Take 5 for business

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Navigating interest rate risk: Why IRRBB matters now

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IRRBB is no longer optional – it's strategic

In today's volatile rate environment, banks must prioritize managing Interest Rate Risk in the Banking Book (IRRBB). This effectively manages the financial exposure created when assets and liabilities reprice at different speeds, compounded by unpredictable customer behavior.

Now, with Bank Negara Malaysia (BNM) aligning to new Basel IRRBB standards, regulatory expectations for IRRBB management are increasing, particularly around challenging areas like modeling non-maturity deposits.

Forward-looking banks are treating this as more than just a compliance exercise. Implementing stronger risk frameworks with improved modeling and stress testing capabilities can help institutions can transform IRRBB into a competitive advantage. Taking action now will safeguard the bank's profitability and facilitate stability amidst market uncertainty.

Key milestones in IRRBB implementation across Asia-Pacific

2010
BNM introduces IRRBB expectations under Risk Weighted Capital Adequacy Framework (RWCAF)

2016
Basel Committee issues the updated Basel IRRBB standards (April 2016)

2018
Singapore and Hong Kong begin aligning with Basel IRRBB standards

2019
Australia and Japan adopt Basel-aligned IRRBB frameworks

2020
Malaysia issues IRRBB policy document with effective from 1 Jan 2020

2025
Expected release of updated IRRBB exposure draft by BNM, aligning with Basel IRRBB standards

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As interest rates become more unpredictable, managing IRRBB is no longer a back-office exercise – it is a board-level imperative. The ability to anticipate earnings and capital impact under multiple rate paths will define the resilience of banks in the years ahead.

Thor Boon Lee
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How leading banks utilize IRRBB to transform

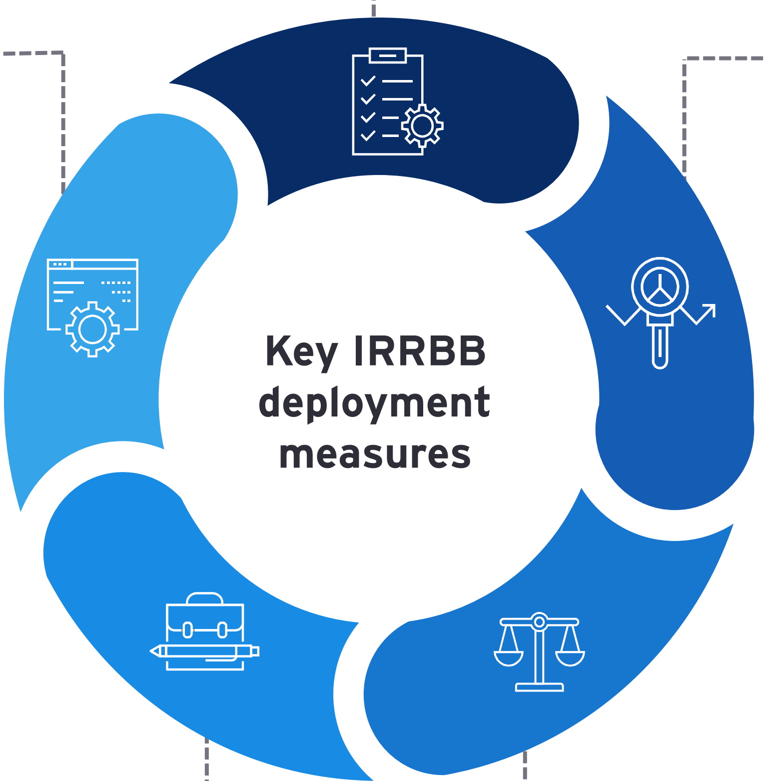
It is important for the banks to consider IRRBB as not just a reporting metric but a strategic measure to manage the balance sheet and profitability. To stay ahead of the curve, leading banks are implementing the following actions:

Elevate IRRBB to board-priority level

- Position IRRBB as a key item on board and asset-liability committee (ALCO) agendas.
- Promote awareness of how IRRBB impacts earnings, capital and shareholder value.
- Establish regular updates and scenario discussions for executive and board levels.

Champion technology and automation

- Approve investments in robust asset liability management (ALM) and IRRBB systems.
- Shift away from spreadsheet-based models to scalable, automated solutions.
- Leverage dashboards and analytics to gain real-time insights into interest rate exposures.



Encourage transparent and defensible modeling

- Documented assumptions for deposit behavior and loan prepayments.
- Use of back testing and sensitivity analysis to validate models.
- Review protocols that anticipate regulatory questions and internal audit scrutiny.

Integrate into business planning

- Embed IRRBB insights into strategic planning, pricing and balance sheet decisions.
- Ensure Net Interest Income (NII) and Economic Value of Equity (EVE) simulations influence Internal Capital Adequacy Assessment Process (ICAAP), fund transfer pricing (FTP) and budgeting processes.
- Support enterprise-wide alignment between risk, treasury and finance teams.

