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Interest Rate Risk in the Banking Book (IRRBB)

February 2025

Association for Financial Markets in Europe
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1. Introduction

Introduction

The landscape of Interest Rate Risk in the Banking Book (IRRBB) is undergoing significant transformation, driven by a confluence of shifting economic conditions, financial stability concerns, market expectations, evolving regulatory frameworks, changing capital requirements, technological advancements, and pressures on profitability and capital. The dynamic nature of interest rates and economic conditions has underscored the importance of robust IRRBB management to underpin earnings, protect capital and thus financial stability, and compliance with regulatory expectations. To navigate these complexities, banks must stay ahead of these challenges to effectively manage interest rate risk within their banking books.

Managing IRRBB involves balancing economic value and earnings-based measures to mitigate potential risks. This thought piece, developed by PwC and the Association for Financial Markets in Europe (AFME), delves into the intricate dynamics of IRRBB management under current and forthcoming regulatory regimes. We will explore the implications of the Net Interest Income (NII) and Economic Value of Equity (EVE) supervisory outlier tests (SOTs), amendments to regulatory stress shocks, and the potential impact of a more standardised approach to interest rate risk.

Additionally, we will examine the evolving clarity around Credit Spread Risk in the Banking Book (CSRBB) and its interplay with IRRBB. Identifying overlaps and how to approach the potential for correlation of risks in the capital approaches to IRRBB and CSRBB is critical for effective risk management. By addressing these areas, banks can better navigate the complexities of interest rate risk and credit spread risk, ensuring financial stability and robust risk management practices in an ever-changing financial landscape.

In this thought piece, we aim to provide detailed insights and practical guidance to help banks and financial institutions align with regulatory expectations, optimise their risk management strategies, and ultimately bolster their resilience in the face of evolving financial market challenges.

Changing Macro Environment and Regulatory Landscape

The current macroeconomic environment is marked by significant interest rate volatility, driven by various factors such as central bank policies, inflationary pressures, and global economic uncertainties. This volatility has heightened the need for banks to implement effective IRRBB management practices to mitigate potential adverse impacts on their economic value and earnings stability.

Market Volatility and Monetary Policy Shifts

In response to the economic impact of the COVID-19 pandemic, central banks around the world implemented significant monetary policy measures, including interest rate adjustments and quantitative easing programs. These policies were designed to support economic stability by lowering borrowing costs and increasing liquidity in the financial system. However, they also had a profound impact on interest rate risk management. The rapid and often unexpected changes in interest rates affected the yield curves, influencing the valuation of fixed-income assets and the behaviour of non-maturity deposit models.

Since 2022, central banks shifted their monetary policy stance, leading to interest rate hikes aimed at curbing inflation post-pandemic. These hikes complicated interest rate risk management, steepened (then inverted) yield curves, and increased market volatility. For banks, these developments heightened the challenges associated with modelling and managing non-maturity deposits, as customer behaviours reacted unpredictably to changing interest rates. Additionally, banks faced the necessity of enhancing their IT infrastructure to support improvements in risk management frameworks, with a stronger emphasis on robust scenario analysis and stress testing.

Periods of market turbulence such as this, underscore the critical need for robust IRRBB management. During this period, banks faced unprecedented challenges with margin compression as a result of emergency cuts to policy rates, and customer behaviour becoming less predictable. The economic uncertainty and fluctuating market conditions, including monetary easing, led to unexpected deposit inflows and outflows, complicating the modelling and management of NMDs. Additionally, the subsequent increases in interest rates posed further challenges, as they intensified interest rate sensitivity and liquidity pressures.

Understanding and anticipating these policy shifts became crucial for effective IRRBB management. Financial institutions needed to closely monitor central bank communications and economic indicators to better predict policy changes. This required enhancing their risk management frameworks to incorporate scenario analysis and stress testing that accounted for a wide range of potential monetary policy outcomes. The experience highlighted the importance of agility and preparedness in managing interest rate risk in an environment characterized by significant and rapid policy shifts.

Banking Crises in the US and Europe (2023)

The banking industry experienced significant turmoil due to crises in the US and Europe in 2023. In the US, regional banks such as Silicon Valley Bank (SVB) and First Republic Bank encountered severe liquidity issues, leading to regulatory takeovers or acquisitions by larger institutions. SVB, in particular, faced critical challenges related to Interest Rate Risk in the Banking Book (IRRBB). With a substantial portfolio of long-term fixed income securities, SVB was exposed to rising interest rates, which sharply reduced the market value of these assets. The bank's failure to effectively manage this interest rate risk led to liquidity strains as it struggled to meet withdrawal demands for deposits that were less 'sticky' than anticipated after considering its monetisation strategy. In Europe, the risk management crisis at Credit Suisse had significant repercussions, leading to its acquisition by UBS. These events highlighted vulnerabilities in banks' asset-liability management and underscored the need for robust IRRBB and CSRBB frameworks.

The turmoil also raises questions about the role and frequency of standardised stress indicators to complement the analytical toolbox available to supervisors under Pillar 2. For example, to what extent should existing indicators be reported/disclosed on a more frequent basis? Is there additional value in developing additional indicators?

Regulatory Landscape

In recent years, the regulatory landscape for IRRBB has evolved significantly. The Basel Committee on Banking Supervision (BCBS) has introduced more expansive guidelines, emphasizing the need for banks to adopt robust risk management frameworks. The updated guidelines require banks to measure and manage IRRBB using both economic value and earnings-based approaches. Moreover, there is a greater emphasis on stress testing, scenario analysis, and the incorporation of behavioural assumptions in risk assessments. CSRBB, on the other hand, while traditionally overshadowed by IRRBB, has gained prominence as market conditions have underscored the potential volatility and impact of credit spreads on banks' balance sheets.

Regulators have increasingly recognised the importance of CSRBB and have begun to integrate it into broader risk management frameworks. The European Banking Authority (EBA), for instance, has provided guidelines that require banks to identify, measure, and manage CSRBB as part of their overall risk management processes. This includes regular monitoring, stress testing, and ensuring that sufficient capital is held against potential adverse movements in credit spreads.

The regulatory landscape for IRRBB and CSRBB has matured significantly, with detailed guidelines and standards now in place to guide banks' risk management practices. However, this maturity is not yet complete. There are still areas where IRRBB and CSRBB risk management practices are not fully integrated with the broader regulatory framework, necessitating continuous refinement and adaptation by banks.

What are the Drivers of Regulatory Changes?

Regulatory bodies such as the Basel Committee on Banking Supervision (BCBS) and EBA have updated guidelines and frameworks to address IRRBB, including revised requirements for measuring, managing, and mitigating interest rate risk. The drivers behind these changes are:

Economic Factors

Higher Interest Rate Environment: The transition from a low-rate to a rising rate environment has led regulators to implement more conservative interest rate shocks. The BCBS's recalibration of shocks in the IRRBB standard, aims to make these shocks more conservative, ensuring banks hold sufficient capital against potential interest rate risks.

Economic Uncertainty: Events such as the COVID-19 pandemic and geopolitical tensions have caused volatile interest rate movements. Regulators, including the EBA, emphasises robust IRRBB management practices to help banks navigate these uncertain times and ensure financial stability.

Credit Spread Volatility: Recent events, including the crisis involving Silicon Valley Bank (SVB), have highlighted the potential for CSRBB to amplify the impacts of IRRBB. While SVB's challenges primarily stemmed from its portfolio of inadequately hedged fixed-income securities, the widening of credit spreads can further decrease valuations, exacerbating liquidity and capital pressures. In response, regulators like the EBA are emphasizing enhanced stress testing and capital buffers to better manage these interconnected risks.

Market Expectations and Regulatory Scrutiny

Investors and stakeholders are increasingly focused on how banks manage their interest rate risk. Regulators view effective IRRBB management as a key indicator of a bank's overall risk management capabilities. Heightened regulatory scrutiny and more frequent stress testing are measures that regulators use to ensure banks effectively manage interest rate risk, and stress the importance of these practices to maintain investor confidence.

The EBA has already updated its guidelines to include more stringent stress testing requirements and enhanced IRRBB management practices. The BCBS, with its upcoming recalibration of shocks in the IRRBB standard, drives banks to strengthen their risk management practices. Banks are under increased pressure to improve their measurement tools and ensure they hold adequate capital to withstand adverse scenarios.

Financial Stability

Poorly managed IRRBB can lead to significant losses, both economically and in accounting terms, affecting individual banks and the broader financial system. This is particularly relevant for securities held as Held to Maturity (HTM). SVB had to sell its portfolio of fixed-income assets, originally held at amortized cost, to meet simultaneous deposit withdrawals, which played a significant role in its failure. This underscores the risk that if unrealised losses of HTM securities are not adequately reflected, regulatory capital might overstate a bank's shock-absorbing capacity. Regulators, including the BCBS, emphasise the need for robust IRRBB frameworks to safeguard financial stability. Banks must adhere to these frameworks to prevent systemic risks and ensure confidence in the financial system, while also considering how accounting practices for HTM securities impact their reported financial health and regulatory capital.

