HSBC

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Basel Committee on Banking Supervision
Bank for International Settlements
CH-4002 Basel
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Dear Sirs,

Subject: Review of the Credit Valuation Adjustment (CVA) risk framework – Consultative Document

HSBC welcomes the opportunity to respond to the Basel Committee on Banking Supervision (BCBS) Consultative Document on the review of the Credit Valuation Adjustment (CVA) risk framework.

We continue to support the objectives of the Basel Committee on Banking Supervision (BCBS)'s CVA reform to capture all CVA risks and gain better recognition of CVA hedges. In this regard, we think it is important to highlight areas of material deficiencies of the CVA framework and provide data in support of the issues and recommendations wherever possible. Recent analysis conducted by the industry highlights specific design issues that we recommend are addressed as part of the alignment of the CVA standard to the updated market risk requirements. Recent QIS data analysis demonstrates that the final CVA framework will result in a substantial increase in capital requirements despite the intended objective of not significantly increasing overall capital requirements.

HSBC has contributed to and fully supports the ISDA/AFME joint response to the CVA review. There are additional issues that HSBC would like to draw to the attention of the Committee. Our high-level observations and views are presented in the body of this letter, while the subsequent annex includes more detailed feedback and empirical evidence.

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As an internationally active bank, we are supportive of the Basel Committee's objective to develop a robust and coherent global framework. Closer alignment of the market risk and CVA frameworks is a crucial part of this, which will in turn decrease potential divergence in national implementation and operational complexity of the framework. Nonetheless, certain divergences between market and CVA frameworks are required to take account of the different nature of the risks arising, and therefore we fully support the enhanced risk sensitivity provided by the targeted revisions proposed.

Furthermore, we are supportive of the changes in terms of risk weight reduction, aggregation formula and index hedge bucket and we are also supportive of the additional proposals, such as the multiplier recalibration and the removal of Securities Financing Transactions from the scope.

From HSBC's perspective, we would encourage the Basel Committee to consider a number of additional revisions such as Credit Spread Risk Weight recalibration to provide a more granular assessment of level and volatility of CDS spreads, and a better recognition of index hedges to reflect good risk management practices. Furthermore, in line with the ISDA/AFME joint industry response, we welcome the reduction in the MPOR for client clearing trades to 5 days and would suggest that MPOR should be revisited for all transactions. An MPOR of 10 days required under the current BCBS proposal is conservative and does not reflect current market practices and CVA risk management practices. For details, please refer to the industry response.

Furthermore, we believe that BCBS should consider an extension to the timelines for the finalisation of the framework, currently planned for 1st January 2022, to allow for appropriate testing, impact analysis and recalibration of the CVA framework. In addition, the approval process and timelines for SA-CVA application is yet to be clarified and aiming to approve the models by 1st January 2022 might also be very challenging for regulators. While we support the integration and alignment of the new CVA framework with the Fundamental Review of the Trading Book (FRTB) market risk framework, we note that FRTB revisions have been ongoing for several years, allowing more time to assess the new proposal, calculate impact and build appropriate systems.

While CVA does not constitute a large portion of overall capital requirements, it constitutes a significant RWA driver for derivatives, which are important tools for end-users' ability to hedge their risks. The proposed approach is likely to raise the cost of prudent hedging, which may be passed on to end-users, potentially driving end-users to leave their risks unhedged, or to pursue less expensive protection providers outside of the regulated banking sector. We would encourage the Basel Committee to give due consideration to the wider economic impact of these proposals before it finalises the CVA framework at the global level.

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We thank you for your consideration and for the continued collaboration with the industry provided by the Basel Committee. We would be happy to answer any questions on the points enclosed.

Yours sincerely,

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