Scenario Design Choices

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Key Design Issues in Scenarios

1. Severity
2. Tuning to unique business model and risks
3. Incorporating bad events
4. Addressing orthogonal risks

The Fed Scenario

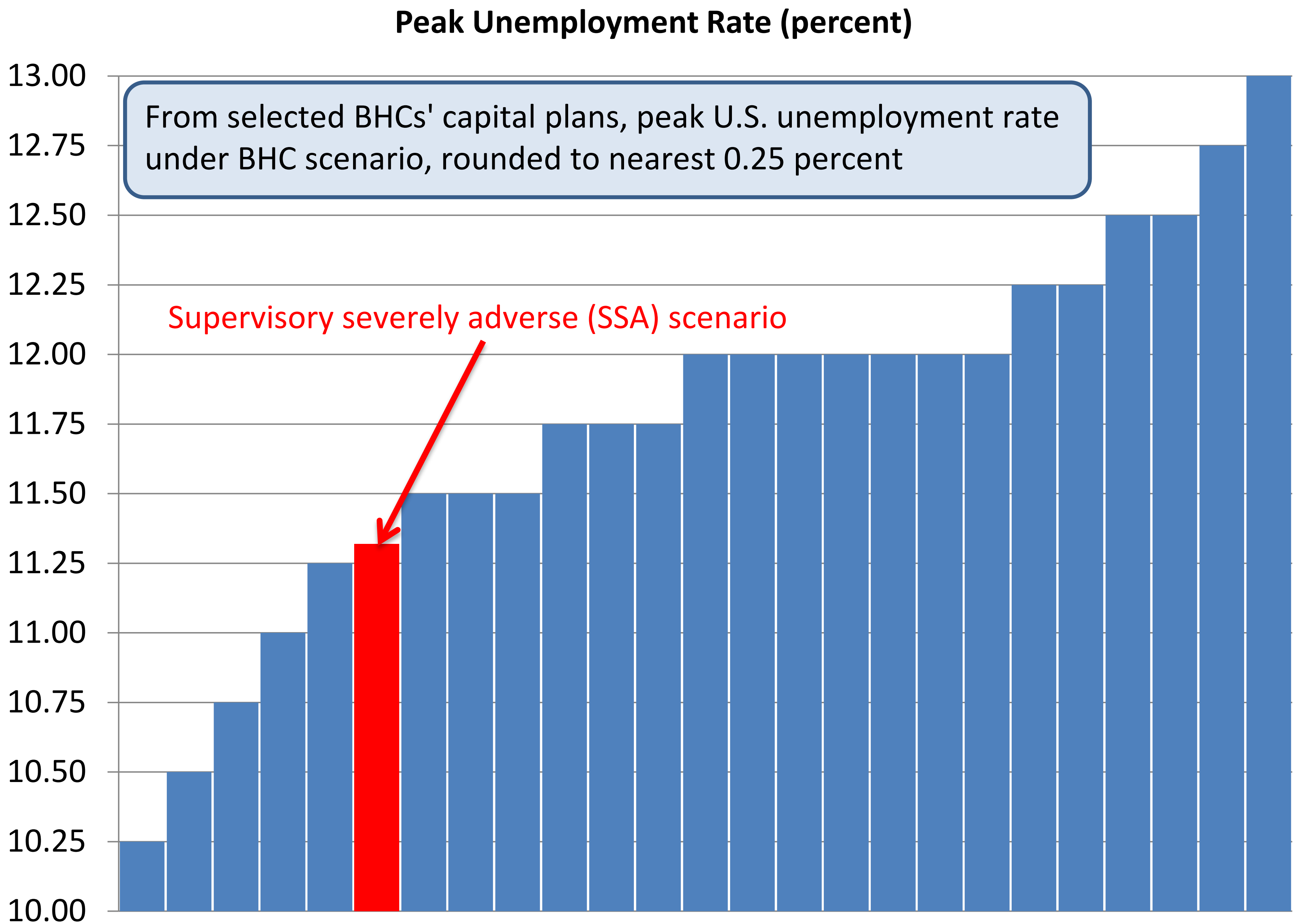
- Can be thought of: A financial panic followed by a severe U.S. recession
- Fairly generic—targets essentially undiversifiable asset price and credit risk
  - Stress time-varying salient risks (e.g. leveraged loans, emerging markets)
  - Global trading shock—financial panic—applied to firms with large trading books
- Adverse (“middle”) scenario is qualitatively different—in 2014 a yield curve steepening

