Bank Governance Leadership Network participants discuss COVID-19 responses

On March 30 and March 31, Bank Governance Leadership Network (BGLN) participants joined two conference calls to discuss the global response to the COVID-19 pandemic and implications for large banks. The key themes that emerged are synthesized below.

Operational resilience and business continuity planning

As large parts of economies globally are "frozen" and employees work remotely to stem the spread of COVID-19, banks have successfully implemented business continuity plans, but are also running into operational challenges.

- **Banks are working hard to support their customers and employees in crisis.** As the economic fallout from the spread of COVID-19 deepens, bank leaders are keen to support their customers and employees. A director said, *"Right now, we are focused on helping our employees and customers get through this safely and we are reorganizing our workflows to enable that, ensuring our business continuity plans are robust and working, providing customer accommodation."* The sudden surge in customer inquiries, however, is straining support infrastructure. As a participant explained, *"We are operating with 50-60% of our call center capacity, we're down 30% of our workforce in branches and have temporarily closed numerous branches. There's been a significant increase in service volumes with a dramatic decrease in staffing."* Another added, *"We're flexing all the muscle in our operational side to make the call centers work and get things passed through, but it's been a challenge."*

  Participants are mindful of the stresses such a challenging environment can inflict on employees. A director said, *"We're working as if it's a sprint at the moment, but it's going to be a marathon. We are trying to figure out how to support the people that have been working incredibly hard to ensure they don't get burnt out."*

- **Operational resilience has been strong, but remains a source of concern.** Participants largely agreed that banks have handled the shift to remote work at scale surprisingly well thus far. A director said, *"With this major shift to remote working, as a board we are getting briefed on both how the bank networks, but also local networks, are handling that increased activity. The bank networks are working well but we're keeping a close eye on the local networks to make sure they can keep operating so that everyone can continue to function. We consider those to be the point of vulnerability right now."* Another added, *"Our business continuity has thus far stood up and worked and we've had no real surprises exactly; all of these things were included in the continuity plans. But what we did not anticipate was the scale, the global impact all at once."* Cybersecurity is also a concern in this environment. A director said, *"As people are working from home, are they unintentionally injecting some cyber risk? Are they practicing cyber hygiene? We haven't seen an uptick in cyber activity but we are watching very carefully."*

Policy responses and the banks' role

Policy makers and regulators around the world have taken a variety of steps to provide economic relief to individuals, SMEs, and large corporations to ease the financial impact of the crisis. Regulators are also providing relief regarding some post-crisis regulatory requirements to enable banks to provide financing and ease the burden of implementing new requirements. The situation has placed banks in the center of the economic response, creating new challenges and opportunities.

Regulators are adjusting requirements and priorities

To give banks more flexibility to supply credit and support the fiscal response from policymakers in mitigating the economic costs of the COVID-19 outbreak, regulators are reviewing their own agendas and priorities. In describing their work to date, a regulator said, *"Agencies have taken a number of steps to encourage banks to work with customers and use their liquidity and capital positions, which were in good shape before this, to support their customers and the economy. We are trying to do more to clarify exactly how that could work."* Some of these steps involve relaxing regulatory requirements, while others will come via supervisory guidance. An EY participant described some of the actions taken to date: *"We have seen a significant amount of supervisory guidance basically providing clarifications or encouragement to regulated institutions, as well as targeted relief to certain reporting deadlines, certain capital and liquidity rules, all of which are supposed to be reinforcing of the actions the central banks are taking to support the economy."* A regulator added, *"There is a lot of work being done on the regulation and supervision side to open up resources for immediate need. For example, the Basel Committee said they are pushing back the final stages of Basel 3 implementation."* Stress tests in Europe and the UK have also been postponed for 2020, while those in the U.S. are continuing.

Regulators and supervisors are also shifting resources to focus on risks that could crystallize in the current environment. One regulator said, *"Given all the work from home, concerns about credit risk, and high-volume trading going on, on the supervision side we have either paused or reoriented our supervision to monitoring credit underwriting and operational risks."* Another said, *"We think transparency into the financial strength of the banking industry is important. We are going to be shifting from the initial focus on market volatility, early moves to address strains in money markets, short term markets, investment funds suffering outflows, etc. Now, we are shifting towards credit risk at banks, towards corporations drawing down credit lines* *and the implications. So far, banks have been beneficiaries of some of the outflows from other industries."*

Participants see challenges and opportunities in rapidly responding to borrowing needs

