Credit Benchmark

Whitepaper // No.2

Credit Benchmark Consensus Risk Estimates for Credit Portfolio Managers

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Consensus Data in Credit Risk

Credit Benchmark has brought together a group of globally important banks that anonymously and securely pool their internal credit risk estimates, creating qualified consensus Probability of Default (“PD”) and senior unsecured Loss Given Default (“LGD”) metrics.

Our Consensus Risk Estimates service, launched earlier this year, offers monthly-updated consensus IRB PD estimates on thousands of obligors at the individual legal entity levels, extending from sovereigns and banks to public and private corporates and funds. Credit Benchmark also offers data on tens of thousands of obligors for use at portfolio level. We will shortly also be launching our consensus LGD estimates service.

Participation in the service is open to all banks using the IRB method for calculating regulatory capital and Credit Benchmark warmly invites interested institutions to become contributors.

In this note, we propose applications for Credit Benchmark data in key areas of the Credit Portfolio Management workflow, including model review, portfolio monitoring, RWA benchmarking and data quality improvement.

Credit Benchmark Consensus Risk Estimates for Credit Portfolio Managers

Credit Benchmark is a market-led response to three of the most critical issues facing credit risk professionals:

- The need to improve credit risk management through internal benchmarking
- The requirement to justify internal model outputs to supervisors
- The insufficiency of robust external data

This note examines the applications for Credit Benchmark Consensus Risk Estimates within the Credit Portfolio Management workflow

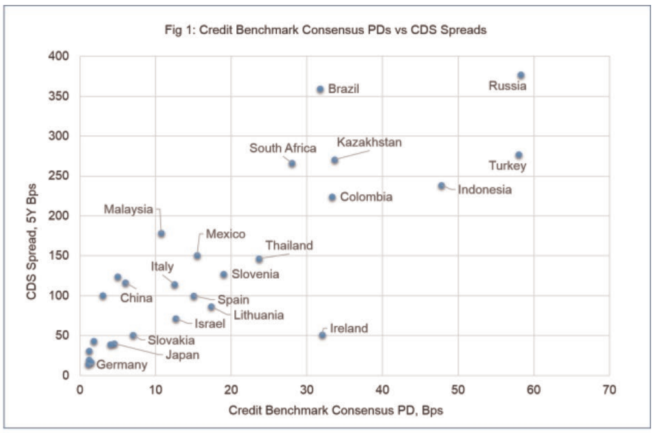
Credit Portfolio Management priorities and Credit Benchmark

1. Model Review

Credit Portfolio Managers must satisfy themselves that their institution’s internal models represent robust ex ante estimates of credit risk.

Internal historical data and back testing can only go so far, but regulators are pressing strongly for reduced reliance on the main currently-available source of external benchmarks – agency ratings – as well as promoting enhanced comparability of capital requirements across banks.

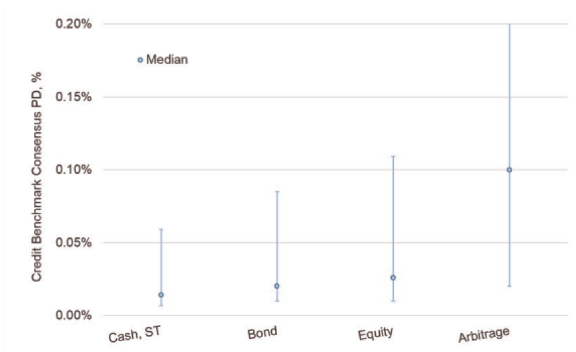
Whilst never a substitute for internal underwriting standards, Credit Benchmark Consensus Risk Estimates provides a robust, flexible external benchmark that allows Portfolio Managers to understand each portfolio in the context of a validated industry view. Analysis of positioning versus a robust industry mean both between portfolios and over time is a powerful tool with which to identify unexpected outliers and transitions.



In the rated obligor universe, Credit Benchmark data can be seen as a complement to existing data sources. We observe meaningful differences between Credit Benchmark data, agency ratings and CDS spreads that we believe add valuable information to CPM processes.

Credit Benchmark Consensus Risk Estimates also offer numeraires for a large number of unrated entities, in particular private companies and funds.

Fig 2: Credit Benchmark Consensus PDs for Selected Fund Groupings



2. RWA Comparisons

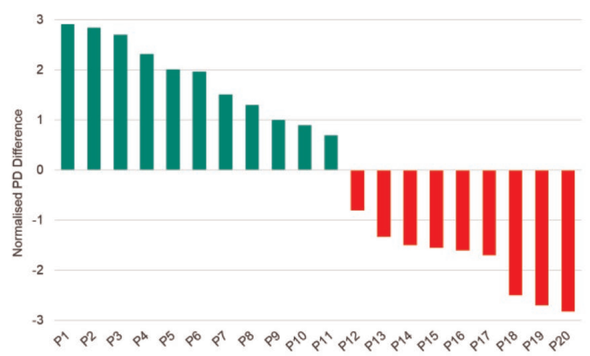
Benchmarking against Credit Benchmark Consensus Risk Estimates enables institutions to themselves identify instances where capital allocation appears notably different to industry levels, analogous to the views created through supervisory hypothetical portfolio exercises. Credit Benchmark's monthly update frequency (which we expect to increase over time) allows banks to increase the risk sensitivity of benchmarking, and provides a powerful additional tool to ensure capital levels are appropriately supporting expected future losses.

3. Bespoke Portfolio Construction and Monitoring

Credit Portfolio Managers need to aggregate portfolios in diverse and bespoke ways that are often not supported by existing external data sources.

Because Credit Benchmark Consensus Data is available at individual legal entity level, portfolios can be matched precisely to a bank's internal sector, obligor type and geographical views.

Fig 3: Analysis of Contributor vs Credit Benchmark Consensus Portfolio PDs



4. Data Integrity

In our experience, Credit Benchmark can play a valuable role supporting internal efforts to improve data integrity. Credit Benchmark does not validate or look through to the drivers underlying contributors' credit estimates: all IRB estimates are eligible for inclusion in the Consensus Data.

However, Credit Benchmark's function as a data pool gives it a unique perspective on extreme outliers and other indications of data challenges, which it reflects back, in confidence, to the relevant contributor. Credit Benchmark is well positioned to assist contributors in identifying and categorizing data quality issues, as well as model selection issues and risk aggregation across corporate hierarchies.

Becoming a Contributor

Credit Benchmark Consensus Credit Risk Estimates are broadened and deepened by every new contributor. We hold regular roundtable meetings that interested institutions are warmly invited to attend. To discuss becoming a contributor, please contact our business development team at the addresses below, or visit our stand at the IACPM Fall Conference in Toronto.

Credit Benchmark

Credit Benchmark Consensus Risk Estimates are:

1. Global, sourced from banks from every geography
2. Robust, reflecting the views of institutions taking risk
3. Broader and deeper than any internal or external data currently available to an IRB bank

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