Bank of England PRA

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Executive Director, Authorisations, Regulatory Technology, and International Supervision

11 January 2024

Dear [Chief Executive Officer]

International banks Supervision: 2024 priorities

We are writing to update you on the Prudential Regulation Authority's (PRA) 2024 priorities for international banks and designated investment firms (together 'firms') active in the UK. These are intended to complement our ongoing supervision and the firm-specific feedback that you will have received following your most recent Periodic Summary Meeting (PSM). This thematic priorities letter is sent to the diverse range of firms that we supervise; therefore, it should not be viewed as exhaustive.

A common theme that underpins this year's priorities is the need for robust governance, risk management and controls at firms to enable the effective and proactive identification, assessment and mitigation of risks in an increasingly challenging and changeable operating environment. Boards and Executives should continuously challenge themselves to ensure they have appropriate structures, processes, capabilities and information in place within their own governance and risk management frameworks.

The events of 2023 show that firms can experience a sudden loss of customer, counterparty or market confidence, with damaging implications that can require regulatory intervention. Firms must remain vigilant and need to ensure they operate with an appropriate risk culture to promote safety and soundness. We expect individuals within our Senior Managers Regime to continue to lead the risk culture of their firms. Operating diverse and inclusive firms, with cognitive variety and clear encouragement to speak up, challenge and question supports prudent decision-making and risk management practices. Firms should also ensure there are appropriate succession plans in place across the Board and Executive to maintain strong governance, risk management and controls in the event there are changes in personnel.

Boards and those accountable need to continuously challenge current thinking and understand that previously improbable events could be within the realms of the possible. As part of this, firms should consider the novel risks that may arise from the rapidly growing use of new technologies. Firms are expected to be forward thinking and imaginative in the scenarios they consider, capturing extreme tail events and the risk management challenges these may present.

Through our supervisory engagement, we will continue to seek assurance that your overall governance, risk management and control frameworks are evolving in line with the changing environment, and the priorities set out in this letter.

We have set out our priorities for 2024 below.

Risk management and controls

Recent thematic reviews have shown that firms still consider risk management in silos, without considering the read-across to other businesses. Firms and their Boards should ensure that the issues highlighted in our 2021 Dear CEO letter on equity financing,[1] and more recently the Dear CRO letter on fixed income financing,[2] are addressed, and that due consideration has been given to how other businesses may be affected. We will continue to probe your firm and senior management on these topics through cross firm thematic reviews, while coordinating closely with international regulatory authorities.

Counterparty credit risk and secured financing risks will remain key priorities in 2024, with a particular focus on exposures to non-bank financial institutions (NBFI) across all business lines. We will look to assess whether your firm's counterparty risk management capabilities are appropriate for the challenges that may lie ahead. We will look for further improvements in firms' ability to identify and assess correlations across financing activities with multiple clients, and for market depth to be taken into

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1 Joint letter to banks operating in the UK: Supervisory review of global equity finance businesses following the default of Archegos Capital Management; available at: **www.bankofengland.co.uk/prudential-regulation/publication/2021/december/supervisory-review-global-equity-finance-businesses**, December 2021.

2 Letter from Nathanaël Benjamin and David Bailey – Fixed income financing thematic review; available at: **www.bankofengland.co.uk/prudential-regulation/letter/2023/fixed-income-financing-thematic-review**, October 2023.

consideration as quantitative tightening reduces the level of reserves in the financial system. We will seek to gain assurance that firms' overall risk management frameworks are evolving in line with the changing macro environment, and in particular that firms can identify and mitigate the novel risks that could arise from distributed ledger technologies and the rapidly growing use of generative AI. Firms with a strong risk culture will be better placed to address all of these issues, others may fail.

Financial resilience

The global macroeconomic outlook is highly uncertain and the risk environment is challenging. Inflation is declining but remains elevated, interest rates remain high and geopolitical tensions continue to introduce volatility. These combined factors place pressure on the finances of households and businesses which are supported by the UK banking sector and therefore on firms' credit portfolios. It is imperative that firms manage their financial resilience to ensure that the financial sector can continue to support businesses and households.

As part of this, firms should reflect on events that have taken place in the global banking sector during the course of 2023 and any implications they can draw from this for their own risk profiles. For example, firms should ensure their treasury management is robust and takes into consideration the interaction between capital and liquidity risks, including through interest rate risk as well as how hedging activity may affect the usability of liquid assets. We also expect firms to consider changes in depositor behaviour in the current funding environment and proactively take into consideration forthcoming changes in bank funding and liquidity conditions. In particular, this includes the normalisation of funding conditions as the COVID crisis-era TFSME[3] unwinds; the way in which quantitative tightening will affect the level of central bank reserves available in the system, and what these changes imply for the way in which firms source and manage liquidity moving forwards.

We will continue to focus on financial resilience through ongoing assessment of individual firm's capital and liquidity positions and planning. In assessing these risks, we will expect to see firms analysing a broad range of forward-looking liquidity and capital indicators, using stress testing to assess their financial resilience and to have realistic and effective contingency plans. Stress testing should not be a box ticking exercise, it needs to be well thought through and expose relevant issues for your firm.

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3 Term Funding Scheme with additional incentives for Small and Medium-sized Enterprises contractual repayments will start in March 2024; available at: **www.bankofengland.co.uk/markets/market-notices/2020/term-funding-scheme-market-notice-mar-2020**.

All firms should be mindful of the upcoming implementation of the Basel 3.1 standards[4] and should ensure that they plan accordingly to maintain financial resilience while continuing to support households and businesses.

