

In 2011-2012 the IACPM, in collaboration with KPMG, undertook a comprehensive benchmarking survey on funding liquidity management and credit portfolio management. The goal of the survey was to assess the growing linkages between Credit Portfolio Management and Asset and Liability Management related to funding costs and portfolio analytics and stress testing, and to benchmark how firms are changing organizational structures and mandates to integrate credit portfolio and liquidity risk management. Thirty-four IACPM member firms, located globally, participated in the study.

A summary of the key themes includes:

- Credit Portfolio Management (CPM) roles and responsibilities are expanding to include significantly greater linkages with liquidity, Treasury and ALM for their organizations as a result of credit market and funding conditions and the Basel III regulations regarding liquidity.
- In many institutions, CPM plays a central - and growing - role in integrating credit and liquidity cost factors into origination strategies with the line of business via transfer pricing methodologies.
- CPM is playing an expanded role in modeling specific aspects of liquidity at many banks, providing ALM with analytical information about the portfolio and funding projections by portfolio, product and, to a lesser extent, obligor.
- Systems, modeling and associated reporting are ongoing challenges as firms work to implement integrated credit, market and liquidity risk management and planning across organizations amid tight budgets.
- Organizational changes continue to be made to align CPM, risk and liquidity functions across the firm and facilitate integrated risk management. Most CPM units see continued expansion of their roles in the future and envisage closer linkages, formal and/or informal, with Treasury.

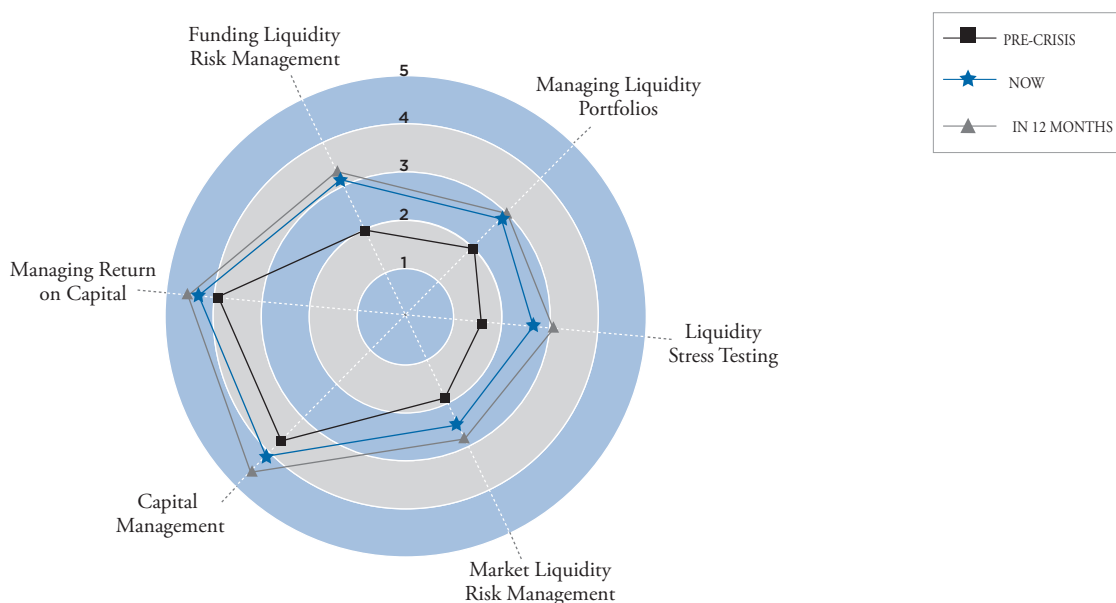
Stepping up to the liquidity challenge: the changing role of CPM...

