A Quantitative Model to articulate the Banking Risk Appetite Framework

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Extended abstract

The purposes of this work are to analyse the structural aspects of the banking Risk Appetite Framework (RAF), and to provide an operational application in the light of the detailed recommendations of the banking supervisors. We develop a quantitative approach that could be used to adapt to the requirements of these regulations and that might be useful for management purposes. This approach is empirically applied to the balance sheets of the Italian banking system. Our main findings show critical single situations, according to the last EBAs’ stress test results, and significant differences across banks, even from the wholesale system. The value of our research could be mainly identified in its practical implications. In particular, external analysts (investors, shareholders, and any other stakeholders), by using our methodology with public information could derive the same significant results of supervisory authorities. Furthermore internal analysts could usefully adopt our methodology to comply with the RAF, as required by supervisory authorities. The present contribution can consequently serve as a useful and original methodological reference for quantifying and solving the numerous problems that will crop up in the course of action to comply with the recently-introduced requirements, as well as an attempt to overcome regulatory and theoretical shortcomings identified on the particularly urgent
and topical issue of risk management in banks. As future development of the research, the proposed quantitative model for first drafting a RAS and then obtaining a global RAF can be applied effectively to different types of risk, making the necessary adjustments according to the particular features of the profile being examined.

**Keywords**
Banks; Credit Risk; Market Risk; Operational Risk; Risk Appetite Framework; Risk Management.

**References**


