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Liquidity Risk

PRMIA

Wednesday 17th June 2008

Bear Stearns, turning big to small

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Bear rescue spooks markets

By Neil Dennis
Published: March 17 2008 08:32 | Last updated: March 17 2008 16:50

Equity markets and the dollar sold off sharply on Monday, as the rescue of stricken investment bank Bear Stearns sparked fears of further financial sector strife.

The dollar tumbled to new lows against most currencies as markets increasingly priced in the likelihood of a 100-basis-points cut in the main Fed funds rate when the US central bank meets on Tuesday.

Shares in US banks opened significantly lower after **JP Morgan Chase** emerged over the weekend as the buyer of rival **Bear Stearns** for $2 a share.

The move came as the Fed announced it was **cutting the discount rate** at which it lends to banks by 25 basis points to 3.25 per cent, and opening up its discount window to 90 days from 30 days.

By midday in New York, Bear Stearns shares were 87.9 per cent lower at $3.74 as the S&P 500 shed 2.1 per cent. **Lehman Brothers** tumbled 34 per cent, while **Morgan Stanley** lost 10.2 per cent and **Citigroup** fell 9.1 per cent.

EDITOR'S CHOICE

- **Lex: Bear and bank runs** - Mar-17
- **In depth: Bear Stearns** - Mar-17
- **Wall St plunges amid banking gloom** - Mar-17

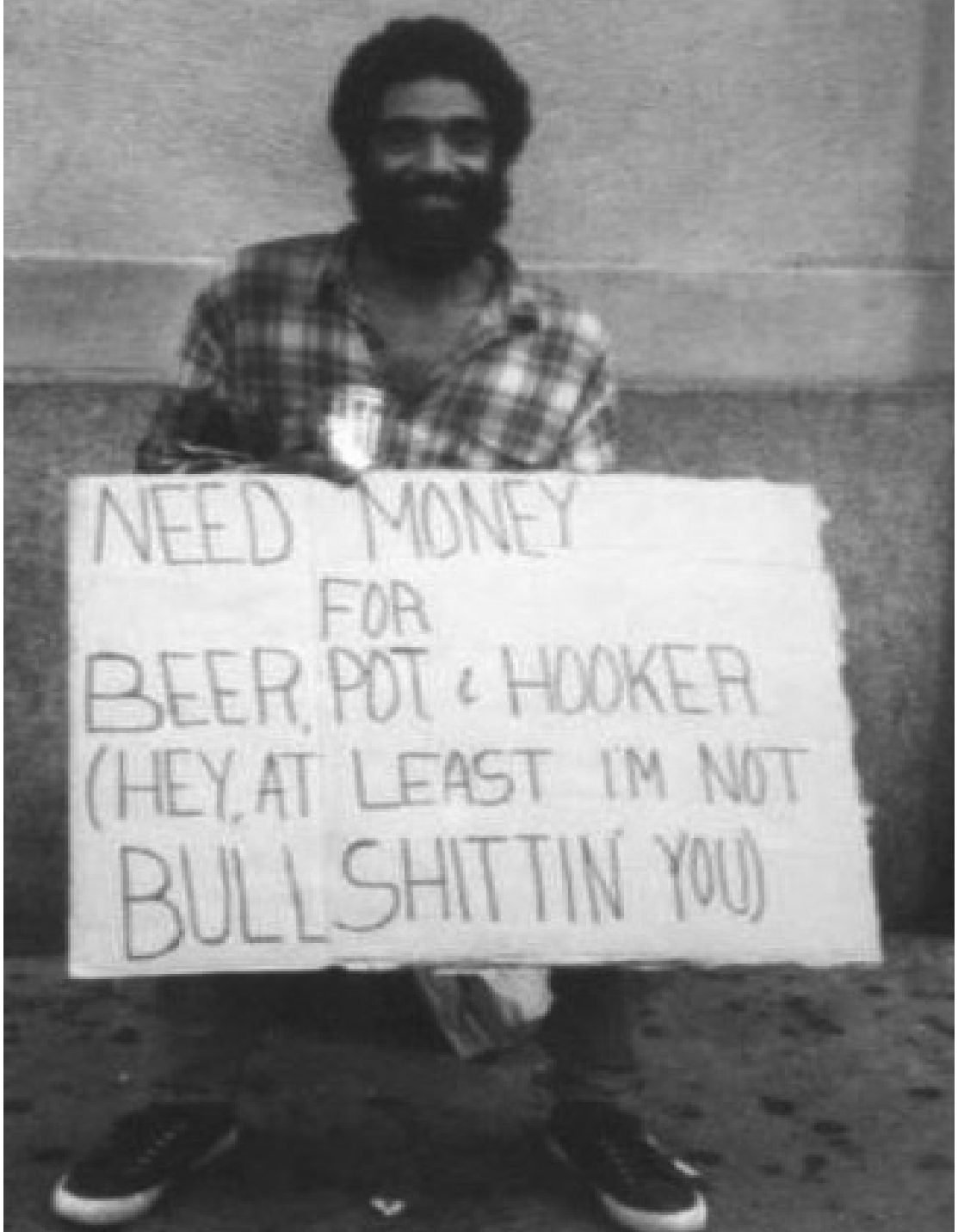
What is Liquidity?

Financial Institution:

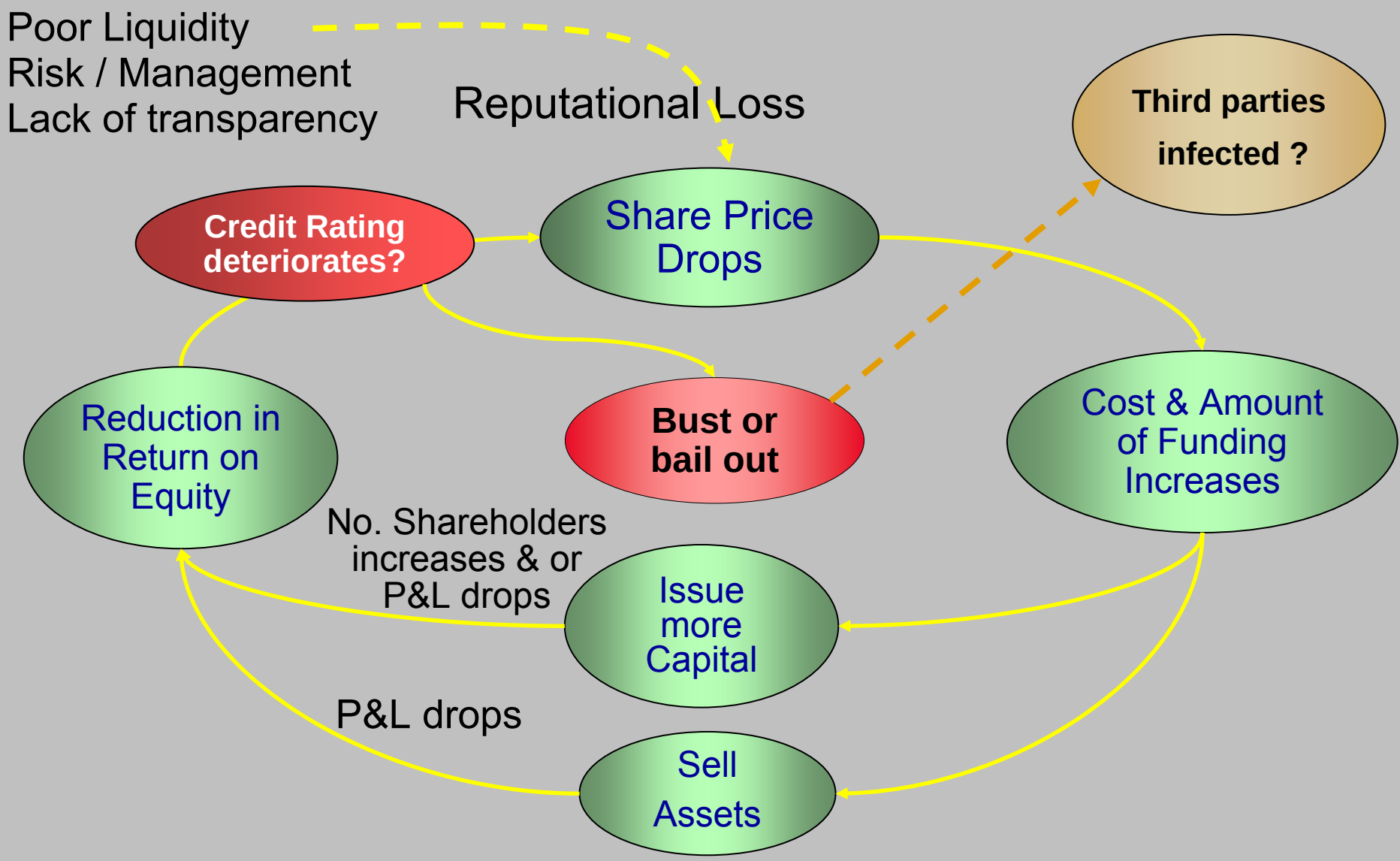
- Ability to raise cash (at a reasonable cost) in order to meet its payment obligations
- The ability to meet both expected and unexpected current and future cashflows

Financial Market:

- Excess (or shortage) of liquid funds (central bank money) in the market
- Ability to sell a Financial Instrument in volume and time, without affecting the market price


NEED MONEY
FOR
BEER, POT & HOOKER
(HEY, AT LEAST I'M NOT
BULLSHITTIN' YOU)

Shrinking Liquidity



Citigroup trouble despite $21 B additional funding

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Citigroup's rescue package 'may not suffice' to save it

4 March 2008

Despite the billions of dollars of handouts that Citigroup has been forced to accept to shore up its balance sheets, the largest bank in the US could need a lot more than it has already received.

According to Bloomberg, bosses at Dubai International Capital have warned that Citigroup could need even more cash injections from investors to help the bank stay afloat.

After the collapse of the US sub-prime mortgage market, Citigroup has lost billions of dollars in bad debts, nearly halving the bank's market value.

But even after Abu Dubai handed over $7.5 billion in November and a further $14.5 billion will come from other investors, including the state funds of Singapore and Kuwait, it still may not be enough.

Sameer al-Ansari, chief executive officer of Dubai International, warned: "It will take a lot more than that to rescue Citi and other financial institutions."

Now analysts at Merrill Lynch are expecting Citi to post a loss of $1.66 per share for the first quarter of 2008 after $15 billion more sub-prime-related writedowns.

Stock in Citigroup dropped a further 30 cents to $22.79 in German trading.

HSBC: Losses of $51 million a day

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HSBC admits $51m daily writedown

4 March 2008

HSBC has confessed that writedowns are currently costing it $51 million every day as people fail to pay off their mortgages, credit cards, and other loans.

Yesterday when HSBC announced its annual results for 2007 it admitted writedowns in the sub-prime mortgage department had lost it $11.7 billion.

Writedowns are an increasing problem, with $1.89 billion lost during the first quarter of the year, rising to $2.19 billion in the second quarter.

A further $3.48 billion was written down in the third quarter while HSBC wrote down $4.63 billion during the final quarter.

The number of loans that are more than two months in arrears has also increased over the year from $7.4 billion to $12.5 billion.

Stephen Green, HSBC's chairman, was quoted by the Times as saying: "We're not in a position to say we've turned the corner or passed the worst."

"But the vast majority of people do want to pay their debts back," he said. "People aren't looking for an excuse to hand their keys in and run."

