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Are banks ready?

With new intraday liquidity safeguards in effect, a Deloitte Advisory survey finds banks face challenges in complying.

Large banks have had years to adapt to the US regulations and international standards that govern long-term liquidity reserve requirements, monitoring, and reporting. Now that similar standards apply to the hour-by-hour playing field of intraday liquidity, how are banks progressing toward compliance? And, how are they realizing the value of a strong foundation program for managing and mitigating their liquidity risk?

The new Intraday Liquidity standards incorporate guidelines from the Basel Committee on Banking Supervision (published as BCBS 248), Federal Reserve Board Letter SR 14-1, and Enhanced Prudential Standards (EPS). Deloitte surveyed representatives from 15 of the largest US bank holding companies (BHCs) and foreign banking organizations (FBOs) to learn more about the perspective and capabilities these institutions are bringing to the task of adapting to the new regulations.

This Deloitte survey of 15 BHCs and FBOs, all with assets exceeding $50 billion, showed widely varying degrees of readiness to address the existing and upcoming regulations around intraday liquidity monitoring, management, and reporting.

The survey also revealed a few significant patterns:

01. Information technology is a common challenge.
Low quality of data, and challenges in data technology capabilities, were consistent findings among banks regardless of the maturity[1] of the approach to intraday liquidity.

02. The distinction between collateral and intraday liquidity persists.
In many banks collateral management is actually treated as distinct from intraday liquidity management, and decision-makers have not yet cracked the code in automating collateral management or reporting.

03. Diffusion of responsibility varies.
For most banks, activities related to intraday liquidity are spread across several different functions. In contrast, the surveyed banks with the most mature approaches to intraday liquidity have shifted these responsibilities solely to treasury and risk.

04. Understanding of how to apply the rules is murky.
At many banks affected by the new rules, decision-makers are mixed in their understanding and interpretation of how to apply US regulations.

[1] Intraday Liquidity Survey scoring methodology: In order to identify the "most mature" participants, a scoring methodology for the survey was applied to specific questions across each of the sections of the survey. Answers to questions in these areas, which were determined to be indicative of a bank with more developed intraday liquidity capabilities, were given a higher weighting than those which indicated a less-developed program.

The top participants with the highest aggregate score were defined as the "most mature" among the respondent banks and the remainder of the participants were defined as "less mature". The survey results are presented with a view of the "most" and "less" mature banks against each other and against the total.

01. Information technology is a common challenge

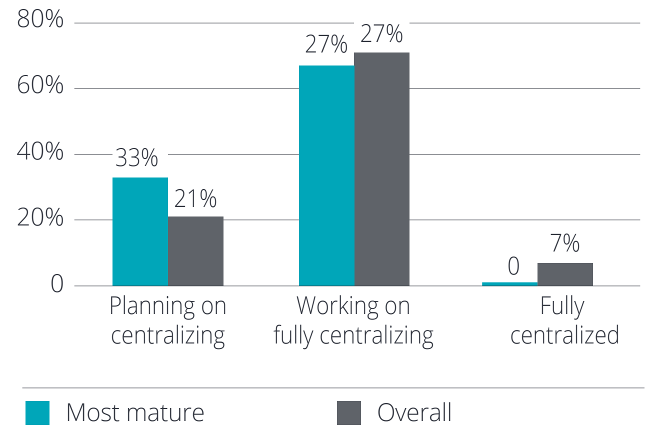
Low quality of data, and challenges in data technology capabilities, were consistent findings among banks regardless of the maturity of their approach to intraday liquidity.

To comply with intraday liquidity reporting requirements, a bank must be able to source, centralize, and standardize the relevant data. Many institutions have capabilities in these areas, but intraday reporting requires a level of speed and detail that many lack.

For example: Should time-stamping be done by the minute, or by the second? Even considerations like time zones and 12- versus 24-hour timekeeping can influence the function of these reporting systems. In addition, banks that use correspondent relationships to provide clearing services need the ability to monitor and report on those accounts, for themselves and for their clients.

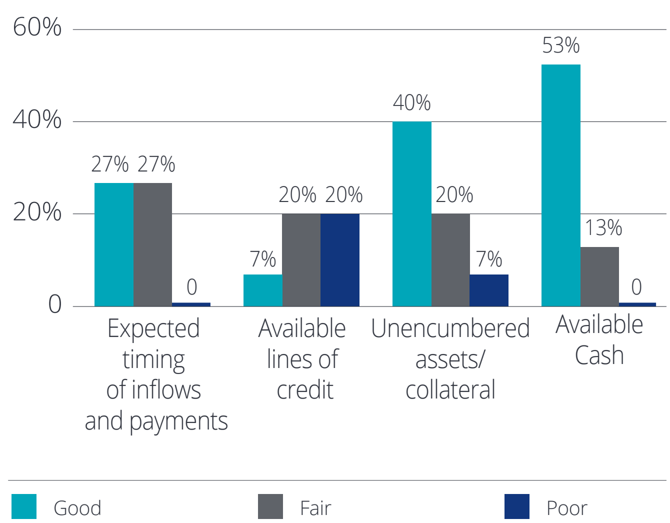
Some kinds of data are in better shape than others. For many of the surveyed banks, data on available cash was comparatively robust.

