PRA publishes Business Plan 2024/25

24 Apr 2024

The Prudential Regulation Authority (PRA) has published its latest Business Plan, focusing on the strength of the banking and insurance sectors, identifying emerging risks, and supporting competitive markets. Paul Young looks at key points for financial services firms.

The regulator shared its annual plan on how it will deliver strategic goals, identifying three key objectives for 2024/25:

1 maintain and build on the safety and soundness of the banking and insurance sectors, and ensure continuing resilience

2 be at the forefront of identifying new and emerging risks, and developing international policy

3 support competitive and dynamic markets, alongside facilitating international competitiveness and growth

Bolstering banks

Basel 3.1

The first near-final PS on Basel 3.1 was published in December 2023. The PRA will soon publish the second near-final PS, covering the remaining elements of credit risk, the output floor, as well as Pillar 3 disclosure and reporting requirements. The PRA will increase supervisory focus on firms' implementation plans.

Bank stress-testing

The PRA will support the Bank of England in updating its framework for concurrent bank stress testing in 2024, drawing on lessons from the first decade of stress testing. The Bank is also conducting a system-wide exploratory scenario, working with the PRA, FCA, and TPR to improve understanding of the behaviours of banks and non-bank financial institutions in stressed financial market conditions.

Stress-testing exercises involving firm submissions of stressed projections are expected to resume in 2025.

Private equity and credit

The PRA is closely monitoring private asset-financing and the risks associated with illiquid private equity financing and private credit, particularly the potential challenges that may arise with exposures to non-bank financial institutions (NBFI).

The PRA will focus on improving firms' ability to identify and assess correlations across financing activities with multiple clients to ensure robust governance, risk management, and controls in the face of an evolving macro-environment that is expected to increase risk management challenges.

Replacing assimilated law

The PRA will consult on proposed rules in 2024/25 to replace relevant firm-facing provisions in Part Two of the CRR with modifications where appropriate, moving towards a more UK-style of regulation.

Model risk management (MRM) and internal ratings-based approach/hybrid models

The PRA will focus on how banks are implementing the principles set out in SS1/23 in 2024, and firms are expected to conduct an initial self-assessment and prepare remediation plans where necessary. The PRA will also continue to work with firms on changes to the IRB approach to credit risk, focusing on the hybrid approach to mortgage modelling and the IRB repair programme, and assess the adequacy of post-model adjustments to mitigate potential capital underestimation.

Liquidity risk management

The PRA will continue to closely supervise firms' liquidity and funding risks, with a focus on deposit outflows experienced by deposit takers and the lessons learnt from the events at CS and SVB.

The PRA will use its L-SREPs to assess firms' liquidity and funding risks and ensure appropriate resources are in place to manage and mitigate these risks. The PRA will also engage with firms and the wider Bank on access to the Sterling Monetary Framework and monitor how firms consider changes in depositor behaviour and forthcoming changes in bank funding and liquidity conditions.

Credit risk management

The PRA is closely monitoring firms' credit risk management practices, especially in light of the uncertain credit risk outlook across key markets.

The PRA will also monitor changes to firms' business mix and credit exposures, with counterparty credit risk remaining a key area of focus, and will undertake a thematic review of smaller firms' credit risk management frameworks in 2024/25.

In addition, the PRA will continue to review its regulatory policies on trading-book risk management, controls, and culture.

Capital

The PRA acknowledges that the UK banking system is well capitalised but the overall environment remains challenging, requiring firms to manage their financial resilience.

The PRA will assess firms' capital positions and planning, including their use of forward-looking capital indicators, stress testing, and contingency plans.

The PRA plans to review its Pillar 2A methodologies for banks after the finalisation of rules on Basel 3.1, with a view to consulting on any proposed changes in 2025.

Securitisation regulation

HMT has prioritised the Securitisation Regulation in transferring assimilated law into regulatory rules and legislation, and the PRA will publish its final policy on replacing or modifying relevant firm-facing provisions in 2024-25.

The PRA intends to consult on draft rules to replace firm-facing requirements, and has gathered views and evidence through DP3/23 to inform its approach to capital requirements for securitisation.

Strengthening the insurance sector

Solvency II reporting reforms

The PRA has published PS3/24, which includes finalised templates and instructions for Solvency II reporting and disclosure phase 2. A single taxonomy package will be published in 2024 Q2, and industry roundtables will be held to help firms prepare for new reporting requirements. The PRA will engage with firms to ensure they can meet the new requirements by the deadline.

Solvency II transfer

The PRA will transfer the remaining Solvency II requirements into the PRA Rulebook and other policy material, which will create a more comprehensive Rulebook and make it easier for firms to navigate the rules that apply to them. A CP will be published in 2024 H1 to outline how this will be done.

Insurance stress-testing

The next stress test for major life insurers will take place in 2025. For the first time, the PRA will publish the individual results of the largest annuity-writing firms to strengthen market discipline.

The PRA will also run its first dynamic stress test for general insurers in 2025, which will involve simulating a sequential set of adverse events over a short period of time. The PRA will engage with industry trade bodies and provide more details on the exercise in 2024.

