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Swedish Bankers' Association



PROPOSED CHANGES TO THE BASEL COMMITTEE / EU CRD IV PROPOSAL FOR NEW LIQUIDITY REGULATIONS

The proposed changes focus on the criteria for the eligibility of covered bonds in the liquidity reserve. Anyway, we think that it is necessary to extend the range of assets which may be included in the liquidity reserve considerably.

Below are listed specific proposed changes to Points 35 and 37 of the Consultative Document "International framework for liquidity risk management, standards and monitoring" issued by the Basel Committee on Banking Supervision on 17 December 2009. Changes are marked with red font.

Liquidity coverage ratio - Definition of liquid assets

35. In addition, the Committee will gather data on the following instruments to analyse the impact of this standard on the financial sector. If included in the stock of liquid assets, these instruments would receive substantial haircuts corresponding to central bank haircuts ; would comprise not more than 50% of the overall stock, and the portfolio would have to be diversified. The haircut would be applied to the current market value of the respective asset. Diversification requirements will apply to all assets. Diversification requirements will be set by national supervisors taking into account the structure of liquidity assets within different markets or currency areas.

37. Covered bonds that, depending on their credit assessment, receive either a 20% or a 40% haircut and satisfy all of the following conditions:

- ~~Central bank eligibility for intraday liquidity needs or overnight liquidity shortages in relevant jurisdictions.~~
- ~~Not issued by the bank itself.~~
- ~~Low credit risk: assets have a credit assessment by a recognised ECAI of at least AA (assigned a 20% haircut), or A- (assigned a 40% haircut), or do not have a credit assessment by a recognised ECAI and are internally rated as having a PD corresponding to a credit assessment of at least AA or A-, respectively.~~
- ~~Traded in large, deep and active markets characterised by a low level of concentration. The bid-ask yield spread has not exceeded 50 bps during the last 10 years or during a relevant period of significant liquidity stress.~~
- ~~Proven record as a reliable source of liquidity in the markets (sale) even during stressed market conditions: ie, maximum decline of price or increase in haircut over a 30-day period during the last 10 years or during a relevant period of significant liquidity stress not exceeding 10%.~~

Covered bonds can be included if they satisfy the following conditions. These include qualitative requirements as well as conditions on a market level and the level of the single covered bond issuer. All three sets of criteria should be met for a covered bond to be eligible for the liquidity buffer:

Qualitative requirements:

- The issuer is subject to special public regulation and supervision and the bonds are covered by high quality assets defined by law (collateral) which are capable of continuously covering claims to the bonds and – in the case of the default of the issuer – would be used in priority to the bond holders (preferential claim)).
- The legal framework requires or the issuers are committed to providing information on the cover pool to investors regularly and at least every three months.

Market level:

- Market depth and significance of the covered bond market within the country's economy
The minimum market size measured by volume of covered bonds issued to be 50bn euro (or euro equivalent) or 25 per cent of total bonds outstanding issued by financial institutions within the jurisdiction.
 - Significance of the covered bond market
The minimum market size measured by outstanding covered bond volume being greater than 15 per cent of national GDP as an average over the last five years.
- Transparency
Transparent pricing and post trade information.

Issuer level

- Minimum outstanding covered bond volume at issuer level
Minimum outstanding volume at issuer level to be 1bn euro (or euro equivalent).
- Central bank repo eligibility
Central bank eligibility for intraday liquidity needs or overnight liquidity shortages in relevant jurisdictions.

Covered bonds issued by the bank itself can be included if they additionally satisfy the following conditions:

- Evidence of legal constraints
The legislation behind the covered bonds ensures bankruptcy remoteness and the issuance of the covered bonds is constrained by the volume of unencumbered assets eligible as collateral for covered bonds on the balance sheet of the issuer.
- Evidence of market robustness
The market of the covered bonds has not significantly been influenced by material events in relation to an issuing bank.
- Evidence of uniform credit quality
The covered bonds are traded at spreads not substantially different from spreads on other covered bonds issued by the bank itself taking account of differences in term to maturity, coupon etc.
- Evidence of third party investors
60 per cent of all covered bonds, backed by the same cover pool, are held by third party investors (outside group).

Net stable funding ratio - Definition of available stable funding

86. Table 1 below summarises the components of each of the ASF categories and the associated maximum ASF factor to be applied in calculating an institution's total amount of available stable funding under the proposed standard.

