



South African Reserve Bank
From the Office of
the Registrar of Banks

C5/2010

2010-12-14

To: All banks, branches of foreign institutions, controlling companies, and auditors of banks or controlling companies

Circular 5/2010 issued in terms of section 6(4) of Banks Act, 1990

Interpretation and application of criteria relating to the granularity for retail exposures

Executive summary

It has come to the attention of this Office that there appears to be uncertainty among banks that adopted the standardised approach (STA) for credit risk with regard to the interpretation and application of the criteria relating to the granularity of retail exposures, as outlined in regulation 23(8)(b) read with regulation 23(6)(b) of the Regulations relating to Banks. This uncertainty has resulted in inconsistency in capital calculations and reporting of regulatory retail exposures in the BA returns.

The purpose of this Banks Act circular is to provide clarity on the interpretation and application of the granularity criteria for retail exposures as specified in regulation 23(8)(b) read with regulation 23(6)(b) of the Regulations relating to Banks. This circular also serves to provide clarity regarding the reporting of the retail asset class for the STA.

1. Introduction

- 1.1 It has come to the attention of this Office that there appears to be uncertainty among banks that adopted the standardised approach (STA) for credit risk with regard to the interpretation and application of the criteria relating to the granularity of retail exposures, as outlined in regulation 23(8)(b) read with regulation 23(6)(b) of the Regulations relating to Banks (the Regulations). This uncertainty has resulted in inconsistency in capital calculations and reporting of regulatory retail exposures in the BA returns.
- 1.2 For an exposure to be included in a bank's retail portfolio and consequently, be risk weighted at the preferential risk weight of 75 per cent, it has to meet **all** four criteria specified in regulation 23(6)(b) of the Regulations.

- 1.3 For example, the Regulations require that the retail portfolios of banks should be sufficiently diversified to warrant a 75 per cent risk weight. In this regard, for inclusion in the retail portfolio, banks are required, among other things, to ensure that no aggregate exposure to a person exceeds 0,2 per cent of the aggregate amount relating to the bank's retail portfolio (i.e., the granularity criteria for retail exposures).
- 1.4 The purpose of this Banks Act circular is to provide clarity regarding the interpretation and application of the granularity criteria for retail exposures as specified in regulation 23(8)(b) read with regulation 23(6)(b) of the Regulations relating to Banks. This circular also serves to provide clarity regarding the reporting of the retail asset class for the STA.

