SPIRE SEARCH PARTNERS:
Model Risk Roundtable 2019

Topics:

- Regulatory Landscape
- Machine Learning
- Model Risk Appetite

Topic 1: Regulatory Landscape

Heads of Model Risk overwhelmingly agree that the ongoing evolution of the regulatory landscape is the #1 factor driving their agenda.

Even with the rising tide supporting a roll back of regulation, all attendees expect no net decrease in regulation – expectations are that:

a) other regulatory agencies/organizations will back fill any area of eased regulation with their own version of that regulation or simply increase their overall regulatory scrutiny

and,

a) While existing regulation may become less broad or far reaching it will instead become more deeply targeted in specific areas and perhaps more complex in those targeted areas requiring no net decrease in the resources and effort required

The differences in regulation between countries continues to be a major challenge for FBOs (Foreign Banking Organizations) operating in the US; those issues involve everything from regulation definition to documentation to model definition and beyond. Most FBOs however, are still in the earlier stages of their framework build out – so while they have the larger US banks as a model, they have yet to see how effective and efficient their frameworks function over longer periods of time.

Key Discussion Points:

o SR 11-7 continues to drive an environment of constant change which is in and of itself a risk being considered by the broader Ops Risk function

o For FBOs in the US, Model Risk leadership also need to contend with managing the differences between expectations / frameworks of the head office and that of the US regulatory construct. This was a topic central to our discussion last year.

Talent Landscape

- Model Risk leadership and CROs continue to place a high value on, and seek talent with, strong leadership and communication skills – this is in direct response to the need to interface with regulators and organizational leadership/boards etc.

- I have also seen an increase in these leadership/communication skills being required at the level or two down as well, perhaps as part of succession planning or a shift in key responsibilities down in the hierarchy as parts of the framework move into a BAU state

- More generally there is has been increased level of "readiness to move" for MRM talent from smaller banks and insurance companies in direct response to the shifting regulatory landscape

Topic 2: Machine Learning

Firms vary in the degree to which they are using ML/AI models; in some cases they are in a pilot phase and in some cases it's quite extensive – but in every case it is a priority topic for Heads of Model Risk. These types of models come with their own set of risks associated simply with their use. While areas such as fraud, AML and consumer marketing were early adopters of ML and AI techniques in their models, increasingly teams are seeing the technique/tool extend to commercial/wholesale credit and market risk.

JPM in particular had a separate group called JPMIS (recently split up into their relevant LOBs) that is working on the commercialization of AI/ML modeling techniques for a broad set of business issues across various LOBS including commercial lending.

Key Discussion Points:

- Vendor models – "black box" models built by outside vendors make up a significant percent of the total model inventory and create ongoing issues for validators

- Tool or Technique – in some cases there is still some question around how best to frame or categorize models that leverage ML/AI

- ML requires a more robust framework which should include ML specific risks such as overlearning. Organizations are still developing a sense of what it should look like and how it should function (ie: level of sensitivity, frequency of recalibration)

- Automation is another topic of interest as Model Risk leadership look to increase efficiencies in their teams and move parts of the framework into BAU. I include that here as many times I see ML talent in risk focusing more on building operational efficiencies than applying the technology to building/validating risk models

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Talent Landscape

There has been an overall increase in demand for ML/AI skilled talent as the applications of it move beyond front office research, fraud and marketing

Hedge Funds/Asset Managers
- Most hedge funds have made the switch to Python as their base language and so has the quantitative talent base
- Larger asset managers are slower to make that skill set/technology shift but in certain cases have make strategic hires in risk to gain credibility and proof of concept around the application of such techniques and promote a broader shift

Banks
- Across risk model development and model risk, the talent base is still in transition. Most are making their own efforts to develop their skills through online coursework and projects as well as online competitions like Kaggle
- This year however, these skills are in higher demand and I'm seeing more MRM professional educating themselves on AI/ML techniques in direct response to the types of models they have to validate
- Within the risk function, ML/AI techniques have been heavily applied to building operational efficiencies and therefore firms selectively seek out that experience
- Automation skills have been a priority skill set for talent in this space for some time; ML/AI has renewed and evolved those efforts

Topic 3: Model Risk Appetite

How model risk should be included in overall risk appetite continues to challenge most financial firms and their Model Risk function.

My contacts who head up operational risk more broadly, struggle with it as well and have been implementing tools/platforms to build a framework for calculating risk appetite.

ERM/ORM heads are increasingly implementing vendor tools and platforms to do this, but there are a number of concerns around those vendor's methods and how they fit into the organization's culture or existing framework. For example a tool might produce calculations for risk appetite that do not effectively convey the nature of the calculations; ie: a number representing a measurement giving a false sense of exactness.

On the back of the roundtables that I hold – risk appetite is typically an area most leaders want to break out to continue the conversation and work through issues with their peers.

Talent Landscape

Peers leading the broader Ops Risk organization are also struggling with risk appetite, but it's not that often that I find either function (Model Risk or Ops Risk) seeking out specialists with just this experience. Exception exist, however, with some of the very largest banks like JPM that have a stand alone "Firmwide Risk Appetite"(FRA) team.

That said it, the experience is certainly valued as part of a broader experience base – the sort of "cherry on top" of an already interesting candidate.

ABOUT SPIRE SEARCH PARTNERS

Launched in 2007 by two tenured financial recruiters both with financial industry experience, Spire Search Partners began as a collection of specialist teams working to provide talent across Risk, Compliance, Accounting/Finance and Quant Analytics to the financial services industry including capital markets, insurance, hedge funds and fintech firms.

In its 10 year history, the firm has placed 100s of specialized and high value professionals in both support and leadership roles with a selection of the top 20 banks, private equity funds, asset managers and insurance firms globally.

The firm has been a valued partner to organizations including Goldman Sachs, Morgan Stanley, TIAA-CREF, BlueMountain Capital, MSCI/RiskMetrics and others.

ABOUT ME

- Degrees in Economics and Finance from Gettysburg College, honors theses on Financial Market Cycles and Hedge Funds

- Early career in industry with Thomson Reuters & UBS Investment Bank in data analytics and delivery, client connectivity, client relationship management and project management

- Began recruiting in the financial services industry in 2004 with Core Financial before launching Spire in 2007

- Spent 1 year working abroad in Hong Kong and 2 years with a top global retained search boutique before rejoining Spire in 2017

- Extensive work for Global Association of Risk Professionals (GARP) as a career advisor and as a volunteer on the selection committee for Venture for America

DENNIS M. GRADY
Director of Risk Search & Market Intelligence
Spire Search Partners

☎ 646.328.1446
✉ dgrady@spiresearchpartners.com

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