As the regulatory change agenda becomes even more all encompassing, the challenge of how to optimise and manage both capital and liquidity is key for Boards and Senior Management. Optimisation of liquidity is now vital - and creates a significant opportunity to utilise the analysis, business and operational skills from across of the business to manage the cash, risks and change required. Credit Portfolio Managers (CPM) have already established a pivotal role in financial institutions, using their skills in key areas such as origination and distribution, profitability enhancement, capital optimisation, and balance sheet management.

Historically, CPM focused on the measurement, modelling, pricing and active management of credit risk. Triggered by the financial crisis in 2008 and the changes in the regulatory, industry and business landscape that followed, financial institutions face ongoing higher funding costs and liquidity risk. CPM teams' responsibilities have therefore been redefined, and widened to include increased involvement in addressing regulatory requirements - as well as funding liquidity risk management in their organisations, with further expansions envisaged in the next year. CPM units are still going through the process of embedding these changes, with many expecting further changes to their roles and responsibilities within the next six months. Organisational structures are changing, breaking down the traditional divisions in functional responsibilities (eg. between Treasury and Credit) and in the way that different risk types are addressed.

The International Association of Credit Portfolio Managers (IACPM) engaged with KPMG in the UK to conduct a survey of its members' developing practices in funding liquidity risk management. 34 IACPM member firms, representing almost half of the eligible IACPM membership, participated in the survey. The survey aimed to understand and benchmark how IACPM member firms adapted to the new environment and ever-evolving financial landscape, and specifically the role of CPM units in this process.

CPM Activities In Order of Importance – Pre - and Post- Crisis (Ranked 1 to 5)



The importance of liquidity risk management for businesses in the post-crisis marketplace and the critical input of the CPM in delivering this effectively becomes apparent from the current and future objectives cited by those surveyed.

Regulatory Challenges...

The global financial crisis has led to wide ranging and ongoing regulatory changes, which are influencing CPM's established roles in institutions.

Regulatory change – particularly the Basel Committee's focus on the Liquidity Coverage Ratio (LCR) and Net Stable Funding Ratio (NSFR) - has forced the industry to focus on liquidity. The changes in managing funding liquidity risk result in evolving roles for CPM and open up new opportunities for CPM teams to add value to their firms. The liquidity requirements set by the Basel Committee are likely to prove an even bigger challenge than those on capital. For many banks, these requirements are 'the iceberg below the water'. Pre-crisis, liquidity was a clear second to capital - until recently, the primary focus had been on the challenges posed by the substantial capital requirements. Now, the additional liquidity standards will necessitate operational, financial and structural change and a significant move away from short-term wholesale funding towards a longer-term funding strategy. Effective liquidity management is now a big boardroom issue.

