Global Regulatory Reform

Shaping tomorrow's business today
Basel III: strategic forecasting
The pressures and complexity generated by the economic and regulatory environment have created the need for improved methods of carrying out stress testing and strategic planning.

Management needs to be able to answer strategic questions quickly and comply with stress-test requests faster and more flexibly. Some of the questions that need answers are set out below:

- How profitable will the bank be under different economic scenarios?
- If the strategic or economic scenario changes, what is the effect on future capital requirements and liquidity?
- How would global restructuring of the business effect required capital and liquidity?
- How would the sale of different portfolios effect bank performance going forward?
- Is the current strategy aligned with risk appetite?

Current bank tools cover capital, P&L and liquidity separately and are not connected to stress testing. In addition, stress-testing approaches are too slow and cumbersome to meet regulatory and internal strategic requirements.
Strategic forecasting concept

Ernst & Young has developed a tool that is more advanced than the current risk, finance and treasury models providing senior management with the means to see, in real time, the full implications of different strategic choices under different economic scenarios. The tool also enhances capacity to respond to requests for new stress tests from regulatory bodies and senior management.

Management decides the strategy given the economic scenario, and the model calculates the capital requirements, liquidity profile, liquid-assets buffer and profitability of the business over three to five years. The tool allows management to change the strategy or the macro scenario, and it will then forecast the effect on business performance and regulatory requirements quarterly over the time horizon.

This provides the following advantages for senior management:
- Enhanced business planning
- Capability for what-if analysis and sensitivity analysis
- Better capability to make optimal strategic decisions
- Improved governance structures linking strategy to stress testing
- Faster response times to stress-test requests

### Strategic forecasting tool

- Enhanced business planning
- Capability for what-if analysis and sensitivity analysis
- Better capability to make optimal strategic decisions
- Improved governance structures linking strategy to stress testing
- Faster response times to stress-test requests

---

**Strategic forecasting concept**

**Outputs**

- Financials over three to five years under different scenarios
- Risk measures
- Profitability measures
- Shareholder value

**Management Information (MI) pack**

- Capital MI
- Liquidity MI
- Profitability MI

**Charts**

- Capital ratios
- Liquidity ratios

---

**Inputs**

- Stress scenarios
- Bank strategy

**Stress outcomes calculated**

- Profitability measures
- Shareholder value
- Risk measures
- Capital MI
- Liquidity MI
Implementation and tool design
The bank can implement the tool with whatever degree of granularity it needs. The granularity needs to be sufficient to reflect core components of each portfolio, which effect likely outcomes in different economic environments and drive the capital requirements and liquid-assets buffer.

The tool is constructed in a modular fashion to achieve the following:
- Each entity or business unit can be considered separately or together as part of the group view.
- It can be customized to reflect the characteristics of particular portfolios.
- Drivers are embedded in the tool to calculate the full effects of any strategy or economic environment, which enables real-time assessment of the effects of a change in the scenario.
- It can be linked into existing systems through an intermediate data store and data demands are not heavy.

Ernst & Young has experience working with a number of banks and is currently implementing the approach in a major international bank to increase the speed and flexibility of stress testing and to facilitate the embedding of risk appetite. We have also used it in cases of bank mergers to demonstrate the viability of the new business model under different economic outputs.
How Ernst & Young can help

We have an EMEIA-wide team of more than 800 risk professionals and a multidisciplinary approach that enables us to mobilize the right team for our clients. Our teams include risk professionals and tax and transaction support, as well as performance improvement for business restructuring. For other projects, we combine strategic forecasting knowledge with governance and risk-appetite experts, bringing greater benefit to our clients.

Working with us gives you access to:
- Large teams on short notice
- Significant insight into varied markets and geographies
- A deep understanding of regulating risk management, risk governance, stress testing and modeling

Contacts
For more information on how we can help, please contact one of our team.

