

ALMA conference – panel on liquidity

The regulatory response – DP07/7

- **A fundamental change or back-to-basics?**

- The FSA begins by asking: how much liquidity should the banking system hold against potential market disruption and is the wider economy prepared to bear the cost?
- Drawing on the lessons learnt since August 2007, DP07/7 points to a two-pronged approach:

Qualitative: much greater emphasis on supervisory expectations of senior management (ie leveraging principles-based regulation)

Quantitative: perhaps combining the current ‘mismatch’ and ‘retail stock’ regimes

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•Qualitative expectations

- More emphasis ‘chronic’ (ie slow burn) events in addition to ‘shock’ (short-term) events. Chronic stresses should allow for:

Prolonged access to conventional sources of long-term funding

Reputational implications of off-balance sheet vehicles

Correlations in periods of disruption between short and longer-term funding markets

Tightening of currency swap markets

Greater differentiation in the behavioural characteristics of categories of ‘retail’ depositors

Other considerations:

Liquidity insurance

Contingency planning

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•Quantitative approach

- The mismatch framework is seen as addressing structural mismatches in assets and liabilities
- The stock approach while having important limitations is seen as ensuring a minimum stock is held of high-quality liquid assets eligible as collateral with the Bank of England.
- The two might be combined so that ***funding*** and ***liquidity*** risks are brought together more explicitly.
- Internal modelling is mentioned, and encouraged, but the FSA recognises that there are inherent difficulties in doing so

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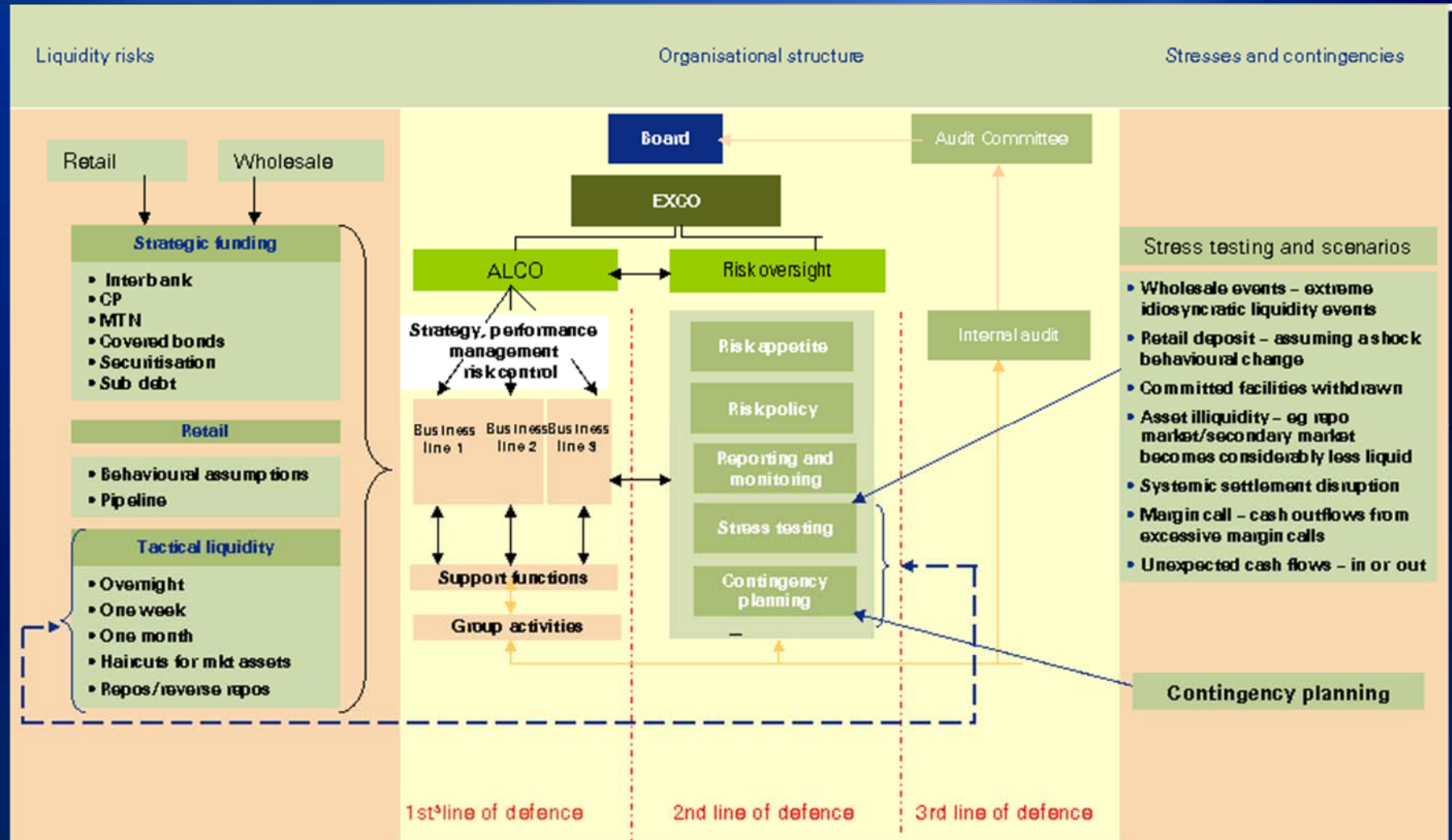
The regulatory response – DP07/7

•Views on DP07/7

- Is this a balanced and proportionate response?
- To what extent should individual firms allow for prolonged market disruption?
- How sensible are the qualitative expectations?
- Would combining the mismatch and stock regimes produce a sensible regulatory minimum standard?

LIQUIDITY RISK MANAGEMENT

– a KPMG view on what the future state might look like





Presenter's contact details

Keith Pooley

KPMG LLP (UK)

+44 (0)20 7 311 6088

Mobile 07824 609372

keith.pooley@kpmg.co.uk

www.kpmg.co.uk