Banks accept their obligation to support government policies in easing the financial pain for customers and to ensure credit continues to flow to support businesses effected by the shutdown. In doing so, participants foresee further operational and risk management challenges, but also some opportunities:

- **Effectively implementing stimulus policies and assisting customers will require improved communication among banks and policymakers.** Participants suggested that more clarity is needed on stimulus program requirements and the potential impact on banks. An EY participant explained, *"There are issues to work out in the specific details of these schemes, the difficulties of operationalizing them in various countries, how to expedite processes while still recognizing there's a credit underwriting role to be done."* A director stated, *"What we've been asked to do is very hard to do quickly … We need a much better understanding by the regulators and government. They have made some good policy interventions that should be applauded, but they need to understand that the conditions in the front line are very difficult and this will be very difficult to produce."* Another participant suggested additional guidance from regulators could help in some instances: *"Are the regulators looking at or discussing rules or guidance for modifications that could be standardized across the industry? The difficulties of servicing are real. Having standardized requirements could be helpful as it was during the last crisis."*

- **Banks will struggle to quickly process loans.** Bank systems are not typically designed to process the expected loan request volumes on an expedited basis. An EY partner said of the U.S. response, *"As the Small Business Administration (SBA) lenders look at how to mobilize their technology, what they have in place today is built for a very specific purpose, with an intensive underwriting process. It is not built for this. I am seeing a challenge across the banks on how you take a high volume - authorized to be ten times what the annual loan volume has been through the SBA program historically - and go through that over a couple of months."* A director described the related challenges banks are managing globally: *"For example, on loans over a certain threshold, you have to take security. That requires documentation, and it will take time. It used to take 14 days if you moved fast, and that was in a pre-crisis environment."* Banks are exploring options to improve processing. An EY participant suggested some approaches: *"There are a few options: You can adapt the technology you have, but that creates a lot of risk. Some banks are bringing in new technologies. We are seeing vendors step up and get involved, which might help create new solutions quickly, but it's a challenge."* Some participants noted that they had worked with regulators to adopt new processes, using bots to automate rapid loan approval and delivery, fully backed by a government guarantee, which eases the strain on credit underwriting.

- **How banks respond could impair or enhance their reputations.** A participant said, *"Banks are going to get a lot of attention. In the U.S., there will not be enough funding for all the small businesses that need it, so there will be a reputational stress on everyone, and if banks can't get this distributed to the borrowers and grantees on a timely basis they could be at the forefront of that."* Some directors see reputational risks in being the transmission mechanism for government policy: *"There is a risk here that the government is sending the message that they've solved all the problems and could blame the banks when it doesn't work perfectly."* Others see an opportunity for banks to be viewed as part of the solution. One director said, *"I think it's a chance for so many banks to catch up on their own reputations. I know there is reputational risk, but banks' reputations have been in the gutter since the last crisis. I see this as a fantastic opportunity to restore the faith of the public in financial institutions and it's certainly up to each institution to stand up and deliver."*

Planning for an uncertain future

Participants anticipate that the unprecedented levels of uncertainty – regarding government policies and the ultimate economic impact - will persist for some time, posing challenges for balance sheets and scenario planning. The "new normal" could also raise longer term strategic and operating questions.

Challenging risk models and assumptions

A director summarized the current situation: *"Immediately the focus is on the now. We are experiencing significant loan growth at a rate that would already exceed what we saw in the last crisis. We need to behave such that we are in a position to support that growth and stop things like buybacks and dividends. We put in place our downcycle plan to manage credit. We are expecting a growth in credit losses and that absorbs capital. We are focused on helping our employees and customers get through this safely."*

But the unprecedented economic shutdown is challenging risk management. One director said, *"We've blown right through some of our stress scenarios, many of the markets are way past the stresses we were using. But we have not updated them yet because there has been so much focus on putting out fires, there has not even been time to think through these scenarios and what they might look like. It feels more unsure than it's ever felt in the past."* While others said they were still within their extreme stress scenarios, they acknowledged that the ultimate impact of the long-term shut down of large parts of the economy would continue to challenge models: *"We are still well off from our extreme stress data for now, but the unemployment figures are way past most high-risk scenarios. So now we're looking through whether some of our assumptions need to be reworked."*

