GLOSSARY

Asset-backed commercial paper (ABCP)	A secured money market debt instrument typically issued by a bank or other financial institution, usually with a maturity of between 90 and 180 days. ABCP is secured by the issuer with the cash flow from a pool of underlying assets such as trade receivables, car loans, or credit card loans.
Asset-backed security (ABS)	A security that is collateralized by the cash flows from a pool of underlying assets, such as loans, leases, and receivables. When the underlying asset is real estate, an ABS is called a mortgage-backed security (MBS). MBS collateralized by mortgages on commercial property are called commercial-mortgage-backed securities (CMBS).
Automatic stabilizer	An existing government tax or payment program in which revenues and expenses automatically increase or decrease to dampen fluctuations in real GDP without any explicit policy action. Examples are unemployment compensation and corporate and individual income taxes.
Basel II	A 2004 accord among national bank supervisory authorities (the Basel Committee on Banking Supervision) that revised the committee's 1988 adequacy standards for bank capital. Basel II proposals made the capital requirement more sensitive to variations in the riskiness of the bank's assets. Basel II also revised its recommended supervision processes and proposed increased disclosure by banks. Pillar 1 of the accord covers the minimum capital adequacy standards for banks; Pillar 2 focuses on enhancing the supervisory review process; and Pillar 3 encourages market discipline through increased disclosure of banks' financial conditions.
Carry trade	A leveraged transaction in which borrowed funds are used to take a position in which the expected interest return exceeds the cost of the borrowed funds. The "cost of carry" or "carry" is the difference between the interest yield on the investment and the financing cost (e.g., in a "positive carry" the yield exceeds the financing cost).
Charge-off	Declaration by a lender that a debt is unlikely to be paid in full.
Clearing	The process of transmitting, reconciling, and, in some cases, confirming payment orders or security transfer instructions prior to settlement. Clearing may include the netting of cash flows and the establishment of final positions for settlement. It can be bilateral or multilateral.
Cliff effect	An abrupt and outsized change (most commonly a drop) in the value of a financial asset or firm beyond expectations based on past prices and the variance around these prices.
Collateral	Assets pledged to a lender to secure a loan. The collateral may be seized by the lender if the borrower fails to meet the repayment terms of the loan.

Committee of European Banking Supervisors (CEBS)	Composed of high-level representatives from the bank supervisory authorities and central banks of the countries in the European Union. It gives policy advice to the European Commission on bank supervision and regulation, promotes the convergence of supervisory practice across the European Union, and facilitates consistent implementation of its guidelines.
Counterparty risk	The risk that one of the parties to a contract fails to meet its payment obligations.
Credit default swap (CDS)	A derivative of a credit instrument that offers protection against a "credit event" involving a weakening (or, most commonly for CDS, default) of the underlying credit instrument (the "reference asset"). The CDS buyer does not necessarily own the reference asset. Payouts under a CDS, which are triggered by a credit event, are "physical" or in "cash." In physical settlement, the protection seller buys the impaired reference asset from the protection buyer at its face value. In a cash settlement, the protection seller pays the protection buyer the difference between the face value of the reference asset and its current market price. In a single-name CDS contract, the reference asset is a single firm or government agency. CDS index contracts reference standardized indices based on baskets of liquid single-name CDS contracts.
Credit derivative	A financial contract that protects against the credit risk associated with a specific reference entity (or specified range of entities). For a periodic fee, the protection seller agrees to make a payment to the buyer in case of a "credit event" involving a weakening of the credit quality or default of the reference entity.
Credit rating	A rating of a debt issuer or debt instrument that measures the risk that repayment terms will not be honored. Ratings, which are issued by private credit rating agencies, are typically expressed as letter grades.
Credit rating outlooks, reviews, and watches	Credit rating agencies typically signal in advance their intention to consider rating upgrades and downgrades. "Reviews" or "watches" indicate that a change is likely within 90 days, and "outlooks" indicate the potential for a change within two years (one year in the case of speculative-grade credits).
Credit spread	The difference in yield between a benchmark debt security and another debt security that is comparable to the benchmark instrument in all respects except that it is of lower credit quality and hence, typically, of higher yield.
Cumulative accuracy profile (CAP), and accuracy ratio	CAP curves and accuracy ratios are statistical tools used by the credit rating agencies to validate the ability of their ratings to rank order default risk.
Delinquencies	Failure to make contractual payments on a loan, usually defined as a payment that is a certain number of days (or more) overdue (e.g., 90 days or more).
EMBIG	Emerging Market Bond Index Global, provided by JPMorgan Chase, which tracks the total returns for traded external debt instruments in 34 emerging market economies with weights roughly proportional to the market supply of debt.

