FÉDÉRATION BANCAIRE FRANÇAISE

2018.06.22

FRENCH BANKING FEDERATION RESPONSE TO THE DRAFT RTS ON THE SPECIFICATION OF THE NATURE, SEVERITY AND DURATION OF AN ECONOMIC DOWNTURN IN ACCORDANCE WITH ART. 181(3)(A) AND 182(4)(A) OF CRR

The French Banking Federation (FBF) represents the interests of the banking industry in France. Its membership is composed of all credit institutions authorised as banks and doing business in France, i.e. more than 390 commercial, cooperative and mutual banks. FBF member banks have more than 38,000 permanent branches in France. They employ 370,000 people in France and around the world, and service 48 million customers.

The French Banking Federation welcomes the opportunity to share its comments with the EBA on its draft RTS on the specification of an economic downturn.

Q1: Do you have any concerns around the workability of the new approach (e.g. data availability issues, burden on the analysis, split between the definition of the economic downturn and its impact on the internal loss data)?

The implementation of this RTS (along with the GL) would be unduly burdensome and complex to maintain such a framework in the model lifecycle process and would create a labyrinthine system as the analysis of period downturn must be done for each economic factor, each downturn period, each type of exposure / asset class etc… We think that some flexibility should be left to banks in order to accommodate the granularity and diversity that banks may have in their classification.
As for the 20 years period for economic factors, they may not be available for all types of data, especially related to commercial real estate asset classes
Also, the most concerning point is how we would correlate the economic factor series with the internal loss data:

- As articles 145 and 176 CRR require a 3 or 6 years of historical data approach, it could be considered that the RTS is illegal or at least un fair
- The internal realized LGD will not be available for twenty years of historical data.
- The link between LGDs and economic downturn is partially covered by the counter-cycle buffer required by the macro-prudential authorities
- The link between LGDs and economic factors may not be simple or evidenced using statistical models

Institutions may face strong multiplicity / iteration in order to respect regulatory requirements and would welcome strong incentives to maintain a risk-sensitive framework and avoid unnecessary burden. Especially, we foresee the settlement of a more harmonized "downturn estimation", which is as of today complex to implement, interconnected with:

- Determination of ECL using IFRS 9 models and its possible review with a new "downturn" approach
- The consistent implementation of IRB Repair program within ambitious timeline and the related supervisory process (2-step approach when applicable, application for model changes…)
- Overlaps with macro-prudential policies which require counter-cycle buffers to tackle the economic downturn
- Rationale for prior experience and data storage requirements which is based on a 3-years approach
- The challenge to keep a consistent framework with the use of internal models, in the context of the finalization of Basel III agreements and especially its European transposition
- The possible application of prudential backstop in NPL and its indirect impact on ELBE / LGD-in-default

We think that flexibility and efficiency are primordial in such context, in order to keep within institutions, existing methodologies which already work especially when they do not show any form of arbitrage and do not understate the final level of LGDs.

Q2: Do you see any issues of applicability of this RTS for estimating conversion factors appropriate for an economic downturn identified in accordance with this RTS?

Most of comments made on the LGD's side work for the CCF's side. As for CCFs, the link between CCFs and economic factors will be even harder to evidence using statistical models.
Additionally, we suggest that the GL should mention explicitly that they do not apply to conversion factors in order to insure an harmonized understanding of the supervisors, as it is mentioned in the GL on PD-LGD estimation and treatment of defaulted assets.