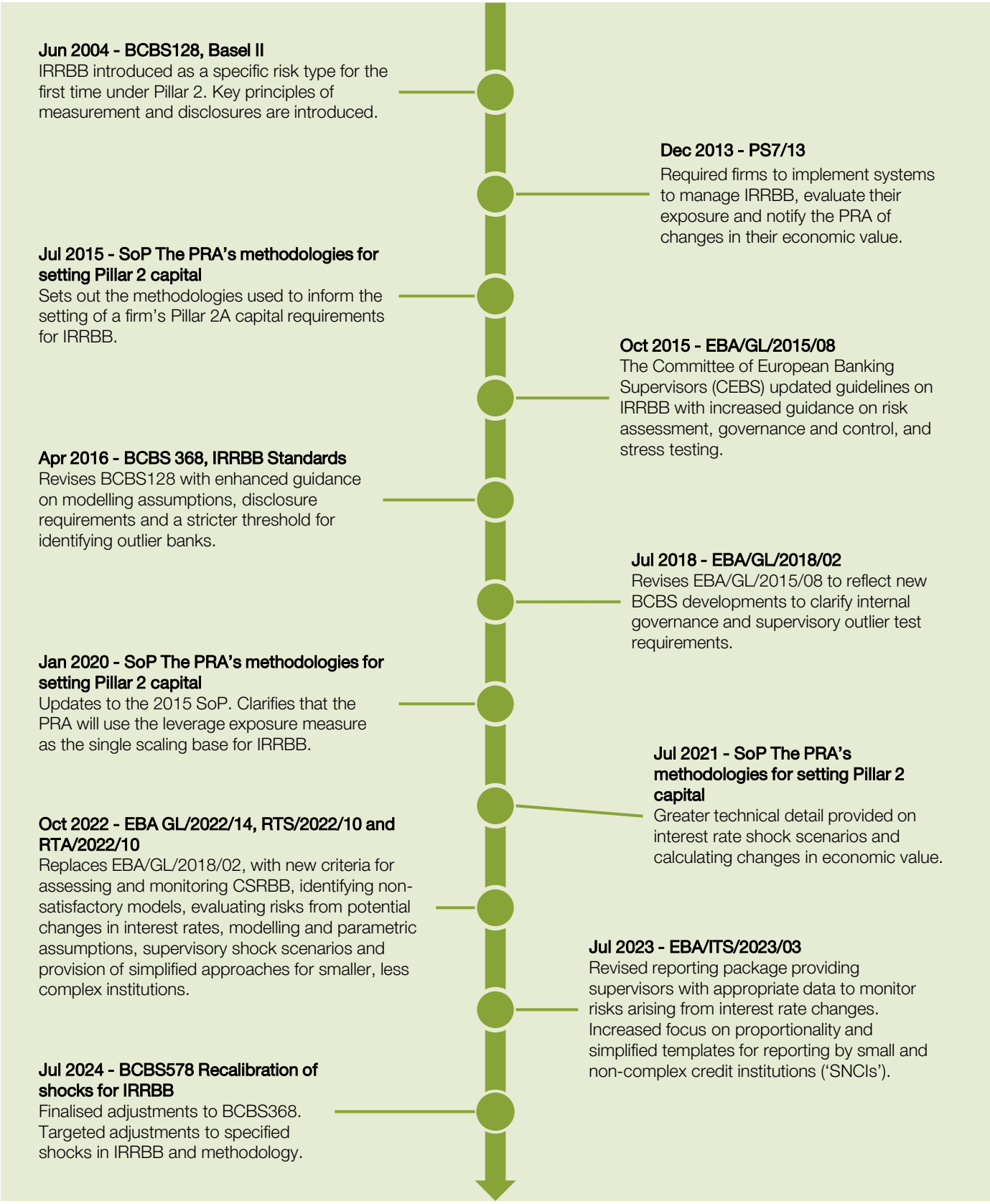
Technological Advancements

Advances in financial technology provide banks with sophisticated tools for managing interest rate risk but also require continuous updates to models and systems. In its October 2022 publication, the EBA emphasised the importance of robust internal models over the standardised approach for managing IRRBB and CSRBB. Regulators encourage the adoption and effective integration of these technologies and models to meet evolving regulatory expectations and market conditions. Banks need to stay current with technological developments and ensure their internal models are regularly updated and validated to comply with regulatory standards.

Evolution of Regulatory Frameworks

Over the past two decades, the regulatory landscape governing IRRBB has evolved significantly. Key milestones in this evolution include:

Figure 1: **Timeline of Key IRRBB Regulatory Developments**



2. Complementary measures: the need to balance both economic value and earnings-based measures

ALM practitioners are well versed in the balancing act which managing IRRBB entails, aiming to smooth the impact to NII from unexpected movements in interest rates. Conventionally this is achieved by increasing asset duration, typically to match the behavioural duration of liabilities or other sources of funding whose pricing is either insensitive to or does not fully move in line with market interest rates.

Take too little asset duration and NII may be inadequately protected against these unexpected rate shocks, add too much and you risk financially underperforming peer institutions or worse, potentially tearing up loss-making hedge positions having overestimated the risk that you were trying to mitigate.

Add to this the fact that risk conditions rarely remain static across the interest rate cycle, and the optionality typically embedded in customer products, and you'll see that an ALM risk manager's role is not so much about eliminating risk given that a single 'risk neutral' position does not exist, more so, it requires the management of competing risks within a holistic risk appetite.

This also manifests in the risk measurement approaches undertaken by banks, with measures of NII or earnings sensitivity to changes in interest rates informing of the risk to income, and economic or present value based approaches considering the impact of longer term duration mismatches in the balance sheet.

The need for both approaches was underscored in the Basel principles on IRRBB (BCBS 368) published in 2016, which formed the basis of subsequent global regulation in this area including from both the EBA and PRA.

Historically though, the regulatory focus has largely been on value-based measures, such as the Economic Value of Equity ('EVE'), or variants of this being used by regulators to identify whether excessive levels of interest rate risk were being taken at an individual institution level. These measures also typically formed the basis of banks' own assessments of the Pillar 2 capital to be held against potential losses related to interest rate risk in the banking book.

Initially, the EVE was subject to a standard outlier test ('SOT') with a threshold of 20% of Tier 1 capital based on a 200bp parallel up or down shock to the yield curve. BCBS 368 introduced a currency level risk-based calibration of the shocks and a further four non-parallel shocks to the curve, with a tightening in the outlier threshold to 15% of Tier 1 capital.

This had the impact of limiting significant interest rate-related mismatches across banks' balance sheets, and the duration risk that banks were willing to take when stabilising income from positions funded by capital reserves, conventionally these being non-interest bearing in nature.

This regulatory focus on value-based measures was often counter-balanced by banks' primary focus being on income stabilisation, and putting in place self imposed appetites on the potential risk to their shorter term commercial performance from unexpected movements in interest rates.

In the EBA publication titled 'Guidelines on IRRBB and CSRBB' released in October 2022, the EBA sought to "book-end" the range of duration that banks could operate within by implementing an NII-based standard outlier test to complement the existing EVE measure. This sought to prevent banks from either being "under-" or "over-" hedged, leading them to operate in an area in between.

Initially this was proposed at 2.5% of Tier 1 capital, then subsequently revised to 5% of Tier 1 capital. The rationale behind this calibration was to reflect the significantly changed interest rate environment since the initial publication. The EBA recognised the need to accommodate the new interest rate conditions pragmatically. This adjustment was intended to provide a more realistic and flexible threshold that aligns with the current economic context. The EBA's decision to revise the threshold was also influenced by ongoing analysis and medium-term reflections on the interest rate environment, ensuring that the regulatory framework remains relevant and effective in the face of evolving market conditions.

Complementary measures

The SOTs represent top-down constraints imposed at an overall industry level, and agnostic of individual business models, assumptions or risk management strategies, with some limitations on assumptions, and elements of standardisation in how the risk is measured (see chapter 4).

Whilst the EVE SOT is well ingrained in banks' risk management frameworks, albeit with a changing calibration over time, the NII SOT is very much a new constraint in terms of universal application to EU-based banks.

This development is particularly acute in markets which may not typically offer long term fixed rate lending products to its customers, either within the EU or through EU-headquartered banks' operations in other markets, who may naturally operate with a higher degree of short term income sensitivity to changes in interest rates.

Other banks may choose to be more prudent in managing their short term NII sensitivity, something that has historically been an area for firms to balance commercial interests with risk management considerations when navigating the interest rate cycle.

All firms will want to review and reflect on the critical assumptions that underpin their NII sensitivity, and how volatile or sensitive these may be to changes in economic or customer behaviour, and therefore the risk that these changes may push exposures towards or in excess of the NII SOT.

With the implementation of both an NII and EVE SOT in the EU, there is a need for banks to balance economic value and earnings-based measures when making institution specific choices.

Firms will need to be conscious of how the calculation of SOT metrics reflect the breadth of business models across Europe (and overseas, where relevant), including idiosyncratic assumptions and institutional choices on risk management strategies, and what this means in the context of the SOT calibrated threshold.

