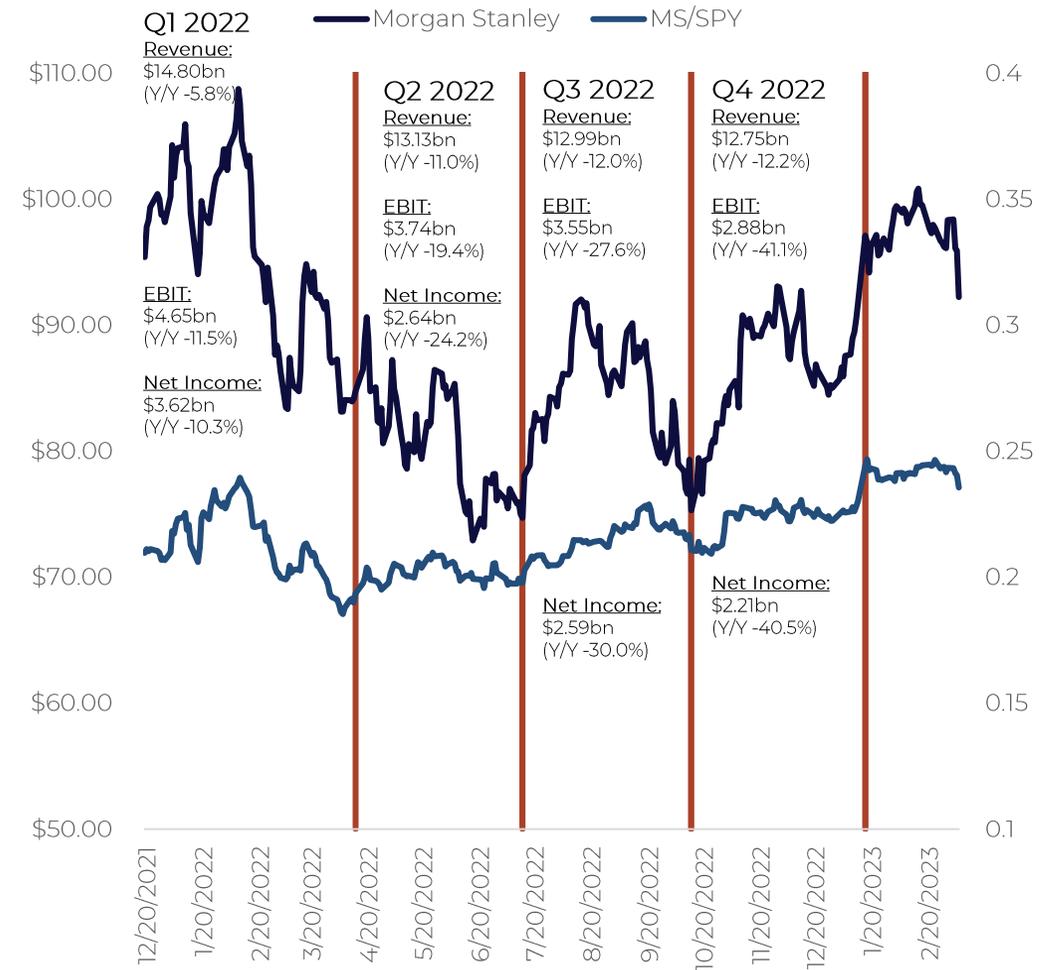
- **Lending Balances:** We've nearly doubled our lending balances over the last 3 years, and we expect to continue to grow attractive high-quality loans.
- **Investment Banking:** Weaker Investment Banking results persisted, reflecting the challenging banking backdrop. Investment Banking revenues were \$5.2 billion for the full year, down 49% from the record prior year.
- **Wealth Management:** For the full year, Wealth Management produced record revenues of \$24.4bn and a record pretax profit of \$6.6bn, resulting in a PBT margin of 27%.
- **Total Deposits:** Total deposits rose 6% sequentially to \$351bn, driven by continued demand for our savings offering among our Wealth Management clients. Approximately 90% of our deposits are sourced from our Wealth Management client base.
- **CET1 Ratio:** Total spot assets were \$1.2 trillion. Standardized RWAs declined by \$9bn sequentially to \$449bn, reflective of our prudent management of resources. Our standardized CET1 ratio was 15.3%, up 50bps from the prior quarter.

