Morgan Stanley



Scenario Design

Morgan Stanley Presentation to the FRB Model Symposium

October 11, 2018

Guidelines for Establishing New Severely Adverse Scenarios

Risk Profile Changes

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External Environment Changes

3

Continued

Process / Model

Enhancements

Reflect the changing composition of the Firm's balance sheet, business mix and risk profile

- Changes to business activities, including new or expanded businesses
- Changes to risk profile, including material concentrations and key basis risks

Consider changes in the operating, market and macroeconomic environment

- Relative changes and starting points for key market / macro drivers
- Modified view around impact of certain operational risk events

Incorporate process improvements that better inform an understanding of key vulnerabilities and drivers of financial performance

- Understanding of risk drivers and model enhancements
- Impact of alternative scenarios
- Sensitivity of models to key scenario features
- Governance and review

Design of Multiple Scenarios

Apply the above principles to both evaluate alternative scenario narratives and associated variable shocks and stress different combinations of the Firm's risks

Macro Scenario Stress Testing → Firm's Capital Stress Testing

Day-to-Day Risk Management

Macro Scenario Stress Testing

- Adverse macroeconomic scenarios that incorporate regional and portfolio vulnerabilities across risk stripes
- Considerably more likely to occur than severely adverse scenarios

Product Stress Testing

- Instantaneous shocks
- Directional risks
- Non-linear risks
- Concentration and basis risks

Capital Adequacy Assessment and Capital Planning

Develop Candidate Scenario Narrative(s)

 Combine risk themes identified from multiple stress scenarios to develop plausible, severely adverse scenarios

Increase Scenario Severity and Broaden Risk Coverage

- Define theme; increase shock severity and stress additional risks
- Incorporate effects on earnings, balance sheet, risk-weighted assets and capital
- Add operational and idiosyncratic risk elements

Evaluate Scenarios for Capital Planning

 Assess scenarios based on relative risk capture, severity and impact to the Firm's capital

Governance

Review and Challenge

Documentation of Scenario Narratives

Integrated Role of Scenario Design into Day-to-Day Capital Planning and Risk Management