Summary of RTS - Supervisory outlier tests (SOTs) changes in the EBA guidelines

Summary of changes in the EBA guidelines

	IRRBB Guidelines (updated July 2018)	RTS on SOT October 2022
Definition of regulatory sensitivity limits	**EVE Sensitivity:** • **< 20%** of total equity under a shock of +/- 200 bps of interest rate curve • **< 15%** of T1 capital under the 6 prescribed scenarios	**EVE Sensitivity:** • Notify the EBA (or PRA, where there is an equivalent requirement for UK firms) if the EVE represents more than 15% of T1 capital (outlier firm). **NII Sensitivity:** • The threshold for a 'large decline' in NII was initially set at 2.5% of Tier 1 capital as of October 2022. This threshold was subsequently changed to 5% of Tier 1 capital in April 2023.
Shock scenarios applicable to EVE and NII	• Six supervisory shock scenarios are prescribed for EVE: ○ Parallel Shock Up ○ Parallel Shock Down ○ Steepener Shock ○ Flattener Shock ○ Short Rates Shock Up ○ Short Rates Shock Down	• The six supervisory shock scenarios are maintained for EVE based on specified sizes of interest rate shocks for major currencies. • The 2 scenarios, parallel shock upwards and parallel shock downwards, are prescribed for the NII sensitivity SOT calculation.
Shock scenarios and shock calculation methods	• The scenarios are calculated on the basis of the interest rate shocks set out in Annex 1 of the Guidelines (the shocks are specified by currency). • The calculation method is specified in the Guidelines for currencies not appearing in the Annex.	• **EVE:** calculated under the assumption of a balance sheet run-off • **NII:** calculated under the assumption of a constant balance sheet
Recalibration of the post-shock interest rate floor	• A maturity-dependent post-shock floor rate to be applied for each currency starting at **-100 bps** for immediate maturities and increasing by **5 bps per year**, reaching 0% for maturities of **20 years** and over.	• **EVE:** a maturity-dependent post-shock floor rate to be applied for each currency starting at **-150 bps** for immediate maturities and increasing by **3 bps per year**, reaching 0% for maturities of **50 years** and over.

Implications for banks of changes to the regulatory frameworks

- Increased regulatory scrutiny on models and assumptions to represent potential behavioural outcomes, and provide a consistent basis for managing NII sensitivity and EVE.
- Potential challenges with the criteria to identify non-satisfactory IRRBB internal models and triggers to use the standardised approach.
- Hedging can be considered a delicate balancing act, invariably with the aim of improving income stabilisation over a given time horizon which may necessarily involve increasing the level of contractual duration risk (the hedge) to mitigate against behavioural duration risk (e.g. deposits) with the potential that the two become not fully or well aligned. An emphasis on the quality of process underpinning this, in addition to focusing on SOT levels and any standardisation of parameters can be beneficial.

3. Regulatory focus on IRRBB

EBA Initiatives: 2024 - Mid 2025

The EBA's initiatives for 2024 to mid-2025 aim to enhance supervisory and risk management tools. Regulatory initiatives are anticipated to concentrate on refining the metrics and indicators employed in the Supervisory Review and Evaluation Process (SREP). Regulators will evaluate whether banks are excessively exposed to IRRBB and whether they manage this risk adequately, with particular focus on the SOT on NII.

Complementary indicators

The application of SOTs is designed to be informative and does not automatically trigger supervisory measures when thresholds are exceeded. The EBA intends to investigate additional complementary indicators for SREP and supervisory stress testing. Feedback from institutions reveals varied approaches: some are using the 5% threshold for the SOT on NII as an internal limit, while others are emphasising alternative early warning metrics. Continuing discussions aim to refine these methodologies and enhance risk management frameworks. Banks will be challenged to integrate these new measures into their existing frameworks, requiring significant changes to current practices, systems and processes to incorporate these indicators.

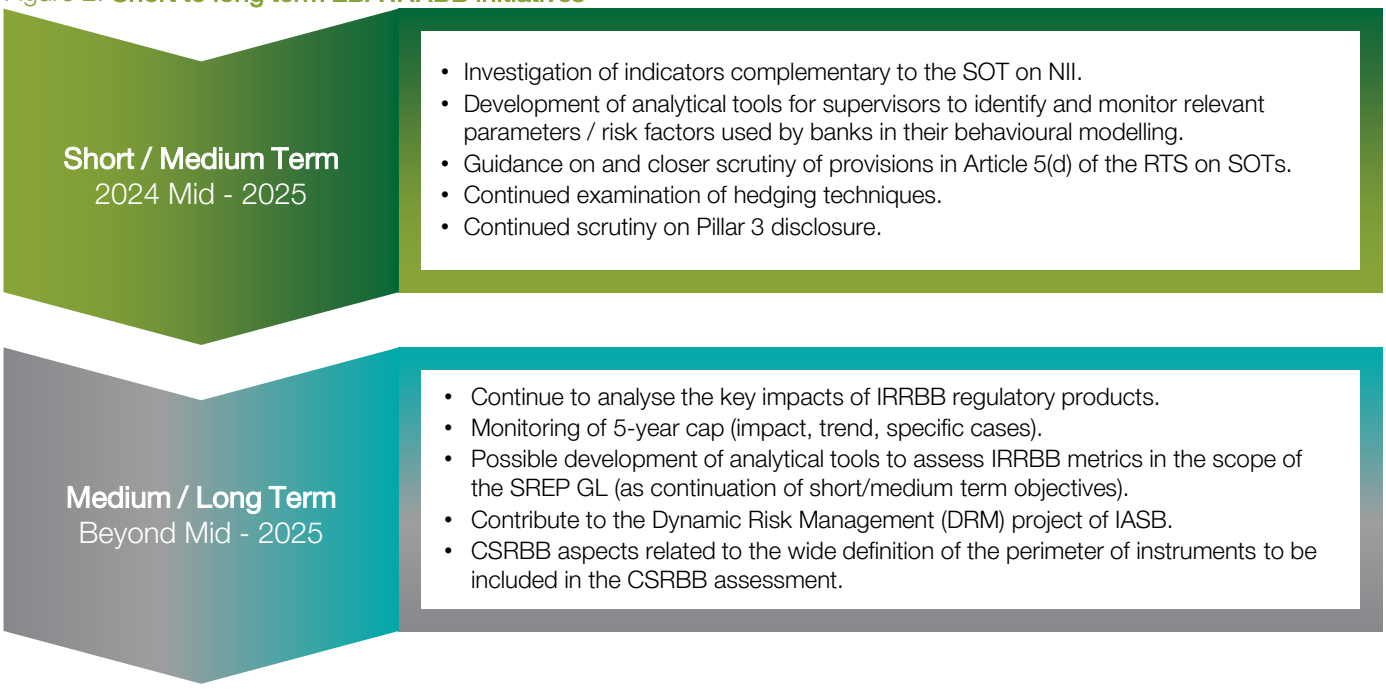
NMD modelling

Regulatory scrutiny on the behavioural modelling of NMDs is expected to intensify. The diverse practices reported by institutions in modelling NMDs suggest that further analysis is necessary, particularly concerning variations in modelling assumptions, estimations of non-core NMDs, and the repricing of retail customer deposits in NII projections. This ongoing analysis will likely continue till mid 2025, with regulators focusing on providing additional guidance where needed.
The work may lead to identifying a non-restrictive list of relevant parameters and risk factors for institutions to consider and for supervisors to monitor.

Analytical tools

The EBA is also exploring the development of analytical tools to support this monitoring, drawing on data from ad-hoc collections and other sources. Additionally, discussions among supervisors and shared experiences will contribute to this effort. Some institutions have indicated potential misunderstandings regarding the constant balance sheet assumptions for the NII metric, which is crucial for accurately reflecting the impact of interest rate changes on NII, particularly in scenarios of rate increases or decreases. The challenge for banks will be the significant cost associated with developing and implementing these tools, as well as the need to recruit skilled personnel to manage them effectively.

Figure 2: **Short to long term EBA IRRBB initiatives**



Regulatory Technical Standards for SOTs

The EBA will provide guidance and closer scrutiny on the provisions of Article 5(d) of the Regulatory Technical Standards (RTS) on SOTs. Compliance with these new regulatory standards will require banks to conduct a thorough review and adjustment of existing processes. This poses a challenge in terms of resource allocation and the potential complexity of understanding and measuring the behaviours driving the repricing of NMDs and migration to term deposits.

Hedge accounting

Banks employ a variety of hedging strategies, often relying on natural hedges or interest rate derivatives to manage interest rate risk. Regulatory scrutiny will concentrate on the diverse hedge accounting practices in use, including cash flow, fair value, micro, and macro hedging methods. Navigating these requirements can be complex, highlighting the intricacies involved in aligning internal practices with regulatory expectations.