	P/E	P/S	Market Cap/FCF	EV/EBITDA	P/B
NTM	12.46	2.68	NA	NA	NA
TTM	14.64	2.84	NA	NA	1.65

*Levered FCF

Sources: Morgan Stanley IR, TIKR, Blue Line Capital

Quarterly Data



Morgan Stanley Expectations & Returns

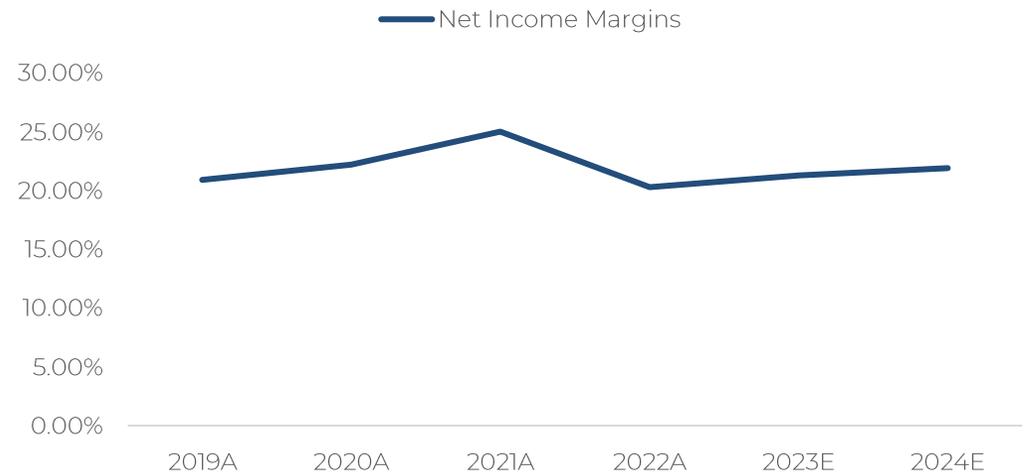
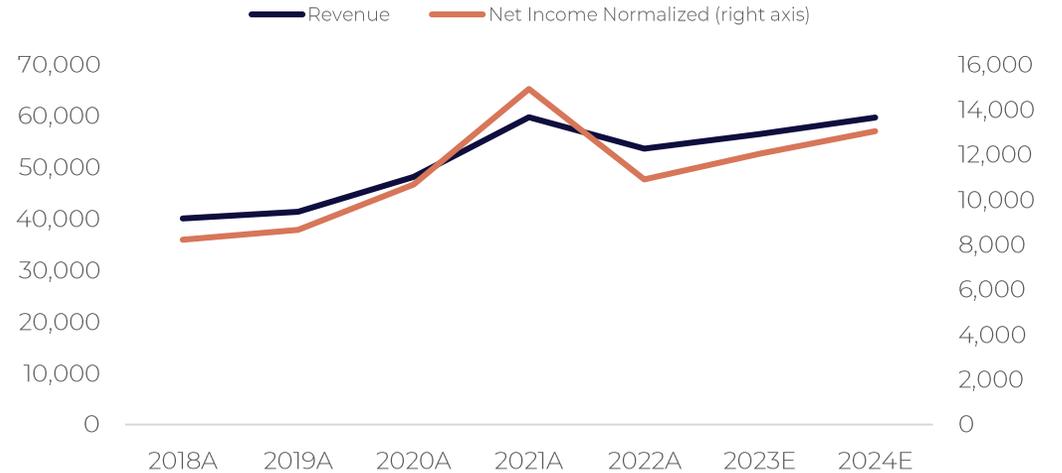
Return Ratios Compared To 2019

Capital Ratios have worsened since 2019 while margins have contracted slightly.

