

Comments

on the EBA Discussion Paper: Implementation in the European Union of the revised market risk and counterparty credit risk frameworks (EBA/DP/2017/04)

Register of Interest Representatives

Identification number in the register: 52646912360-95

Contact: Dr. Silvio Andrae

Telephone: +49 30 20225-5437

Telefax: +49 30 20225-5404

E-Mail: silvio.andrae@dsgv.de

Berlin, 15-03-2018

The **German Banking Industry Committee** is the joint committee operated by the central associations of the German banking industry. These associations are the Bundesverband der Deutschen Volksbanken und Raiffeisenbanken (BVR), for the cooperative banks, the Bundesverband deutscher Banken (BdB), for the private commercial banks, the Bundesverband Öffentlicher Banken Deutschlands (VÖB), for the public-sector banks, the Deutscher Sparkassen- und Giroverband (DSGV), for the savings banks finance group, and the Verband deutscher Pfandbriefbanken (vdp), for the Pfandbrief banks. Collectively, they represent more than 1,700 banks.

Coordinator:

German Savings Banks Association
Charlottenstraße 47 | 10117 Berlin | Germany

Telephone: +49 30 20225-0

Telefax: +49 30 20225-250

www.die-deutsche-kreditwirtschaft.de

The European Banking Authority (EBA) published the discussion paper "Implementation in the European Union of the revised market risk and counterparty credit risk frameworks" for consultation on 18 December 2017. We appreciate the opportunity to submit our comments.

I. General comments

Without pre-empting the outcome of ongoing legislative discussions with respect to CRR2, the EBA believes that it is necessary to address open questions relating to the issues of market risk and counterparty credit risk within the context of the Discussion Paper. The German Banking Industry Committee supports this initiative. However, the scope and level of depth of the questions raised by the EBA show that a large number of issues are still open – including from a conceptual perspective. That is why the Basel Committee on Banking Supervision is also working hard in 2018/2019 to clarify the open issues.

For this reason, the German Banking Industry Committee advocates removing in particular the issue of FRTB from the current legislative discussions in the first instance. We wish to point out that the BCBS will clarify and define key points relating to the FRTB this year. A reliable legislative process could then be initiated on this basis. Care should therefore be taken to ensure that the EBA does not arrive at any advance decisions based on the Discussion Paper that could contradict the assessments of the BCBS. This will simplify the implementation of the requirements at the institutions by avoiding duplication of effort.

In the following we address the questions posed by the EBA. In some cases, a response is allocated to several questions.

II. Specific comments

Q1. Do you have views on the proposed prioritisation of work?

Generally, we agree with the EBA's prioritisation and welcome the approach of discussing important technical aspects of the SA-CCR and FRTB at an early stage with the industry. However, we believe that the definition of the revised trading book boundary should also be addressed at an earlier stage in order to give guidance on implementation and investment decisions. In particular, it is necessary to arrive at an understanding of exceptional circumstances and reclassification at an early stage to allow for the alignment of risk and accounting functions. Additionally, the boundary definition will have an impact on the trading desk structure.

SA-CCR – Mapping of derivative transactions to risk categories

Q2. Would the proposed allocation for the products in the list be appropriate in all cases? If not, please provide an explanation.

The allocation of products to the risk categories proposed by the EBA is understandable and correct. In our opinion, the list is easy to understand and can be implemented without any great effort.

Q3. Would you include in the above list other derivative transactions for which there would be an unambiguous primary risk driver? In particular, do you consider that bond forwards on investment-grade bonds or cross-currency swaps should be included? Please provide some justification for your answer.

As a general principle, bond forwards on investment-grade bonds and cross-currency swaps are standard OTC derivatives in customer trading activities in exactly the same way as other products on the list.

The categorization of bond forwards should be dependent on the quality of the bonds. We believe that bond forwards on investment grade bonds should be assigned to the Interest Rate category. Bond Forwards on non-investment grade bonds should be allocated to the Credit risk category.