Centralizing data required for liquidity-related reporting



Only seven percent (7%) of bank executives said their institutions have fully centralized their data sourcing, while seventy-one percent (71%) said they were working on it now or planning to do so. It appears that even for banks that reach minimum compliance standards by "Day 1," there will remain plenty of "Day 2" work to be done on data centralization and cleansing.

Data quality



Reporting on unencumbered assets was "good" but not ranked as highly. Few banks, at either end of the maturity spectrum, reported having high-quality data on the expected timing and inflow of payments—a potentially critical factor for banks that must monitor certain accounts minute by minute.

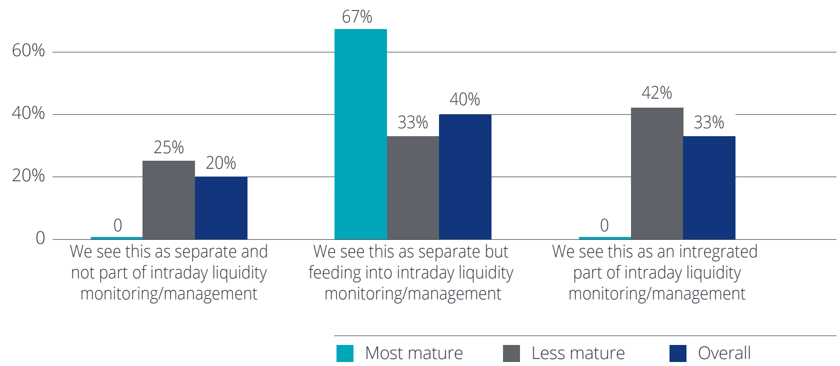
02. The distinction between collateral and intraday liquidity persists

In most banks, collateral management is actually treated as distinct from intraday liquidity management, and decision-makers have not yet cracked the code in automating collateral management or reporting.

Many of the surveyed executives said their banks address collateral management as a separate activity apart from intraday liquidity, rather than as an integral component of it. Intraday collateral reporting is often limited to a few updates a day and most banks have reporting available only at the end of the day. This impedes a bank's ability to leverage unencumbered collateral for the generation of additional liquidity intraday.

The survey also found that most banks do not have the ability to report on unencumbered assets intraday—instead, they produce reporting on unencumbered assets at EOD, and use this reporting to assist them in pledging collateral for funding or to secure intraday credit lines throughout the following day.

How do bank executives view the relationship between collateral management and intraday liquidity management?



- Only thirty-three percent (33%) of surveyed bank leaders overall and none from the "most mature" banks viewed collateral management as integral to intraday liquidity.
- Twenty percent (20%) of surveyed bank leaders saw collateral management as a separate activity from intraday liquidity management altogether.

Some banks are using their collateral reporting to pledge collateral to secure intraday credit lines.

- Forty percent (40%) of surveyed banks overall are tracking and reporting on the collateral pledged to central banks and twenty percent (20%) are tracking and reporting on financial market utilities (FMUs).
- Eighteen percent (18%) are not tracking or reporting on this pledging activity at all.
- Only twenty percent (20%) of banks overall are tracking and reporting on the collateral used to facilitate intraday timing mismatches between payment inflows and outflows.

Because regulators are likely to increase their focus on collateral management, executives should consider not only how to improve the management and reporting of collateral intraday, but also the fundamental role collateral plays in the management of intraday liquidity.

03. Diffusion of responsibility varies

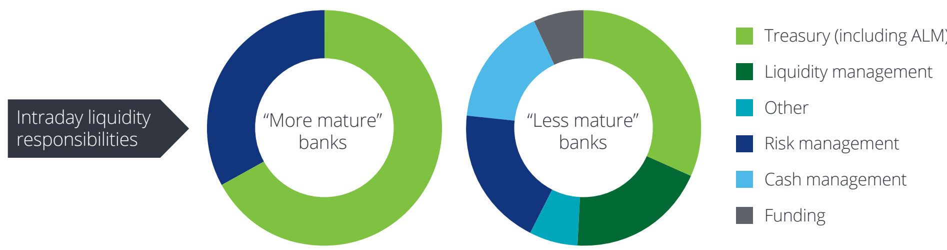
For the majority of banks surveyed, activities related to intraday liquidity are spread across several different groups. In contrast, the banks with the most mature approaches to intraday liquidity have shifted these responsibilities solely to treasury and risk.