European Financial Stability Facility (EFSF)	An institution set up by the 16 euro area countries to preserve financial stability. The EFSF can provide financial assistance to euro area national governments by selling bonds or other debt instruments on the open market. Such instruments are backed by an allocation of funds from the member countries. The EFSF's funds can be combined with loans from the European Financial Stabilization Mechanism (EFSM), with funds raised by the European Commission and guaranteed by the EU budget, and with funds from the IMF.
Event study	A statistical method to assess the short-term impact of an event, such as an announcement of a new credit rating.
Exchange traded fund (ETF)	An investment fund traded on stock exchanges. In many cases, the price tracks an index, such as the S&P 500. ETFs offer low costs and tax efficiency.
Financing gap	In this report, the gap between projected credit demand and projected credit supply. When the time of the projected credit demand arrives, changes in interest rates and the use of quantity rationing bring credit demand and supply into balance.
Foreclosure	The act of a mortgage lender that takes ownership of the residential or commercial real estate pledged as collateral on a loan that has become delinquent. The intention of the lender in foreclosing is to sell the real estate to recover part or all of the amounts due from the borrower.
Funding	In this report, the process by which banks issue or assume liabilities that are associated with assets on their balance sheets. In retail funding, the liabilities are to individual and business depositors. In wholesale funding, they are to institutional investors.
Funding liquidity risk	Risk that a financial institution will not be able to meet its short-term payment obligations by raising the funds from unsecured sources such as very short term loans from other banks or the issuance of certificates of deposits and commercial paper.
Generally accepted accounting principles (GAAP)	National guidelines for financial accounting.
Government-sponsored enterprise (GSE)	A financial institution established by government but privately owned to provide credit or credit insurance to specific groups, such as farmers, homebuyers, or students. In the United States, the housing-related GSEs Fannie Mae and Freddie Mac were placed under the conservatorship of the federal government in 2008.
Haircut	A discount applied by a lender to the current market value of collateral that it receives as security for a loan. The haircut reflects the risk that, at a later date, if the borrower defaults, the collateral may be worth less or be less easy to sell.
Hedge fund	An investment pool, typically organized as a private partnership or entity. Being only lightly regulated, hedge funds are more free than other types of investment vehicles to combine a variety of investment techniques—including short positions, transactions in derivatives, and high leverage.
Hedging	Offsetting an existing risk exposure by taking an opposite position in the same or a similar risk—for example, in related derivatives contracts.

Home Affordable Modification Program (HAMP)	A U.S. Treasury program providing incentives to qualifying mortgage borrowers and their servicers to modify the loan's terms, such as monthly payment amount or balance owed, to improve its affordability.
Home bias	The tendency to invest or spend in the domestic market rather than in the international market.
Intangible assets	See tangible assets.
Interest rate derivative	An investment contract whose yield is linked to that of one or more reference interest rates.
International Financial Reporting Standards (IFRS)	The business accounting framework adopted by the International Accounting Standards Board (IASB). Widely used in the European Union and Japan. U.S. and other national authorities using their own versions of generally accepted accounting principles (GAAP) are in various stages of conversion to IFRS.
Investment- and speculative grade	An entity or transaction is considered to be investment-grade if its credit rating is BBB- or better (Baa3 on the Moody's scale). Otherwise it is considered speculative, or high-yield, grade.
Jump-to-default risk	The risk that a credit counterparty defaults before a lender, bondholder, or exposed counterparty has time to sell or hedge its position.
Large and complex financial institution (LCFI)	A financial institution involved in a diverse range of financial activities and, often, geographical areas. Typically it is interconnected to other financial institutions and is thus considered systemically important.
Lender of last resort (LOLR)	An institution willing to extend credit when no one else will. Such an institution is usually a country's central bank, which acts as a wholesale lender of last resort. A lender of last resort serves as a stopgap to protect depositors, prevent widespread panic withdrawals from depository institutions, and otherwise avoid disruption in intermediation that can harm the real economy.
Leverage	The proportion of debt to equity (also assets to equity or capital to assets in banking). Leverage can be built up by borrowing (on-balance-sheet leverage, commonly measured by debt-to-equity ratios) or by using off-balance-sheet transactions. In this report, the term is also used to refer to the ratio of credit to GDP.
LIBOR	The London interbank offered rate, an index of the interest rates at which banks offer to lend unsecured funds to other banks in the London wholesale money market.
Loss-sharing (or loss allocation) agreement	An agreement among participants in a clearing or settlement system regarding the allocation of any losses arising from the default of a participant in the system or of the system itself.
Margin call	The additional collateral requested when the value of the original collateral falls below a specified amount.
Mark-to-market valuation	The act of recording the price or value of a security, portfolio, or account to reflect its current market value rather than its book value.

