EBA/DP/2013/02

European Banking Authority
Sent by email to: EBA-DP-2013-02@eba.europa.eu

Re: Discussion paper on retail deposits subject to higher outflow for the purposes of liquidity reporting under the draft Capital Requirements Regulation (CRR)

Dear Sirs
HSBC Banking Group appreciates this opportunity to respond to the European Banking Authority regarding its discussion document on "Retail deposits subject to higher outflow for the purposes of liquidity reporting under the draft Capital Requirements Regulation (CRR)"
HSBC understands the objective of the paper and supports the increased requirements for granularity, transparency, management, control, governance and reporting around retail deposits.

A.General Comments

Whilst we appreciate and support the EBA's goal to better manage the risk associated with retail deposits there are some areas where HSBC would seek clarifications regarding the proposed framework.

B. Single Rulebook

We believe that the LCR should continue to support the Single Rulebook concept embedded within the CRR in that, as much as possible, LCRs in different jurisdictions are reasonably comparable. This helps all stakeholders-external analysts/investors/depositors and regulators- understand the risk appetite and therefore risk/return tradeoff that an institution is prepared to take within the short dated liquidity environment. Any national discretion associated with deposit outflow should be exceptions and also clearly backing a specific national risk.

C. Definitions in internal systems

We also believe that the definition of any retail deposit should be objective so that there is not any perception/incentive of possible arbitrage and also that the definitions support clearly implementable cuts of data within bank systems.

D. Response to questions posed by EBA

> Q1.How do respondents assess the availability of data to empirically substantiate work on criteria for identification of retail deposits subject to higher outflows, as well as setting such outflow rates?

HSBC Banking Group agrees with the EBA on the difficulty to empirically assess the identification of retail deposits subject to higher outflows and the setting of such outflows from our own data. This is due to the fact that, in the current crisis, we have seen mainly inflows within our institution and in a business as usual environment any analysis of deposit movements (via trend or seasonal factors) will not reveal a statistically significant position to rely upon due to the tail event scenario that the LCR is looking to insure to.

However notwithstanding the above statement HSBC believes that it is important to set a risk appetite that is appropriate for the risks that a bank takes in maturity transformation.

Q2. Can you identify any other factors that may lead to higher outflow, especially in relation to the introduction of innovative products designed to lower outflow rates?

We see no other material factors that may lead to higher outflows. Geographical concentrations and socio-economic grouping concentrations are minor factors, but the danger here is that in becoming too granular the reliance that could be placed upon the LCR as a minimum pillar 1 measure may be diluted.

Q3. Do you agree with this characteristic? Should the local DGS amount be used instead of a fixed 100,000 EUR? Is it sensible to distinguish between high and very high value deposits? What are the concentration analysis and management tools used internally as regards high value deposits?

HSBC's framework is set up to identify the reaction function of our depositors to a stressed event and this generally correlates to the level of sophistication associated with the deposit. The higher the value of a deposit the more likely it is to be professionally managed however against this you need to take into account the offsetting factor which is the level of engagement with a customer (e.g. personal relationship managers).

The local DGS should be used rather than the €100,000.

The value of high and very high deposits is not necessarily consistent as it does not explicitly link to any underlying drivers of liquidity management sophistication and, in addition, does not take into account the size of a balance sheet and the number of customers etc. The size of any balance needs to be correlated to the size of the liquid assets on the balance sheet and the nature of the bank (e.g. retail/wholesale/investment bank or universal)

We use a concentration analysis by top 5, 10 and 20 depositors (but more wholesale), a catch all size filter that is correlated with business line and the jurisdiction we operate in as our main filters.

Q4. Do you agree with the criteria for deciding which products can be considered as rate-driven?

The price of deposits does not overtly relate to the liquidity risk, it is an indirect metric for the level of sophistication associated with the management of a deposit. Therefore although we understand rate can absolutely be a driver of stickiness in some cases, comparing against peers rather than an index brings in a level of subjectivity that is in danger of reducing the explanatory nature of LCR to users of this metric. We suggest that this would be decided upon internally by banks depending on the situation. As an example, to suggest a level of 25% above peers could be meaningless if rates are close to the zero boundary- say 10 basis points versus 1 basis point, but when rates are closer to more normal levels, such as 4-6%, when one bank is paying 4% and a comparable peer is paying 5% would indicate high levels of stress to the market already. We therefore are not in favour of using relative peer pricing for LCR.