Mark-to-market cross-currency swaps (MtM-CCS), also known as resettable cross-currency swaps, are a very common variety of cross-currency swaps (CCS). In these transactions, the notional amounts are adjusted (reset) to reflect the current exchange rate in each case at the end of each interest period. This minimises the foreign currency risk. MtM-CCS should therefore be allocated to the Interest rate risk category. In this case, currency pairs would additionally be mapped as hedging rates in this risk category.

For CCS whose notional amount does not change over their term, on the other hand, the exchange rate is the primary risk driver; for this reason, these transactions should be allocated to the Foreign exchange risk category. The transactions can then be allocated within the existing currency pair hedging rates.

Total return swaps and performance swaps should also be added to the list in either the Credit risk or Equity risk category.

In general, institutions should be allowed to develop own lists containing derivative transactions with one unambiguous primary risk driver based on their internal policy (e.g. based on ISDA SIMM).

Q4. If a list of criteria is to be developed instead of (or combined with) a list of derivatives, what could such criteria be? Please use the table below in order to give examples of allocation based on simplicity-related criteria.

We do not believe that a list of criteria is very expedient because it would require more effort to implement and creates scope for interpretation that would run counter to consistent implementation in the EU.

Q5. What are your views about the qualitative approach used as a starting point under step 2?

The proposals are reasonable, although their implementation does appear to entail a certain degree of effort/complexity. We are also concerned that step 2 will not only be applicable in just a few exceptional cases.

Q6. Which would be the most appropriate option for the quantitative approach? Would you recommend another option?

Option 3 with risk weights that make the sensitivities of different risk categories more comparable (and that do not necessarily have to be oriented on the FRTB) appears to be a suitable compromise between accuracy and effort. However, this could already be too effort-intensive for small institutions. A final assessment is therefore difficult. The standardised approach should be relatively easy to calculate, but still sufficiently risk-sensitive.

Q7. What values would be reasonable for the threshold(s) (X, Y, and their equivalents for Options 3 and 4) that determine the number of material risk drivers? Please provide rationales for proposed levels.

With regard to step 2, the institutions should be able to decide on the basis of internally defined criteria which and how many risk drivers are material. If such criteria are not available in an appropriate form, we consider the following thresholds and methods to be suitable for assessing the materiality of risk drivers:

With regard to threshold Y in Option 2, we consider a value of 70% to be appropriate. We derive the value $Y=70\%$ from the reciprocal of the alpha factor of 1.4. This constitutes an add-on for model inaccuracies, and we believe it would be appropriate to use it here (for Y% the reciprocal of the alpha factor: $1/1.4 = 71.4\%$, rounded to 70%).

We also have two more proposals for modifying Option 2. They can be considered in isolation, but nor would they be mutually exclusive. The goal is to simplify the approach somewhat and avoid risk drivers for derivatives that are, in reality, of very secondary importance, from being defined as "material". In principle, these proposals are also applicable to Option 3 (if risk weights are additionally considered) and possibly also to Option 4.

Proposal 1: Combine relative sensitivities by risk categories:

The sensitivities of the risk drivers in steps 1 and 2 in paragraph 72 should be combined by risk categories. In our view, a derivative for which several risk drivers in a risk category exceed Y% in the aggregate should only be allocated to that one risk category. This would allow market risk to be appropriately taken into consideration (also against the background of the alpha factor). In addition, the derivative is in any case only allocated within the risk categories in accordance with Article 277(5) of the draft CRR2 to the hedging rate that exhibits the higher sensitivity.

Example 1 (assume $Y=70\%$):

The following five risk drivers were identified for a derivative and the relative sensitivities calculated:

Risk driver	Relative sensitivity per risk driver a_i/s_i
Interest rate risk driver 1	65% (= a_1)
Interest rate risk driver 2	10% (= a_3)
Interest rate risk driver 3	6% (= a_4)
FX risk driver 1	15% (= a_2)
Credit risk driver 1	4% (= a_5)

In accordance with the Discussion Paper, the outcome would be that this derivative would have to be allocated both to the Interest rate risk category and the FX risk category. The reason is that the percentage $Y=70\%$ is only exceeded when the relative sensitivities of the interest rate risk driver are added up ($a_1+a_2=80\%$), although a total of 81% ($=a_1+a_3+a_4$) of the sensitivities are attributable to interest rate risk and FX risk is secondary to interest rate risk.