Despite the writedown crisis, an anonymous HSBC director received an annual salary and bonus totalling around $20 million.

UBS – progressive write-offs

UBS writedowns double to $37bn

1 April 2008

Swiss bank UBS has announced a further $19 billion in asset writedowns from the US sub-prime mortgage crisis.

This figure is in addition to the $18.4 billion it wrote off during 2007 and means that losses from US real estate and associated credit agreements now total $37 billion (£18.5 billion.)

Consequently, the bank also said that it expects 2008 first quarter net losses to total £12.1 billion.

It was announced that chairman Marcel Osper will not seek re-election, and the bank will create a business devoted to the now worthless US property assets.

The bank said that it has "substantially reduced its real estate related positions through both valuations adjustments and significant disposals".

Freddie predicts losses of $7.6 Billion

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Freddie Mac posts record-breaking loss

29 February 2008

Freddie Mac, the largest mortgage finance firm after Fanny Mae, has posted $2.45 billion loss for the final quarter - the most in its history.

The impact of mortgage defaults at the finance company was even bigger than analysts expected. They had guessed that the net loss per share would be $2.06, but it actually hit values by $3.97.

These losses included writedowns and miscellaneous expenses of $2.1 billion, mostly related to derivatives contracts.

Some $912 million of losses went on credit expenses, according to Bloomberg.

Freddie Mac, which buys and guarantees 45 per cent of US home loans, dropped by four per cent in early New York trading.

Chief executive officer Richard Syron said that Freddie Mac is entering 2008 "extremely" cautiously.

"Today's economy represents one of the most severe housing downturns in American history and our results reflect that difficult environment," he said.

Freddie Mac predicted that credit losses would reach $2.2 billion this year and $2.9 billion in 2009.

Societe Generale – $7.2 billion

SocGen fallout to trigger review

By Peggy Hollinger and Martin Arnold
Published: February 3 2008 22:07 | Last updated: February 4 2008 02:23

French banking regulations could be tightened by the government on the suggestions of a finance ministry report into the rogue trading scandal at Société Générale.

The report, being prepared by the ministry and the Bank of France, will be handed to Prime Minister François Fillon on Monday.

It is expected to form the basis for the government's reaction to the scandal, which led to a €4.9bn ($7.2bn) loss at SocGen and threw the credibility of the bank, and France's financial system, into doubt.

SocGen's troubles will be compounded on Monday when its chairman, Daniel Bouton, is forced to interrupt an investor roadshow in support of the bank's €5.5bn emergency rights issue to appear in a French court. Mr Bouton has been summoned over money-laundering charges concerning a dirty cheques ring

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Credit squeeze

IMF puts cost of credit crisis at $945bn

By Krishna Guha in Washington
Published: April 8 2008 19:10 | Last updated: April 8 2008 19:10

The financial sector faces potential losses of almost $1,000bn as a result of the credit crisis, the International Monetary Fund said on Tuesday, warning of further losses and writedowns on prime mortgages, commercial real estate, leveraged loans and consumer finance.

The IMF said total losses and writedowns would reach about $945bn, based on market prices in mid-March. Banks would suffer slightly more than half the total losses, with the rest falling on insurance companies, pension funds, hedge funds and other investors.

The IMF believes that banks have already taken most of the writedowns needed on US subprime loans – with about $193bn taken already and only about $80bn to come. But it warned that as the US economy weakened, pain was spreading to other forms of lending.

"The deterioration in credit has moved up and across the credit spectrum," Jaime Caruana, head of monetary affairs and capital markets at the Fund said.

The estimate is set out in a gloomy Global Financial Stability Report, which challenges the more optimistic tone in the markets since the rescue of Bear Stearns by the Federal Reserve and JP Morgan Chase. The report says "systemic risks have risen sharply" since October.

EDITOR'S CHOICE

IMF points to high cost of global credit crisis - Apr-08
Fed hints at end to big rate cuts - Apr-08
In depth: The credit crisis - Apr-08
Editorial comment: IMF's Instability Report - Apr-08
Wall St banks seek to ring-fence bad assets - Apr-02
Analysis: UK threat of US-style house prices - Apr-01

Inflation at 14 year high

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Brussels - **Economy**

Eurozone inflation at 14-year high

By Ralph Atkins in London
Published: March 14 2008 13:06 | Last updated: March 14 2008 22:23

Eurozone inflation fears were stoked further on Friday when February's rate was revised upwards to a fresh 14-year high of 3.3 per cent, strengthening the European Central Bank's case for keeping its interest rates firmly on hold.

The latest figure, up from the 3.2 per cent reported initially, provided the latest evidence that the surge in price pressures is proving significantly longer-lasting than the ECB had envisaged. The rise has been driven by fuel and food price increases.

The figure for March could be even higher, analysts said. "Inflation could hit 3.4 per cent this month, which may be the peak, though we think the average for the year will be about 3 per cent – the highest since the launch of the euro," said Nick Matthews at Barclays Capital.

The ECB, which aims to keep annual inflation "below but close" to 2 per cent, has left its main

EDITOR'S CHOICE

ECB study warns on renmint peg - Mar-13

Editorial Comment: Intervene on dollar's fall - Mar-13

Trichet signals alarm at euro's rise - Mar-11

Euro hits record after Triche rates signal - Mar-07

Business chiefs warn of

Gold and Oil set new records

Gold and oil pass milestones

By Chris Flood
Published: March 14 2008 19:09 | Last updated: March 14 2008 19:09

Gold breached the $1,000 a troy ounce mark this week, marking a historic milestone for global financial markets, while oil prices extended their run above the $100 level as the dollar plumbed new lows.

With record prices being achieved across energy, metals and agricultural markets this year, investors inevitably question the sustainability of the latest rally in commodities.

"Conventional wisdom would assume that commodity prices are close to peaking, given already long bull market runs, [but] we strongly disagree and believe that we are in the 'middle innings' of a powerful secular up-trend," said Anthony Carpet of Goldman Sachs.

Gold hit an intraday nominal record of $1,007.10 a troy ounce, up $16.1 an ounce Friday as news that a rescue operation has been launched by the Federal Reserve

Arbitraging the Rating Agencies

- Reuters reported on May 21, 2008 that Moody's admitted that programming errors resulted in CDO credit ratings that were too high. Many have argued that only CDO deals where ratings are in error will be brought to investors.

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Moody's stock suffers record plunge on rating error

Wed May 21, 2008 2:56pm EDT

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GFT FREE PRACTICE ACCOUNT
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By Walden Siew

NEW YORK (Reuters) - Shares of Moody's Corp (MCO.N: Quote, Profile, Research) fell more than 13 percent on Wednesday, the biggest one-day drop since becoming an independent company in 2000, after the rating agency said a computer snafu resulted in incorrect top ratings for complex debt.

The Financial Times first reported a coding error resulted in wrong "Aaa" ratings for debt known as Constant Proportion Debt Obligations, known as CPDOs.

Moody's shares fell over 13 percent to $37.95 in the largest one-day drop in the stock since it was spun off from Dun & Bradstreet in 2000.

A Moody's spokesman in New York said the rating agency is "conducting a thorough review" of its rating methods for European CPDOs specifically, due to the computer glitch. The review of its computer coding does not extend to subprime mortgage debt, collateralized debt obligations or corporate bonds, Moody's said.

"Moody's is simply telling the truth slowly, and there's more truth to be told," said Janet Tavakoli, a consultant and president of Tavakoli Structured Finance in Chicago.

"Up until now I thought the rating agencies were incompetent rookies in structured products," Tavakoli said. "Now I'm suspicious that they may be crooked."

Read imagescdn.reuters.com

Merrill VAR: $92 million. Actual loss: $18 billion

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CME Is in Preliminary Discussions to Acquire Nymex for About $11.1 Billion

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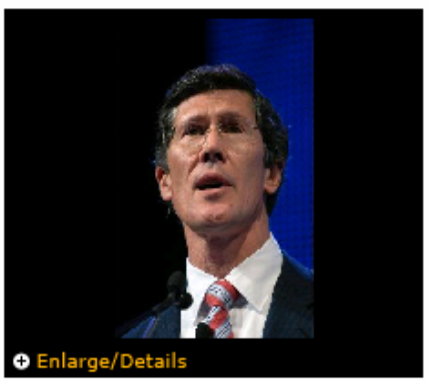
Death of VaR Evoked as Risk-Taking Vim Meets Taleb's Black Swan

By Christine Harper



Jan. 28 (Bloomberg) -- The risk-taking model that emboldened Wall Street to trade with impunity is broken and everyone from Merrill Lynch & Co. Chief Executive Officer John Thain to Morgan Stanley Chief Financial Officer Colm Kelleher is coming to the realization that no algorithm or triple-A rating can substitute for old-fashioned due

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Bloomberg PRESS

Basel II – Pillar 2: 10 Principles of ICAAP

Internal Capital Adequacy Assessment Process (ICAAP) linking the bank‘s strategy, future business development, the risks related to these and the capital adequacy

1. Every institution must have a process for assessing its capital adequacy relative to its risk profile (an ICAAP)
2. The ICAAP is the responsibility of the institution
3. The ICAAP‘s design should be fully specified, the institution’s capital policy should be fully documented, and the management body (both supervisory and management functions) should take responsibility for the ICAAP
4. The ICAAP should form an integral part of the management process and decision making culture of the institution
5. The ICAAP should be reviewed regularly
6. The ICAAP should be risk based
7. The ICAAP should be comprehensive
8. The ICAAP should be forward looking
9. The ICAAP should be based on adequate measurement and assessment processes
10. The ICAAP should produce a reasonable outcome

AAA - Continental Illinois 1984 – a short story

COURTSHIP

- 1976 – 1981-> strategy of rapid growth lending to corporate and industrial clients. Lending grew from $5 to $14 billion. High loan to deposit ratio.
- Way above average return on equity. Share price doubled in 3 years

MARRIAGE

- Concentrated lending in a particular sector for which it was considered an expert (Energy). Bought a large share of Penn Square Bank‘s lending book
- Funding
  - very small retail presence (< 20% of total funding position)
  - Heavily dependent on wholesale funds (CDs) and Fed Funds
- 1981 - Oil prices dropped significantly and continued to fall
- 1982 – Penn Square Bank collapsed followed by default of Mexican debt
- 1983 – Government Backing weakened
- 1984 – non performing loans totalling over $3 billion

DIVORCE

- May 9 – Liquidity crisis begins. Flight of billions of dollars (rollovers stopped rolling over)
- May 11 – forced to borrow $3.6 billion through Fed discount window
- May 17 – FDIC bailout package announced