Disclosures

The preliminary assessment of the ITS on Pillar 3 disclosure has identified a range of practices. Scrutiny of Pillar 3 disclosures emphasises the need for transparency and quality in regulatory reporting. Some institutions have opted for shock scenarios lower than the standard regulatory shock of 200 bps, such as 25bps, 50bps, or 100 bps, and have used different modelling assumptions. Furthermore, not all qualitative information is disclosed, such as the average maturity of non-maturity deposits (NMDs), which is required under the ITS. Supervisors will be increasingly focused on these aspects. Additionally, some institutions are disclosing the internal methodologies used to measure changes in Economic Value of Equity (EVE) and Net Interest Income (NII) apart from the regulatory metrics.

This diverse landscape reflects the complexity and intricacies involved in aligning internal practices with regulatory expectations, highlighting areas where institutions may face challenges in ensuring comprehensive and consistent disclosures. Improving the comprehensiveness and clarity of these disclosures can be challenging, requiring meticulous attention to detail and possibly the development of new reporting mechanisms. This demands a significant commitment of resources and may require banks to overhaul existing reporting frameworks, particularly in aligning shock scenarios and qualitative disclosures with regulatory expectations, and expanding the associated control frameworks.

EBA Initiatives Beyond Mid - 2025

Looking beyond mid-2025, the EBA continues to enhance its regulatory framework for IRRBB, introducing additional challenges and opportunities. A key focus is the ongoing analysis of the impacts of the product set within the scope of IRRBB. Continuously adapting to these changes ensures that risk management practices remain current and effective, enhancing the bank's resilience to interest rate fluctuations.

NMD modelling parameters

Monitoring the five-year repricing maturity cap for Non-Maturity Deposits (NMDs) and the repricing approaches used across business lines and products remains under regulatory scrutiny. This involves navigating the complexities of accurately assessing core deposit stability amid varying customer behaviours and interest rate scenarios. While modelling the repricing of operational NMDs from financials is permitted as indicated in paragraph 110 of the EBA Guidelines on IRRBB and CSRBB, institutions are adopting different modelling practices.

A closer examination of the behavioural assumptions for NMDs reveals this diversity in approach. As part of this process, banks might need to consider NMDs' characteristics and their stratification according to thresholds for retail and SMEs. Additionally, banks might need to reassess their assumptions regarding the stability and behaviour of these deposits over this period, impacting both liquidity management and risk modelling. Existing hedging frameworks might require adjustments to align with new repricing timelines, necessitating significant changes in interest rate risk management strategies that could potentially affect both Net Interest Income (NII) and Economic Value of Equity (EVE).

Moreover, aligning internal measurement systems with this new cap necessitates enhancements or, for some, involves sophisticated data analytics and stress-testing capabilities to ensure accurate monitoring and management of interest rate and liquidity risk. This shift represents a significant step toward a more uniform approach to handling NMDs across the industry, prompting institutions to adapt their business models and financial strategies to this standardized horizon. Although assessing the impact and trends related to this cap requires detailed analysis and continuous monitoring, it provides valuable insights into specific cases and broader market trends, aiding banks in adjusting their strategies to mitigate potential risks and maintain financial stability.

Analytical tools

The development of new analytical tools to assess IRRBB metrics within the Supervisory Review and Evaluation Process (SREP) guidelines represents a significant initiative. With the diverse range of models implemented by institutions, regulators and supervisors aim to gain a deeper understanding of how IRRBB risks are assessed and managed. This includes examining the adaptation of modelling assumptions, repricing rates, hedging strategies, back-testing methods, and the application of expert judgment and manual adjustments. These efforts have the potential to enhance the precision of risk evaluations and ensure readiness to meet regulatory demands. However, navigating these areas may present challenges in aligning existing risk assessment methodologies with evolving regulatory expectations.

In addition to these technical developments, there is a broader assessment of interest rate risk management from a prudential perspective. This involves scrutinizing changes in modelling assumptions and hedging strategies, as well as exploring potential implications for business models and lending strategies in the context of current interest rate environments. The complexity arises from having to align internal practices with external regulatory expectations, which can impact strategic decision-making, risk management, and operational processes. However, harmonizing institutional practices with evolving prudential standards remains a challenge, requiring careful alignment with regulatory expectation.

Hedge accounting

Furthermore, regulators will continue to monitor and engage with institutions on macro hedging and its alignment with the International Accounting Standards Board (IASB) project on Dynamic Risk Management. Institutions will need to align risk management practices with emerging global standards.. Such efforts are crucial in complementing the management of interest rate risks while maintaining competitiveness and regulatory compliance. However, participating in this initiative might require additional resources and coordination, presenting a challenge for institutions as they strive to integrate these global standards into their existing frameworks.

CSRBB

The EBA also emphasises the importance of addressing Credit Spread Risk in the Banking Book (CSRBB) by expanding the scope of instruments included in the assessment. Broadening the perimeter of CSRBB assessments can be complex and resource-intensive, but it ensures a comprehensive evaluation of all relevant risks, enhancing the bank's ability to manage and mitigate credit spread risks effectively.

Overall, these initiatives from 2024 through beyond mid - 2025 by the EBA require banks to continually adapt and refine their risk management frameworks. While these efforts demand significant resources and continuous attention, they offer substantial benefits in terms of alignment between regulatory and internal practices, enhanced risk management, and overall financial stability.

IRRBB Heatmap Implementation: 1st Phase- Short/Medium Term Action Plan

The IRRBB heatmap latest publication in February 2025 introduces significant updates in four key areas: refining NMD behavioural assumptions, incorporating complementary dimensions to the SOT on NII, enhancing the modelling of commercial margins of NMD in the SOT on NII, and optimizing hedging strategies. These updates aim to address the complexities of NMD modelling, improve the assessment of IRRBB exposures, ensure consistent commercial margin modelling, and leverage interest rate swaps for effective hedging.

NMD behavioural assumptions

The EBA highlights the complexity involved in modelling non-maturity deposits due to their unique characteristics. It underscores the importance of understanding the repricing behaviour of NMDs, which is influenced by various risk factors, including customer, institution, and market profiles. A toolkit is proposed for supervisors to analyse NMD modelling, incorporating segmentation, peer benchmarking, stress testing, expert judgment, and historical data analysis. Banks face regulatory scrutiny on modelling these deposits as they face challenges in accurately assessing core deposit stability due to varying customer behaviours and interest rate scenarios, necessitating adjustments in hedging frameworks to align with new repricing timelines. As a next step, EBA will extend its analysis to include a broader range of products, ensuring a comprehensive approach to NMD modelling.

Complementary dimensions to the Supervisory Outlier Test (SOT) on the NII metric

The EBA is exploring additional dimensions for the SOT on the NII metric, such as market value changes of fair value instruments, and interest rate sensitive fees, to provide a more comprehensive understanding of IRRBB exposures. It clarifies that the SOTs are framed under the SREP as indicators, with no automaticity in the exercise of supervisory measures for institutions exceeding the SOT threshold. It proposes additional dimensions to support supervisors in assessing IRRBB exposures and management for institutions identified as outliers, without setting new requirements, limits or thresholds. Banks will face challenges in integrating these new measures into their existing frameworks, which may involve additional resource allocation and system upgrades. As a next step, the EBA plan to develop additional indicators to support supervisors in their assessments and ensure integration into the broader regulatory framework.

Modelling commercial margins of NMD in the SOT on NII

The updates provide detailed guidance on modelling and projecting commercial margins of NMD in the SOT on NII, emphasising consistency with internal measurement systems and suggesting a constant spread over the risk-free rate if specific modelling assumptions are absent. It also highlights the importance of considering behavioural options, such as the elasticity of product rates to market interest rate changes, and recommends a prudent and conservative approach to modelling commercial margins, taking into account the current spread environment and the distance from a zero or negative rate environment. Additionally, the EBA sets supervisory expectations for institutions to apply modelling assumptions conservatively, with a default solution of constant margins if modelling assumptions are not applied. Challenges for banks include aligning their internal systems with regulatory expectations, and adapting modelling practices where necessary. As a next step, the EBA plans to extend the analysis of commercial margin modelling in the SOT on NII to include products beyond NMDs, aiming to enhance understanding and management across various financial products.

Hedging strategies

The EBA analysis shows institutions primarily use interest rate swaps to mitigate open IRRBB risk positions. Variability in hedging practices exists, with no outliers in the SOT on EVE, but potential outliers if derivative hedges are disregarded. The EBA recommends using derivatives for hedging, not speculation. It points out the fragmented landscape of hedging practices across institutions and advises against changing liability repricing assessments based on asset profiles. The quality of the process underpinning hedging strategies is emphasised, along with the need for standardization of parameters to ensure effective risk management. Banks may face challenges in aligning these strategies with evolving regulatory expectations.

The EBA will continue examining hedging techniques and contribute to the IASB's Dynamic Risk Management project, with ongoing monitoring of hedging strategies.

Re-calibration of regulatory interest rate stress shocks

With eight years having passed since the original calibration of the Basel standardised interest rate shocks for IRRBB, and an eventful recent few years, given the sharp rise in global central bank policy rates to combat rising post-pandemic inflation levels, a recalibration of the Basel methodology and shock levels was widely expected.