		LTM	2019
Return Ratios	RoA	0.90%	1.10%
	RoC	NA	NA
	RoE	10.80%	11.30%
Margins	Gross Profit Margin	87.00%	88.70%
	EBITDA Margin	NA	NA
	Net Income Margin	20.70%	21.90%
	Levered Free Cash Flow Margin	NA	NA
Asset Turnover	Asset Turnover	NA	NA
	Fixed Asset Turnover	NA	NA
	Receivables Turnover	NA	NA
	Working Capital Turnover	NA	NA
Solvency	Total Debt/Equity	363.00%	366.70%
	Total Debt/Capital	78.40%	78.60%
	Tier 1 Capital Ratio %	17.20%	18.60%
	Total Capital Ratio %	19.30%	21%

Sources: Morgan Stanley IR, TIKR, Blue Line Capital

Revenue and Net Income Estimates



Morgan Stanley Valuation Vs. Peers

	EV/EBITDA	NTM P/E	Past 3M Return	Past 6m Return	Past 12m Return
Morgan Stanley (MS)	NA	12.46	-1%	3%	18%
Goldman Sachs (GS)	NA	9.55	-10%	0%	13%
JP Morgan (JPM)	NA	10.50	0%	15%	16%
Bank of America (BAC)	NA	8.82	-8%	-11%	-6%
StoneX (SNEX)	NA	10.8	5%	14%	32%
Charles Schwab (SCHW)	NA	13.4	-27%	-20%	-5%
Blackstone (BX)	NA	16.64	-3%	-15%	-17%
Median	NA	10.80	-3%	0%	13%
Mean	NA	11.74	-6%	-2%	7%

Sources: TIKR, Google Finance, Blue Line Capital

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Blue Line Capital maintains a long position in Morgan Stanley.

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BLUE LINE CAPITAL

United Health

Healthcare In A Slowing Economy



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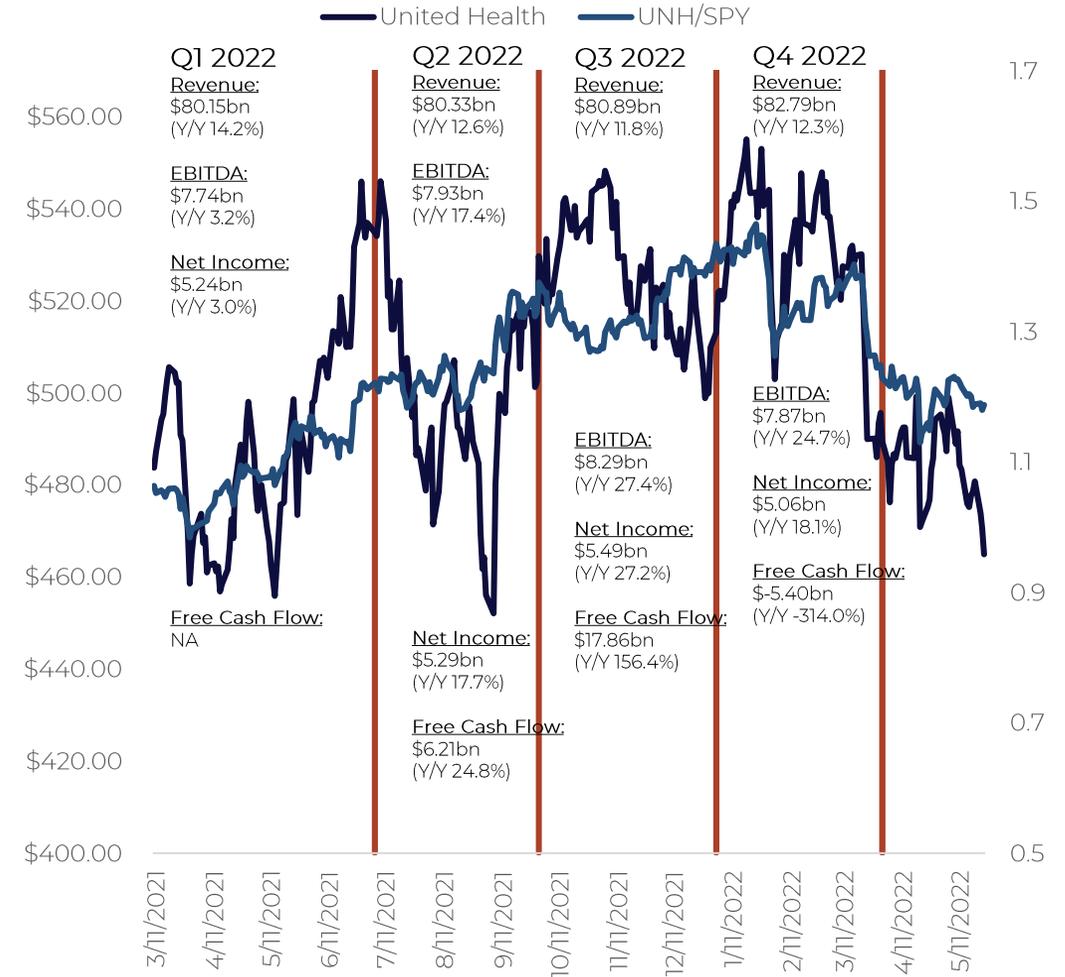
United Health Earnings Highlights & Stock Performance