AAA - Continental Illinois 1984 – a short story

HONEYMOON

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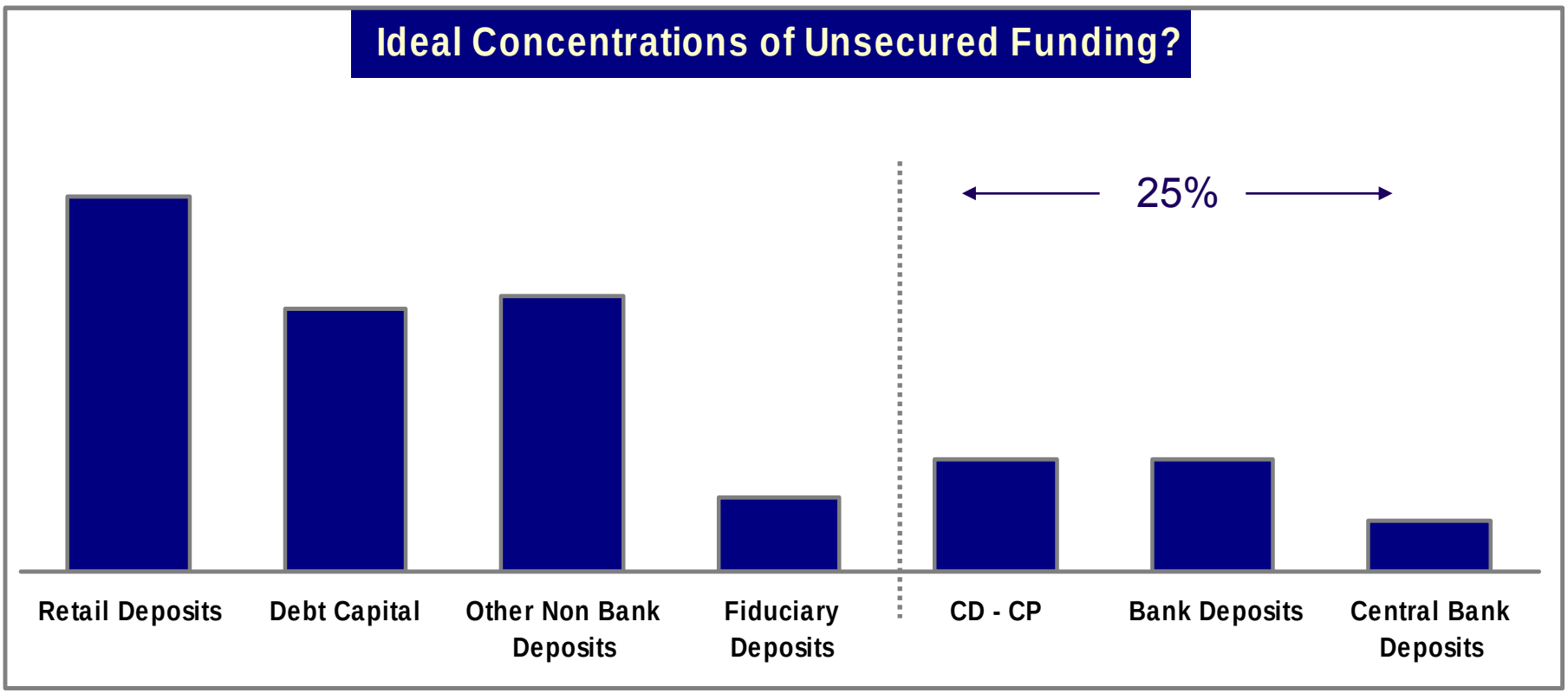
AAA - Continental Illinois 1984 – a short story

- Early-cycle default rates are reassuringly but deceptively low – risk of lending at rates that don't offset default risk early in the business cycle

- Contingency plans are made in times of good liquidity. Are they relevant for the crisis?

Concentration Risk - Security in diversification?

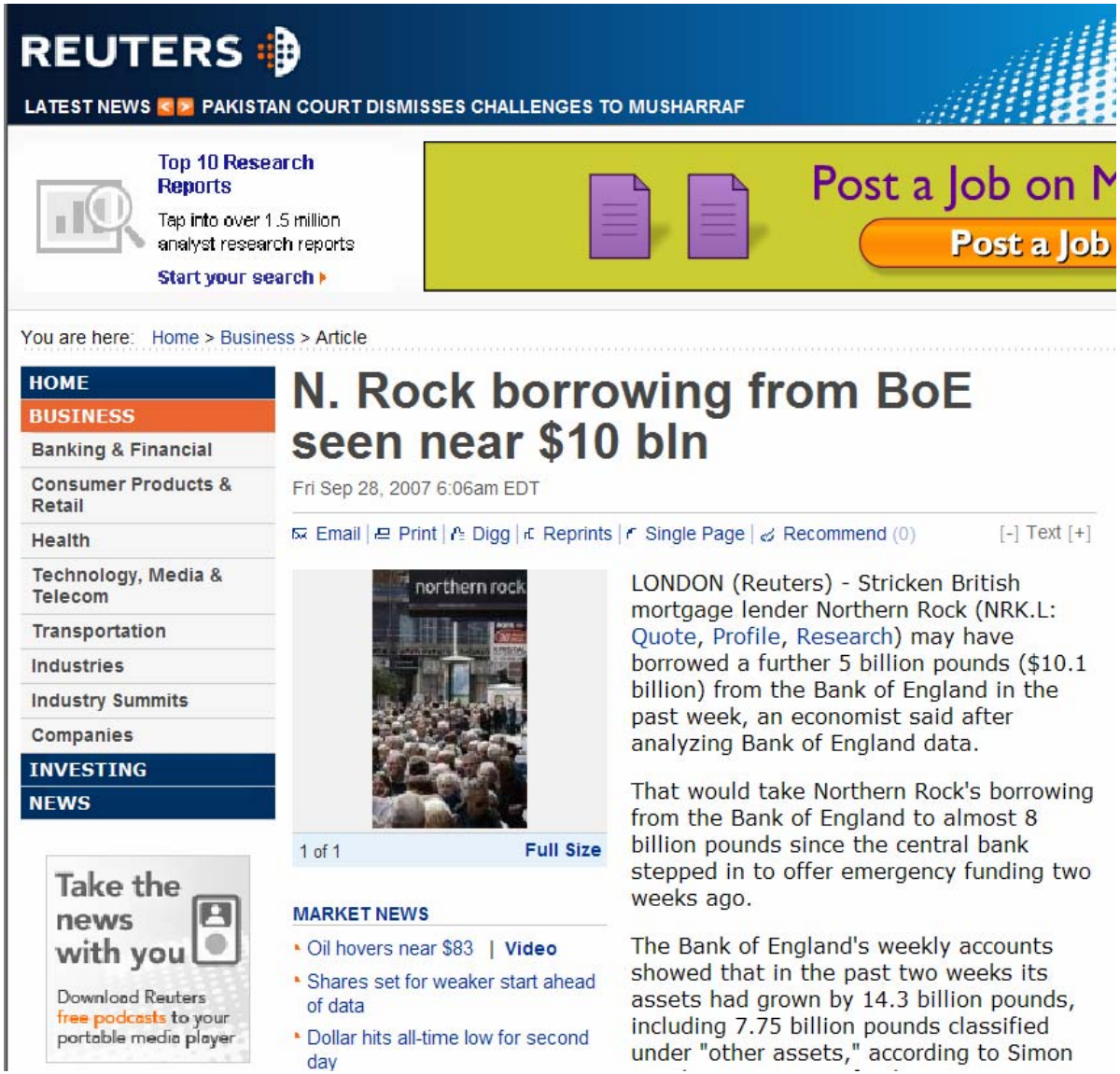


- Stability in deposits and mid to long term liquidity sources required to fund loan position
- Dependence upon wholesale funding an important, but comparatively reduced form of unsecured funding

Concentration Risk

September 28: Northern Rock borrowings

- By September 28 Reuters was reporting that Northern Rock borrowings from the Bank of England had reached almost 8 billion pounds



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N. Rock borrowing from BoE seen near $10 bln

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MARKET NEWS

- Oil hovers near $83 | Video
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LONDON (Reuters) - Stricken British mortgage lender Northern Rock (NRK.L: Quote, Profile, Research) may have borrowed a further 5 billion pounds ($10.1 billion) from the Bank of England in the past week, an economist said after analyzing Bank of England data.

That would take Northern Rock's borrowing from the Bank of England to almost 8 billion pounds since the central bank stepped in to offer emergency funding two weeks ago.

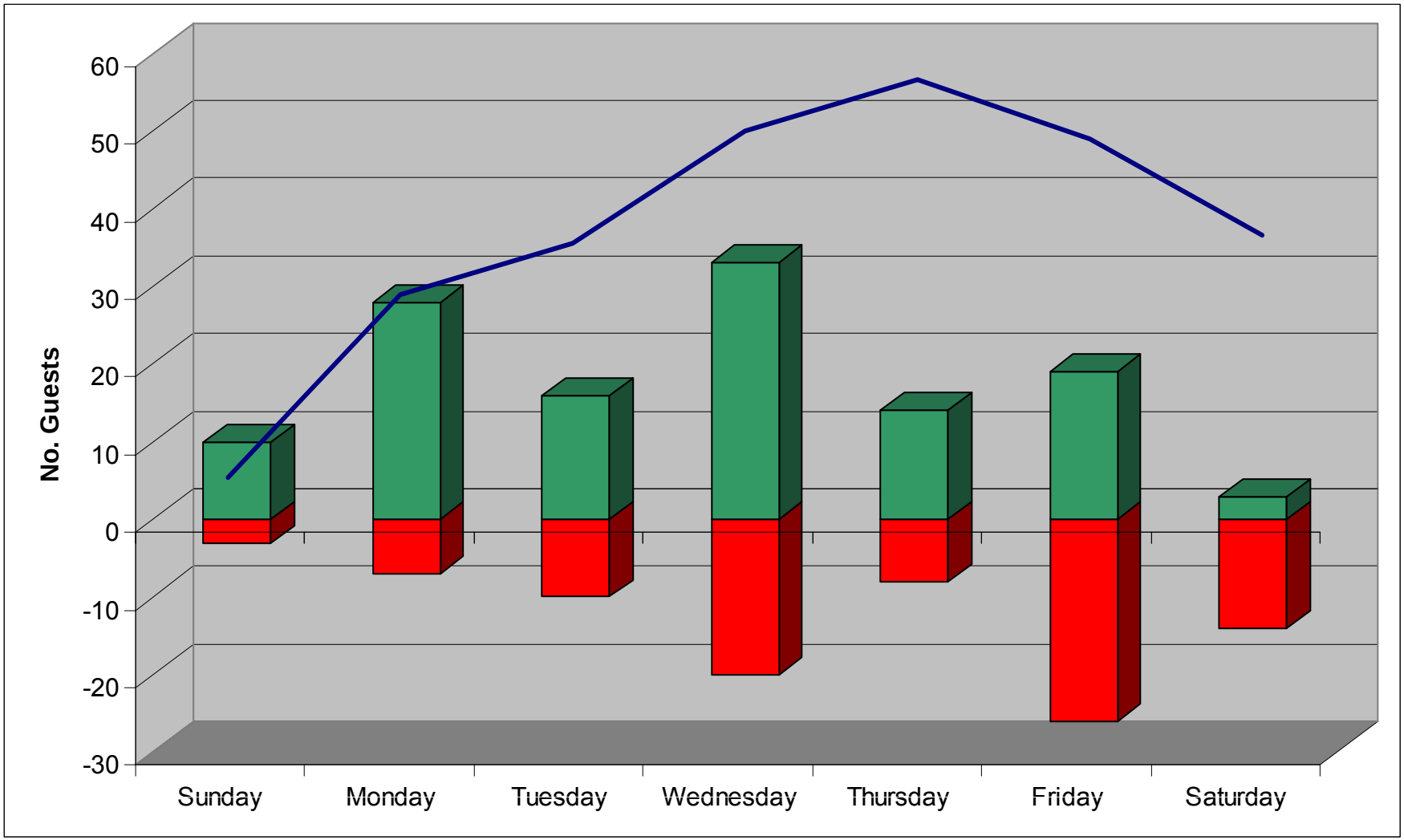
The Bank of England's weekly accounts showed that in the past two weeks its assets had grown by 14.3 billion pounds, including 7.75 billion pounds classified under "other assets," according to Simon

