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The Modeling Continuum

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Abstract

Because there are so many models and so many different ways to build them, the task of organizing our thinking about models can seem overwhelming. Sorting these differences into a framework should help our understanding of models and model risk management. The paper proposes four categories that form a continuum from least to most complex. The categories are identified as "simple factor," "complex single scenario," "constrained multi-scenario" and "unconstrained enterprise specific." The categories are compared across seven different attributes. With this comparison as a framework, a number of practical questions are addressed. These include whether some modeling approaches are better than others, or whether different approaches are better for different purposes, and whether all models should aim for the same level of model risk management maturity.

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