This was also brought into focus by the US regional bank failures in Spring 2023, with the sharp rise in interest rates being a primary contributor to their demise, and prior to that, the UK "mini budget" stress of September 2022, causing a spike in gilt yields and disorderly market conditions.

The update came with a revision of the' methodology to calibrate shocks using a *relative* rather than *absolute* approach, and linking it to individual currency specific factors, rather than a uniform global approach, which was deemed to improve consistency across different time periods and rate environments.

Upcoming amendments to the stress shocks, and how this compares to other risk frameworks

- The calibration approach for the IRRBB shocks is aligned with the methodologies used in the Fundamental Review of the Trading Book (FRTB) and the Advanced Measurement Approach (AMA) for operational risk. Both FRTB and AMA employ a 99.9% confidence interval, ensuring that banks hold sufficient capital for extreme market and operational events.
- By design the shocks are based on more extreme outlier events rather than what might be considered more plausible but adverse movements. The 99.9% confidence interval calibration equates to the 6th most severe data point out of ~6,000 observations, and therefore may be prone to reliance on momentary outlier points that may not necessarily result in a sustained impact.
- If the shocks had remained calibrated at the previous level of 99% confidence interval, the extension of the time period to incorporate the most recent rate hike activity would have led to some increases in the resulting shocks.
- It could be considered that there is already a degree of conservatism built into the approach in that the shocks are calibrated based on historical 6-monthly movements in interest rates, but applied as instantaneous shocks.

Figure 3: **Relative impacts for GBP, EUR and USD**

Specified size of current and updated interest rate shocks

	ARS	AUD	BRL	CAD	CHF	CNY	**EUR**	**GBP**	HKD	IDR	INR
Parallel	400	~~300~~ 350	400	200	~~100~~ 175	~~250~~ 225	**~~200~~ 225**	**~~250~~ 275**	~~200~~ 225	400	~~400~~ 325
Short	500	~~450~~ 425	500	~~300~~ 275	~~150~~ 250	300	**~~250~~ 350**	**~~300~~ 425**	~~250~~ 375	500	~~500~~ 475
Long	300	~~200~~ 300	300	~~150~~ 175	~~100~~ 200	150	**~~100~~ 200**	**~~150~~ 250**	~~100~~ 300	300	~~300~~ 225

	JPY	KRW	MXN	RUB	SAR	SEK	SGD	TRY	**USD**	ZAR
Parallel	100	~~300~~ 225	400	400	~~200~~ 275	~~200~~ 275	~~150~~ 275	400	**200**	400 ~~325~~
Short	100	~~450~~ 425	500	500	~~300~~ 375	~~300~~ 425	~~200~~ 250	500	**300**	500
Long	100	~~200~~ 300	~~300~~ 200	300	~~150~~ 250	~~150~~ 200	~~100~~ 225	300	**~~150~~ 225**	300

Source: BCBS578

Illustrative impact analysis

The recalibration of the shocks, all other things being equal, would lead to a more adverse outcome under both the NII and EVE SOTs which can often form the basis of institutions' risk appetite metrics.

Assuming an existing 2.5% NII SOT (relative to a firm's T1 capital), with exposures majorly concentrated in EUR and/or GBP, this would lead to an estimated increase in the metric to 2.8%.

Similarly, assuming an existing 7.5% EVE SOT, with exposures majorly concentrated in EUR and/or GBP, may lead to even greater increases, with the metric potentially being adjusted up 8.5% under the parallel shocks, and up to 10% or even higher should the non-parallel shocks be most binding.

4. Introducing greater standardisation within a Pillar 2 framework

IRRBB is a critical aspect of a bank's overall risk management framework. Historically, banks have used institution-specific approaches to measure and manage IRRBB, which allowed them to tailor the assessment of risk to their unique asset and liability profiles, and their specific behavioural assumptions regarding customer actions. However, the existing profiling restrictions within the SOT, with the potential for further restrictions or standardisation in the future, can have significant impacts on how banks manage and report these risks.

During Pillar 2 reviews, the use of certain standardised approaches or parameters might effectively nudge banks towards standardisation or adopting more uniform practices without formal rule changes.

Comparability and Transparency: One of the main benefits is improved comparability across institutions, allowing regulators and market participants to more easily assess banks' exposure to interest rate risk. Enhanced transparency in risk exposures and methodologies also makes it easier for stakeholders to understand and evaluate a bank's risk profile. However, the challenge lies in ensuring that the standardised measures accurately reflect each bank's unique risk characteristics.

Regulatory Consistency: A uniform regulatory framework ensures consistency in requirements and supervisory expectations, reducing ambiguity and subjectivity. This simplifies supervision and compliance enforcement. Yet, the challenge is that a one-size-fits-all approach may not fully capture the nuances of individual banks' risk profiles, potentially leading to less precise risk assessments.

Risk Sensitivity: While a standardised approach aims to create uniformity, it may result in the loss of sensitivity to specific risk factors unique to individual banks. Standardizing behavioural assumptions, such as customer deposit withdrawal patterns, might not reflect actual behaviours, leading to misalignment between measured and actual risks.

Operational Impact: Transitioning to a standardised approach involves significant implementation costs, including system upgrades, staff training, and changes to risk management frameworks. Furthermore, it may introduce new operational complexities in compliance and reporting, especially if banks need to manage both standardised and internal model-based approaches simultaneously.

Strategic Implications: Banks may need to adjust their business models and strategies to align with standardised risk measures, impacting product offerings, pricing strategies, and balance sheet management. Additionally, the impact on capital requirements could lead to higher or lower capital buffers, depending on how the standardised measures align with the bank's internal risk assessments.

Capital Implications: The standardised approach might affect the pillar 2 capital requirements for IRRBB, potentially leading to higher or lower capital buffers depending on how the standardised measures align with the bank's internal risk assessments.

Assessment of Pillar 2A Capital for IRRBB - SS31/15 methodology

Standardised methodology

The PRA reviews the internal policy limits used by a firm. If appropriate (and these are most usually based on the economic impact of a 200 basis point shift in interest rates) the policy limits are used as the basis for determining IRRBB. The PRA does not assess Pillar 2A for basis risk. Nevertheless, the PRA expects that a bank or building society mitigates its basis risk by setting limits on its exposure to basis risk for each type of basis risk mismatch; and the sensitivity of its net interest margin to basis risk. The PRA may allow firms, on a case-by-case basis, to allocate maturities based on behavioural assumptions.

- Applicable to smaller and less complex firms.
- IRRBB capital requirements is based on firms' internal policy limits (usually 200bps parallel shift) and where appropriate, basis risk.
- The PRA does not assess pillar 2A for basis risk under this approach but firms are expected to mitigate basis risk by setting limits on basis risk mismatch and sensitivity of NII.
- Standard models for EVE and NII required, if internal models are non-satisfactory.
- Caps and maturity restrictions for NMDs.
- The PRA may allow allocation of maturities based on behavioural assumptions.
- Use of pre-defined shock-scalars.