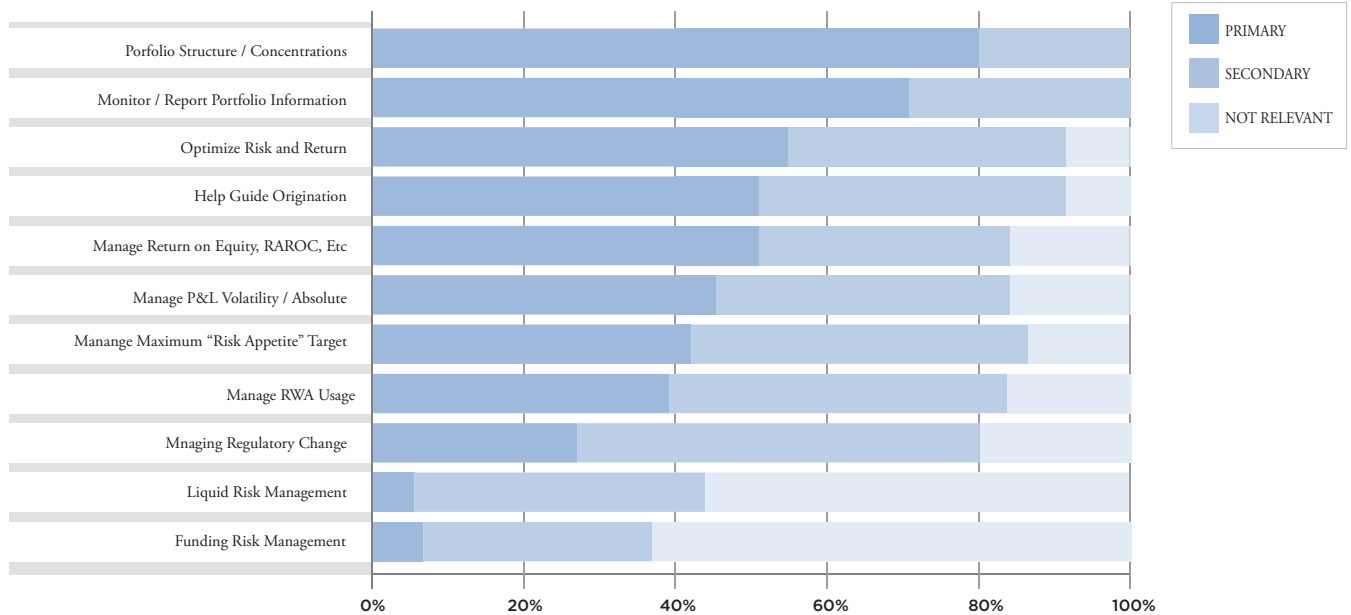
The scarcity and cost of funding, combined with the need to hold High Quality Liquid Assets, is affecting decisions around asset origination and the management of credit portfolios. The impending implementation of the Basel 3 regulation is changing the way institutions manage funding liquidity risk. As a result, liquidity considerations are demanding significant time and attention from financial institutions - and from more and more credit portfolio managers. New regulations in funding liquidity risk have been a significant driver for change in the business - and preparing for the implementation of new rules and for further change is a key focus for banks and an essential part of their plans for the future. In this new operating environment, CPM units have gained a strong involvement in the internal assessment of regulatory change and in determining the options to manage the new requirements.

CPM units are addressing the practical aspects of managing changes required by regulators, providing insight into the impact of these changes and acting as internal sources of expertise.

The new regulatory rules continue to drive additional liquidity, capital, stress testing and reporting requirements, to which CPM provides an increased amount of insight, experience and operational input related to implementing change and addressing operational aspects of managing risk. In improving the integration of the management of risk types, CPM is engaging with the challenges of systems and modelling enhancements, associated analytical reporting and a closer interaction with key stakeholders - notably Treasury - and these remain the key areas of focus.

CPM is playing an increasingly central and growing role in integrating credit and liquidity cost factors into origination strategies via transfer pricing methodologies, serving as a central conduit for providing integrated market, cost and liquidity information to the line of business. As regulatory requirements related to liquidity are being implemented, the role of CPM in providing credit and liquidity costs and related portfolio acquisition/distribution strategies is growing. In most firms, Treasury/ALM determines funds transfer pricing and funding strategies for the institution and provides them to CPM and the line of business. CPM units now serve as focal point for coordination between Treasury and the line of business to integrate relevant costs for credit/loan origination, assist in framing forward-looking risk management strategies for credit origination, and executing risk distribution where appropriate.