Cyber underwriting risk

The PRA will share the findings of its recent thematic project on cyber underwriting risk with the industry and continue to identify and assess potential risk drivers.

Model drift

The PRA identified several findings in its 2023 model drift analysis related to non-life firms' levels of allowances for inflation uncertainty, expected underwriting profits, reinsurance costs and benefits, and limited allowance for economic and geopolitical uncertainties.

In 2024, the PRA will address systemic trends that may weaken model robustness across the market and focus on improving internal model validation to enable firms to identify and address potential challenges.

Funded reinsurance

The PRA will closely monitor the increasing use of funded reinsurance transactions in the UK life insurance market and the risks they pose to policyholder protection and UK financial stability, particularly regarding erosion in asset collateral standards and concentrated exposures to credit-focused counterparties.

The PRA will examine exposures to the recapture of funded reinsurance in the 2025 life insurance stress test and finalise its policy expectations for UK life insurers that use funded reinsurance arrangements in 2024.

Impact on general and claims inflation

While reserves have increased, the PRA anticipates a continued lag in the emergence of claims inflation in the data, which insurers should be alert to. The PRA will continue to monitor the impact through regulatory data and supervisory activities in 2024. If the PRA's assessment of the risk changes, it may consider further focused work.

Liquidity risk management

The PRA will develop liquidity reporting requirements for insurance firms most exposed to liquidity risk, building on the existing liquidity framework set out in SS5/19.

The PRA will work closely with firms to inform them about these requirements and explore the necessity of a minimum liquidity requirement as part of a future policy consultation.

Credit-risk management

The expected growth in the bulk purchase annuity (BPA) market may lead to further credit risk exposure and potentially concentrations in internally valued and rated assets.

The PRA will continue to focus on the effectiveness of firms' credit risk management capabilities and assess the evolution of their credit risk management frameworks in line with supervisory expectations. The PRA will review the suitability of firms' current and forward-looking internal credit assessment validation plans and approaches and provide feedback on a firm-specific or thematic basis as appropriate.

Cross-sector

Operational risk and resilience

The PRA will work closely with the FCA to assess firms' progress, particularly their ability to deliver important business services within defined impact tolerances during severe but plausible scenarios over a reasonable timeframe, and no later than March 2025. The PRA will also monitor threats to firms' resilience, such as growing dependency on third parties, while maintaining proportionality.

Critical third parties to the UK financial sector

In December 2023, the PRA, Bank, and FCA jointly published CP26/23 - Operational resilience: Critical third parties to the UK financial sector, proposing how these powers could be used to assess and strengthen the resilience of services provided by CTPs to firms and FMIs, reducing the risk of systemic disruption. The PRA will work with other authorities to develop the final policy and oversight approach in 2024.

Additionally, the PRA is developing regulatory expectations on incident reporting, aligned with its operational resilience expectations.

Review of enforcement policies

The PRA is committed to holding individuals accountable and taking regulatory and/or enforcement action against those who breach its standards.

In January 2024, the PRA published PS1/24 - The Bank of England's approach to enforcement, which sets out the revised approach to enforcement across the Bank's full remit, including when acting as the PRA. PS1/24 introduced a new Early Account Scheme (EAS) that provides a new path for early cooperation and greater incentives for early admissions to reach outcomes more quickly in specific cases.

Diversity and inclusion in PRA-regulated firms

In September 2023, the PRA published CP18/23 - Diversity and inclusion in PRA-regulated firms, proposing that all in-scope firms must understand their D&I position, develop appropriate strategies to make meaningful progress, and monitor and report on progress.

In 2024, the PRA will continue its industry engagement, assess responses to CP18/23, and provide a further update in due course.

Identifying emerging risks and supporting competitive markets

The PRA also outlined it’s focus on it’s two other objectives.

On identifying and mitigating emerging risks, the regulator laid its plans on:

- international engagement and influencing regulatory standards
- supervisory co-operation
- overseas bank branches
- operational and cyber resilience
- managing the financial risks arising from climate change
- artificial Intelligence and Machine Learning
- international policy on digitalisation and managing associated risks
- digital money and innovation

On maintaining market competition, the PRA highlighted its commitments on:

- regulatory change – embedding the PRA's approach to rule-making
- secondary competitiveness and growth objective (SCGO)
- strong and simple framework
- insurance Special Purpose Vehicles regime
- remuneration reforms
- implementing changes to the Senior Managers & Certification Regime (SM&CR)
- complete the establishment of the Cost Benefit Analysis (CBA) Panel
- PRA Rulebook
- banking Data Review
- supporting and authorising new market entrants via new 'mobilisation' regime
- ease of exit
- ring-fencing regime
- effective authorisation processes

To learn more about the PRA's areas of focus, contact Paul Young.

Authors

- 

  Paul Young Paul Young, I lead a team of technical SMEs covering all aspects of finance, risk and compliance. We review operational models for these functions as well as detailed subcomponents such as credit, market, operational risk, regulatory reporting (COREP/FINREP/BOE), Senior Manager Regime, AML, financial crime, CASS, market abuse etc. View Profile