Table 1 Components of Available Stable Funding and Associated ASF Factors	
ASF Factor	Components of ASF Category
100%	<ul style="list-style-type: none"> The total amount of capital, including both Tier 1 and Tier 2 as defined in existing global capital standards issued by the Committee. The total amount of any preferred stock not included in Tier 2 that has an effective maturity of one year or greater taking into account any explicit or embedded options that would reduce the expected maturity to less than one year. The total amount of secured and unsecured borrowings and liabilities (including term deposits) with effective maturities of one year or greater excluding any instruments with explicit or embedded options that would reduce the expected maturity to less than one year.
[100%]	<ul style="list-style-type: none"> <u>The total amount of issued covered bonds with a maturity of less than one year that has historically proven to be a stable source of funding and where a conservative refinancing plan exists. The respective covered bond market should be a liquid covered bond market (as defined in the LCR). The issuing credit institution has to show that the issuance conditions of covered bonds have historically not been significantly influenced by heightened credit risk for the institution. In addition, the maturing of covered bond should avoid a concentration at a single point of time.</u>
85%	<ul style="list-style-type: none"> "Stable" non-maturity retail deposits and/or term retail deposits (as defined in the LCR) with residual maturities of less than one year. "Stable" unsecured wholesale funding, non-maturity deposits and/or term deposits with a residual maturity of less than one year, provided by small business customers (as defined in the LCR). This category consists of deposits and other extensions of funds made by non-financial small business
70%	<ul style="list-style-type: none"> "Less stable" (as defined in the LCR) non-maturity retail deposits and/or term retail deposits with residual maturities of less than one year. "Less stable" (as defined in the LCR) unsecured wholesale funding, non-maturity deposits and/or term deposits with a residual maturity of less than one year, provided by small business customers (as defined above). <p>Less stable deposits, as outlined in the LCR and determined by each jurisdiction, could include deposits which are not covered by effective deposit insurance, high value-deposits, deposits of sophisticated or high net worth individuals and deposits which can be withdrawn quickly (eg internet deposits) and foreign currency deposits.</p>
50%	<ul style="list-style-type: none"> Unsecured wholesale funding, non-maturity deposits and/or term deposits with a residual maturity of less than one year, provided by non-financial corporate customers.
0%	<ul style="list-style-type: none"> All other liabilities and equity categories not included in the above categories

Net stable funding ratio - Definition of required stable funding for assets and off-balance sheet exposures

89. Table 2 briefly summarises the specific types of assets to be assigned to each asset category and their associated RSF factor. Diversification requirements will apply to all assets including holdings of assets with a zero per cent required funding factor. Diversification requirements will be set by national supervisors taking into account the structure of liquidity assets within different markets or currency areas. Annex 2 fully outlines the assets in each category and should be used by banks in conducting the NSFR.

Table 2 Summary Composition of Asset Categories and Associated RSF Factors (see Annex 2 for full description)	
Summary Composition of Asset Categories	Summary Composition of Asset Categories
Cash, money market instruments Securities with effective remaining maturities of less than one year Outstanding loans to financial entities having effective maturities of less than one year.	0%
Unencumbered marketable securities with residual maturities \geq one year representing claims on sovereigns, <u>regional governments, local authorities</u> , central banks, BIS, IMF, EC, non-central government PSEs or multilateral development banks which are rated AA or higher and are assigned a 0% risk weight under the Basel II standardised approach, provided that active repo-markets exist for these securities.	5%
<u>Unencumbered covered bonds with an effective maturity of \geq one year which are eligible as high quality liquid assets in the LCR, i.e. traded in large, active and liquid markets with transparent pricing and which at issuer level also have a demonstrated history of being a reliable liquidity source. Self issued covered bonds included if they are eligible under the LCR.</u>	<u>[0]%</u>
<u>Unencumbered covered bonds with an effective maturity of \geq one year which are not eligible as high quality liquid assets in the LCR.</u>	<u>[15]%</u>
<u>Unencumbered marketable securities with residual maturities \geq one year representing claims on sovereigns, regional governments, local authorities and PSEs which are assigned a 20 % risk weight under the Basel II standardised approach.</u>	<u>[15]%</u>
Unencumbered corporate bonds (or covered bonds) rated at least AA with an effective maturity of \geq one year which are traded in deep, active and liquid markets and which also have a demonstrated history of being a reliable liquidity source in a stressed market environment.	20%
Gold Unencumbered equity securities listed on a major exchange and included in a large capital market index and unencumbered corporate bonds rated AA- to A- with an effective maturity of \geq one year, which are traded in deep, active and liquid markets and which also have a demonstrated history of being a reliable liquidity source in a stressed	50%

market environment.	
Loans to non-financial corporate clients having a residual maturity of less than one year.	
Loans to retail clients having a residual maturity of less than one year.	85%
All other assets.	100%