Management Commentary From Q4 2022 Earnings Call

Business Trends:

- Optum Health:** We expect 4 million people will participate in fully accountable value-based care provided by Optum Health, almost 1.8 million more than we served as we enter 2022.
 - Revenues grew by 32% in '22 to \$71bn as we expanded the number of patients served under value-based care arrangements by about 1 million. Revenue per consumer grew by 29%.
- Pharmacy:** We engage 1 million people every day...simplifying access through digital solutions in order to make the process uneventful for them. By the end of 2023, we expect to have more than 750 community pharmacies, nearly 200 more than we had at the beginning of 2020. We continue to see the impact these services have at a very local and personal level, helping providers deliver more complete care and better outcomes including medication adherence rates, which are about 90% compared to the 50% U.S. average.
- Optum Insights:** Revenues grew 20% to \$14.6bn in '22.
- OptumRx:** Revenues grew 9%, approaching \$100bn for the year.
- United Healthcare:** Full year revenues of nearly \$250bn grew 12%. Expect to serve up to 900,000 more people in '23 across our individual, group and dual special needs offerings.

Quarterly Data



	P/E	P/S	Market Cap/FCF	EV/EBITDA	P/B
NTM	18.46	1.19	17.25	13.26	NA
TTM	21.73	1.32	18.87	15.47	5.53

*Levered FCF

Sources: United Health IR, TIKR, Blue Line Capital

United Health Expectations & Returns

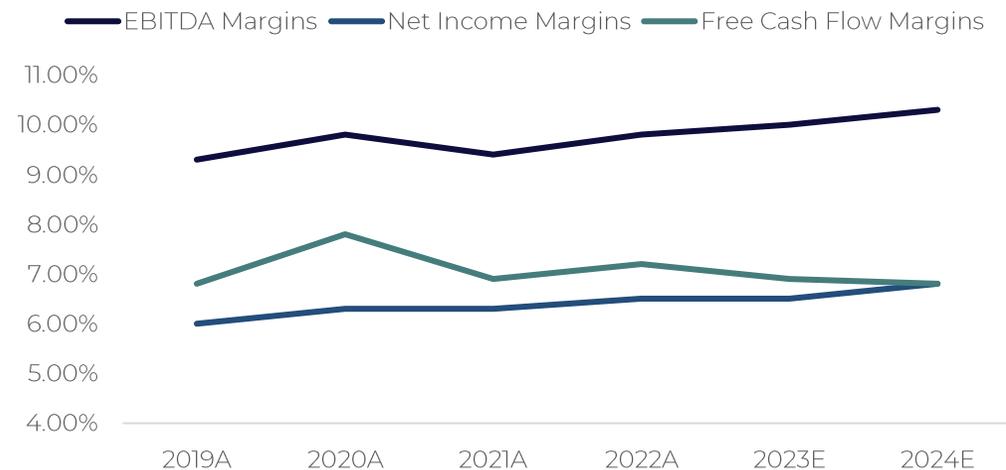
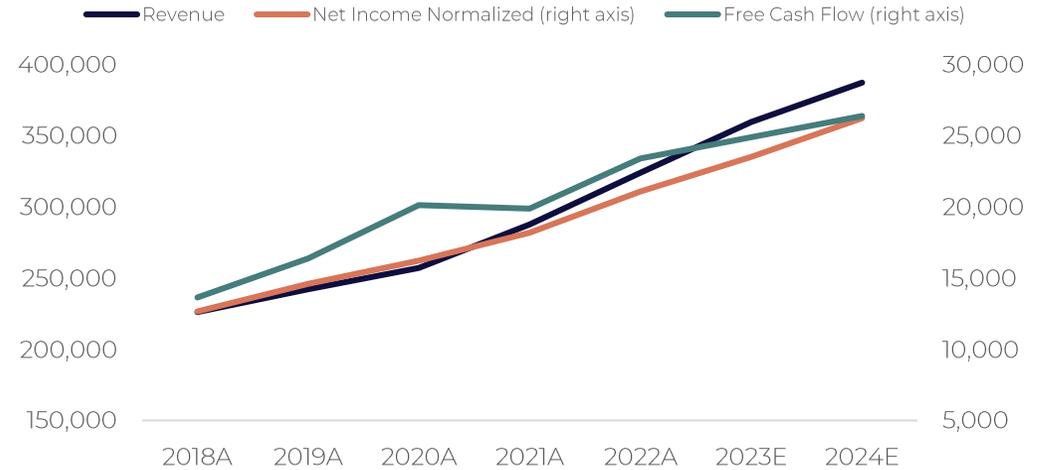
Return Ratios Compared To 2019

