

Basel III

Updates on the current status of regulatory work

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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:**

$$\text{Leverage ratio} = \frac{\text{Capital measure (Tier 1 capital according to the new definition)}}{\text{Exposure measure (on-balance sheet and off-balance sheet items)}}$$

- **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”
- Derivatives: *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 OR simple quarter-end calculation?*
 - *Scope of consolidation: Prudential OR 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:**
$$\frac{\text{Stock of high quality liquid assets}}{\text{Net cash outflows over a 30 – day time period}} \geq 100\%$$
- **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 high-quality 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
- **Design/formula:**
$$\frac{\text{Available amount of stable funding}}{\text{Required amount of stable funding}} > 100\%$$
- **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)