Comprehensive methodology

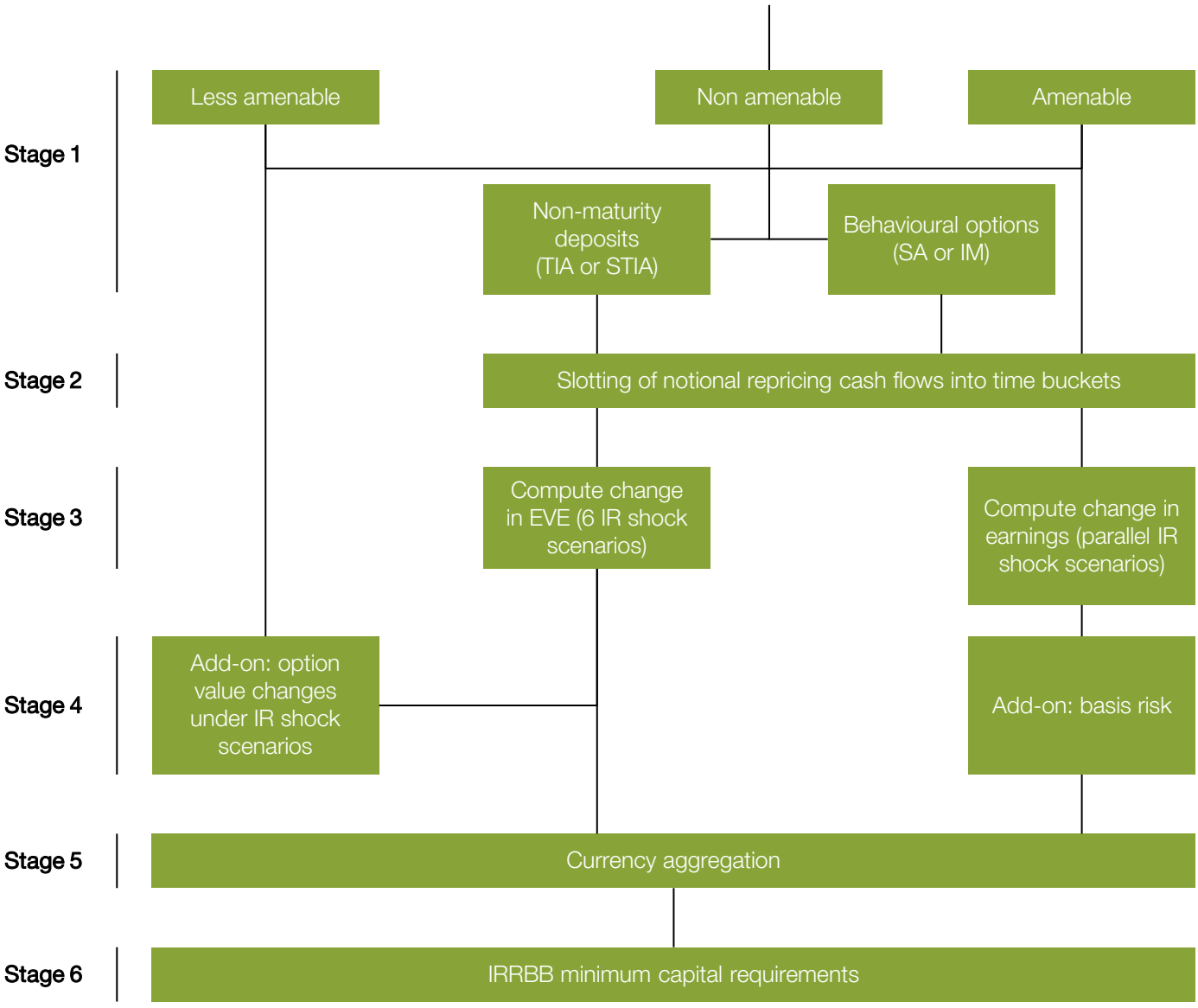
For larger or more complex firms the PRA employs a comprehensive approach to its IRRBB risk assessment that reviews duration risk, basis risk and, as necessary, optionality risk. These firms are subject to a comprehensive risk assessment process. This assessment involves the collection and processing of granular risk data provided by the firm and a review process including firm meetings and discussion. Other IRRBB risks that may be considered, if material, include the risks arising from legacy market rates, hedge accounting operations and structural foreign exchange exposures. The PRA monitors these and other emerging risks to ensure such risks are capitalised adequately.

- Applicable to large firms or those with more complex IRRBB risk exposures.
- Involves collection and processing of granular risk data.
- Individual capital requirements add-ons for the different sub-components of IRRBB (duration risk, basis risk, option risk) and fair value effects. The capital requirements are summed to calculate a firm's IRRBB capital requirement based on the data provided.
- The PRA conducts a review process including firm meetings and discussion.
- A range of value-at-risk and earnings-at-risk based measures are used to calculate capital requirements.
- FSA017 and ALM022 regulatory returns can be used by PRA to validate data provided.
- Assesses the quality of the firm's management, data and governance of IRRBB and considers any additional capital required to reflect failings in a firm's practice.

IRRBB Pillar 2 capital requirement

The flowchart in figure 4 outlines steps that some banks might use to compute the capital charge for IRRBB, considering both the EVE and earnings-based approaches.

Figure 4: **Flowchart for computing minimum capital requirements for IRRBB that certain banks may consider using**



Stage 1. Interest rate-sensitive banking book positions are allocated to one of three categories (i.e. amenable, less amenable and not amenable to standardisation).

Stage 2. Determination of slotting of cash flows based on repricing maturities. This is a straightforward translation for positions amenable to standardisation. For positions less amenable to standardisation, they are excluded from this step. In particular, for positions with embedded automatic interest rate options, the optionality should be ignored for the purpose of slotting of notional repricing cash flows.

NOTE: For positions that are not amenable to standardisation, there is a separate treatment for NMDs and behavioural options.

Stage 3. Determination of change in EVE and change in earnings for relevant interest rate shock scenarios for each currency.

Stage 4. Add-ons for changes in the value of automatic interest rate options (whether explicit or embedded) are added to the EVE changes and basis risk add-ons to changes in earnings.

Stage 5. Currency aggregation. For both EVE capital requirements and NII capital requirements, currencies incurring losses are offset by some weighted sum of currencies that incur gains for each scenario under consideration.

Stage 6. IRRBB minimum capital requirements. Depending on the various potential options, minimum capital requirements will be some maximum of worst aggregated reductions to EVE and, where applicable, NII across the six prescribed interest rate shock scenarios.

5. Clarity and definition of CSRBB

The evolving regulatory landscape and the increasing complexity of financial instruments have made the management of Credit Spread Risk in the Banking Book (CSRBB) a critical area and a focal point for financial institutions, complementing the well-established framework for IRRBB. Both risks have significant implications for a bank's economic value and earnings, but they operate through different mechanisms.

CSRBB refers to the risk of financial losses due to fluctuations in credit spreads that affect the value of financial instruments held in the banking book. CSRBB is distinct from default risk and focuses on changes in the market perception of credit quality and liquidity factors.

The EBA's updated guidelines (EBA/GL/2022/14) provide an evolved framework for the management of CSRBB.

While the European Banking Authority (EBA) and other regulatory bodies have made strides in providing clarity around the definition and approach to CSRBB, particularly through the EBA guidelines there are still areas where ambiguity persists and challenges still remain in terms of practical implementation and interpretation.

The EBA aims to provide a structured framework for managing this risk. However, the implementation of these standards is not without challenges.

CSRBB Definition

The updated EBA guideline issued in October 2022 have significantly increased the requirements for the identification and measurement of CSRBB. This is expected to present banks with substantial challenges in the coming years.

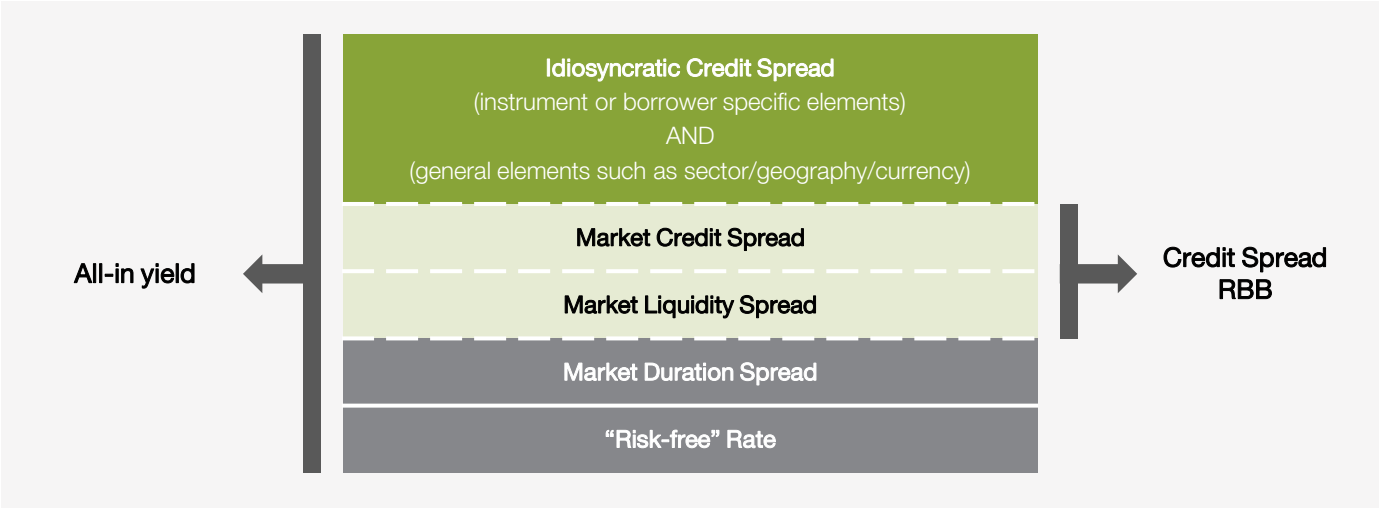
Based on the EBA guidelines, CSRBB captures a combination of two key elements:

(a) The changes in the "market credit spread" or "market price of credit risk" (distinct from idiosyncratic credit spread) which represent the credit risk premium required by market participants for a given credit quality;

(b) The changes in the "market liquidity spread" which represent the liquidity premium that influences market appetite for investments and the presence of willing buyers and sellers.

The EBA suggests excluding idiosyncratic credit spread to avoid overlap with the credit risk framework. However, if these elements are not included in other risk frameworks, idiosyncratic credit risk can be incorporated.

Figure 5: **CSRBB**



Implementation challenges of CSRBB Technical Standards

While the technical standards for CSRBB provide a foundation for managing credit spread risk, there is significant variability in how banks interpret and implement these standards. The interplay between CSRBB and IRRBB adds complexity to risk management, requiring clear differentiation and comprehensive approaches. The industry's practices in managing CSRBB can vary widely, influenced by factors such as the scope of coverage, choice of methodologies, and the extent to which both assets and liabilities are considered. As regulatory frameworks evolve, there may be a push towards greater standardization to reduce ambiguity and enhance comparability across institutions.

How Much is Open to Interpretation?