Key objectives for CPM

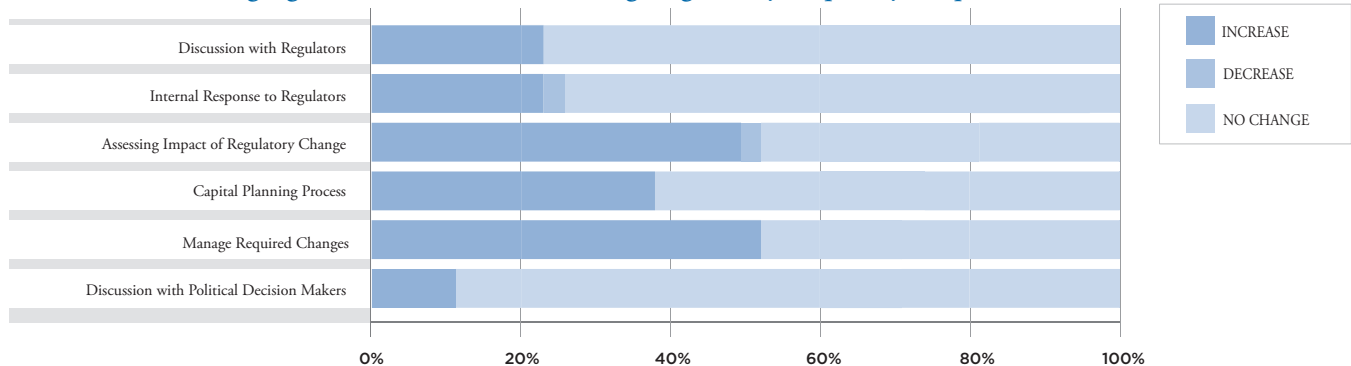


Significant Challenges...

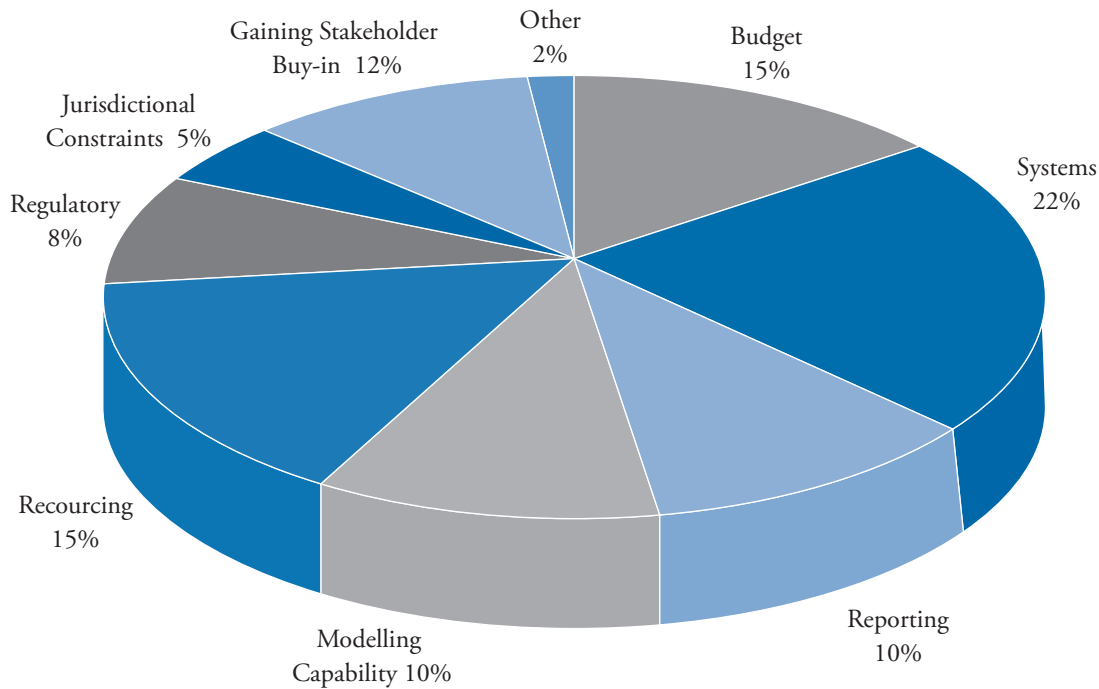
These significant changes come with multiple challenges. Some of the key challenges include a lack of the right system requirements and the anticipated budget and resource constraints.