If the relative sensitivities are previously combined on a risk category basis in a first step, the following relative sensitivities a_i would result:

Risk driver	Relative sensitivity per risk driver	Relative sensitivity per risk category a_i/s_n
Interest rate risk driver 1	65%	81% (= a_1)
Interest rate risk driver 2	10%	
Interest rate risk driver 3	6%	
FX risk driver 1	15%	15% (= a_2)
Credit risk driver 1	4%	4% (= a_3)

In this case, the derivative would only be allocated to the Interest rate risk category because the risk drivers for the Interest rate risk category exceed 70% in the aggregate. The FX risk category would not be considered, which we think would be justified from a risk perspective.

Proposal 2 (assume $Y=70%$): Introduction of an Option 1 element:

This proposal introduces an element of Option 1 into Option 2, by introducing a comparison of the sensitivities of the primary risk driver with the sensitivities of the other risk drivers. This would ensure that only the primary risk driver would be relevant for allocation to the risk category, even if its relative sensitivity falls below Y . To do this, the sensitivities of the other risk drivers are considered in relation to the primary risk driver (threshold X).

Example 2 (assume $Y=70%$ and assume $X=30%$):

Risk driver	Relative sensitivity a_i/s_n
Interest rate risk driver 1	15% (= a_2)
FX risk driver 1	65% (= a_1)
Credit risk driver 1	12% (= a_3)
Other risk driver 1	8% (= a_4)

If Option 2 in the Discussion Paper is applied, the derivative would have to be allocated to the FX and Interest rate risk categories, because only the total of a_1+a_2 exceeds the threshold $Y=70%$. If our proposal is applied with the introduction of another threshold (X), the derivative would only be allocated to the FX risk category because the sensitivity of the second-highest risk driver relative to the primary FX risk driver is lower than the threshold $X=30%$ ($15\%/65\% = 23\%$). In our opinion, this would also be appropriate because interest rate risk is considerably lower than FX risk.

Q8. Do you have any views on the appropriateness of devising a fallback approach? Can you identify any cases where reverting to the fallback approach is necessary?

Q9. Do you have any views on the appropriateness of a cap on the number of risk categories to which a single derivative transaction can be allocated? If yes, what value would you recommend for that cap (three or four)?

Q10. Do you have any further comment or consideration on the mandate under discussion?

Article 277(6)(a) of CRR2 requires the EBA to develop a technical standard for identifying the material risk drivers for derivatives in the banking book. Based on the wording, we presume that the present Discussion Paper is designed to contain a corresponding proposal. However, this would mean that derivatives in the banking book that do not match the list in paragraph 64 (step 1) could only be included as

part of the fallback approach (step 3). The reason for this is that market risk sensitivities cannot be determined for derivatives in the banking book in the revised market risk standardised approach, so step 2 cannot as a rule be applied to these banking book derivatives.

For derivatives in the banking book, we therefore suggest using an internally defined, qualitative approach for the allocation to risk categories as part of step 2. Processes and decisions under this qualitative approach should be documented appropriately and understandably, and would have to be demonstrated to the competent authority on request.

In addition, the CRR2 review appears to indicate that the initial application of the FRTB will be delayed. It suggests that the SA-CCR would be initially applied prior to the initial application of the FRTB. This means that no sensitivities would be available for derivatives in the trading book when the SA-CCR is initially applied, although these would be necessary for the allocation to risk categories and hedging rates. It is therefore necessary to introduce transitional arrangements (e.g. a qualitative approach as for step 1).

We therefore propose voluntarily abandoning the application of step 2 and mapping all cases that cannot be unambiguously allocated to step 1 to the risk drivers using the conservative step 3. This approach could mean a lower effort for technical implementation, which could benefit some banks.

Q9. Do you have any views on the appropriateness of a cap on the number of risk categories to which a single derivative transaction can be allocated? If yes, what value would you recommend for that cap (three or four)?