2006	Within 3 months £m	After 3 months but within 6 months £m	After 6 months but within 1 year £m	After 1 year but within 5 years £m
Assets				
Cash and balances with central banks	890.9	–	–	–
Loans and advances to banks	5,483.8	122.5	15.0	–
Loans and advances to customers	26,029.8	4,706.0	10,148.4	42,877.8
Investment securities	4,649.0	55.3	461.5	981.0
Other assets	–	–	–	–
Total assets	37,053.5	4,883.8	10,624.9	43,858.8
Liabilities				
Deposits by banks	1,991.8	88.4	23.0	3.0
Customer accounts	19,923.0	1,422.4	3,688.7	1,833.5
Debt securities in issue	51,499.9	622.3	1,397.4	6,331.0
Subordinated liabilities	–	–	–	291.6
Tier one notes	–	–	–	–
Other liabilities	–	–	–	–
Shareholders' equity	–	–	–	–
Non shareholders' equity	–	–	–	–
Total liabilities	73,414.7	2,133.1	5,139.1	8,459.1
Total interest rate sensitivity gap	(36,361.2)	2,750.7	5,485.8	35,399.7
Cumulative interest rate sensitivity gap	(36,361.2)	(33,610.5)	(28,124.7)	7,275.0

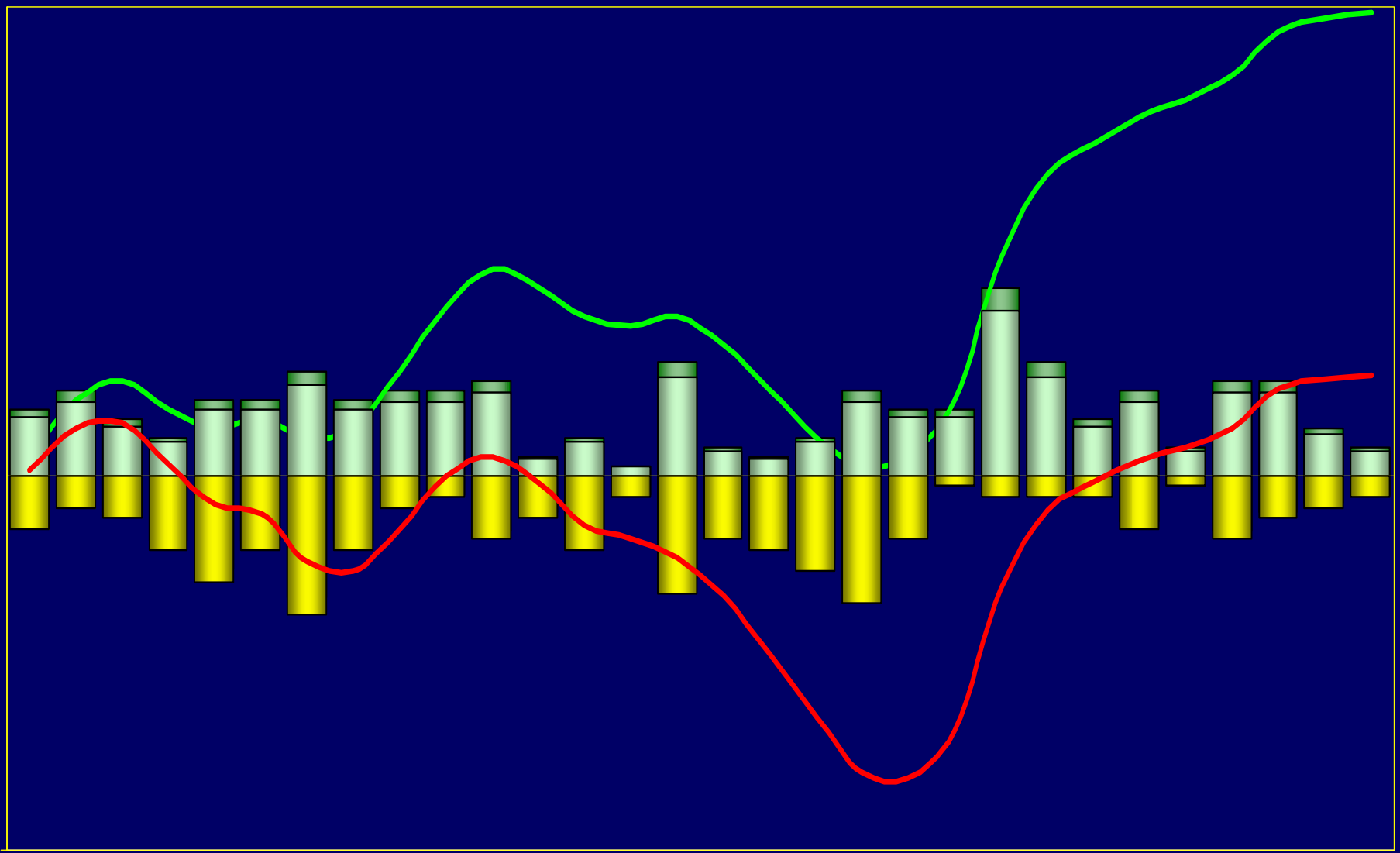
(36,361)

(51,499)

Gap reports – how well do we know them?