We will focus on firms' continued monitoring and risk management of credit portfolios, in particular exposures to global commercial real estate, long dated infrastructure projects, as well as vulnerable sectors. We will continue to press firms to identify and manage counterparty concentrations, in particular across the NBFI sector. Firms should expect ongoing heightened engagement with us on counterparty and credit risk, including targeted requests for enhanced data and analysis.

Financial risks arising from climate change continue to present an increasingly material risk to firms and the financial system. Our assessment of firms against PRA expectations[5] indicates that, while firms are progressing their approaches to managing these risks, there is still considerable work for all firms to do in their development of climate-related financial risk management capabilities and linking these more concretely into decision-making.

During 2024, we expect firms to further progress and demonstrate the development and integration of processes to identify, measure, manage and mitigate climate-related financial risks in line with our expectations, including consideration of trading book exposures. Firms should also consider tailored and ambitious stress scenarios to enhance their assessment of the impact of climate change on their businesses and financial and operational resilience. We will continue to assess firms' progress in managing climate-related financial risks and expect firms to increase their efforts now. We will also commence work to update supervisory statement 3/19 which will include, among other things, identified effective practice and developments in wider regulatory thinking.

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4 PRA policy statement 17/23 – Implementation of the Basel 3.1 standards near-final part 1; available at: **www.bankofengland.co.uk/prudential-regulation/publication/2023/december/implementation-of-the-basel-3-1-standards-near-final-policy-statement-part-1**.

5 Supervisory statement 3/19 – Enhancing banks' and insurers' approaches to managing the financial risks from climate change; available at: **www.bankofengland.co.uk/prudential-regulation/publication/2019/enhancing-banks-and-insurers-approaches-to-managing-the-financial-risks-from-climate-change-ss**, April 2019 and letter from Sam Woods 'Thematic feedback on the PRA's supervision of climate-related financial risk and the Bank of England's Climate Biennial Exploratory Scenario exercise': **www.bankofengland.co.uk/prudential-regulation/letter/2022/october/managing-climate-related-financial-risks**, October 2022.

Operational resilience

Firms have just over a year left to meet the Operational Resilience expectations (as set out in supervisory statement 1/21).[6] By no later than March 2025, firms should be able to demonstrate that they can remain within impact tolerances for all their important business services (IBS). To get ready for this, firms should have a clear plan to identify and remediate any vulnerabilities which could impact their ability to deliver their IBS. This includes identifying which resources are needed to support the delivery of each IBS, running tests using scenarios which are severe but plausible and learning lessons from any operational disruptions. We expect these scenarios to include cyber-related disruptions, which will help firms to identify what is needed to both withstand a cyber-related incident and to recover from one. Boards and senior management need to actively oversee the delivery of their firms' operational resilience programme. As we have stated previously, we expect branches to have approaches that deliver similar outcomes. We will look to work with Home State Supervisors for both subsidiaries and branches.

We continue to observe firms engaging with third party providers (who may themselves have third party dependencies), undertaking significant transformations and utilising Cloud Computing capabilities. We expect these to be well managed in line with our supervisory statement 2/21,[7] including mitigating the risks associated with these relationships and notifying the PRA of material arrangements. Firms should also consider the impact of outsourcing and third party relationships for IBS (in line with SS1/21), identifying and mitigating vulnerabilities to ensure they can remain within impact tolerances regardless of third party involvement.

The RTGS Core Ledger[8] is scheduled to be replaced in June 2024. We expect all RTGS Account Holders, particularly participants in payment schemes, to manage these changes appropriately, participate in the Bank of England's testing and go live activities.

Data risk

As we have said before, the submission of complete, timely, and accurate regulatory returns remains the foundation of effective supervision. Our ongoing programme of

6 PRA supervisory statement 1/21 – Operational resilience: Impact tolerances for important business services: **www.bankofengland.co.uk/prudential-regulation/publication/2021/march/operational-resilience-impact-tolerances-for-important-business-services-ss**, March 2021.

7 March 2021: **www.bankofengland.co.uk/prudential-regulation/publication/2021/march/outsourcing-and-third-party-risk-management-ss**.

8 The renewed RTGS service – key benefits; available at: **www.bankofengland.co.uk/payment-and-settlement/rtgs-renewal-programme/the-renewed-rtgs-service-key-benefits**, April 2023.

skilled persons reviews of regulatory reporting across a significant sample of firms has repeatedly identified deficiencies in the controls over data, governance, systems, and production controls related to regulatory reporting. We expect firms to consider our feedback, take remedial action as needed, and maintain appropriate focus on regulatory reporting.[9] and we will continue to make targeted use of our supervisory tools in this area in 2024, including using skilled persons where appropriate.

Looking ahead, we are continuing our work on the long-term reforms to the way we collect data as part of the Transforming Data Collection Programme,[10] and on which data we collect as part of the Banking Data Review.[11] The first phase of our work focuses on improving the information received on firms' counterparty exposures, as well as identifying areas where we can reduce the information submitted by firms. We will continue to engage with you on these topics and via the industry forum.

This letter in conjunction with your firm's PSM letter, should convey a sense of our planned work for 2024.

Yours sincerely,

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Supervision

9 Letter from David Bailey and Rebecca Jackson 'Thematic findings on the reliability of regulatory reporting' available at: **www.bankofengland.co.uk/prudential-regulation/letter/2021/september/thematic-findings-on-the-reliability-of-regulatory-returns**, September 2021.

10 Available at: **www.transformingdatacollection.co.uk**.

11 Available at: **www.bankofengland.co.uk/prudential-regulation/banking-data-review**.