**Executive Summary: Capital Optimization & S-VaR Reduction**

The goal of this initiative is to assess whether **data enhancements alone can significantly reduce our S-VaR-to-J-VaR ratio (from 7x to 2x) or lower S-VaR P&L by 50-80%.** While there is **room for data improvement** (e.g., reducing proxies, increasing granularity, fixing incorrect mappings), the expected impact will be **marginal** unless the **pricing methodology, shifting methodology, P&L methodology, and exposure management are also revised.**

Currently, **COVID-19 stress scenarios drive capital requirements more than the 2008 GFC period.** Data refinements will offer noticeable improvements for 2008, but their impact on COVID-era capital charges will be limited. Structural factors such as **S-VaR shifts, hedging practices, and methodology choices** play a more significant role.

This discussion aims to clarify:  
✅ **The extent to which proxies, time series, and data issues impact capital requirements**  
✅ **Whether refining data alone can meaningfully reduce S-VaR or if broader methodological changes are required**  
✅ **Examples from different asset classes to illustrate where data enhancements will and won’t deliver meaningful capital relief**

**Key Considerations & Findings**

1️⃣ **Data Issues Exist, But They Are Not the Root Cause of High S-VaR**

* Common concerns: **incorrect proxies, lack of time series, overuse of proxies, and insufficient granularity.**
* Fixing these will **help** but will not single-handedly bring S-VaR down to peer levels.
* **Methodological choices (PnL shifts, pricing models, hedging) are the primary drivers.**

2️⃣ **2008 GFC vs. COVID-19: Where Data Enhancements Matter**

* **2008 GFC:**
  + Data issues (missing time series, incorrect proxies) significantly impacted results.
  + Improving data would **noticeably reduce capital charges** for that period.
* **COVID-19:**
  + Capital charges are driven by the nature of the shocks themselves, not just data quality.
  + **Data refinements alone won’t materially lower capital requirements.**

3️⃣ **Asset-Class-Specific Observations**

* **CMBS (Commercial Mortgage-Backed Securities)**  
  ✅ FNMA DUS is the main driver of P&L.  
  ✅ FNMA proxies all agencies – this is **reasonable and defensible**.  
  ⚠️ **Overuse of rating proxies in CMBS Non-Agency.**
  + Increasing granularity may offer **some** S-VaR benefit but could **expose hidden risks.**
* **RMBS (Residential Mortgage-Backed Securities) – Agency (TBA, Pool, CMO)**  
  ⚠️ CMO shifts **are higher than TBA shifts**, but they are:
  + **Driven by an approved model (CoE & TBA assumptions).**
  + **Backtested and regulatory-approved – model changes are unlikely to be approved.**  
    **🔍 Conclusion:** No major capital relief from data refinements.
* **CMBX (Commercial Mortgage-Backed Securities Index)**  
  ✅ **Large moves in S06 & S08 are expected.**  
  ✅ CMBX tranches mature in 10 years—maturity events drive volatility (sell-offs, extensions).
* **Credit (Corporate Bonds & CDS)**  
  ⚠️ **Heavy reliance on rating-based proxies.**  
  ⚠️ Granular risks are not always captured (e.g., individual issuer risk vs. broad rating category).  
  ✅ **If the portfolio is diversified (e.g., weighted toward JP Morgan bonds), data refinements offer little marginal benefit.**

**Conclusion & Next Steps**

✅ **Data refinements are necessary but will not drive transformational capital efficiency improvements.**  
✅ **S-VaR is primarily impacted by methodology choices, exposure management, and hedging practices.**  
✅ **COVID-era shocks drive capital more than 2008 GFC – data enhancements will have limited impact.**  
✅ **Refining proxies and granularity can offer small gains but won’t close the gap vs. peers (~7x to ~2x S-VaR ratio).**  
✅ **Leadership needs to decide: Are we willing to introduce hedging strategies or methodological shifts to optimize capital?**

📌 **Next Step:** Focus on **methodology refinements, potential hedging strategies, and further internal alignment on S-VaR methodology to assess where optimization is feasible.**