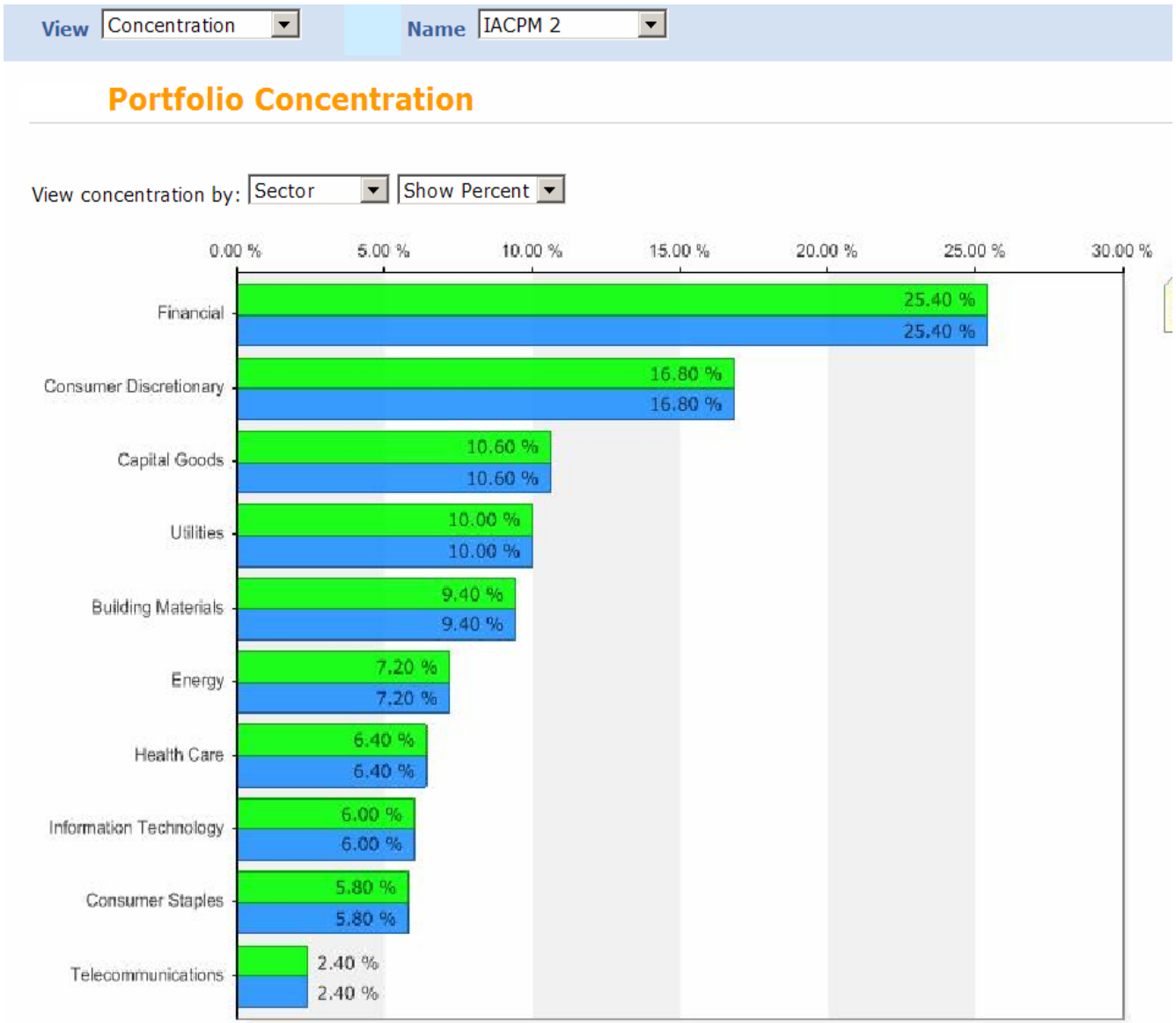


Aggregating Cashflows



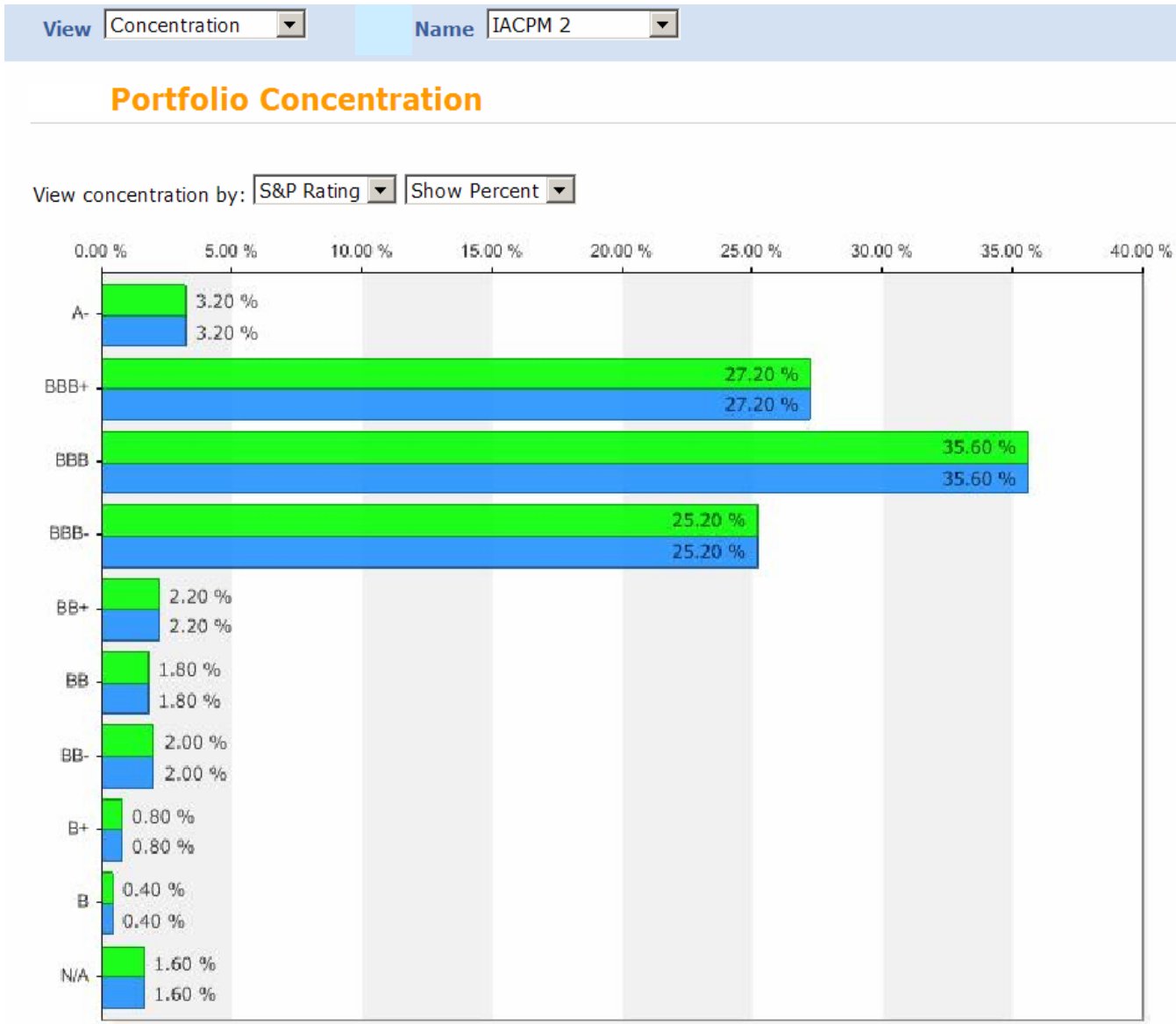
Concentration by Industry Sector

- Concentration by industry sector as well for the reference portfolio



Concentration by Credit Rating

- Evolving ratings by updating composition by ratings daily



Know your audience

Board of Directors / Management

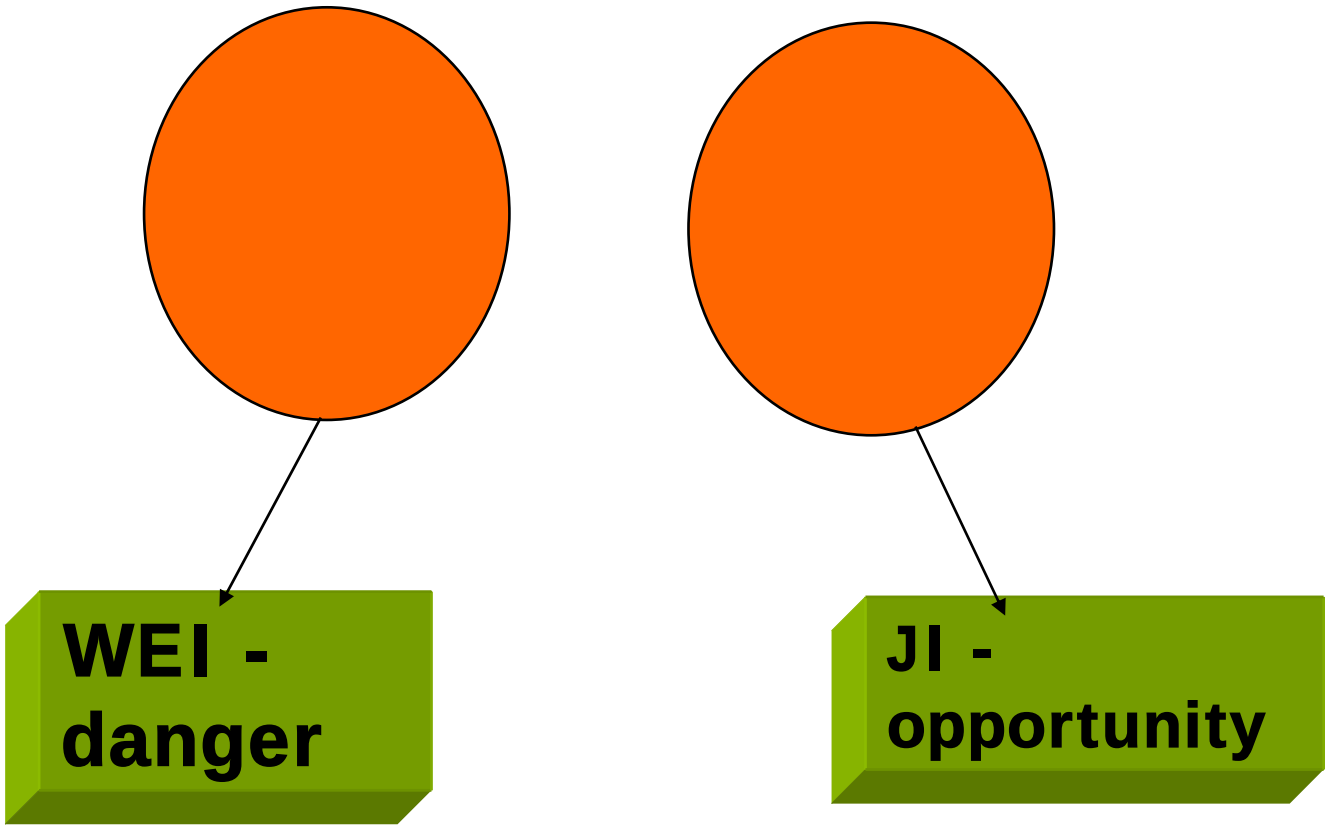
Shareholders

Regulators

Rating Agencies

Counterparties

Common Fallacies About Risk



What it doesn't mean is:

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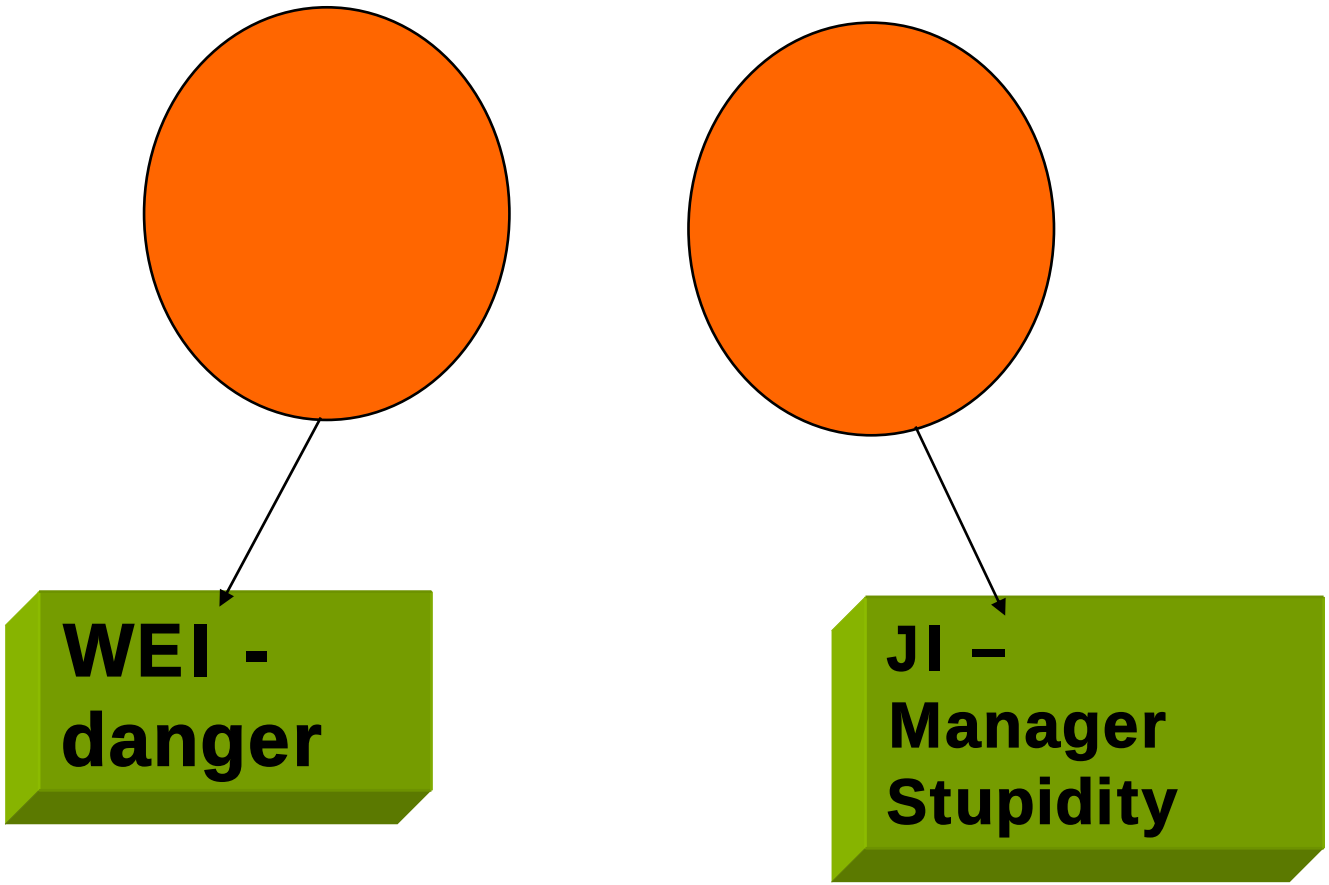
Common Fallacies About Risk



Wake up call

Approaches to managing Liquidity Risk

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Understandable reporting processes

Concentrations

Limits

Contingency

Indicators

Scenario Testing not just simulation

Approaches to managing Liquidity Risk

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Understandable reporting processes

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Scenario Testing not just simulation

Liquidity Stress Testing

Scenario	Liquidity Impact	Liquidity Gap (EUR mn)[1]	Minimum net liquidity position (EUR mn)	Severity
Market Risk	Gradually increasing	9,767	14,827 on day 1	
Emerging Markets	Gradually increasing	13,480	16,498 on day 1	
Prolonged Global Recession	Gradually increasing	18,973	14,470 on day 1	
Systemic Shock	Immediate, duration 5 days	19,751	14,469 on day 1	
1 Notch Downgrade	Gradually increasing	13,403	14,720 on day 1	
Operational Risk	Immediate, reputational effects lasting up to 3 weeks	10,381	14,827 on day 1	
Merger & Acquisition	Gradually increasing, bump in week 6	38,550	14,827 on day 1	
3 Notch Downgrade	Gradually increasing	73,532	14,326 on day 1	
German Banking Crisis	Gradually increasing	43,953	12,327 on day 1	

(1) Liquidity gap after assumed renewal of liabilities. All assets are assumed to be 'sticky'.
(2) Maximum liquidity generation based on counterbalancing and asset saleability opportunities.
(3) Maximum liquidity generation from same day as maximum liquidity gap

Maximum liquidity gap EUR 50bn, no shortfall on any day
Maximum liquidity gap over EUR 50bn
Liquidity shortfall on any day

Stress Test Process - Downgrade

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1. Starting point (for all scenarios)

   Project expected cashflows by product class based on the following assumptions:

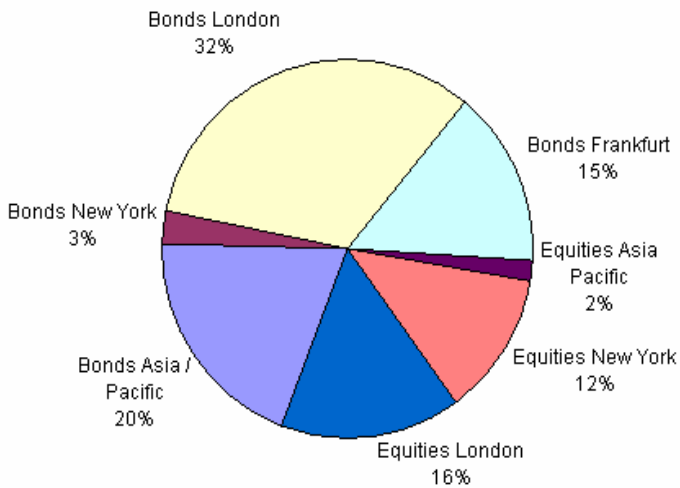
   – All assets are rolled over and need to be funded
   – All liabilities roll-off at maturity (renewal ratio = 0%)

2. Determine roll over vector for liabilities under 3 notch downgrade scenario (by product class)

Product Class	*Description*	*Rollover vector*
CP	10% renewal ration with same maturity structure	10%
CD	50% loss of roll overs	50%
Interbank deposits	Assume counterparts reduce line by 30% and current usage is 100%	70%
Non bank deposits	Loss of 50% from large and 10% from small depositors	60%
Fiduciary deposits	Only 50% renewal from maturing deposits	50%
Secured funding	Haircut increased from 2% to 10%	
Sight deposits	Scenario has no impact, behaviour as modelled	100%
Off market savings deposits	Scenario has no impact, behaviour as modelled	100%
Additional Collateral reqs	Additional EUR 2bn over 2 weeks	
Committed facilities	No additional drawings	
Central Bank deposits	Loss of 75%	25%

Asset Saleability

Asset Saleability												
Weeks								1				
Days	Update	1	2	3	4	5	6	7	8	9	10	11
Bonds Asia / Pacific	29.Aug.2003	6,583	10,273	11,892	11,892	11,892	14,428	15,271	15,938	16,281	16,475	16,475
Bonds New York	29.Aug.2003	921	987	1,188	1,312	1,470	1,592	1,780	1,920	2,008	2,175	2,226
Bonds London	29.Aug.2003	5,969	10,199	17,299	24,376	27,623	29,740	30,745	31,669	32,593	33,517	33,517
Bonds Frankfurt	29.Aug.2003	-	1,210	2,419	3,629	4,553	5,477	5,477	5,477	6,165	6,861	7,549
Equities Asia Pacific	30.Sep.2002	-	-	-	347	579	694	926	1,041	1,215	1,388	1,504
Equities New York	29.Aug.2003	-	-	2,757	2,757	2,757	2,868	5,147	5,156	5,273	6,254	6,371
Equities London	29.Aug.2003	1,357	4,393	7,641	10,278	12,142	12,478	12,478	14,452	14,452	14,452	14,452
Equities Frankfurt		-	-	-	-	-	-	-	-	-	-	-
Total asset liquidiation		**14,830**	**27,061**	**43,196**	**54,592**	**61,015**	**67,277**	**71,824**	**75,653**	**77,986**	**81,121**	**82,093**



2005 - 2006

Scenario	Funding gap[1] (in € bn.)	Liquidity impact	Gap closure[2] (in € bn.)
Market risk	8.7	Gradually increasing	117.7
Emerging markets	23.7	Gradually increasing	140.1
Systemic shock	31.5	Temporary disruption	84.2
Operational risk	19.3	Temporary disruption	124.9
DB downgrade to A1/P1 (short term) and A1/A+ (long term)	30.2	Gradually increasing	155.0
DB downgrade to A2/P2 (short term) and A3/A- (long term)	108.0	Gradually increasing	155.0

1 Funding gap after assumed partially impaired rollover of liabilities.

2 Maximum liquidity generation based on counterbalancing and asset liquidity opportunities.

Approaches to managing Liquidity Risk

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Understandable reporting processes

Concentrations

Limits

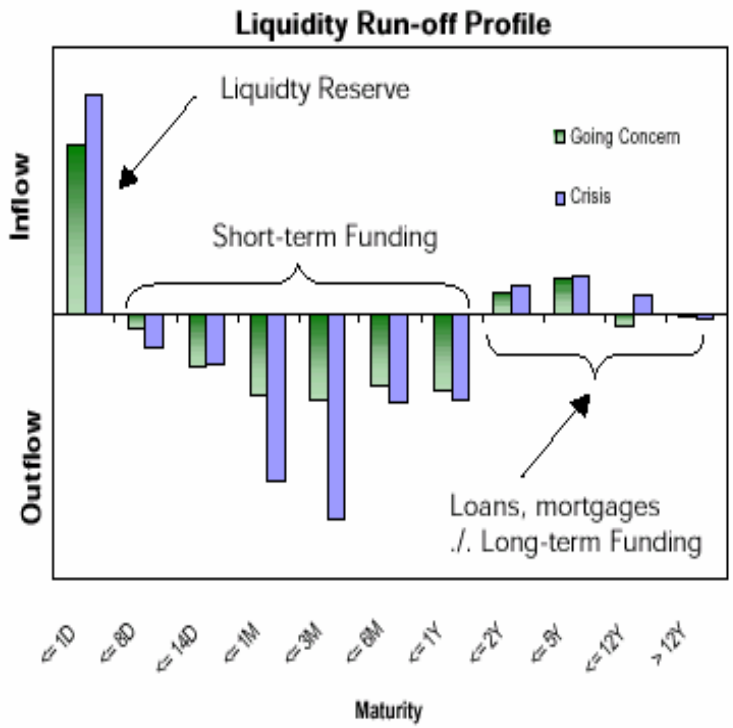
Contingency

Indicators

Scenario Testing not just simulation

Scenario Assumptions
Liquidity Run-off Profile

Dresdner applies two liquidation scenarios which are both on average more conservative than the Principle II scenario



Going Concern

- O/N: Inflow excess because of liquidity reserve
- 8D < 2Y: Outflow excess due to short-term funding & distribution of core levels for term, savings and sight deposits
- > 2Y: Inflow excess due to long-term loans and mortgages; funding by capital markets issues and domestic core levels

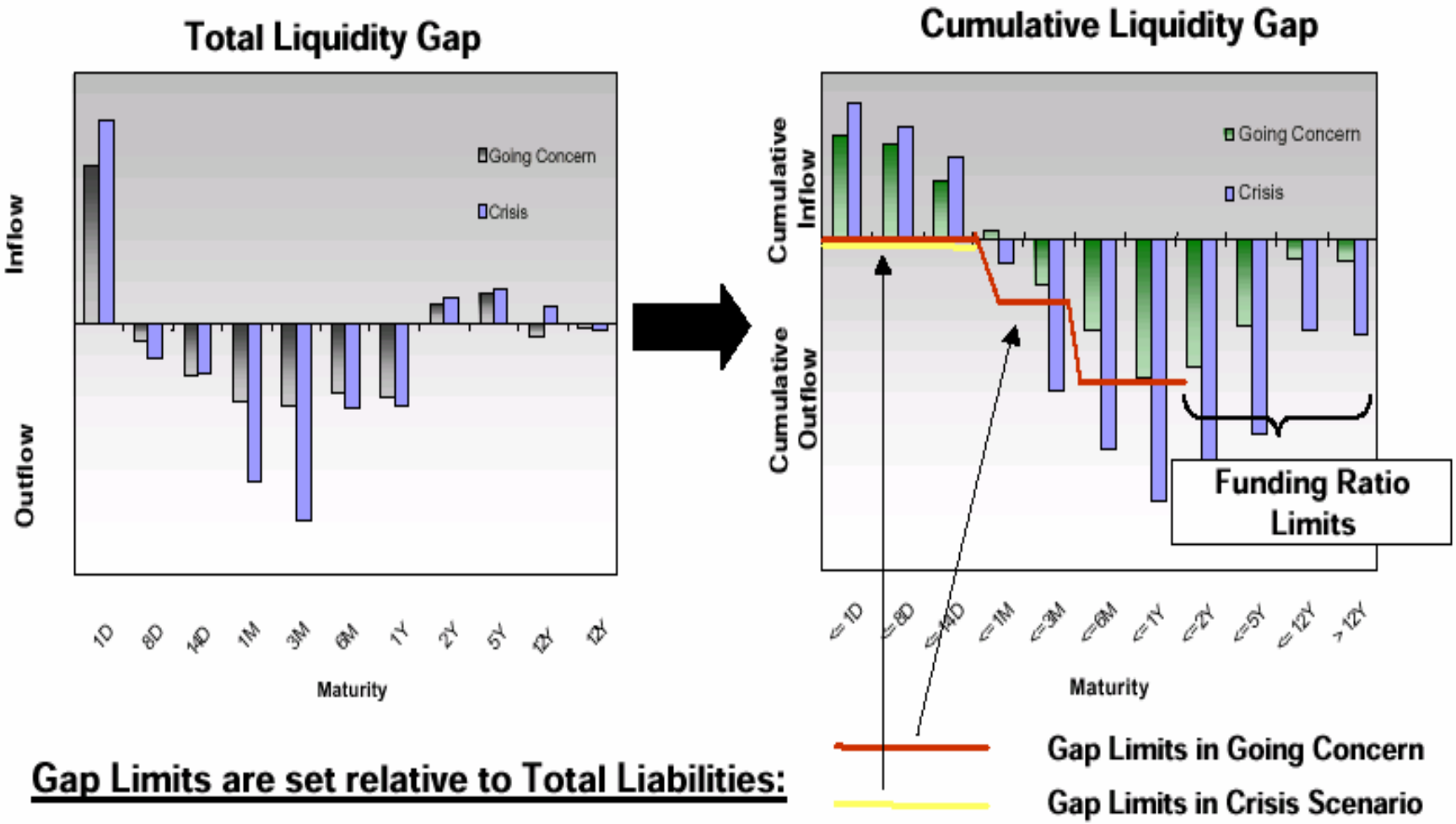
Crisis

- O/N: Enhanced inflow due to immediate liquidation of liquid assets
- 8D < 2Y: Enhanced outflow due to
  - shorter maturity assumptions of liabilities
  - reduced asset volume due to higher haircut (market liquidity risk)
  - enhanced drawing on committed lines & guarantees
- > 2Y: Enhanced inflow due to short maturity assumption of liabilities

• With Permission of Liquidity Risk Management and Control, Dresdner Bank

Scenario Output & Limit System

Liquidity Gap & Funding Ratio Limits



Gap Limits are set relative to Total Liabilities:

- With Permission of Liquidity Risk Management and Control, Dresdner Bank

Approaches to managing Liquidity Risk

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Scenario Testing not just simulation

General early warning indicators

- Funding becomes costly (widening spreads)
  - Temporary funding difficulties, or rejected borrowing requests
- Closing in on limits
- Increased dependency on best funding sources
- Declining stock prices (relative to peers?)
- Decline in earnings

Top Fund Providers

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Top 15 Fund Providers for 31-01-2007