Profit margins have improved across the board as solvency ratios have shown mixed developments.

		LTM	2019
Return Ratios	RoA	7.80%	7.50%
	RoC	18.80%	18.60%
	RoE	25.40%	24.10%
Margins	Gross Profit Margin	24.60%	23.80%
	EBITDA Margin	9.50%	9.00%
	Net Income Margin	6.20%	5.70%
	Levered Free Cash Flow Margin	7.00%	6.40%
Asset Turnover	Asset Turnover	1.32	1.39
	Fixed Asset Turnover	57.3	42.15
	Receivables Turnover	NA	NA
	Working Capital Turnover	-13.36	-10.9
Solvency	Total Debt/Equity	72.30%	65.40%
	Total Debt/Capital	41.20%	38.40%
	EBITDA/Interest Expense	15.36	12.73
	(EBITDA-Capex)/Interest Expense	14.02	11.51

Sources: United Health IR, TIKR, Blue Line Capital

Revenue, Net Income, and FCF Estimates



United Health Valuation Vs. Peers

	EV/EBITDA	NTM P/E	Past 3M Return	Past 6m Return	Past 12m Return
United Health (UNH)	13.26	18.46	-16%	-10%	-1%
CVS Health (CVS)	7.59	8.72	-26%	-23%	-16%
Cigna Group (CI)	9.23	11.14	-19%	-4%	12%
HCA Healthcare (HCA)	9.04	14.35	2%	16%	36%
Humana (HUM)	11.61	17.06	-9%	2%	11%
Cardinal Health (CAH)	7.74	12.1	-10%	7%	39%
Molina Healthcare (MOH)	7.79	13.21	-26%	-24%	0%
Median	9.04	13.21	-16%	-4%	11%
Mean	9.47	13.58	-15%	-5%	12%

Sources: TIKR, Google Finance, Blue Line Capital

Adobe

The Future Of SaaS In This Economy



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Adobe Expectations & Returns