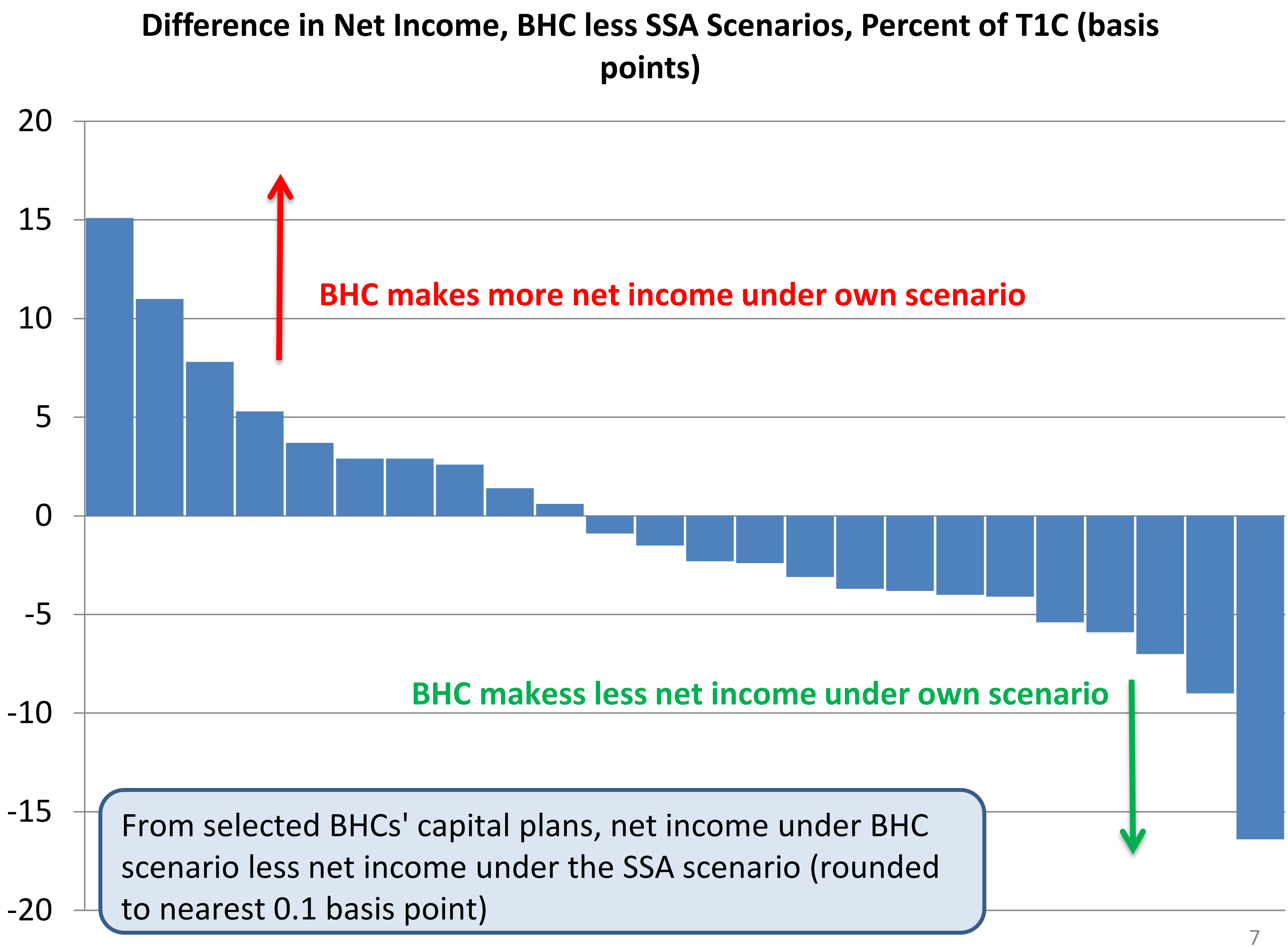
BHC Scenarios

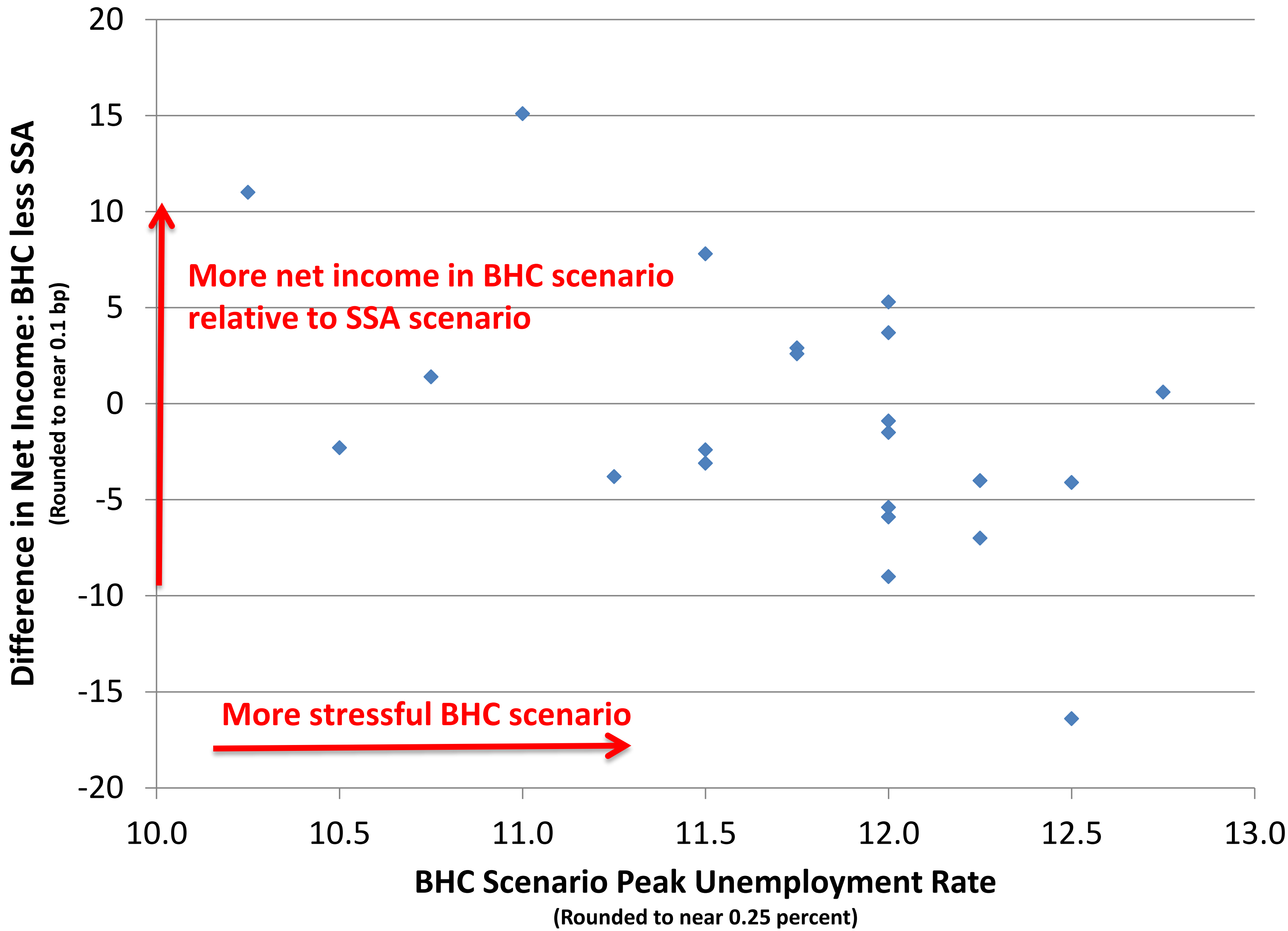
- Should reflect firms' unique vulnerabilities
  - Creatively tailor scenarios
  - Capture features missed by the Fed scenario
- Severity of outcome—higher <u>losses</u> under BHC scenario than under Fed scenario
- Broad scenario tuned to primary weakness in business model
  - Steep vs. flat yield curve, low vs. high oil prices etc.
- Bank is in a position of weakness—e.g. rogue trader, IT breakdown, ratings downgrade, etc.

Comparing Severity and Outcomes

- Compare severity of BHC scenario to net income
- Some important caveats
  - Peak unemployment rate not a perfect measure of severity
  - No requirement that peak unemployment rate in the BHC scenario exceed that in the Fed scenario
  - Net income affected by additional non-macro features such as the global market shock and counterparty default assumptions


Peak Unemployment Rate (percent)
From selected BHCs' capital plans, peak U.S. unemployment rate under BHC scenario, rounded to nearest 0.25 percent
Supervisory severely adverse (SSA) scenario
13.00
12.75
12.50
12.25
12.00
11.75
11.50
11.25
11.00
10.75
10.50
10.25
10.00


Difference in Net Income, BHC less SSA Scenarios, Percent of T1C (basis points)
20
15
10
5
0
-5
-10
-15
-20
BHC makes more net income under own scenario
BHC makess less net income under own scenario
From selected BHCs' capital plans, net income under BHC scenario less net income under the SSA scenario (rounded to nearest 0.1 basis point)


Difference in Net Income: BHC less SSA
(Rounded to near 0.1 bp)
20
15
10
5
0
-5
-10
-15
-20
More net income in BHC scenario
relative to SSA scenario
More stressful BHC scenario
10.0
10.5
11.0
11.5
12.0
12.5
13.0
BHC Scenario Peak Unemployment Rate
(Rounded to near 0.25 percent)