A long tail

Some participants cautioned that this crisis could have a much longer tail than many initially predicted: *"The next four weeks will be truly horrendous …But we are looking at a timescale of at least six months with the current measures in place,"* said one. In such a scenario, recovery timing and trajectory becomes increasingly difficult to project. One participant said, *"The whole concept of viability I think is gone for the next 6-12 months."* Further, the recovery may be more gradual than the v-shaped recovery some initially hoped for: *"For the economy to really recover from this, we need consumer confidence back. People will think differently, about needing a nest egg to protect against something like this in the future, for example. You will get people going outside again and to a restaurant or two, sure, but don't think we'll get consumer confidence back to the levels it has been for some years."* As a result, participants see significant credit losses. One noted, *"Most businesses, if they haven't got three-to-six months of sales, they are not going to last. So, I think banks have no option but to help companies get through this period. But banks are heading for huge credit losses under any scenario."* Another observed, *"Depending on how long this lasts some of these businesses that we're asked to lend to will not be viable. So, it's not about whether we can lend to them quickly or not; it's a much bigger issue."* In some cases, one participant predicted, *"Debt for equity swaps will happen."* Ultimately, governments and central banks will likely end up as the backstop.

The longer economic shutdowns persist, the more the current crisis will also raise important questions for banks and directors about the future. One director observed, *"One fascinating outcome of the shift to remote work is seeing how, with so many branches closed, we've been able to repurpose many of our closed branch people into contact center people. How should we think about the branch footprint going forward? What about the blurring of the line between centralized and localized contact support? What does this mean for retraining employees?"*

Meeting participants

- Homaira Akbari, Non-Executive Director, Santander
- Jeremy Anderson, Audit Committee Chair, UBS
- Nora Aufreiter, Corporate Governance Committee Chair, Scotiabank
- Win Bischoff, Chair of the Board, JPMorgan Securities
- Norman Blackwell, Chair of the Board, Nominations & Governance and Committee Chair, Lloyds Banking Group
- Amy Brinkley, Non-Executive Director, TD Bank
- Agnes Bundy Scanlan, Non-Executive Director, Truist Financial
- Bethany Dugan, Deputy Comptroller for Large Bank Supervision, OCC
- Terri Duhon, Risk Committee Chair, Morgan Stanley International
- Tim Flynn, Non-Executive Director, JPMorgan Chase
- Morten Friis, Non-Executive Director, RBC
- Michael Gibson, Director of the Division of Banking Supervision and Regulation, Federal Reserve System
- Tobias Guldimann, Audit Committee Chair, Commerzbank
- Lauren Hargraves, Senior Vice President and Manager, Wholesale Product Office, Federal Reserve Bank of NY
- Petri Hofsté, Chair Audit Committee, Rabobank
- Mark Hughes, Former Chief Risk Officer, RBC, Non-Executive Director Elect, UBS
- Simonetta Iannotti, Member of Secretariat, FSB
- Leslie Ireland, Non-Executive Director, Citigroup
- Christine Larsen, Non-Executive Director, CIBC
- Richard Meddings, Chair of the Board, TSB Banking Group
- Scott Moeller, Risk Committee Chair, JPMorgan Securities
- Maria Moutafis, Director, Corporate Governance, OSFI
- Bill Parker, US Bank
- Marty Pfinsgraff, Risk Committee Chair, PNC Financial

- Nathalie Rachou, Non-Executive Director, Societe Generale
- David Roberts, Chair of the Board, Nationwide Building Society
- Alex Rolfe, General Business and Industry, FDIC
- John Sutherland, Senior Advisor, FCA
- Kevin Walsh, Deputy Comptroller for Market Risk, OCC

EY

- Omar Ali, Managing Partner, UK Financial Services
- Jan Bellens, Global Banking and Capital Markets Leader
- Anthony Caterino, Vice Chair, Regional Managing Partner, Financial Services Organization
- Peter Davis, Americas Financial Services Advisory Leader
- Gary Hwa, Global Financial Services Office Markets Executive Chair and Asia-Pacific Financial Services Office Regional Managing Partner
- James Karwel, Americas Banking and Capital Markets Leader
- Michael Lee, Global Wealth and Asset Management Leader
- John Liver, Partner, EMEIA Financial Services
- Nigel Moden, EMEIA Financial Services Banking and Capital Markets Leader
- Marc Saidenberg, Financial Services Global Regulatory Network Co-Lead, Principal US Financial Services Advisory
- Marcel van Loo, EMEIA Financial Services, Regional Managing Partner

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- Brennan Kerrigan, Senior Associate
- Tucker Nielsen, Principal