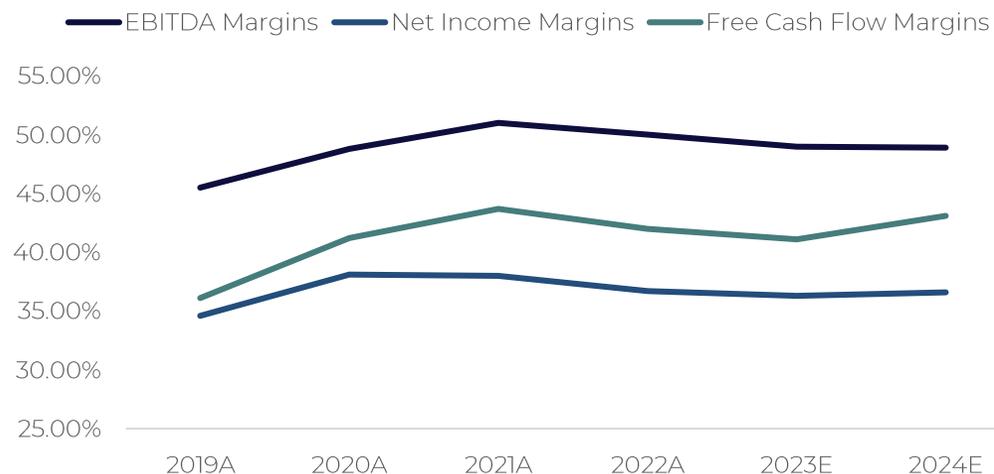
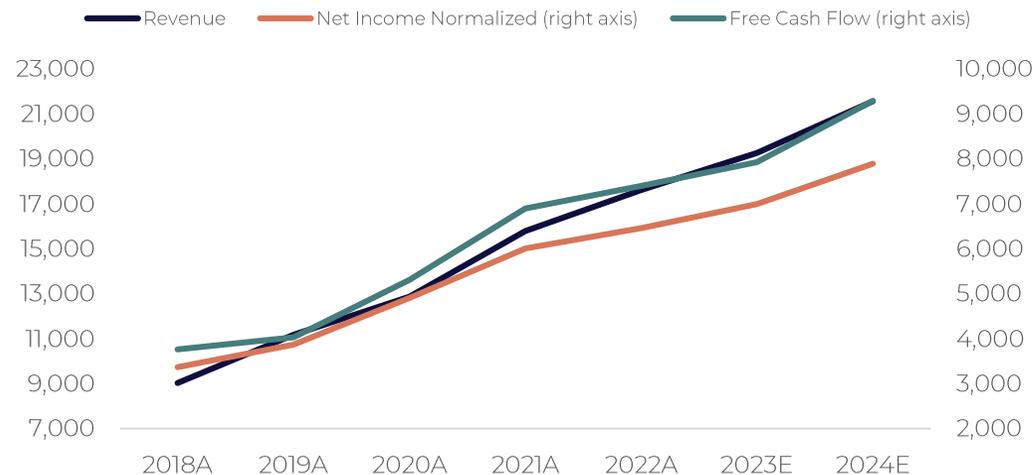
Return Ratios Compared To 2019

Return ratios have strengthened across the board and so have profit margins.

		LTM	2019
Return Ratios	RoA	14.00%	10.30%
	RoC	32.60%	22.10%
	RoE	33.00%	29.70%
Margins	Gross Profit Margin	87.70%	85.00%
	EBITDA Margin	38.10%	36.00%
	Net Income Margin	27.00%	26.40%
	Levered Free Cash Flow Margin	35.60%	28.20%
Asset Turnover	Asset Turnover	0.65	0.54
	Fixed Asset Turnover	7.95	9.43
	Receivables Turnover	8.93	7.84
	Working Capital Turnover	202.8	-6.59
Solvency	Total Debt/Equity	33.00%	39.30%
	Total Debt/Capital	24.80%	27.90%
	EBITDA/Interest Expense	61.04	25.64
	(EBITDA-Capex)/Interest Expense	57.1	23.12

Sources: Adobe IR, TIKR, Blue Line Capital

Revenue, Net Income, and FCF Estimates



Adobe Vs. Peers

	EV/EBITDA	NTM P/E	Past 3M Return	Past 6m Return	Past 12m Return
Adobe (ADBE)	15.86	21.56	-3%	-11%	-13%
Microsoft (MSFT)	17.18	25.11	-2%	-1%	-1%
Shutterstock (SSTK)	10.95	17.45	38%	30%	27%
Getty Images (GETY)	10.75	25.89	-4%	-54%	-50%
Salesforce (CRM)	16.94	24.27	30%	10%	3%
Alphabet (GOOGL)	9.30	17.71	-3%	-13%	-17%
Avid Technology (AVID)	14.42	17.32	5%	12%	12%
Median	14.42	21.56	-2%	-1%	-1%
Mean	13.63	21.33	9%	-4%	-6%

