



PRESS RELEASE

Federal Deposit Insurance Corporation

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FDIC PROPOSES REQUIREMENTS FOR BANKS TO BETTER PREDICT MARKET RISK

FOR IMMEDIATE RELEASE

The FDIC today proposed new rules to require banks with large trading portfolios to more accurately project their future losses. Banks would have to compare past estimates of market risk with actual results -- a process known as "backtesting." Banks proven to have a poor record predicting market risks could be required to increase their capital holdings.

The Office of the Comptroller of the Currency and the Federal Reserve Board are expected soon to issue the proposal for the banks they regulate.

"Regulators and bankers alike agree that 'backtesting' is an important ingredient that should be carefully evaluated in the overall framework of risk management. For that reason we are requesting comments on this proposal," FDIC Chairman Ricki Helfer said. "The goal is to give banks incentives for understanding and addressing market risks, without creating undue regulatory burdens."

Today's proposal expands on a July plan to establish a capital requirement for market risk in foreign exchange and commodity activities and in the trading of debt and equity securities.

As with the July proposal, institutions with large trading activities would calculate their risk-based capital requirements using their own internal models of "value-at-risk" -- essentially the maximum amount a trading portfolio is likely to decline during a set period. Today's proposal, on which comments are requested, would require the banks to backtest their internal models each quarter by comparing actual net gains or losses to the previous projections. If the tests show the quality and accuracy of the bank's risk



Congress created the Federal Deposit Insurance Corporation in 1933 to restore public confidence in the nation's banking system. It promotes the safety and soundness of these institutions by identifying, monitoring and addressing risks to which they are exposed. The FDIC receives no federal tax dollars — insured financial institutions fund its operations.

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management system to be lacking, the institution could be required to increase capital. The first backtesting would begin in January 1999 comparing internal model projections to actual trading results since January 1998.

The FDIC will accept public comments on the new proposal for 30 days after it appears in the Federal Register. The proposal was developed on an interagency basis. Under the system proposed in July, approximately 25 of the largest U.S. banks plus a few smaller banks would be required to base their capital levels partly on projections of market risk.