The changing regulatory environment and the move towards implementation of established rules continue to challenge the industry. Regulation is a significant cause of these changing systems and reporting requirements, forming one of the biggest challenges faced by CPM teams. Regulatory change is also driving other business challenges, such as the cost impact on business planning and deal assessment - especially in pricing. The differing regulatory approaches and stages of implementation (e.g. local regulators versus Basel 3) are an area where CPM teams are having an effect on business planning and operational change – meaning that the CPM is now working even more closely with the business, especially Treasury, as a key function.

CPM Units' Changing Involvement in Addressing Regulatory Liquidity Requirements



The Biggest Challenges

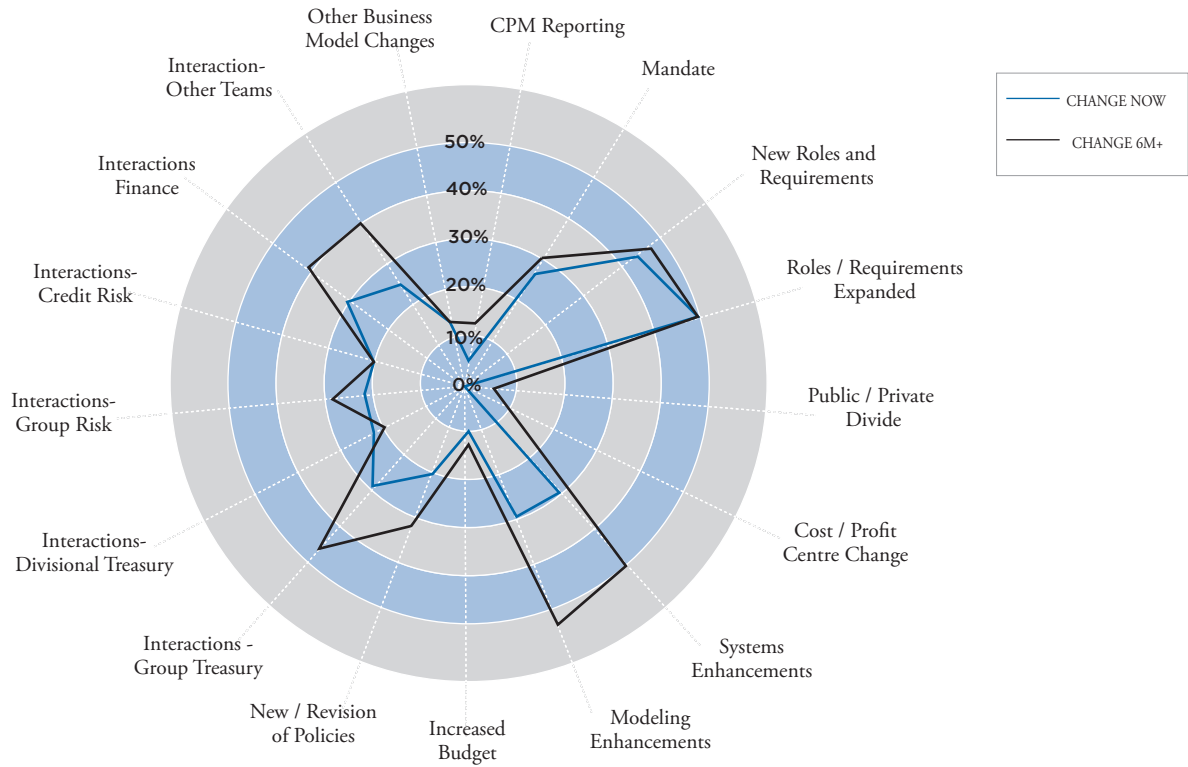


Managing Liquidity Risk...