Q5. What criteria do you propose to address potentially higher outflow rates connected to term deposits?

We do not currently use term as a driver of liquidity in the retail environment as we believe we would allow retail deposits to break term deposits in stress. We therefore model as if the deposit was a call deposit. The only exception to this is where regulation does not permit the early repay of depositors.

Q6. What are the other characteristics identified capture the key attributes of retail deposits subject to higher outflow? What is the internal policy extended to detect other characteristics?

There are many other factors that could be considered including economic and political environment of jurisdiction within which you operate and also the regulatory framework, cultural issues etc…

> Q7. In your view are the descriptions applied to the characteristics and their analysis sufficiently comprehensive?

We agree the characteristics are sufficiently comprehensive.

> Q8. Is the threshold based on the guaranteed amount and the threshold of € 500,000 appropriate?

The threshold based on a guarantee scheme is appropriate, but the €500,000 seems random, however the EBA may be implicitly expressing a risk appetite.

> Q9. Is the definition of products with rate-driven and preferential features precise enough? If not please specify what additional specification would you include?

As alluded to above we do not see the value of LCR capturing rate- driven features. The price of a deposit does not overtly express its liquidity risk, it is an indirect link to the possible professional management of a deposit under stress, and this is the most important aspect.

> Q10. Is it feasible to assess the proposed characteristics on robust operational grounds?

Most of the characteristics are capable of being operationally implemented. Please note that this needs to be considered as LCR will be required to be calculated daily and manual adjustments do not help in this process.

> Q11. How much and what additional resources will be needed by institutions to implement this assessment? How much and what additional resources will be needed by institutions to run the assessment on an ongoing basis? Could you explain what will drive the costs?

We are already implementing LCR requirements; the costs are really associated with pulling cashflow data from front office systems and putting it into a single database with the relevant product and customer characteristics to then correctly map data to outflows. The cost of this project is material and in the multi hundreds of millions of dollars.

> Q12. Are there any factors which appear to be associated with higher outflow on retail deposits? If yes, which factors?

We have no other characteristics to suggest at this point.

> Q13. Do institutions view the combination of any of these factors as more prone to lead to liquidity risks?

An example would be the correlation of high value deposits obtained via a broker channel when they do not have a direct relationship with us. These types of deposits would be likely to withdraw early under stress due to their level of sophistication.

> Q14. What is your opinion on the feasibility and resource-intensiveness of implementing the proposed methodology in your jurisdiction?

We recommend that there is a trade-off between the amount of liquid assets you hold, the requirement to understand how your position moves on a daily basis (so pulling data from a downstream system rather than a General Ledger) and the fact that in trying to model deposit outflow you are in effect modeling an unknown-unknown (you don't know when a run will occur and also how customers will actually react).

Therefore, at times, it is arguably better to hold more liquidity, get a more up to date report on the liquidity position and understand that liquidity entails a confidence factor as much as any spurious accuracy that modeling can provide, this is not market risk. Your liquidity buffer should in effect be a statement of your risk appetite. In addition you are probably better focusing on the longer dated funding requirement to counter much of the risk.

> Q15. What is your opinion on the composition of the 2 groups of the characteristics ranked according to riskiness?

This seems reasonable.

> Q16. Do you believe it would be appropriate to allow derogations from the application of outflow rates on the basis of uniform strict criteria?

Although this sounds feasible it runs a serious danger of rendering the LCR meaningless for comparative purposes. On this basis we are hesitant about this.

> Q17. What are in your opinion factors that could lead to the application of the above-described derogation mechanism?

Any derogation would have to be very specific to a customer type/product type or characteristic and be comparable and implementable across all jurisdictions.

HSBC Group appreciates the opportunity to share feedback and is happy to engage with regulators to further consider the issues around retail deposit outflows under stress.

Sincerely,
HSBC Group Asset and Liability Management