The technical standards for CSRBB, while comprehensive, leave several areas open to interpretation. This flexibility is designed to accommodate the diverse risk profiles and business models of different banks, but it also leads to variability in implementation. Key areas open to interpretation include:

Definitions and scope

- The EBA's guidelines indicate that the scope of instruments for CSRBB should include a broad range of assets held in the banking book that are sensitive to credit spread movements. This includes both market credit spread risks, which reflect broader market conditions, and idiosyncratic credit spread risks, which are specific to individual issuers.
- Institutions have flagged the need for more clarity regarding the perimeter of instruments subject to CSRBB assessments. They seek guidance that aligns with their collective experience and risk management practices, ensuring that the criteria for inclusion are not overly complex or burdensome to implement. Clear and consistent regulatory guidance is crucial for maintaining industry-wide reliability and comparability in managing CSRBB.

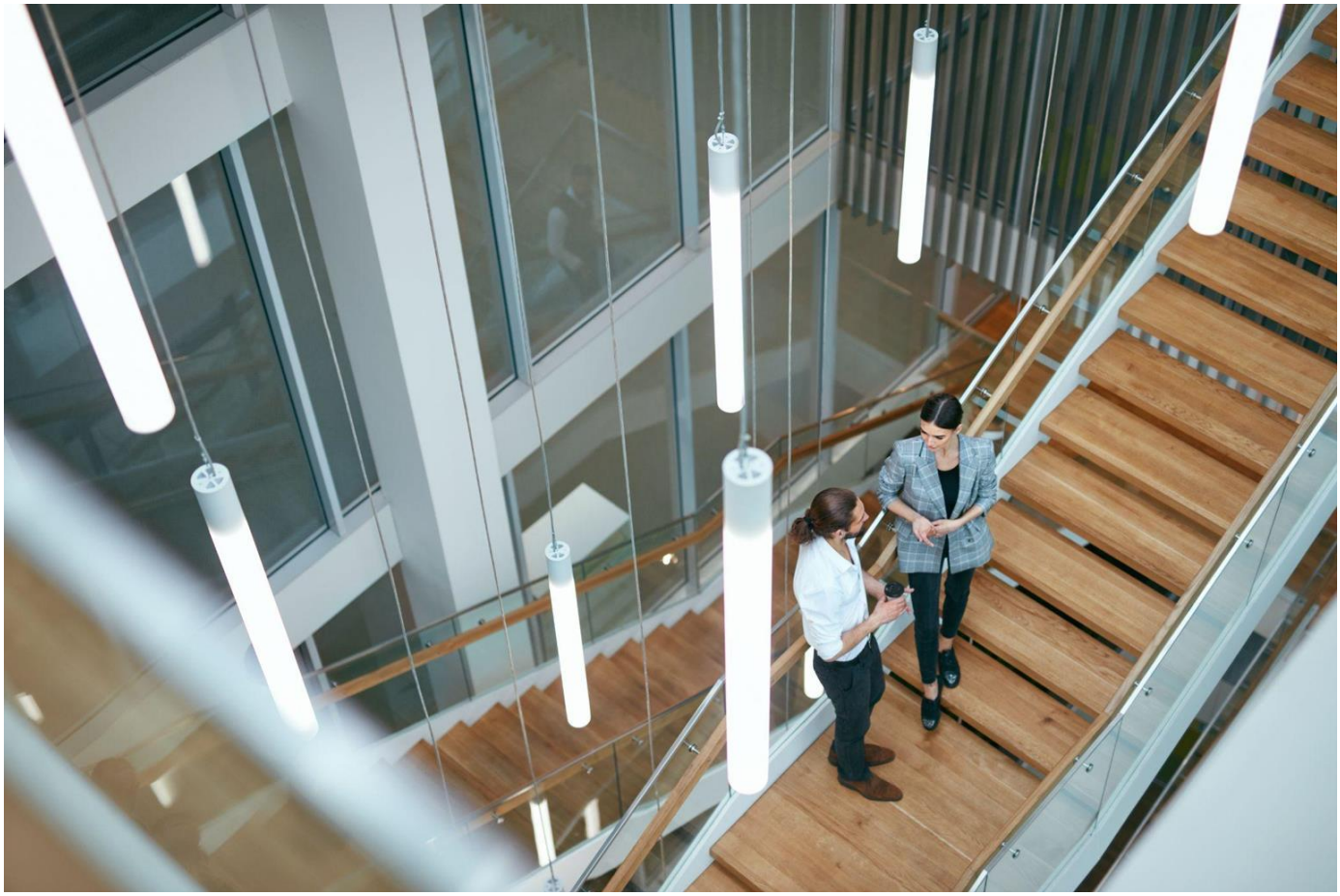
Measurement and methodology

Banks are likely to seek flexibility in the choice of models and underlying assumptions for measuring CSRBB. However, they also require clear regulatory expectations to ensure proper capitalisation of the risk.

- The choice of models and underlying assumptions for measuring CSRBB.
- The design and parameters of stress scenarios.

Integration with risk management

- The specific governance structures and roles for overseeing CSRBB.
- The level of detail and content of disclosures.
- The methodologies for integrating CSRBB with other risks, particularly IRRBB.



Implications for Financial Institutions

The interpretative nature of the CSRBB technical standards has several implications for financial institutions:

Variability in risk management practices

- The flexibility in the standards can lead to significant differences in how banks identify, measure, and manage CSRBB. This variability can affect the comparability of risk profiles and the effectiveness of risk management practices across the industry.

Regulatory challenges

- Regulators may face challenges in assessing and benchmarking banks' CSRBB practices due to the lack of standardisation. This can complicate regulatory oversight and the enforcement of consistent risk management standards.

Modelling

- Given the CSRBB methodology is not clearly defined in the regulation, deciding how to strip the market credit spread and market liquidity spread from observable market data.
- When observable market data are not available (i.e. illiquid positions), deciding the assumptions to be used for the modelling of the market credit spread and market liquidity spread.
- Assumptions to the normal NII and EVE models would need to be amended to incorporate CSRBB (e.g. new business assumptions for NII).
- System changes to include the CSRBB requirements e.g. include the credit risk spreads to yield curves.

Model risk and governance

- The reliance on internal models and interpretations introduces model risk and governance challenges. Banks need to ensure robust model validation and governance frameworks to manage these risks effectively.

Transparency and disclosure

- The variability in disclosure practices can impact transparency and stakeholders' ability to assess banks' risk profiles comprehensively. Enhanced guidance on disclosure requirements could help improve consistency and transparency.

Regulatory frameworks

- Compliance with regulatory frameworks for both IRRBB and CSRBB can be demanding. Adhering to guidelines on capital adequacy, risk measurement, and governance strategies may be resource-intensive. Regulatory expectations necessitate the implementation of robust risk management frameworks that can withstand scrutiny. This involves regular testing, validation, and documentation of risk models and assumptions. Continuous dialogue with stakeholders is important to monitor the application of IRRBB and CSRBB aspects and address potential unintended effects. This helps ensure that regulatory frameworks remain effective and relevant.

Different practices being undertaken

Assets vs. Liabilities

- Some banks primarily focus on managing CSRBB for asset portfolios, such as loans and bonds.
- Other banks include liabilities with embedded credit spread risks in their CSRBB assessments to capture a comprehensive risk profile.

Extent of coverage

- Large banks often adopt a comprehensive approach, covering a wide range of instruments.
- Smaller banks may focus on high-risk instruments or portfolios, selectively applying CSRBB assessments based on strategic priorities.

Methodologies

- Some banks use market-based models, relying on observable market data like credit default swap (CDS) spreads.
- Other institutions use internal ratings-based models, incorporating internal assessments of credit quality and spread movements.

6. Interplay between IRRBB and CSRBB

In today's dynamic financial environment, the interplay between IRRBB and CSRBB is becoming increasingly significant, presenting both challenges and opportunities for financial institutions. As interest rates fluctuate, they not only affect traditional measures of interest rate risk but also exert a profound influence on credit spreads, crucial indicators of market perceptions of credit risk. The interplay also presents significant considerations across measurement and management, assumptions and modelling, and capital allocation. Banks will need to navigate operational complexities, stringent regulatory expectations, and changing market conditions to effectively manage these risks.

Interdependencies and Implications of IRRBB and CSRBB

Measurement and management

Banks are required to measure and manage IRRBB and CSRBB separately, as each risk type has unique characteristics and impacts. IRRBB primarily concerns the potential adverse effects of interest rate changes on a bank's economic value and net interest income, while CSRBB pertains to the risk of changes in credit spreads affecting the market value of credit-risky instruments. Despite the need for separate assessments, there is an acknowledgment that diversification benefits may exist between IRRBB and CSRBB. However, these benefits must be conservatively estimated and validated to ensure stability even during economic downturns. The separation of IRRBB and CSRBB management can lead to operational complexities, as banks often maintain distinct processes and systems for each risk type to avoid double counting and ensure accurate risk assessment, but it can strain resources and require sophisticated risk management frameworks. Ensuring compliance with regulatory expectations for both IRRBB and CSRBB is demanding. Banks must adhere to guidelines on capital adequacy, risk measurement, and governance strategies, which can be resource-intensive.