The Deloitte survey found that one distinguishing characteristic of "most mature" banks was that they have concentrated intraday liquidity responsibilities in two departments, treasury and risk.

In comparison, the majority of banks surveyed have parceled out the responsibility for intraday liquidity among multiple groups including treasury, liquidity management, risk management, cash management, funding, and others.

Many institutions are challenged to define the operating models that will carry out these new monitoring, management, and reporting tasks.

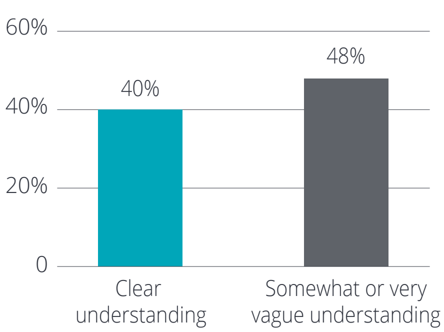
Functions with primary responsibility for intraday liquidity



This dispersion of responsibility creates a situation where not everyone clearly understands what must be done in a new environment where operations are now highly visible to senior management.

04. Understanding of how to apply the rules is murky

At many banks affected by the new rules, decision-makers are mixed in their understanding and interpretation of how to apply US regulations.



The new intraday liquidity rules apply broadly—eighty-eight percent (88%) of surveyed bank leaders confirmed their institutions are affected. However, far fewer of those bank leaders said they are clear on what's required. Almost half said they have a "somewhat or very vague" understanding of the new regulations. Only two in five said they understand them clearly, and some plan to turn instead to guidance from Basel that offers more detail.

The fact that executives do not think they have mastered the new intraday liquidity regulations might be less significant if their institutions were moving ahead with the required process changes anyway—for example, to satisfy internal, strategic aims.

However, fifty percent (50%) of all the surveyed executives, and thirty-three percent (33%) of those at the "most mature" banks, said their primary motivation for changes in this area were the regulations themselves, not the opportunity to benefit internally from enhanced capabilities.

Intraday liquidity opportunities

This survey demonstrates that many bank executives know the new requirements are out there, and they are beginning to take the initial steps to develop the understanding and strategic vision to carry out a new standard of intraday liquidity management. However, it also shows more work is still needed in a few key areas.

Technology and data

As banks work to consolidate data sources, repurpose existing technology, and build new systems, building an understanding of intraday liquidity requirements into the mix is a major challenge. The pressure of the moment can spawn quick, tactical fixes, but the long term will call for a more thorough approach. The better able a bank is to identify and track liquidity, the more opportunities there will be to take advantage of all liquidity sources, creating additional value for the bank while satisfying regulators.

Collateral management and reporting

While not a focus to date for most banks, it is a key component of intraday liquidity management. Seeing the connection, and adjusting the focus and sense of urgency to match, is an imperative. If bank leaders don't adopt this view, it's still likely that regulators will.

Roles and responsibilities

Operations responsibilities are now being given much more attention and importance as items such as fails, payments management, payments volume, extension of credit, and available collateral have been under more scrutiny by regulators. Transitioning ownership and/or oversight to groups like treasury and risk may be the step decision-makers need to take to enable delivery of new processes that align to regulator expectations.

Understanding and adopting regulatory requirements

Banks must turn to the regulators they already know, along with experienced people inside and out, to help them develop and deepen their understanding of these rules. In this spirit, reviews such as CLAR aren't just tasks—they're also opportunities. Only with better understanding of the requirements can bank executives build the governance structures and operating models to implement them.

Because these are common issues, bank leaders should consider participating in industry forums and roundtables to share leading practices. There are also vendors who specialize in helping financial institutions meet these challenges. Intraday liquidity is a time-critical, specific concern, but banks that work to master it can improve their overall risk management capabilities.

About the survey

Deloitte's Advisory Banking and Securities Treasury practice conducted the survey from September to November, 2015, and summarized the results during the first quarter of 2016.

Of the 15 BHCs and FBOs represented, all had assets exceeding $50 billion; 47 percent (47%) had assets greater than $500 billion, and 20 percent (20%) had assets greater than $250 billion.

Sixty-six percent (66%) of the banks were US-based, and 7 percent (7%) were in other North American locations. Twenty percent (20%) were EMEA institutions and 7 percent (7%) were located in the Asia-Pacific region. Respondents included treasurers and other senior executives across treasury and liquidity management, funding, cash operations, and finance. There was one representative response collected per bank.

Participants were asked to respond to questions across the following five areas: Regulatory requirements and readiness, drivers and challenges, rules and responsibilities, process and reporting, and technology.

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