There should be no general cap on the number of risk categories to which a single derivative transaction can be allocated. Instead, institutions should be given flexibility to assess the best allocation on a case by case basis. The thresholds and procedures for assessing the materiality of risk drivers should be considered.

SA-CCR – Corrections to supervisory delta

Q11. Do you have any views on the most appropriate approach to compute supervisory delta in a negative interest rates environment? Please elaborate.

The proposed lambda shift is one way of modelling negative interest rates in a Black-Scholes model. It should be noted in this case that the implied Black-Scholes volatility is dependent on lambda, i.e. the implied volatility would have to be adjusted to arrive at the same result if there is a change in lambda. This effect prompts the question of the extent to which a fixed supervisory option volatility is appropriate for the Interest rate asset class. Considering a Black-Scholes model with a normal distribution (i.e. no log-normal distribution or shifted log-normal distribution) would bypass this problem. We would therefore propose using a model with a normal distribution to avoid the problems associated with the lambda shift. This would render superfluous the discussion about the level of the lambda shift and the EBA would also not have to issue any further updates.

Q12. Which one of the two options do you think is more appropriate from an EU perspective (i.e. maximum harmonisation)? Are you aware of any issue these two options could raise?

To avoid this, we strongly urge using a normal distribution in order to eliminate the problems with the lambda shift (see Q11).

However, if the usage of lambdas is necessary, we propose using bank-specific lambdas set at trade level.

Q13. Do you agree that the definition of a long position in the primary risk driver and a short position in the primary risk driver in Article 279a(2) of the CRR2 proposal is sufficiently clear for banks to determine whether they hold a long or a short position?

The definition is generally understandable.

FRTB – Trading book boundary

We welcome the early initial assessment by the EBA of the new boundary between the trading and banking book. However, we do have comments on some of the statements above and beyond the questions.

As one example, we do not agree with the EBA's stated opinion in paragraph 101 that "In the event of conflict between a list in Article 104 and the institution's purpose, it is expected that the list prevails". This stands in contradiction to Article 104(4) of the CRR2, which allows institutions to assign a trading book instrument referred to in Article 104(2)(e) to (i) of the CRR2 to the banking book if no trading intent is being followed. EBA should ensure that the stipulations are harmonised with the final CRR2. This also applies to Article 102.

In addition to this, we believe that the EBA's proposed approach for instruments for which there is a conflict between the two CRR2 lists is not a satisfactory solution. Paragraph 107 states that allocation to the banking book should have priority. Nevertheless, the trading intent should also be taken into consideration in order to ensure the appropriate allocation of the instruments. This is done on the basis of the policies and procedures established in accordance with Article 104(1) of the CRR2. Moreover, the ability to use the option to demonstrate the lack of a trading intent in accordance with Article 104(4) and the option to assign the instrument to the banking book should be anchored more strongly.

Q14. Do you agree that changes in instruments' circumstances that imply a shift between the presumptive lists should be accepted as 'exceptional circumstances'? Please provide examples.

Under certain circumstances, it may happen that the conditions for allocating a financial instrument to the trading or banking book no longer apply (e.g. a lack of market liquidity in an instrument). This does not necessarily have to involve "exceptional circumstances". We are seeking clarification about the situations under which "exceptional circumstances" would apply.

Q15. Do you agree that CTP positions that become illiquid must remain in the TB?

This depends on the reason for illiquidity. If only single positions become illiquid, this is not understood as an "exceptional circumstance". If an entire market breaks down, we think that this is an exceptional circumstance and re-designation should be possible, but without an obligation to do so.

Q16. Please provide examples of cases where exceptional circumstances might warrant the approval of reclassification.

Exceptional circumstances could be:

- breakdown of an entire market segment (market disruption, severe restrictions on tradability)
- restructuring of a bank's business model, e.g. closing down of certain trading activities (or all trading activities)

We think the goal should be to synchronise the regulatory trading book and the accounting trading portfolio. Both IFRS 9 (IAS 39) and German GAAP (HGB) have similar rules for re-designation based on "rare" or "exceptional" circumstances.

