Large Regional and Global Banks...

Have all the dominoes fallen? What can institutions do now to avoid being the next domino in line?

Five financial institutions have shuttered in just five months – four in quick succession in March alone – something that has not happened in almost a century. Several remain under pressure and market scrutiny. And while the industry and media have a lot of opinions about recent events, financial institutions must be pragmatic and quickly solidify their understanding of the root causes and prepare both short- and long-term action plans to address them.

Every day, more than 200 clients use Adenza's treasury and trading solutions; an additional 150+ use its regulatory solutions for liquidity and capital. In this article we summarize the recent events and share key takeaways for our client community.

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The Run-Up To The Fall

Over the past few weeks, a lot of ink has been spilled as to why SVB failed. Following is a distillation of the of events leading up to it:

- Concentrated risk in a homogeneous set of depositors and borrowers who propelled the bank's growth in deposits and long-dated fixed-income securities.
- Accumulation of unhedged interest-rate and liquidity-flight risks in the balance sheet, coupled with a loose US-regulatory framework that lacked any incentives for banks to adjust their risk level – accumulated other comprehensive income (AOCI) capital deductions.
- A downgraded-economic context that caused depositors to withdraw cash to sustain their activities and the Federal Reserve to raise interest rates multiple times in 18 months. This resulted in a first loss on bond portfolios that would, in isolation, have been manageable from a capital standpoint.
- Rumors of imminent bankruptcy once the financial situation was communicated. This caused the stock to be attacked, initiating massive withdrawals, and ultimately resulting in the bank selling its long-term, low-yield bonds that should've been held to maturity.
- A failed bailout. The lender of last resort refused the proposed solutions to cover the subsequent loss that exceeded bank's capital.

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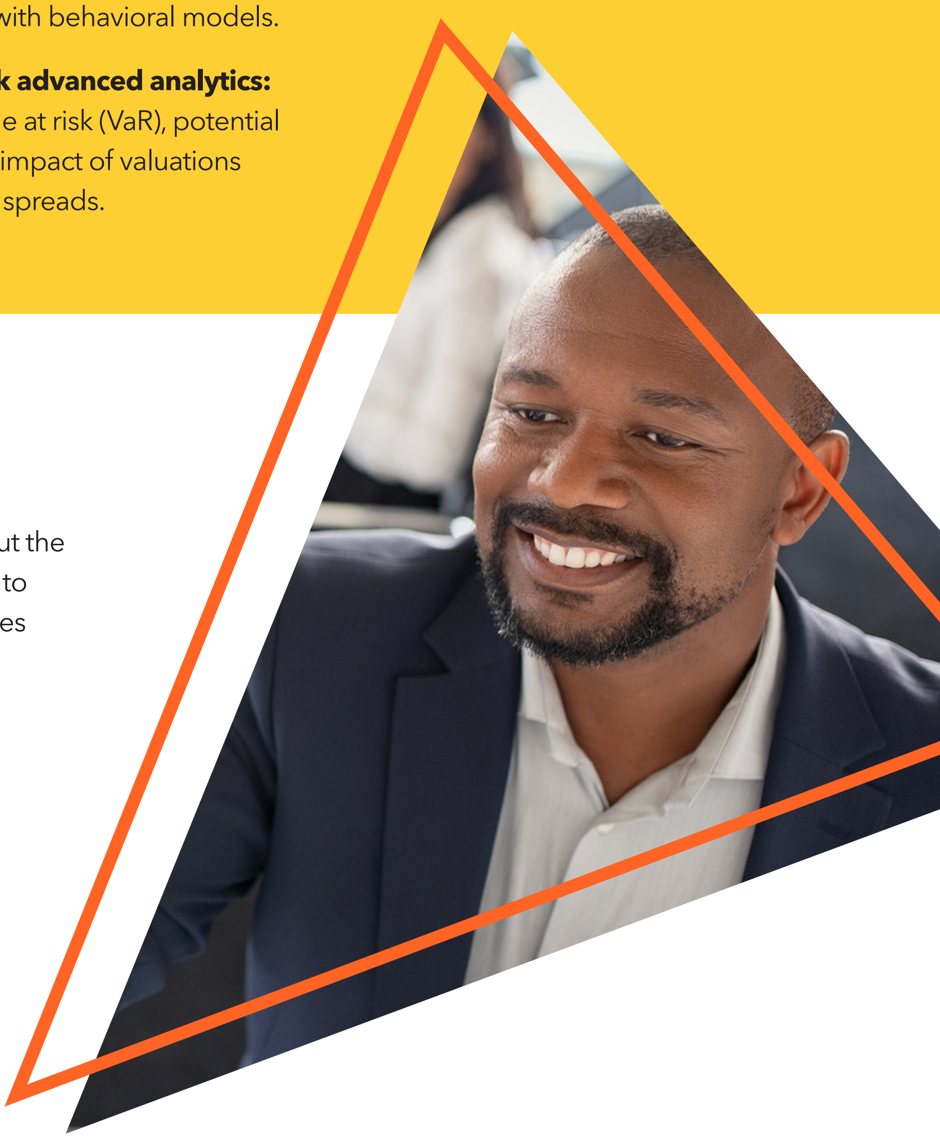
A Moment Of Clarity – 7 Key Takeaways

Hindsight is always 20-20. As financial institutions absorb the implications of these events, here are seven highly relevant areas of focus from the Adenza lens:

1. **Regulatory remediation:** Matters Requiring Attention (MRA/MRIA) were left outstanding for extended periods of time. A heightened focus to proactively remediate this, in steady and measurable phases, is critical.
2. **Interest Rate Risk in the Banking Book (IRRBB):** The economic value of equity (EVE) calculation is a simple but powerful measure to capture duration risk in the banking book.
3. **Liquidity stress testing:** Modeling idiosyncratic scenarios on the same, complete, and reconciled data used for FR 2052a reporting.
4. **Deposit analytics**: Better understanding of customer mobility with a heightened focus on accounts by ownership right and capacity (ORC) exceeding the FDIC's insurance limits.
5. **Treasury consolidation of trading and banking books:** Ability to simulate interest-rate (IR) curve movements and recompute IR gaps and other IRRBB metrics with full drilldown.
6. **Balance-sheet stress testing:** Shocking IR and FX rates, credit default swap (CDS) spreads in combination with behavioral models.
7. **Market and counterparty credit risk advanced analytics:** Enterprise-wide stress scenarios, value at risk (VaR), potential future exposure (PFE), limits, and the impact of valuations adjustments (XVA) due to rising CDS spreads.

What's Next

As financial institutions think about ways to put the takeaways into action, one of those might be to find a solution that provides a range of features that help them understand, simulate, and actively manage risks, including a holistic view of banking and trading books, collateral, risk, etc., risk-metrics updates throughout the day, simulation tools, and a top-down approach to treasury analytics.



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Contact Adenza to start a conversation about how we can help you with your capital markets and regulatory needs.

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