Text Item	Parent	USD Balance Sheet	Rank	% of Total	Counterparty	USD Balance Sheet	Total Corp Deposits
Corp Deposits	ТРАНСНЕФТЬ	548,060,927.61	1	39.009%	ОАО "Акционерная компания по трансп орту нефти "Транснефть"	518,443,515.06	2,423,088,949.68
Corp Deposits					Общество с ограниченной ответственностью "Специализированный морской нефтеналивной порт Приморск"	28,791,383.73	
Corp Deposits					ОАО "Институт по проектированию маг истральных трубопроводов"	368,218.72	
Corp Deposits					Филиал Закрытого акционерного общество "Страховая компания"Транснефть"	362,075.39	
Corp Deposits					ООО КОМПЛЕКСНОЕ СПЕЦИАЛИЗИРОВАННОЕ УПРАВЛЕНИЕ "СИБНЕФТЕПРОВОДСТРОЙ"	46,636.63	
Corp Deposits					Общество с ограниченной ответственностью"Балтийские магистральные нефтепроводы"	40,128.74	
Corp Deposits					Общество с ограниченной ответственностью "МонтажСпецСтрой"	2,792.77	
Corp Deposits					ОАО "Центр технической диагностики"	2,176.93	
Corp Deposits					ОАО "Черноморские магистральные неф тепроводы"	1,707.58	
Corp Deposits					ООО "Балтийские магистральные нефте проводы"	527.34	
Corp Deposits					ООО "Восточно-Сибирские магистральн ые нефтепроводы"	380.11	
Corp Deposits					ОАО "Приволжскнефтепровод"	254.37	

General early warning indicators

- Increase in level of non performing assets
- Pressure to buy back liabilities or support market
- Short term maturing debt increasing relative to peers
- Changes to competitive environment
  - price wars
  - changes to nature of banking (eg. internet will change „stickiness“ of deposits)

Late indicators

- Successive quarterly losses
- Downgrade
- Continual growth of problem loans and loan losses
- Successive ratings downgrades
- Significant and prolonged change in customer behavior

Institution Specific Indicators

- Above average return on equity
- Rapid growth - significant asset growth
- Models are too successful for too long
- Concentrations: customers, sectors, industries, regions (because they comntribute to rapdi growth)
- Global community - Market and Economic indicators: rates, GDP, S&P (rate of growth too quick = pending crisis)
- Changes in trends in the market

Something to think about

- BAD NEWS - There is no table of universal indicators

  = You have to think and not just leave this to your regulator

- Herding effects may be reduced if each institution have their own indicators

Approaches to managing Liquidity Risk

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Understandable reporting processes

Concentrations

Limits

Contingency and Responsibility

Indicators

Scenario Testing not just simulation

Feel familiar?

1. PROMOTE THE CRO TO THE BOARD

- You can only implement risk limits if you can first measure risk
- Board to set desired risk tolerance per risk driver and the appropriate limits (ie interest rates, inflation, credit)
- VaR – use it to help determine limits but don‘t recognise it as a measure of maximum loss

Risk tolerance per risk driver

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SCB Market Risk Management

Internal Model - Parametric Value at Risk

Provisioning Data : FX Position on Sierra

Measuring Currency	THB
Confidence Level	99%
Time Series	250 Days
Data as of	7/19/2005
Process Date	20/07/2005 3:37 PM

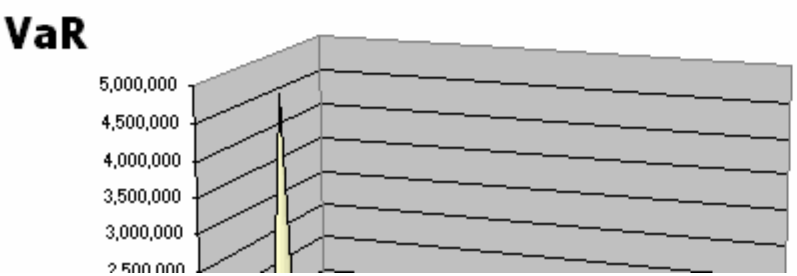
Portfolio	FX	FX Swap <= 1 Year	Aggregate	Portfolio
Risk Type	FX	Interest Rate		Portfolio
Exposure	798,032,107.59	84,100,894.87	882,133,002.46	% Loss o
Individual VaR	5,450,283.13	4,825,099.76	10,275,382.89	Hypo. Ch
Diversified Benefit	1,343,639.81	1,593,920.27	2,937,560.08	Hypo. Ch
Component VaR	4,106,643.33	3,231,179.48	7,337,822.81	O/N Posit
Risk Limit	39,000,000.00	3,900,000.00	42,900,000.00	Overnigh
Utilised Limit(%)	10.53%	82.85%	17.10%	Utilised L

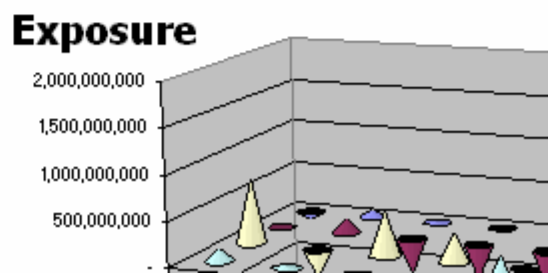
VaR grouped by Currency

Potential Loss on Port (Diversified VaR)		FX	Interest Rate				
0.8318%	7,337,822.81	5,450,283.13	687,101.99	1,332,166.95	691,726.99	2,683,059.65	1,8
JPY	1,372,354.42	1,369,937.50	36,111.54	2,438.11	22,471.79	9,911.54	
THB	3,623,304.30	-	647,828.72	1,355,838.27	727,242.74	1,515,304.86	1,9
USD	5,274,377.91	4,691,499.47	294,830.70	420,444.22	250,543.10	49,736.62	2
EUR & Other	3,620,028.15	2,362,911.35	279,165.93	22,975.57	3,524.01	2,475,325.15	

Exposure grouped by Currency

Total	882,133,002.46	FX	Interest Rate				
JPY	46,122,652.75	(101,634,285.27)	75,614,305.98	5,922,639.31	(45,894,559.06)	61,998,969.66	88,4
THB	(3,258,735,939.39)	-	181,652,050.48	(418,467,357.41)	(397,734,753.47)	(416,570,688.84)	(1,528,8
USD	3,526,008,702.55	744,380,397.59	(313,854,784.88)	512,401,982.85	341,194,839.29	(29,683,815.32)	369,1
EUR & Other	568,737,586.55	155,285,995.27	33,772,055.17	3,452,847.01	(532,013.04)	373,083,786.61	3,6





Risk tolerance per risk driver

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VAR Risk Factor Analysis - 31 March 2005

All amounts represented in MUR equivalent

Sensitivity of Present Value	Product							
Risk Factor	TREASURY BILLS - HTM	TREASURY BILLS - HFT	BONDS	LOANS	OVERDRAFTS	FIXED DEPOSITS	SAVINGS ACCOUNTS	All
JSD 2Y Rate				(61,198,475)		974		(61,197,501)
JSD SPOT				(52,080,625)	9,353,082	549,122	2,591,038	(39,587,383)
MUR 6 Month Rate	(4,953,342)	(2,263,052)		(33,382)		115,309		(7,134,467)
EUR 2Y Rate				(6,810,291)		1,092		(6,809,198)
MUR 2Y Rate		(726,070)	(5,476,870)	(973,837)		959,438		(6,217,340)
MUR 1Y Rate	(680,224)	(2,810,039)	(22,246)	(30,674)		103,521		(3,439,662)
EUR SPOT				(8,927,417)	5,475,374	286,228	462,575	(2,703,240)
MUR 3 Month Rate	(1,543,339)			(3,785)		16,665	0	(1,530,459)
MUR 1 Month Rate	(749,880)			(7,748)	457	747	816	(755,607)
JSD 1Y Rate				(345,229)		3,083		(342,146)
JSD 6M Rate				(325,775)		9,140		(316,634)
JSD 3M Rate				(289,188)	35,145	39,197	1,740	(213,107)
CHF SPOT				(451,154)			260,001	(191,153)
EUR 1Y Rate				(235,948)		44,950		(190,998)
EUR 6M Rate				(136,783)		19,470		(117,313)
EUR 3M Rate				(89,185)	1,708	18,890	389	(68,197)
CHF 2Y Rate				(35,070)				(35,070)
JPY 3M Rate					(59)			(59)
CHF 6M Rate				(25)				(25)
CHF 3M Rate				(18)				(18)
JPY 1M Rate					(10)			(10)

Contingency and Responsibilities

- Weekly monitoring of Liquidity - DAILY in times of a crisis
- If you think liquidity is going to be tight – limit lending to 30 days or less
- Close out positions against certain borrowers
- Your liquid assets may not be liquid in times of crisis.
- Short term liquidy gap < liquid govt. securities

Triggers - scenarios and indicators

- Yellow light – Warning level
  - extraordinary meeting of ALCO
  - Interim scenarios may be introduced in times of „warnings“
- Red light – Trigger level
  - Action plans launch - without requiring extraordinary board meeting
  - Interim scenarios
- Risk management is dynamic and actions will change with underlying factors

Liquidity Stress Testing

Scenario	Liquidity Impact	Liquidity Gap (EUR mn)[1]	Minimum net liquidity position (EUR mn)	Severity
Market Risk	Gradually increasing	9,767	14,827 on day 1	
Emerging Markets	Gradually increasing	13,480	16,498 on day 1	
Prolonged Global Recession	Gradually increasing	18,973	14,470 on day 1	
Systemic Shock	Immediate, duration 5 days	19,751	14,469 on day 1	
1 Notch Downgrade	Gradually increasing	13,403	14,720 on day 1	
Operational Risk	Immediate, reputational effects lasting up to 3 weeks	10,381	14,827 on day 1	
Merger & Acquisition	Gradually increasing, bump in week 6	38,550	14,827 on day 1	
3 Notch Downgrade	Gradually increasing	73,532	14,326 on day 1	
German Banking Crisis	Gradually increasing	43,953	12,327 on day 1	

(1) Liquidity gap after assumed renewal of liabilities. All assets are assumed to be 'sticky'.
(2) Maximum liquidity generation based on counterbalancing and asset saleability opportunities.
(3) Maximum liquidity generation from same day as maximum liquidity gap

Maximum liquidity gap EUR 50bn, no shortfall on any day
Maximum liquidity gap over EUR 50bn
Liquidity shortfall on any day

Heat Maps

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KRIS™ Kamakura Risk Information Services

Monday, June 16

KRIS Su

KRIS Home | Analysis | History | Ranking | Risk Map | Correlations | Portfolio | CDO

Distribution by Rating Go! Model KDP-jc4 Term 1 Year Date 2008 Jun 13 Portfolio ALL Country

Distribution by Rating

Click on a colored cell to view the underlying companies.