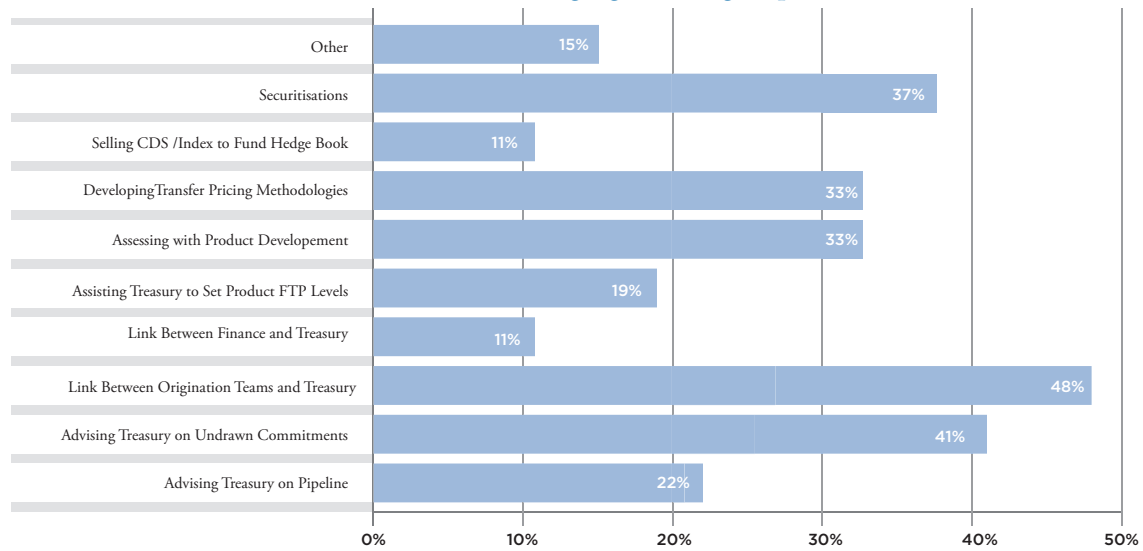
The survey identified that CPM now has a strong coordination role between other business units and with Treasury itself. A few firms are already fully integrated and around 20 percent are merging some functionality. This is part of an ongoing process of embedding these new roles and the new mandate for CPM units within the firm. CPM and Treasury units are working together to implement and enhance systems that incorporate liquidity costs in new deal pricing and profitability assessment. There is also evidence that firms are enhancing their transfer pricing approaches.

CPM units have expanded their functional responsibilities beyond traditional areas of credit portfolio management and risk/return into the area of funding liquidity risk management, increasingly working alongside treasury colleagues and providing expertise, insight and a link to the operational side of their businesses. They are leveraging their usual coordination role by liaising among the various business units, leading to better risk management for the firm. Almost three quarters of CPM respondents report having an increasing role in liquidity risk management, mostly in an operational and internal advisory capacity.

