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South African Reserve Bank
Prudential Authority

Ref.: 15/8/1/1

C2/2025

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

Draft Circular issued in terms of section 6(4) of the Banks Act 94 of 1990

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

<u>Executive summary</u>

The purpose of this draft 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 proposed amendments to the Regulations relating to Banks (Regulations). This draft Circular also serves to provide clarity regarding the reporting of the retail asset class on the standardised (STA) approach for credit risk which impacts the calculation of the minimum required amount of capital and reserve funds, and the related reporting requirements.

The draft Circular will become effective from the implementation date of the proposed amendments to the Regulations.

This draft Circular is intended to replace Circular 5 of 2020, dated 7 December 2020. As such, Circular 5 of 2020 shall be withdrawn upon implementation of this draft Circular.

1. Introduction

1.1 Regulation 23(8)(b), read with regulation 23(6)(b), of the proposed amendments to the Regulations specifies, among others, criteria relating to the granularity of retail exposures.

1.2 For an exposure to be included in the retail portfolio and consequently risk-weighted at the preferential risk weight of 75 per cent, it has to meet all five criteria specified in regulation 23(6)(b) of the proposed amendments to the Regulations.

1.2.1 For example, the proposed amendments to the Regulations require that the retail portfolios must be sufficiently diversified to warrant a 75 per cent risk weight. In this regard, for inclusion in the retail portfolio, banks, controlling companies and branches of foreign institutions (hereinafter collectively referred to as ‘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).

1.3 Furthermore:

1.3.1 the aggregate exposure to a person[1] referred to in regulations 23(6)(b)(iii) and 23(6)(b)(iv) of the proposed amendments to the Regulations must be calculated after the application of the relevant specified credit conversion factors (CCFs).

1.3.2 regulation 23(6)(b)(ii) of the proposed amendments to the Regulations specifically excludes exposures to retail products such as securities (listed and unlisted, bonds and equities), derivative instruments and residential mortgage loans, from the category of retail exposures to which a risk weight of 75 per cent is applied.

1.3.3 regulation 23(6)(b)(v) of the proposed amendments to the Regulations provides information on the treatment of other retail exposures and how these should be risk-weighted (i.e. the regulatory retail exposures that arise from exposures to transactors).

1.3.4 If the aggregate exposure[2] to a person is in excess of R12.5 million, the person must be excluded from the retail portfolio.

1.4 The purpose of this draft 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 proposed amendments to the Regulations.

2. Clarification of the application of the granularity criteria

2.1 The Prudential Authority's application and interpretation of regulation 23(8)(b), read with regulation 23(6)(b) of the proposed amendments to the Regulations is set out below:

2.1.1 To ensure that the retail portfolio is sufficiently diversified, the granularity criteria is applied to the remainder of the retail portfolio, after taking the relevant requirements envisaged in paragraphs 1.2 and 1.3 into consideration. In cases where the aggregate exposure to a person exceeds the 0.2 per cent threshold, excluding past due loans, as 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.

2.1.2 The granularity criteria should be applied to the total retail exposure of the banking group to a person, that is, on a controlling company consolidated basis. This means that exposures classified as retail exposures to the same counterparty across multiple banking group entities should be aggregated for the purposes of meeting the granularity criteria. This approach ensures that the banking group's total retail exposure to a single counterparty is fully captured, regardless of how these exposures are distributed among the various banking group entities.

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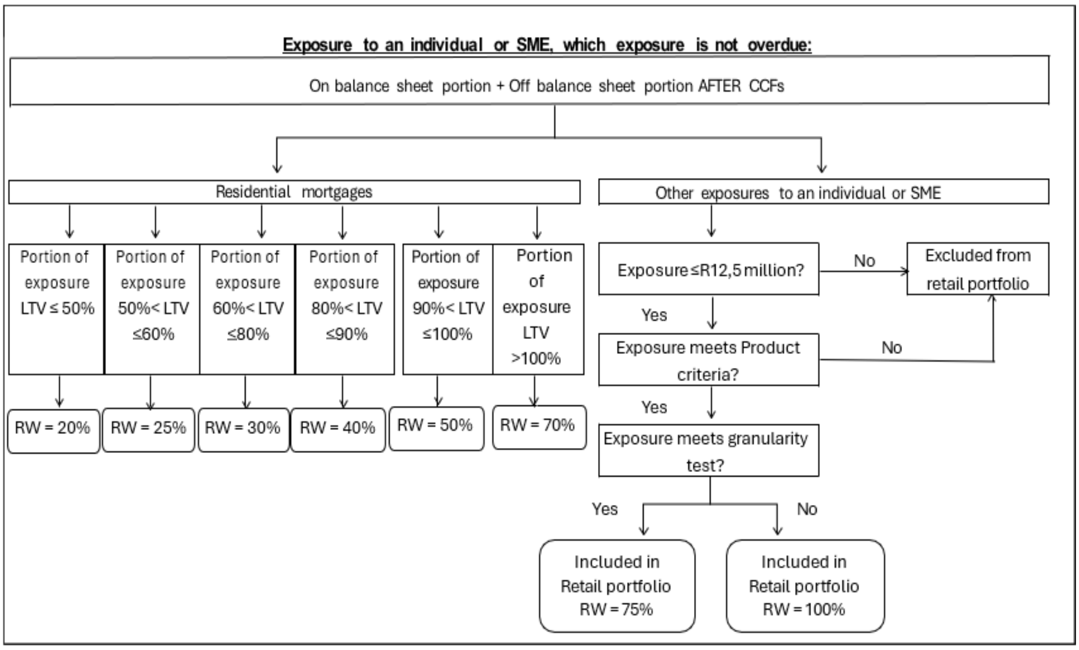
1 As defined in regulation 67 of the Regulations.

2 Aggregate exposure means the gross amount of all forms of debt included in the retail portfolio, before any form of credit risk mitigation is taken into consideration, excluding residential real estate exposures (refer to regulation 23(6)(b)(iv) of the proposed amendments to the Regulations).

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



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

Information of Bank A

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 R12.5 million	R0.05 billion

Calculation of threshold for Bank A

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 R12.5 million	
Retail portfolio, excluding residential mortgage loans	R1.05 billion
Less: Exposures to persons that individually exceeded the threshold of R12.5 million	(R0.05 billion)
	R1 billion
Step 3: Calculate the 0.2 per cent threshold	
Threshold (**R1 billion x 0.2 per cent**)	**R 2 million**

Step 4: Apply risk weights
Step 4a: Aggregate exposures to a person that meets the relevant other requirements relating to retail exposures[3] 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 meets the relevant other requirements relating to retail exposures[3] and are greater than R2 million shall be risk weighted at 100 per cent and included in the retail portfolio for regulatory reporting purposes.

3. Effective date

3.1 The respective requirements specified in this draft Circular shall be effective from the implementation date specified in Guidance Note 3/2023.

4. Acknowledgement of receipt

4.1 Kindly ensure that a copy of this draft Circular is made available to 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 the PA at the earliest convenience of the aforementioned signatories.

Fundi Tshazibana

Fundi Tshazibana
Chief Executive Officer

Date: 22/05/25

[3] Requirements contemplated in regulations 23(6)(b)(i) to 23(6)(b)(iv) of the of the proposed amendments to the Regulations.