% From	% To	AAA	AA+	AA	AA-	A+	A	A-	BBB+	BBB	BBB-	BB+	BB	BB-	B+	B	B-	CCC+	CCC	CCC-	CC	C	D	NR
0.00	0.02	7	3	24	30	59	85	88	105	126	87	43	60	50	27	10	4	-	1	-	-	-	-	3441
0.02	0.05	2	1	5	7	10	26	24	37	45	42	17	22	35	12	4	2	-	-	-	-	-	-	1498
0.05	0.10	-	1	4	7	5	19	15	21	28	16	7	13	16	12	9	1	1	-	-	-	-	-	1405
0.10	0.20	3	1	3	2	7	8	11	20	10	20	17	14	19	14	4	3	-	-	-	-	-	-	1664
0.20	0.30	1	-	1	8	4	9	7	14	6	4	2	8	6	7	7	1	-	-	-	-	-	-	1147
0.30	0.40	-	1	2	1	3	4	4	4	6	5	6	5	9	10	4	-	-	-	-	-	-	-	865
0.40	0.50	-	-	4	-	-	1	6	5	6	4	3	2	5	4	2	1	-	-	-	-	-	-	715
0.50	0.60	-	-	5	-	1	2	3	4	1	4	-	1	5	4	3	-	-	-	-	-	-	-	584
0.60	0.70	-	-	-	-	-	2	3	5	4	1	2	5	6	5	2	-	-	-	-	-	-	-	528
0.70	0.80	-	-	-	1	-	2	1	1	2	1	-	1	4	5	1	1	-	-	-	-	-	-	407
0.80	0.90	-	-	-	-	-	1	1	-	1	3	1	1	6	5	-	1	1	-	-	-	-	-	375
0.90	1.00	-	-	-	-	1	1	1	1	2	-	1	-	1	-	3	-	-	-	-	-	-	-	332
1.00	1.25	-	-	1	1	-	1	1	5	4	4	3	5	7	3	11	3	3	-	-	-	-	-	707
1.25	1.50	-	-	-	1	1	-	1	2	2	1	-	1	2	2	1	2	-	-	-	-	-	-	557
1.50	1.75	-	-	-	-	1	-	1	1	1	3	-	-	2	5	3	2	-	-	-	-	-	-	435

Contingency and Responsibilities

- Limits are strict and not to be broken
- Best performers of limit compliance should be rewarded (with limit increases) next year
- Think about hedging long term mortgages by making them immune to business cycles phases
- A Rogue trader is still a rogue trader when he makes money

Top Fund Providers – any currency

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Top 15 Fund Providers for 31-01-2007 Currency = USD

Text Item	Parent	USD Balance Sheet	Rank	% of Total	Counterparty	USD Balance Sheet
Corp Deposits	ТВЭЛ	120,000,017.75	1	38.172%	ОАО "Атомное и энергетическое машин остроение"	120,000,000.00
Corp Deposits					ОАО "ТВЭЛ"	17.75
Corp Deposits	МНТЦ	37,195,366.11	2	11.832%	МЕЖДУНАРОДНЫЙ НАУЧНО-ТЕХНИЧЕСКИЙ ЦЕНТР/ISTC	37,188,437.08
Corp Deposits					Федер.госуд. унитарное предприятие"Научно-производст.объединение"Радиевый институт им. В.Г.Хлопина"	6,773.04
Corp Deposits					ФедеральноеГосударственноеУнитарноеПредприятие научно-исслед. институт гигиены, токс. и профп.	155.99
Corp Deposits	АДМИРАЛТЕЙСКИЕ ВЕРФИ	28,578,070.58	3	9.091%	Федеральное государственное унитарное предприятие "Адмиралтейские верфи"	28,578,070.58
Corp Deposits	Erglis Limited	25,000,000.00	4	7.953%	Erglis Limited	25,000,000.00
Corp Deposits	Undefined	21,152,471.89	5	6.729%	Undefined	21,152,471.89
Corp Deposits	ГРУППА КОМПАНИЙ "СОДРУЖЕСТВО"	16,035,549.96	6	5.101%	Закрытое акционерное общество "Содружество-Соя"	16,035,549.96
Corp Deposits	ОАО "Юг Руси"	11,003,963.00	7	3.500%	ОАО "Юг Руси"	11,003,963.00
Corp Deposits	ТНК-РЕГИОНЫ	10,909,226.54	8	3.470%	Открытое акционерное общество "Корпорация Югранефть"	10,908,781.75
Corp Deposits					Открытое акционерное общество Компания "РУСИА Петролеум"	444.79

Total Corp Deposits
380,334,198.64

Kamakura Risk Manager™

Risk Management
Interest Rate Risk
Market Risk
Credit Risk
Liquidity Risk
Operational Risk
Enterprise Risk
Portfolio Risk
Performance
Risk Based Pricing
Product Profitability
Unit Profitability
Economic Capital
Compliance
Basel Capital
National Regulatory
Accounting

Logout

Summary Cash Flow Coverage Ratios

X4

Repo

Scenario	5/1/00	5/2/00	5/3/00	5/4/00	5/5/00	5/31/00	6/30/00	7/31/00	8/31/00	9/30/00	10/31/00
Bank Specific - mild credit problems											
Actual	1.03	0.97	1.02	1.01	1.03	0.95	1.05	1.02	1.05	0.96	1.05
Minimum	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0
Bank Specific - mild loss of confidence											
Actual	1.01	1.04	1.0	1.04	1.02	1.02	1.0	0.96	0.95	0.97	1.02
Minimum	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0
Bank Specific - severe credit problems											
Actual	0.76	0.84	0.82	0.77	0.83	0.9	0.75	0.78	0.84	0.85	0.8
Minimum	0.85	0.85	0.85	0.85	0.85	0.85	0.85	0.85	0.85	0.85	0.85
Bank Specific - severe loss of confidence											
Actual	0.82	0.84	0.79	0.84	0.76	0.78	0.89	0.85	0.89	0.84	0.82
Minimum	0.85	0.85	0.85	0.85	0.85	0.85	0.85	0.85	0.85	0.85	0.85
Business Cycle - high rates											
Actual	1.22	1.18	1.12	1.21	1.25	1.19	1.05	1.06	1.1	1.22	1.05
Minimum	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1
Business Cycle - industry downturn											
Actual	1.07	1.06	1.15	1.24	1.07	1.16	1.05	1.11	1.05	1.16	1.25
Minimum	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0
Business Cycle - low rates											
Actual	1.17	1.14	1.24	1.05	1.23	1.07	1.19	1.25	1.19	1.13	1.15
Minimum	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1
Business Cycle - mild recession											
Actual	1.16	1.25	1.23	1.22	1.05	1.06	1.21	1.25	1.06	1.14	1.25
Minimum	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0
Business Cycle - rate ramps											
Actual	1.2	1.16	1.07	1.22	1.21	1.14	1.19	1.1	1.07	1.21	1.2
Minimum	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1
Business Cycle - rate shocks											
Actual	1.24	1.14	1.14	1.21	1.06	1.06	1.16	1.15	1.14	1.2	1.08
Minimum	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1
Business Cycle - severe recession											
Actual	0.75	0.77	0.87	0.9	0.75	0.78	0.77	0.89	0.79	0.9	0.83
Minimum	0.85	0.85	0.85	0.85	0.85	0.85	0.85	0.85	0.85	0.85	0.85
Market Risk Events - mild											
Actual	1.04	1.03	1.03	1.04	0.97	1.0	0.97	0.95	0.98	1.03	0.99
Minimum	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0
Market Risk Events - severe											
Actual	0.77	0.78	0.81	0.85	0.86	0.9	0.75	0.88	0.78	0.85	0.76
Minimum	0.85	0.85	0.85	0.85	0.85	0.85	0.85	0.85	0.85	0.85	0.85
Market Risk Events - short and limited											
Actual	1.11	1.1	1.19	1.24	1.09	1.24	1.07	1.16	1.06	1.08	1.14
Minimum	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1

Heat Maps

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Current Date: 01-June-2005

Warning signals: Net Income/Total Assets

A rise in the net income/assets ratio lowers the default probability

TIC	Name	Country	Warning	Today	-5days	-10days	-20days	-50days	-75days	-120days	-180days
ug	PEUGEOT SA	FRA	Value	0.0064	0.0064	0.0064	0.0064	0.0064	0.0064	0.0064	0.0064
			Risk Alert	0%	0%	0%	0%	-1%	-1%	-1%	-1%
por3	PORSCHE AG	DEU	Value	0.0174	0.0174	0.0174	0.0174	0.0174	0.0174	0.0224	
			Risk Alert	-4%	0%	0%	0%	0%	0%	-22%	
rnl	RENAULT SA	FRA	Value	0.0146	0.0146	0.0146	0.0146	0.0146	0.0106	0.0106	0.0106
			Risk Alert	18%	0%	0%	0%	0%	37%	37%	37%
vow	VOLKSWAGEN AG	DEU	Value	0.0028	0.0028	0.0028	0.0028	0.0028	0.0028	0.0028	0.0002
			Risk Alert	308%	0%	0%	0%	0%	0%	0%	1231%
bmw	BMW AG	DEU	Value	0.0076	0.0076	0.0076	0.0076	0.0076	0.0076	0.0076	0.0076
			Risk Alert	0%	0%	0%	0%	0%	0%	0%	0%
dcx	DAIMLER CHRYSLER AG	DEU	Value	0.0038	0.0038	0.0038	0.0038	0.0038	0.0054	0.0054	0.0029
			Risk Alert	-10%	0%	0%	0%	0%	-30%	-31%	29%
f	FORD MOTOR CO	USA	Value	0.0041	0.0041	0.0041	0.0041	0.0003	0.0003	0.0009	0.0038
			Risk Alert	321%	0%	0%	0%	1112%	1112%	370%	9%
fr	FIAT SPA	ITA	Value	0.0059	0.0059	0.0059	(0.0100)	(0.0100)	(0.0114)	(0.0087)	(0.0030)
			Risk Alert	-160%	0%	0%	-160%	-160%	-152%	-168%	-297%
			Value	(0.0024)	(0.0024)	(0.0024)	(0.0024)	0.0013	0.0013	0.0010	0.0029

Approaches to managing Liquidity Risk

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Understandable reporting processes

Concentrations

Limits

Contingency and Responsibility

Indicators

Scenario Testing not just simulation

Scenario testing

- History provides - „could happens“
- Can cause complacency
- VaR is not the maximum loss
- TARGET – high P&L with limits and triggers. If triggers are activated, then target high liquidity at the cost of P&L

  (Can only happen if CRO is board member)

Scenario testing

- Create a set (12) of understandable and tangible scenarios for your „audience“
- Test in line with known events:
  - Emerging market crisis (Mexico, Brazil)
  - Bond market crisis (1994)
  - Oil price surge
  - Russian crisis (LTCM)
  - Kobe earthquake
  - Sub-prime
  - Economic stagnation – eg. Japan

Scenario testing

- Look for Bubbles = concentration in one sector
- Test in line with unknown events: „Grey Swans“

  no evidence of existence ≠ evidence of no-existence

  - Hedge fund collapse (Bubble)
  - Oil (Bubble)
  - China (Bubble)
  - Internet attack
  - War –> who vs who?
  - Correlations – what if they change by 500%
  - Weather catastrophe

Jim’s short, short list

- **DON‘T** waste time doing capital allocation assessment for Liquidity.
  - It‘s a 2nd order risk that occurs if you manage your risks poorly
- **DO** spend time managing and understanding your risks
- Compare yourself to your peers
  - eg. short term maturing debt. Will they have the problem or you?

DO THINK FOR YOURSELF!

YUL
B.
NEX T

Selected Local Clients

Fiserv. | IPS-Sendero

Alfa-Bank

ALM & Market valuation - 2007

FTP – Nov 2007

Credit Risk - 2008

Bank of Moscow

Asset and Liability Management – Sep 2007

Market Risk

ROSBANK

Sendero Asset and Liability Management – 2002

Advanced ALM - 2008

Промсвязьбанк

Credit Risk, Limits Management, ALM, Liquidity, Market Risk & FTP – Feb 2008

And the winner is !

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Liquidity Risk

Complete » Connection