Strengthen governance and ownership

- Define clear accountabilities across risk, treasury and finance teams for IRRBB processes.
- Set risk appetite limits, escalation protocols and performance indicators.
- Conduct periodic board-level reviews of IRRBB frameworks and outcomes.

Implementation road map for IRRBB readiness

With the upcoming release of BNM's 2025 IRRBB exposure draft, banks are encouraged to examine their IRRBB readiness now. Based on the scope of work, system maturity and behavioral modeling needs, a full end-to-end implementation aligned with Basel IRRBB 2016 may require 12 to 18 months to complete.

1. Planning and gap assessment

- Conduct a structured gap analysis against Basel IRRBB 2016 requirements and assess existing NII/EVE models, stress testing, data availability and governance.
- Define the implementation roadmap, project structure and key stakeholders.

2. Behavioral modeling and development

- Analyze historical data to calibrate deposit stability and prepayment assumptions.
- Build behavioral segmentation and term structures.
- Perform sensitivity testing and back testing and document methodologies.

3. Model development and calibration

- Develop IRRBB engines for NII and EVE simulations using regulatory and internal rate shocks.
- Calibrate internal risk limits, align assumptions with ICAAP and FTP as well as define early warning indicators.

4. Technology enablement and calibration

- Implement IRRBB/ALM systems, integrates data from treasury and core platforms, configure automated simulations, limit monitoring and reporting dashboards.
- Migrate from spreadsheets where applicable.

5. Stress testing and ICAAP linkage

- Design standardized and internal stress scenarios, embeds IRRBB outputs into ICAAP and internal liquidity adequacy assessment process (ILAAP) and aligns with risk appetite frameworks.
- Define escalation protocols and board-level communication templates.

6. Independent validation and governance

- Perform independent validation including replication, sensitivity analysis and documentation review.
- Assess governance structure and model robustness, with final recommendations for compliance and risk assurance.

7. Final review, reporting, go live

- Conduct full-cycle runs and back testing, finalize disclosures and dashboard reporting for ALCO and the board.
- Secure internal audit sign-off to confirm readiness for regulatory review.

Key challenges of IRRBB implementation

IRRBB implementation can transform banks' vulnerability into a managed risk but is also marked by challenges. Set out below are anticipated concerns that need to be addressed to avoid impeding full end-to-end deployment of IRRBB.

1

Limited behavioral data

- Banks may lack sufficient historical data on customer behaviors, such as early loan repayments, deposit withdrawal tendencies and rollover patterns.
- Without this data, behavioral models for non-maturity deposits (NMDs) and embedded options remain theoretical, reducing credibility with regulators.

2

Over-reliance on spreadsheets

- Spreadsheet-based simulations are labor-intensive, error-prone and difficult to scale.
- They limit the ability to perform multi-scenario analysis quickly and consistently, making it harder to react to emerging risks or regulatory requests.

3

Weak model governance

- Inadequate documentation of assumptions, calibration logic and validation processes leads to weak model defensibility.
- Unclear roles and responsibilities across risk, finance and treasury teams result in oversight gaps and accountability issues.

4

Fragmented integration with ICAAP and ALCO

- IRRBB results are often siloed from capital planning (ICAAP) and decision-making at ALCO.
- This disconnect reduces the usefulness of IRRBB insights in pricing, liquidity and capital strategies.

5

Inadequate scenario design and stress testing

- Failing to implement both prescribed (e.g., parallel shocks) and internally relevant scenarios (e.g., non-parallel shifts, behavioral shocks) limits foresight.
- Poor scenario coverage weakens risk understanding and limits strategic response planning.

6

Lack of technology enablement

- Without integrated ALM/IRRBB systems, banks struggle with data quality, simulation automation and reporting consistency.
- This reliance on manual processes slows down turnaround time and impairs decision-making under pressure.

Ready to future-proof your IRRBB approach?

EY provides an end-to-end IRRBB solution covering behavioral modeling, independent validation, system enablement and governance support. Our services help banks meet Basel and BNM expectations while embedding IRRBB insights into risk, capital and pricing decisions. Banks can consider the following actions:

1

End-to-end behavioral modeling advisory

Support the development, calibration and validation of behavioral models to enhance the realism and defensibility of IRRBB projections.

2

Independent model validation and review

Provide an objective, regulator-aligned review of IRRBB models, focusing on accuracy, governance and defensibility.

3

Technology enablement and IRRBB system design

Enable scalable, automated and analytics-driven IRRBB execution through system architecture and process integration.

4

Governance documentation and capability building

Strengthen IRRBB oversight, transparency and knowledge retention across teams and stakeholders.

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