Course Description for Basel II: Retail Activities
BASEL II: RETAIL ACTIVITIES

TYPE OF PARTICIPANT TARGETED

This course is designed as a supplementary course for safety and soundness examiners and supervision staff who have an interest or anticipate having a responsibility for examining mandatory or opt-in Basel II banks.

PRE-COURSE PREPARATION

Prior to attending the course, participants are expected to complete the precourse online study modules developed on FSI Connect. Access can be provided by contacting the learner’s training department to obtain an FSI Connect account number.

COURSE OVERVIEW

This 3.5 day course is directed to examiners/supervisory staff who have been identified as Level 2 - Basel II Specialist for Quantification and Validation, or designated as needing this level of training. Upon completion of this course, examiners will have intermediate knowledge of quantification concepts for wholesale mortgage, credit card, student loans, auto loans, small business, and other retail portfolio activities. Additional training objectives will include knowledge of key components of model structure (e.g., credit risk, probability of default, loss given default, exposure at default, estimated loss, correlation, and unanticipated losses). The goal of this course is to provide a general understanding of the Basel II Internal Ratings-based (IRB) approach as applied to retail portfolios for examiners/supervisory staff that will be participating in IRB reviews.

COURSE OBJECTIVES

By the end of this 3.5 day course, participants will be able to:

- Describe the conceptual framework behind the international capital accords
- Differentiate between regulatory, available, and economic capital
- Explain basic statistics (such as descriptive statistics, distributions, and regression) underlying the credit capital calculations of Basel II
- Segment the retail portfolios based on risk homogeneity
Apply the risk parameter estimate technique, specific for PD, LGD, and EAD

POST-COURSE INTERVENTION

After completing Basel II Retail, the examiners with this level of knowledge will be able to compare the bank's current risk measurement practices against the Advanced Internal Rating Based Approach requirements for retail quantification and report where those practices may fall short of supervisory expectations. It is expected that individuals with this level of knowledge would work closely with Level 3 specialists in model evaluation.

OVERVIEW OF CURRICULUM

BASEL II RETAIL AGENDA

Day One

<table>
<thead>
<tr>
<th>Time</th>
<th>Module</th>
<th>Time Assigned</th>
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<tbody>
<tr>
<td>10:30 AM</td>
<td>Building Blocks 1 Intro</td>
<td>1.5 hours</td>
</tr>
<tr>
<td>12:00 PM</td>
<td>Building Blocks 2 Fundamental Statistics</td>
<td>1.0 hours</td>
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<tr>
<td>1:45 PM</td>
<td>Building Blocks 3 Regulatory Capital</td>
<td>1.0 hours</td>
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<tr>
<td>3:00 PM</td>
<td>Home Host Issue and Statistics Exercise</td>
<td>2.0 hours</td>
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Day Two

<table>
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<tr>
<th>Time</th>
<th>Module</th>
<th>Time Assigned</th>
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<tbody>
<tr>
<td>8:30 AM</td>
<td>Segmentation – Intro and Design</td>
<td>1.5 hours</td>
</tr>
<tr>
<td>10:30 AM</td>
<td>Segmentation – Applications &amp; Example</td>
<td>1.0 hours</td>
</tr>
<tr>
<td>11:30 AM</td>
<td>Quantification - Process</td>
<td>1.0 hours</td>
</tr>
<tr>
<td>1:30 PM</td>
<td>Quantification – Practice and Capital Functions Activity</td>
<td>1.5 hours</td>
</tr>
<tr>
<td>3:00 PM</td>
<td>Probability of Default – Intro, Data, Model, and PD Quantification</td>
<td>2.0 hours</td>
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Day Three

<table>
<thead>
<tr>
<th>Time</th>
<th>Module</th>
<th>Time Assigned</th>
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</thead>
<tbody>
<tr>
<td>8:30 AM</td>
<td>Loss Given Default – Overview and Estimation</td>
<td>2.5 hours</td>
</tr>
<tr>
<td>11:30 AM</td>
<td>Securitization</td>
<td>1.0 hours</td>
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May, 2009
Day Four

<table>
<thead>
<tr>
<th>Time</th>
<th>Module</th>
<th>Time Assigned</th>
</tr>
</thead>
<tbody>
<tr>
<td>8:30 AM</td>
<td>Validation – Developmental Evidence, Monitoring, Sensitivity, Stress and Statistical Tools</td>
<td>3.5 hours</td>
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LEARNING OBJECTIVES

By the end of this course, learners should be able to:

Building Blocks

- Summarize differences between Basel I and Basel II
- Explain the framework of Basel II
- Differentiate between regulatory capital, economic capital, and available capital

Segmentation

- Explain the purpose of segmentation as applied in credit risk management and IRB credit risk systems
- Explain the general segmentation design and model development issues
- List the specific IRB requirements for retail credit risk segmentation

Quantification

- Explain the three risk parameters to be quantified for A-IRB
- Describe the four components of any quantification process

Probability of Default (PD)

- Explain the role that PD plays in total losses
- List the requirements for IRB quantification of PD
• Identify issues in PD quantification:
  • Data availability over economic cycles
  • Measurement time horizon
  • Modeling/estimation techniques
  • Drivers of PD

Loss Given Default (LGD)
• Define LGD
• Measure loss for retail exposures
  • Economic loss
• Estimate LGD
  • Based on periods of high credit losses
• LGD for residential mortgage exposures
  • Unique aspects
  • Example – risk sensitivity

Securitization
• Determine structures which retail exposures fall under the securitization framework
• Discuss the hierarchy of capital allocation approaches available under the Final Rule
• Discuss issues related to the implementation

Exposure at Default (EAD)
• Describe the Loan Equivalent Measure (LEQ) and methods for estimating this parameter
• Describe the key differences between the fixed horizon and cohort methods of calculating the EAD measure

May, 2009
• Describe the requirement for LEQ and EAD to be estimated during periods of high credit loss

**Validation**

• Describe supervisory expectations about validation
• List various techniques that may be used in the validation of IRB segmentation systems and quantification processes

**CLASS SIZE**

Minimum class size is 10 with a maximum of 30.

**INSTRUCTORS**

There are usual 4-5 instructors for this course.