With regard to the determination of exceptional circumstances, we can understand that the ex ante identification of reasons is relatively difficult. However, we reject the introduction of a notification requirement to the EBA, as proposed in paragraph 111. Permission to reclassify is issued by the national competent authorities or the ECB. There is no provision for a notification obligation to the EBA on the part of the institutions, nor do we believe that it is necessary. Please delete this notification obligation due to a lack of any legal basis.

FRTB – Treatment of non-TB positions subject to FX or commodity risk

Q17. Do institutions have any particular issue in identifying non-trading book FX and commodity positions subject to market risk? What kinds of transactions do those positions correspond to and how material are they with respect to current RWAs for market risks?

In general, the identification of non-trading book FX positions is not an issue and is carried out on a daily basis. Front office and risk systems flag these positions based on associated portfolios and the presence of foreign exchange risk. Nonetheless, identification issues might arise for portfolios outside the scope of market risk when modified investment and hedging strategies lead to new foreign exchange risks. This could typically be the case for non-monetary items (equity investments, funds, real estate) with low materiality.

Q18. What issues would institutions face to value those positions in order to calculate the own funds requirement for market risks using the FRTB standards? Currently, do you revalue all components for the purposes of computing the own funds requirement for market risks? If not, which ones? Currently, how frequently are those positions valued?

The valuation of non-trading book FX positions under FRTB standards does not differ from trading book positions and is performed by front office systems. Currently, only the FX component of these positions is revalued. Valuation is performed on a daily basis.

The valuation of positions subject to the own funds requirement for market risk is based on the valuation used for the calculation of economic P&L (by the risk department; independent of trading) for the vast majority of positions with FX risk exposures. In some institutions, those calculations are also taken from Pillar 2 measurement systems. Therefore, most positions are marked to market on a daily basis, even if they are not accounted for at fair value, including loans in foreign currencies.

There are only a few positions, such as pension provisions of foreign branches or non-financial assets, that are neither accounted for at fair value nor marked to market in the economic P&L. As a general rule, those positions are valued for accounting purposes on a monthly basis at the accounting date. These values are used for the purpose of computing the own funds requirement for FX risk.

Q19. For the non-trading book positions subject to the market risk charge that are not accounted for at fair value (or in the case of FX, are non-monetary), do stakeholders have the capacity to mark these positions to market and how frequently can this be done? Do stakeholders have the capacity to “mark to market” the FX component of the non-monetary item subject to FX risk on a frequent basis (for example daily)?

The FX components of non-trading book positions subject to market risk are revalued by marking to market per currency on a daily basis. In general, non-trading book positions are only marked to market if a market value can be assigned meaningfully or otherwise observed. This is done irrespective of the accounting treatment. Exceptions to this are credit components, loans not designated at fair value and equity investments. If there is no MtM valuation for the economic P&L, the most current available accounting value is used (see question 18).

Q20. Does IFRS 13, i.e. Fair Value Measurement, have an impact on the frequency of non-trading book revaluations? If yes, please explain how.

No - IFRS 13 does not prescribe frequency of accounting valuation, but regardless of the treatment for accounting purposes, most non-trading book items subject to FX risk are marked to market daily via economic P&L (see Q18, Q19).

Q21. Are there other factors (for example impairments or write-downs) that can affect the valuation of non-trading book FX positions?

Yes, there can be other factors that can affect the valuation of non-trading book FX positions. Impairments and similar factors are often taken into account for valuation (e.g. valuation of loans comprises impairments on a daily basis).

Q22. Do stakeholders have a view on what minimum number of notional trading desks should be allowed? What would be the negative consequences of applying some restrictions to the number of notional trading desks allowed (for example only one notional desk for FX positions and only one for commodities)?

We presume that the requirements in chapter 4.4 “FRTB – Treatment of non-TB positions subject to FX or commodity risk” relating to notional trading desks are not relevant for institutions that perform asset/liability management of FX risks solely in the banking book, so we requesting the wording to be tightened up accordingly. In our view, putting the requirements for notional trading desks on an equal footing with those for trading desks is too far-reaching and unreasonable, especially for banking book institutions. The BCBS standard indicates that FX and commodity risks in the banking book should be treated for capital backing purposes as if they were being traded on a notional trading desk. However, the equivalence of the requirements for notional trading desks with those for trading desks addressed by the EBA additionally contains process-related and organisational aspects and thus goes beyond the BCBS requirements.