Assumptions and modelling

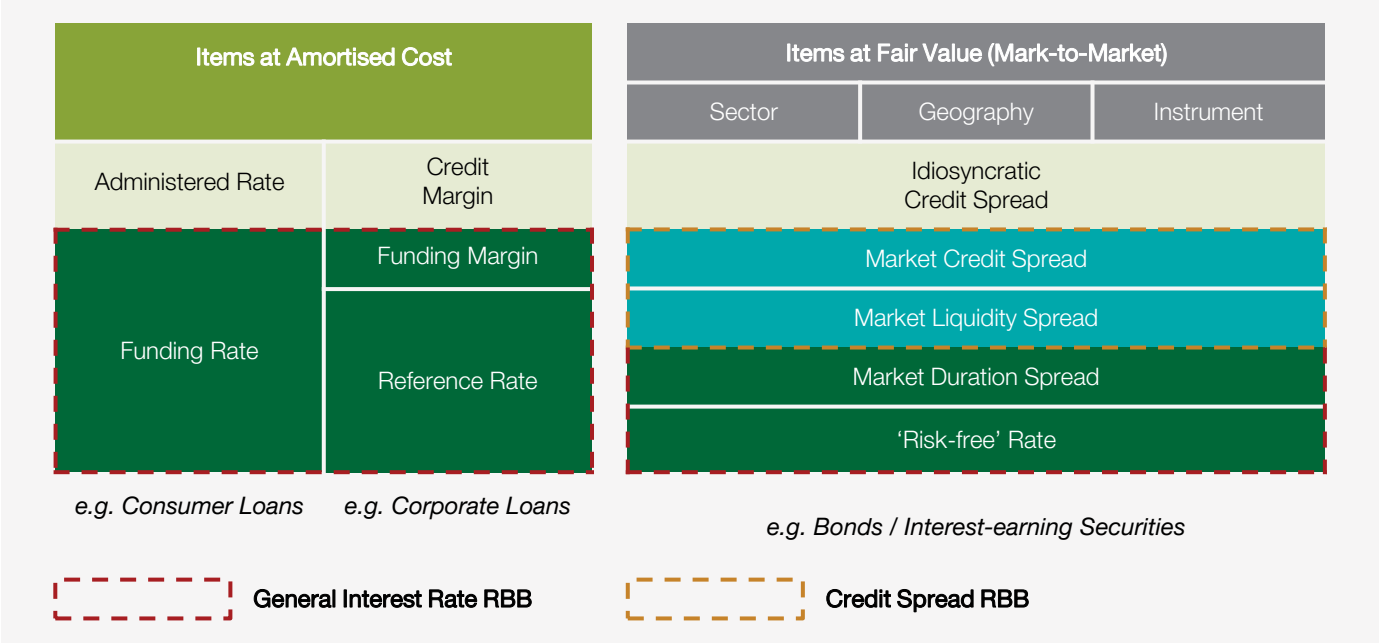
The assumptions and methodologies used for measuring CSRBB should be well-documented and aligned with the bank's business strategies. These assumptions need regular testing and validation to ensure they remain relevant under changing market conditions. For IRRBB, banks must consider all interest rate-sensitive instruments, including non-performing exposures, to accurately assess and manage their risk exposures. Changing market conditions necessitate frequent reviews and updates to risk measurement assumptions. Banks must be agile in adapting their strategies to maintain resilience against both interest rate and credit spread fluctuations. Developing and validating assumptions and methodologies for CSRBB, and ensuring they align with business strategies, can be complex. This requires regular testing and validation to ensure relevance under changing market conditions.

Capital allocation

The capital allocated for IRRBB should reflect the institution's actual measured level of risk and its risk appetite. This involves using internal measurement systems and considering key assumptions and risk limits.

For CSRBB, banks are encouraged to develop their own assumptions and calculation methods, ensuring these are adequate for the complexity of their operations. Allocating capital for IRRBB and ensuring it reflects the institution's actual measured level of risk and risk appetite involves using internal measurement systems and considering key assumptions and risk limits. This process must be robust and compliant with regulatory standards. For CSRBB, banks are encouraged to develop their own assumptions and calculation methods, which must be adequate for the complexity of their operations. This can be demanding, especially for institutions seeking more advanced methodologies for the assessment of CSRBB.

Figure 6: **Components of interest rates**



Correlation (Benefit) Between Interest Rate Risk and Credit Spread Risks Through Capital Approach

Correlation analysis

- The correlation between interest rate changes and credit spread movements can complicate risk management. While diversification benefits may exist, they should be conservatively estimated and validated to ensure stability during economic downturns. Market dynamics, such as shifts in economic conditions or changes in market sentiment, can simultaneously affect interest rates and credit spreads. Adapting risk management strategies to these changing conditions is essential for maintaining resilience.
- To address potential overlaps and inefficiencies, banks should conduct detailed correlation analysis between interest rate movements and credit spread changes. Understanding the historical and potential range of future correlations helps in better quantifying the combined impact of these risks.

Integrated risk models

- Developing integrated risk models that capture the correlations between IRRBB and CSRBB can provide a more accurate representation of the bank's risk profile. These models should be capable of simulating various market scenarios and their combined effect on both interest rates and credit spreads.

Capital efficiency

- By recognizing the correlation (or lack thereof) between IRRBB and CSRBB, banks can achieve capital efficiency. For instance, negative correlations (where one risk mitigates the other) might justify lower combined capital requirements. Conversely, positive correlations (where risks amplify each other) would necessitate higher capital buffers.

Regulatory acceptance

- Any integrated approach to capital allocation must be acceptable to regulators. Dialogue with regulatory bodies is crucial to ensure that integrated models and correlation benefits are recognised in regulatory capital requirements.

Challenges in Consistently and Adequately Delineating the Measurement of IRRBB and CSRBB

Definitional ambiguities

- The precise definitions of market credit spread and market liquidity spread in CSRBB, and their distinction from IRRBB, can be ambiguous. These ambiguities complicate the consistent measurement and management of these risks.

Model risk and assumptions

- Customer behaviour, such as loan prepayments or deposit withdrawals, can significantly impact both IRRBB and CSRBB. Incorporating behavioural assumptions into risk models is necessary to accurately assess and manage these risks. Behavioural assumptions should be regularly reviewed and updated to reflect current market conditions and customer behaviour patterns. This helps ensure that risk management strategies remain relevant and effective.
- Different banks may use varying models and assumptions to measure IRRBB and CSRBB, leading to inconsistencies. For example, assumptions about customer behaviour (e.g., prepayment rates) affect both risks but may be modelled differently.

Overlap in stress scenarios

- Designing stress scenarios that adequately capture the interplay between interest rate and credit spread risks without double counting is challenging. Stress scenarios need to be carefully crafted to ensure that the same economic shock is not redundantly accounted for in both risk categories.
- Separating the management of IRRBB and CSRBB is important to avoid double counting of risks. Maintaining distinct processes and systems for each risk type ensures accurate risk assessment. Avoiding overlap in risk measurement and management processes is crucial for maintaining the integrity of the risk management framework. This requires careful coordination and validation of risk models.

Governance and oversight

- Effective governance frameworks are essential to delineate responsibilities and ensure consistent risk measurement. Clear roles and responsibilities, regular oversight, and robust internal controls can help mitigate the risk of double counting.

Data and technology

- High-quality data and advanced technological tools are necessary to accurately measure and manage IRRBB and CSRBB. Ensuring data accuracy, completeness, and consistency across different risk models is critical.

Notes

Contacts

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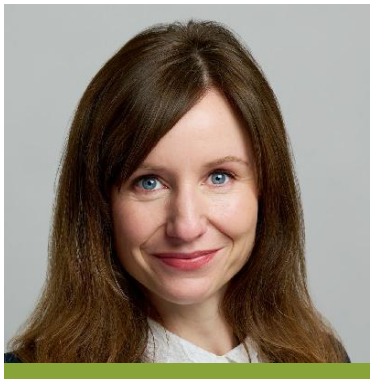

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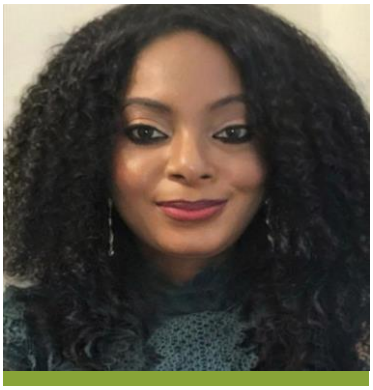

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About AFME

The Association for Financial Markets in Europe (AFME) is the voice of all Europe's wholesale financial markets, providing expertise across a broad range of regulatory and capital markets issues.

We represent the leading global and European banks and other significant capital market players.

We advocate for deep and integrated European capital markets which serve the needs of companies and investors, supporting economic growth and benefiting society.

We aim to act as a bridge between market participants and policy makers across Europe, drawing on our strong and long-standing relationships, our technical knowledge and fact-based work.

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