<table>
<thead>
<tr>
<th>Name</th>
<th>Country</th>
<th>Phone Number</th>
<th>Email</th>
</tr>
</thead>
<tbody>
<tr>
<td>Patricia Jackson</td>
<td>UK</td>
<td>+44 20 7951 7564</td>
<td><a href="mailto:pjackson@uk.ey.com">pjackson@uk.ey.com</a></td>
</tr>
<tr>
<td>Max Weber</td>
<td>Germany</td>
<td>+49 711 9881 15494</td>
<td><a href="mailto:max.weber@de.ey.com">max.weber@de.ey.com</a></td>
</tr>
<tr>
<td>Laurent Denayer</td>
<td>Luxembourg</td>
<td>+352 42 124 8340</td>
<td><a href="mailto:laurent.denayer@lu.ey.com">laurent.denayer@lu.ey.com</a></td>
</tr>
<tr>
<td>Victor Martin</td>
<td>Spain</td>
<td>+34 915 727906</td>
<td><a href="mailto:victormanuel.martingimenez@es.ey.com">victormanuel.martingimenez@es.ey.com</a></td>
</tr>
<tr>
<td>Marie-Laure Delarue</td>
<td>France</td>
<td>+33 1 4693 7321</td>
<td><a href="mailto:marie-laure.delarue@fr.ey.com">marie-laure.delarue@fr.ey.com</a></td>
</tr>
<tr>
<td>Frank de Jonghe</td>
<td>Belgium</td>
<td>+32 2 774 9956</td>
<td><a href="mailto:frank.de.jonghe@be.ey.com">frank.de.jonghe@be.ey.com</a></td>
</tr>
<tr>
<td>Marc Ryser</td>
<td>Switzerland</td>
<td>+41 58 286 4903</td>
<td><a href="mailto:marc.ryser@ch.ey.com">marc.ryser@ch.ey.com</a></td>
</tr>
<tr>
<td>Nico Warmer</td>
<td>Netherlands</td>
<td>+31 88 4071400</td>
<td><a href="mailto:nico.warmer@nl.ey.com">nico.warmer@nl.ey.com</a></td>
</tr>
<tr>
<td>Luis Oliveira Rodrigues</td>
<td>Portugal</td>
<td>+351 21 791 2032</td>
<td><a href="mailto:luis.oliveirarodrigues@pt.ey.com">luis.oliveirarodrigues@pt.ey.com</a></td>
</tr>
<tr>
<td>Giuseppe Quaglia</td>
<td>Italy</td>
<td>+39 0272212429</td>
<td><a href="mailto:giuseppe.quaglia@it.ey.com">giuseppe.quaglia@it.ey.com</a></td>
</tr>
<tr>
<td>Cormac Murphy</td>
<td>Ireland</td>
<td>+353 1221 2750</td>
<td><a href="mailto:cormac.murphy@ie.ey.com">cormac.murphy@ie.ey.com</a></td>
</tr>
</tbody>
</table>
About Ernst & Young

Ernst & Young is a global leader in assurance, tax, transaction and advisory services. Worldwide, our 152,000 people are united by our shared values and an unwavering commitment to quality. We make a difference by helping our people, our clients and our wider communities achieve their potential.

Ernst & Young refers to the global organization of member firms of Ernst & Young Global Limited, each of which is a separate legal entity. Ernst & Young Global Limited, a UK company limited by guarantee, does not provide services to clients. For more information about our organization, please visit www.ey.com.

About Ernst & Young’s Banking & Capital Markets Center

In today’s globally competitive and highly regulated environment, managing risk effectively while satisfying an array of divergent stakeholders is a key goal of banks and securities firms. Ernst & Young’s Global Banking & Capital Markets Center brings together a worldwide team of professionals to help you achieve your potential — a team with deep technical experience in providing assurance, tax, transaction and advisory services. The Center works to anticipate market trends, identify the implications and develop points of view on relevant industry issues. Ultimately it enables us to help you meet your goals and compete more effectively. It’s how Ernst & Young makes a difference.

© 2012 EYGM Limited.
All Rights Reserved.

EYG No. EK0091

In line with Ernst & Young’s commitment to minimize its impact on the environment, this document has been printed on paper with a high recycled content.

This publication contains information in summary form and is therefore intended for general guidance only. It is not intended to be a substitute for detailed research or the exercise of professional judgment. Neither EYGM Limited nor any other member of the global Ernst & Young organization can accept any responsibility for loss occasioned to any person acting or refraining from action as a result of any material in this publication. On any specific matter, reference should be made to the appropriate advisor.