independent middle office that's doing the number crunching."

Sorasio adds that the EBRD is somewhat more limited in terms of its risk taking than typical commercial banks.

"We do not take any risk in equities, commodities or foreign exchange," he says. The bank takes no active positions in such markets – and any risks arising in them are hedged immediately.

• Bonds and swaps

EBRD deals mainly in fixed income instruments. It also trades interest rate swaps and currency swaps to hedge bond issues and some caps/floors, says Sorasio.

The risk management enhancement program was established at in the spring of last year, adds le Blanc. It deals with a number of issues related to organising the bank's risk management and procedures.

"We've ranked ourselves against the G30's recommendations on the use of derivatives," says le Blanc. "At this moment we're complying with all those recommendations at the level of an end-user. But we would like to go a little bit beyond that – so there are a number of things to do."

Besides creating the risk control unit, the bank is also taking other steps to meet the G30 guidelines. These include increased disclosure of derivatives use in EBRD's annual report.

The bank's 1995 annual report is due out in the next few weeks, says le Blanc. "This is the first time we are going to disclose some of our treasury activities, particularly those related to the use of derivatives." ■

Technology & Integration

First Union Bank develops fixed income risk management system

U.S. super-regional First Union National Bank of North Carolina's Section 20 securities subsidiary has gone live with a proprietary value-at-risk market and credit risk management system.

First Union officials say the bank built the new system for two purposes: to provide internal risk management and to comply with the Bank for International Settlements' Tier II capital standards.

Russ Hovanec, fixed income manager at First Union, anticipates the unit's use of the VAR system evolving over time to include designing structured fixed income hedging strategies.

• Automated VAR

"The idea was to take all the positions in our Section 20 portfolios and be able to run them through a risk model, producing daily VAR figures in an automated fashion," says Hovanec.

First Union's new system supports VAR analysis for the entire range of the subsidiary's fixed income portfolios, including government bonds, corporate bonds, municipal bonds, mortgage-backed securities, money market instruments, OTC options on cash bonds and options on fixed income futures.

The bank brought its new VAR-based risk management system online last year. It is linked to market data sources and stores 180 days worth of market history. The system also includes yield curve generators that drive the VAR calculations using stress-testing and benchmarking techniques.

First Union's project was completed in relatively short period of time, says Hovanec. The bank hired a team of risk management consultants that helped to integrate data and design the unit's VAR methodologies.

The application was then benchmarked with other systems and external sources. "Thus far, the system has performed up to our expectations," says Hovanec.

"We brought it up in a little over four months. That included building the system's methodology, getting it all together and doing the stress-testing and benchmarking."

'You have to realise that you're going to be facing issues where there are no accepted standards'

In addition to its Section 20 subsidiary, First Union has formed an independent five-member risk management group that validates the bank's overall VAR models and performs its own risk analysis.

Hovanec says the construction