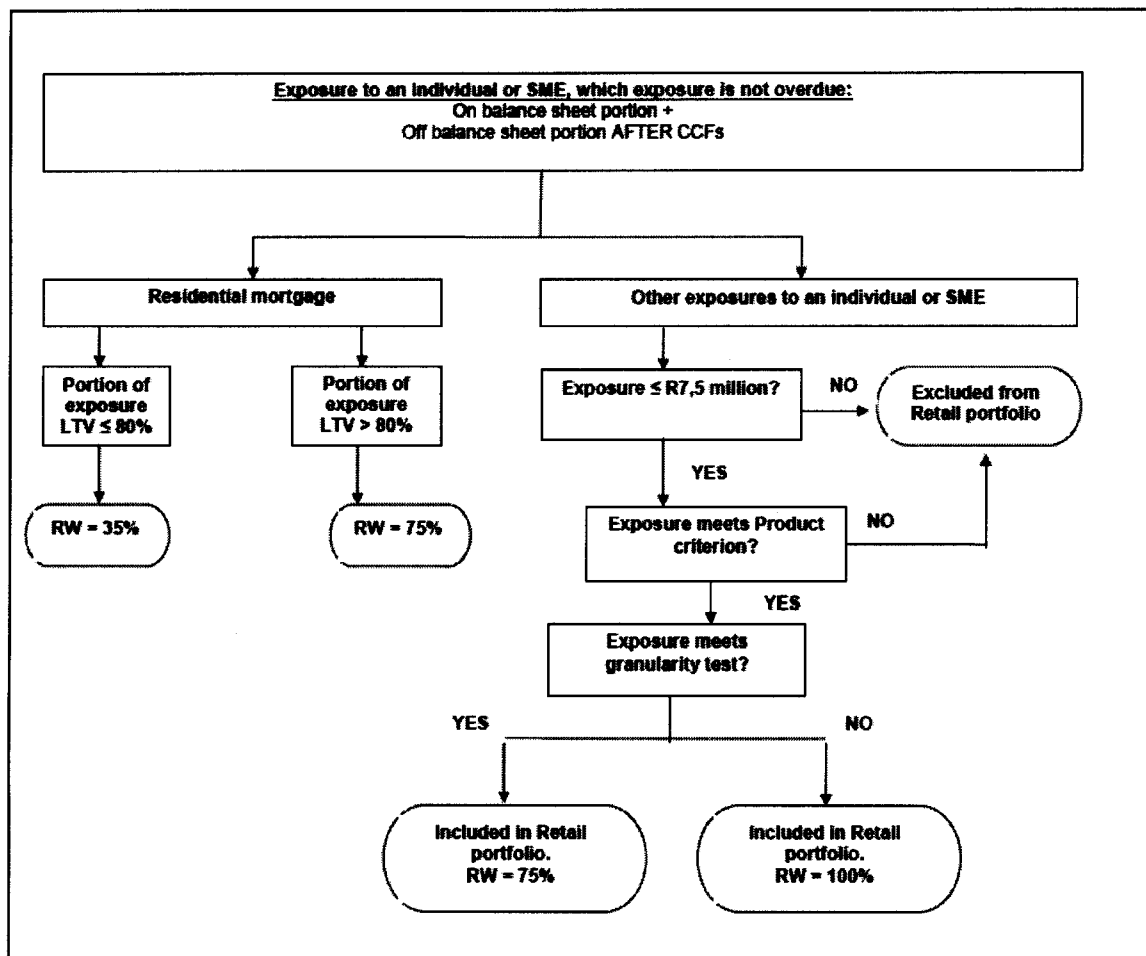
2. Regulation references

- 2.1 Regulation 23(8)(b) read with regulation 23(6)(b)(iii) of the Regulations stipulates that for an exposure to be included in the bank's retail portfolio and, consequently, be risk weighted at the preferential risk weight of 75 per cent, a bank shall, among other things, apply the granularity criteria to this exposure.

3. Banks Act circular

- 3.1 This Office's application and interpretation of regulation 23(8)(b) read with regulation 23(6)(b) of the Regulations is set out below:
 - 3.1.1 The aggregate exposure to a person referred to in regulations 23(6)(b)(iii) and 23(6)(b)(iv) of the Regulations shall be calculated *after* the application of the relevant specified credit conversion factors (CCFs).
 - 3.1.2 Furthermore, regulation 23(6)(b)(ii) of the Regulations specifically excludes residential mortgage loans, as specified in regulation 23(6)(c) of the Regulations from the category of retail exposures to which a risk weight of 75 per cent is applied.
 - 3.1.3 If the aggregate exposure, excluding residential mortgage loans, to a person is in excess of R7,5 million, the person shall be excluded from the retail portfolio.
 - 3.1.4 To ensure that the retail portfolio is sufficiently diversified, the granularity criteria are applied to the remainder of the retail portfolio as discussed above. In cases where the aggregate exposure to a person exceeds the 0,2 per cent threshold calculated by the bank at each reporting date, the exposure shall remain in the retail portfolio for regulatory reporting purposes and be risk weighted at 100 per cent.

3.2 The impact of the above interpretations on the classification of retail-exposures can be summarised as follows:



3.2.1 The above interpretation can be further explained by way of the following example:

Information of Bank X

Total retail portfolio, excluding any exposures that are overdue, after the application of the specified CCFs:	R1,35 billion
Mortgage loans that are included in the category of claims secured by residential property	R0,30 billion
Aggregate exposures, excluding residential mortgage loans, to persons that individually exceeded the threshold of R7,5 million	R0,05 billion

Step 1: Exclude residential mortgages

Total retail portfolio, excluding any exposures that are overdue, after the application of the specified CCFs: R1,35 billion

LESS Mortgage loans that are included in the category of claims secured by residential property R0,30 billion

R1,05 billion

Step 2: Exclude exposures to a person in excess of R7,5 million

Retail portfolio excluding residential mortgage loans R1,05 billion

LESS: Exposures to persons that individually exceeded the threshold of R7,5 million R0,05 billion

R1 billion

Step 3: Calculate the 0.2 per cent threshold

Threshold (R1 billion x 0.2 per cent) R2 million

Step 4a: Aggregate exposures to a person that meet the relevant other requirements relating to retail exposures and are less than, or equal to, R2 million shall be risk weighted at 75 per cent.

Step 4b: Aggregate exposures to a person that meet the relevant other requirements relating to retail exposures and are greater than R2 million shall be risk weighted at 100 per cent and included in the retail portfolio for regulatory reporting purposes.

4. Acknowledgement of receipt

- 4.1 Two additional copies of this Banks Act circular are enclosed for the use of your institution's independent auditors. The attached acknowledgement of receipt, duly completed and signed by both the chief executive officer of the institution and the said auditors, should be returned to this Office at the earliest convenience of the aforementioned signatories.



E M Kruger
Registrar of Banks

The previous circular issued was Banks Act Circular 4/2010, dated 1 November 2010.