

#### **Basel III**

### Updates on the current status of regulatory work

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Frankfurt, Germany
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Note: Any opinions expressed are only the presenters' own and should not be regarded as opinions of the European Central Bank or the Eurosystem.

#### **Outline**

#### 1. Leverage ratio

- Objectives and original proposal (Basel III)
- Proposed revisions (June 2013 consultative paper)
- Reactions and open issues

#### 2. Liquidity Coverage Ratio (LCR)

- Objectives
- January 2013 revisions
- On-going work

#### 3. Net Stable Funding Ratio (NSFR)

- Objectives
- On-going work

# Leverage Ratio: Objectives and original proposal

- 2 objectives: (i) Constrain the build-up of leverage in the banking sector and (ii) reinforce the risk-based requirements with a simple, non-risk based "backstop" measure
- Design/formula:

Leverage ratio = Capital measure (Tier 1 capital according to the new definition)

Exposure measure (on-balance sheet and off-balance sheet items)

- Exposure measure:
  - On-balance sheet items (accounting measure), with specific treatments for
  - Securities and Financing Transactions (SFTs), including repos:
     Accounting measure of exposure and "Basel II netting"
  - <u>Derivatives</u>: Accounting measure of exposure + Add-on for potential future exposure (PFE)
  - Off-balance sheet items (OBS): Apply credit conversion factors (CCFs)

# Leverage Ratio: Proposed revisions (June 2013)

- Consultative document (June 2013): Revised Basel III leverage ratio framework and disclosure requirements
- Revisions to the framework relate primarily to the exposure measure
  - Specification of a broad scope of consolidation for the inclusion of exposures: Exposure measure to be measured consistently with capital
  - Clarification of the general treatment of derivatives and related
     collateral: Specification of netting rules; no netting of collateral
  - Enhanced treatment of written credit derivatives: To account for notional credit exposure arising from the creditworthiness of the reference entity
  - Enhanced treatment of Securities Financing Transactions: No accounting netting; add-on for counterparty credit risk (current exposure)

## Leverage Ratio: Reactions and open issues

- Consultative ended on 20 September 2013: 63 feedback letters received
- Main issues: Calibration, incentives, scope of consolidation and modalities of the calculation; the Basel Committee is currently looking into the following:
  - Securities and Financing Transactions: The required gross treatment
     (the ECB is currently analysing potential monetary policy implications)
  - **Derivatives:** Treatment of collateral and centrally cleared derivatives
  - Written credit derivatives: Maximum possible loss; eligible hedges
  - Off-balance sheet items: Introduce a more gradual treatment?
  - Frequency of calculation: Average of the 3 month-end LR over a given quarter <u>OR</u> simple quarter-end calculation?
  - Scope of consolidation: Prudential <u>OR</u> extended scope (June 2013)?

# Liquidity Coverage Ratio

- **Objective:** To establish a minimum level of high-quality liquid assets to withstand an acute stress scenario lasting one month
- **Design/formula:**  $\frac{Stock\ of\ high\ quality\ liquid\ assets}{Net\ cash\ outflows\ over\ a\ 30-day\ time\ period} \geq 100\%$
- January 2013 revisions: (i) inclusion of an additional level of liquid assets; (ii) material revisions in in- and outflow factors and (iii) a long phase-in
- Remaining work by the Basel Committee:
  - Disclosure framework: Starting date, Granularity, Frequency.
  - Interaction with monetary policy: Restricted-Committed Liquidity
     Facility
  - Market-based indicators of liquid assets: Assess options to define highquality liquid assets based on quantitative asset characteristics
- Work under the EBA on MBI: large scale quantitative assessment; EBA public hearing suggested some important departures from Basel definition

# Net Stable Funding Ratio

• **Objective:** To ensure a closer alignment of the funding of longer-term assets or activities by more stable medium or longer-term liability and equity financing

Available amount of stable funding

• Design/formula:  $\frac{\text{Preduced amount of stable funding}}{\text{Re quired amount of stable funding}} > 100\%$ 

- Issues under discussion: general calibration of the NSFR
  - Below 1-year bucketing
  - Encumbrance
  - Short-term matched funding
  - Derivatives
- QIS Indications
  - Based on 2010 NSFR Basel banks report an NSFR of 100% (42% meet 100% minimum)

## Set of Monitoring Tools

• **Objective:** to complement the LCR and to further strengthen and promote global consistency in liquidity risk supervision.

#### • Set of tools:

- Contractual maturity mismatch
- Concentration of funding by counterparty and product
- Available unencumbered and encumbered assets
- By significant currency

#### Issues of on-going work under EBA

- Implementation time (1 January 2015)
- Remittance period (15 days)
- Proportionality criteria (balance sheet size and cross-border activities)