Moreover, we see a risk that FX instruments for purely banking book positions will have to be double-counted both in the IRRBB and under the FRTB. Double-counting must be ruled out from a regulatory perspective (e.g. hedging a fixed-rate instrument in an FX position using a cross-currency swap).

In the case of institutions that manage FX risks out of their trading book, the number of notional trading desks needed might be dependent on the institution’s business model. Typically, notional desks for treasury units will be clustered according to the maturity of affected positions. Additionally, each branch might

require a notional desk of its own if management of positions is carried out individually. Restricting the number of notional desks allowed to just one would obstruct integrated interest rate and liquidity management by forcing institutions to separate FX positions from multiple banking book units to a single combined FX notional desk. This would reduce governance on affected positions.

However, if institutions have only one notional desk for FX, they should not be forced to have more desks. It really depends on the institution's business model and size.

Q23. Do you consider that trading book positions should not be included in notional trading desks? Would you agree that, for trading desks that include trading and non-trading book instruments, all the trading desk requirements should apply? Do you consider that for notional trading desks all the trading desk requirements should apply? If this is not the case, which qualitative requirements of Article 104 b(2) of the CRR2 proposal could not practically apply to notional trading desks?

We wish to refer again at this point to our positions originally stated in response to question 22 and are seeking clarification that the requirements do not apply to institutions that perform their asset/liability management of FX risks solely in the banking book. The proposed approach far exceeds the BCBS requirements.

Generally, we agree that trading book positions should not be included in notional desks due to the different nature of a notional desk compared with a trading desk. Most of all the qualitative requirements of Article 104b(2) of the CRR2 should not apply to notional desks. Where appropriate the notional trading desks may be included in desk reporting and limiting.

However, if an institution wishes to include trading book positions in notional trading desks it should be allowed to do so. This might be useful due to organisational constraints. Especially for smaller branches, it is not always reasonable to separate access to the market from other units. Not all trading desk requirements should apply for those combined desks, especially if a waiver according to Article 104b(4) of the CRR2 is granted for SA-only banks. Organisational and reporting requirements in particular should be adapted to banking books (points (a) and (d) from Article 104b(2) of the CRR2).

Q24. Do you see a reason why backtesting requirements should not apply to notional trading desks?

Based on the status quo, backtesting requirements might apply at the notional trading desk level. However, we wish to draw attention to the known issue (e.g. from partial-use models) in backtesting a single risk component (in this case FX risk). The question of how to deal with theta effects and what will be covered by theta effects needs to be well defined. In the end, the coverage of FX rate returns will only be backtested. As a result we suggest removing backtesting requirements for notional desks.

Q25. Do you see a reason why P&L attribution requirements should not apply to notional trading desks?

Based on known issues regarding P&L attribution for well-hedged desks, P&L attribution requirements should not apply to notional trading desks. Since FX risk in the non-trading book is extremely well hedged (nearly zero exposure), for many banks P&L attribution is not applicable in a meaningful way.

FRTB – Residual risk add-on

Q26. Do you agree with the proposed general definitions of instruments referencing an exotic underlying and instruments bearing other residual risks? Do you think that these definitions are clear? If not, how would you specify what is an 'exotic underlying' and what are 'instruments that reference exotic underlyings'? Please provide your views, including rationale and examples.

We agree with the proposed general definition.

Q27. Do you agree with complementing, for the sake of clarity, those definitions with a non-exhaustive list of instruments bearing other residual risk? Similarly, do you agree with retaining the possibility of excluding some instruments from the RRAO?

We are seeking a principle-based approach and not a fixed list of instruments. As a minimum, the possibility of excluding instruments from RRAO is needed so that individual circumstances can be reflected, allowing institutions to define "other risks" along the lines of their internal risk governance. This approach also follows the intentions of the trading book boundary definition.