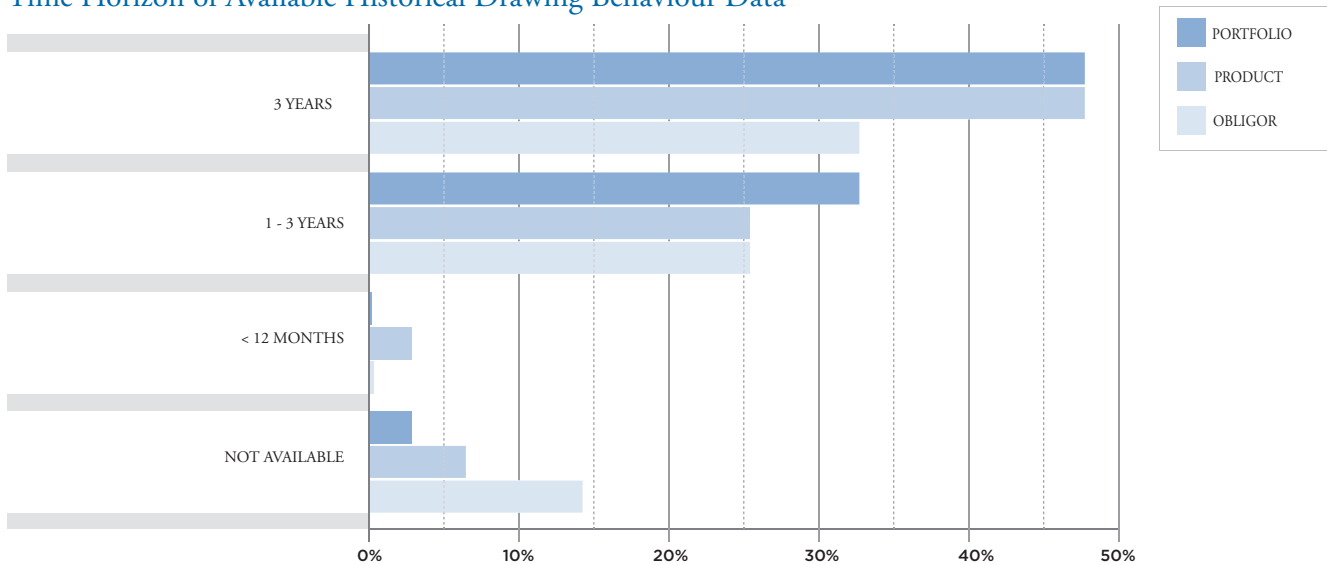
Evolving CPM Activities in Response to Enhanced Liquidity Risk Management Requirements



Current Areas of CPM Involvement in Managing Funding Liquidity Risk



Time Horizon of Available Historical Drawing Behaviour Data



Modelling Liquidity Risk...

Improving and developing the different aspects of modelling liquidity risk is an area of focus for most senior management - and an area where firms want to become more sophisticated. CPM teams are now involved in modelling liquidity risk due to their role as providers of analytical outlook and portfolio information and their ability to draw on historical information on a portfolio, product and, to a lesser extent, specific obligor level. Treasury and ALM have traditionally determined the scenarios for liquidity stress testing.

CPM is actively working to develop modelling and systems in liquidity risk management. There is a wide range of approaches and degrees of sophistication. For example, the reference curves for fund transfer pricing are diverse across institutions. Infrastructure and systems are seen as one of the major hurdles in developing to meet the new requirements of liquidity risk management.

A Continuing Journey..

New regulations in funding liquidity risk have been a significant driver for change in the business - and preparing for the implementation of the regulations and for further change is a major part of the plans for the future. CPM units have gained a strong involvement in the internal assessment of regulatory change and in determining the options to manage the new requirements, playing an important part in helping businesses address the many challenges in the current marketplace and helping their organisation to manage funding liquidity risk effectively.

CPM now plays a central role in integrating credit and liquidity cost factors into origination and distribution strategies via transfer pricing methodologies, serving as a focal point between Treasury and the line of business. These new roles and organisational models are still - as well as tactical issues relating to systems, data and models being addressed. Challenges remain - including budget constraints – as banks work to integrate the different risk types and systems.

Successful firms will continue to leverage the position of CPM to address the wider cost and profitability considerations associated with liquidity - in addition to managing credit portfolio risks. The overall benefits will see improved risk management across the firm and the optimisation of risk/return within institutions that are fully exploiting their CPM advantage.

This new journey has only just begun, and there is still more change to come...

CONTACTS

IACPM

Som-lok Leung

Tel +1-646-289-5434
E-mail somlok@iacpm.org

Marcia Banks

Tel +1-646-289-5432
E-mail marcia@iacpm.org

Juliane Saary-Littman

Tel +1-646-289-5433
E-mail juliane@iacpm.org

KPMG

Rob Kiernan

Tel +44 (0) 207-311-5441
E-mail rob.kiernan@kpmg.co.uk

Guido Previde Massara

Tel +44 (0) 207-694-2493
E-mail guido.massara@kpmg.co.uk

Robert Smith

Tel +44 (0) 207-694-5629
E-mail robert.smith@kpmg.co.uk