Market liquidity risk	Element of liquidity risk related to a financial institution's capacity to meet short-term payment obligations by means of secured funding sources. The risk is that the market value of collateral pledged as part of the institution's funding operations could rapidly decline.
Money market mutual fund	An open-ended mutual fund that invests in short-term securities.
Moral hazard	The incentive of individuals or firms to take unreasonable risks when the consequences will not be borne by them. For example, financial institutions have incentives to take excessive risks if they believe that governments will step in and provide support to them in crisis periods.
Mortgage-backed security (MBS)	A security that derives its cash flows from principal and interest payments on pooled mortgage loans. MBSs can be backed by residential mortgage loans or loans on commercial properties.
Nonbank financial institutions	A financial institution that does not have a full banking license or is not supervised by a national or international banking regulatory agency. These institutions facilitate bank-related financial services, such as investment, risk pooling, contractual savings, and market brokering, and can include money market mutual funds, investment banks, finance companies, insurance firms, pension funds, hedge funds, currency exchanges, and microfinance organizations.
Over-the-counter (OTC) derivative	A financial contract whose value derives from underlying security prices, interest rates, foreign exchange rates, commodity prices, or other market indices, and that is traded bilaterally rather than through an exchange.
Overnight index swap (OIS)	An interest rate swap in which the compounded overnight rate in the specified currency is exchanged for some fixed interest rate over a specified term.
Point-in-time (PIT) and through-the-cycle (TTC) credit ratings	With through-the-cycle ratings, credit rating agencies seek to ensure rating stability by assigning ratings based on the entity's or transaction's ability to survive cyclical troughs. Point-in-time ratings tend to focus on current conditions.
Primary dealer	Financial institutions that actively participate in the issuance of local and global equity and fixed income securities and derivatives and act as market makers. They are mainly large commercial and investment banks and securities houses.
Procyclicality	The tendency of asset prices to move in the same direction as changes in macroeconomic outlook and financial sector performance. In secured funding markets, the application of mark-to-market valuations of collateral causes large price movements, first with increases in collateral values and lower margin in the upswing of a financial or economic cycle and then to a rapid escalation of margin requirements and accelerating declines in prices in the downswing.
Quantitative easing	An expansion of a central bank's balance sheet through purchases of government securities, funded through the creation of base money (reserve balances of banks and cash).

Regulatory arbitrage	An action by a regulated institution to exploit differences in regulatory treatment across countries or different sectors, as well as differences between economic risk and risk measured by regulatory guidelines, to reduce regulatory burden—typically, in the case of financial institutions, to reduce regulatory capital requirements.
Repurchase (repo) agreement	A sale of securities coupled with an agreement to repurchase the same securities at an agreed price at a future date. This transaction occurs between a cash borrower (or securities lender), typically a fixed-income securities broker-dealer, and the cash lender (or securities borrower), such as a money market mutual fund or a custodial bank. The securities lender receives cash in return and pledges the legal title of a security as collateral.
Risk aversion	The degree to which an investor who, when faced with two investments with the same expected return but different risk, prefers the one with the lower risk. That is, it measures an investor's aversion to uncertain outcomes or payoffs.
Securities Markets Program (SMP)	A program under which the European Central Bank intervenes to restore depth and liquidity to dysfunctional segments of euro area public and private debt securities markets. The aim is to support the operation of the monetary policy transmission mechanism.
Securitization	The creation of securities from a reference portfolio of pre-existing assets or future receivables that are placed under the legal control of investors through special intermediaries created for the purpose, known as special-purpose vehicles or special-purpose entities. So-called synthetic securitizations are created from a portfolio of derivative instruments.
Segregation	A method of protecting client assets by holding them separately from those of a custodian, other clients, or other parties acting on behalf of the client.
Settlement	The act that discharges obligations involving funds or securities transfers between two or more parties.
Structured investment vehicle (SIV)	A legal entity whose assets consist of asset-backed securities and various types of loans and receivables. An SIV's funding liabilities are usually divided into segments of varying risk and include short-and medium-term debt. The solvency of the SIV is put at risk if the value of its assets falls below the value of its liabilities.
Sudden stop	A sudden slowdown in private capital inflows into emerging market economies. Sudden stops are usually followed by a sharp decrease in output, private spending and credit to the private sector, and real appreciation of the currency.
Swap	An agreement between counterparties to exchange periodic payments based on different reference financial instruments or indices on a predetermined notional amount.
Swap spread	The differential between the government bond yield and the fixed rate on an interest-rate swap of the equivalent maturity.

Systemic (solvency) risk	The risk that the failure of a financial institution would cause large losses to other financial institutions, thus threatening the stability of financial markets.
Tangible assets (TA)	Total assets less goodwill, deferred tax assets, and other intangible assets.
Tangible common equity (TCE)	Total balance sheet equity less preferred debt less intangible assets.
Through-the-cycle (TTC) credit ratings	See point-in-time (PIT) and through-the-cycle (TTC) credit ratings.
Tier 1 capital	The core capital supporting the lending and deposit activities of a bank. It consists primarily of common stock, retained earnings, and perpetual preferred stock.
Too-important-to-fail institutions	Private financial institutions believed to be so large, interconnected, or critical to the workings of the financial system that their disorderly failure would threaten the stability of the financial system and hence of the real economy.
Trade repository	A storage center where electronic records of trades are kept. It captures various contractual details, such as counterparty identifiers, payment dates, and calculation methods.
Tripartite (or tri-party) repo	A tri-party agent facilitates a repo transaction by providing operational services, such as custody of securities, settlement of cash and securities, valuation of collateral, and optimization tools to allocate collateral efficiently.
Value-at-risk (VaR)	An estimate of the loss, over a given period, that is unlikely to be exceeded at a given level of statistical probability, usually as calculated according to historical returns, covariances, and volatilities.
Writedown	A recognition by a financial institution that the value of an asset has declined.