Q30. Do you think there are any instruments, not meeting the general definitions above, whose risk would however be poorly captured within the standardised approach and should therefore be included in the list of instruments subject to the RRAO?

We do not believe that there are any more instruments that need to be included additionally in the RRAO list.

Q36. Do you have in mind any risk factor categories or subcategories to add to those listed in Table 2 of Article 325be of the CRR2 proposal?

We are of the opinion that Table 2 of Article 325be should be amended to include the additional risk factor categories and liquidity horizons listed in the FAQ published in January 2017 (paragraph 2.2).

Q37. Would you think that Q&As could be sufficient to provide additional guidance (instead of RTS)?

The assignment of risk factors to appropriate risk driver categories/subcategories is sufficiently clear. Uncertainties affecting some risk factors can be clarified by Q&As. An explicit RTS is therefore not required.

Q39. If you agree with the threshold outlined, would you agree that the list of selected currencies should be updated on a triennial basis following the publication of the BIS OTC derivative statistics?

The proposed triennial update of the list makes sense and is in line with the initial definition of the list. Additionally, an update of the list should be possible if there is a significant market event (e.g. introduction of the euro).

Q40. If you do not agree with the threshold outlined, please provide reasoning for establishing another selection criterion.

It is worth noting that in relation to FRTB NMRF, many data providers such as MarkIT or Bloomberg are currently launching initiatives so that a liquidity by-product overview can be studied. Ideally, the regulators could leverage such information to allow the better calibration of the FRTB liquidity horizons.

Q41. What is your view on the definition and level of the threshold used for currency pairs to be considered most liquid?

The proposed definition of “most liquid currencies” is understandable, but the list should be extended by the application of the suggested triangulation logic in paragraph 161, which we find very useful.

We find it difficult to understand the definition of the level of the threshold. How was the threshold of USD 45 billion arrived at? From our perspective, it should be possible to define a “most liquid currency pair” using a lower threshold.

Q42. If you agree with the threshold outlined, would you agree that the list of selected currencies should be updated on a triennial basis following the publication of the BIS OTC derivative statistics?

The proposed triennial update of the list makes sense and is in line with the initial definition of the list. Additionally, an update of the list should be performed if there is a significant market event (e.g. introduction of the euro); the list should be extended by application of the approach suggested in paragraph 161.

Q43. If you do not agree with the threshold outlined, please provide reasoning for establishing other selection criteria.

In addition to the quantitative limit, the application of the approach suggested in paragraph 161 makes sense and should be applied, as already stated above. However, we would welcome a lower threshold in order to integrate currency pairs such as EUR/CHF and EUR/NOK, among others, into the list.

Q44. Do you consider that triangulation of currency pairs should be allowed? Is triangulation used in practice to hedge less liquid FX positions?

Triangulation of currency pairs should be included in the definition of most liquid currency pairs. It is an appropriate and common way to hedge FX risks.

Q45. What is your view on the definition and level of the threshold for defining small and large capitalisations for equity price and volatility?

The proposal to combine absolute and relative criteria (differentiation by equity markets; member in an equity index etc.) in the categorisation of companies makes sense. However, we believe that the proposed solution of using only the list of equity indices published by ESMA is not sufficient. It should be extended at least to large companies that are not part of an index and to companies of a reasonable size that are part of a liquid index that is not on the ESMA list (e.g. SDAX companies).

Other implementation issues

Q73. Do you agree that a recalibrated version of the current standardised approach – for banks below the EUR 300 million threshold (as currently proposed in the CRR2 proposal) – is preferable in the EU to the implementation of the BCBS reduced SBM? Do you agree that the recalibration should be carried out simply at the risk class level by applying a scalar, such that the recalibrated approach is generally more conservative – but not systematically more conservative – than the FRTB SA?

In this respect, retaining the existing Basel II standardised approach as a simplified alternative approach appears to be a more appropriate solution for achieving the stated goal of less complex calculation. The advantage of such an approach is that the institutions in question would not have to make any far-reaching adjustments to procedures and processes.

We agree that a simple risk-sensitive recalibration could be based on different weightings of risk factors or groups of risk factors, as also contained in the pro-posed sensitivities-based methods.