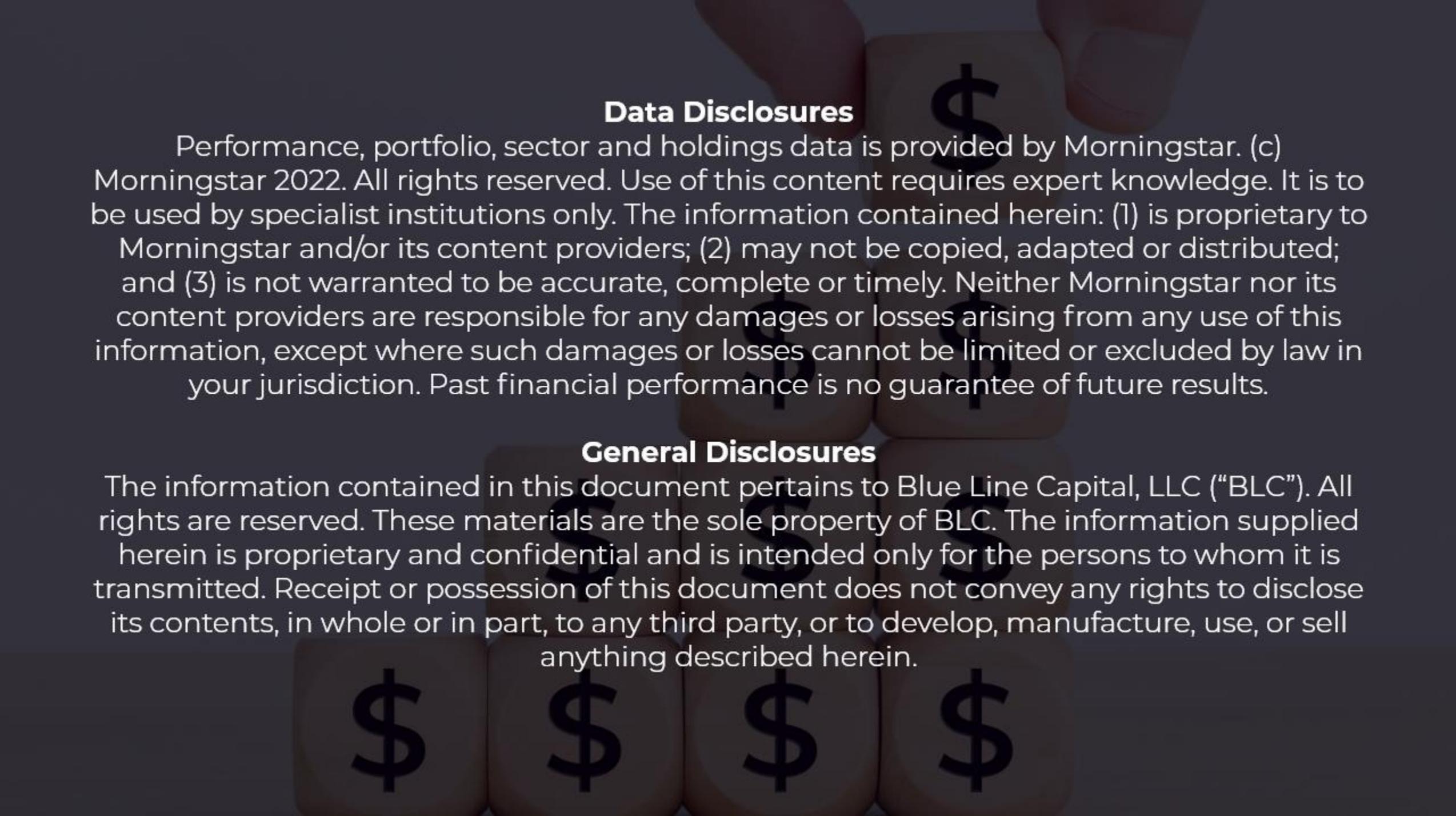
Sources: TIKR, Google Finance, Blue Line Capital

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Blue Line Capital maintains a long position in Adobe.

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