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South African Reserve Bank
Prudential Authority

Ref.: 15/8/1/3

D11/2022

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

Directive issued in terms of section 6(6) of the Banks Act 94 of 1990

National discretion related to the liquidity coverage ratio

Executive summary

The purpose of this Directive is to replace Directive 7/2014 which was issued by the Prudential Authority (previously the Bank Supervision Department) to communicate to the industry the decisions related to national discretion items to be applied by banks, branches of foreign institutions and controlling companies (hereinafter collectively referred to as 'banks') in the calculation of the liquidity coverage ratio (LCR).

1. Introduction

1.1 The amended Regulations relating to Banks (Regulations) included the framework for the LCR which was implemented with effect from 1 January 2013.

1.2 The Basel III LCR framework[1] makes provision for supervisors to specify factors relating to national discretion items.

1.3 Since the issuance of Directive 7/2014, the environment within which banks conduct business has changed.

1.4 As such, this Directive replaces Directive 7/2014.

2. Directive on items of national discretion related to the LCR

2.1 Based on the aforesaid information, and in accordance with the provisions of section 6(6) of the Banks Act 94 of 1990, banks are hereby directed as follows:

2.1.1 Treatment of cash reserves when calculating the bank's LCR:

i. Banks must include their statutory cash reserves as envisaged in Regulation 27(2) of the Regulations as Level 1 high-quality liquid assets (Level 1 HQLA); and

ii. All excess cash reserve balances held in a bank's settlement account at the end of the day, at 23h59, must also be included as part of the bank's level 1 HQLA.

[1]Basel Committee on Banking Supervision. January 2013. *Basel III: The Liquidity Coverage Ratio*

2.1.2 Haircuts on level 1 HQLA

i. The Prudential Authority (PA) regards it as appropriate at this stage not to impose haircuts on South African level 1 HQLA.
ii. Furthermore, for the purposes of banks' holding of foreign currency-denominated level 1 HQLA to cover foreign currency-denominated net cash outflows, banks must implement the same haircuts specified by the relevant home central bank in its open market operations for those specific assets.

2.1.3 Use of level 2B HQLA

i. The PA shall allow the use of level 2B HQLA envisaged in the Regulations, subject to the limits, haircuts and qualifying criteria specified for those relevant assets specified in the revised Basel liquidity framework read with the related amended Regulations.
ii. In the case of equities, the PA shall only consider equities listed on the JSE's main exchange and included in the Top 40 Index for inclusion as level 2B HQLA.

2.1.4 Foreign-currency liquid assets

i. The PA has decided to permit foreign-currency denominated level 1 HQLA to be kept for LCR compliance in the local currency, that is, to cover domestic currency net cash outflows until 31 December 2023. Banks are therefore allowed to hold liquid assets in a currency that does not match the currency of the associated liquidity risk. However, this does not detract from the requirement for banks to hold foreign currency denominated HQLA to cover foreign currency denominated net cash outflows, although compliance is only measured in the consolidated reporting currency.

In addition, currencies will be limited to the top ten most liquid currencies as determined in the Triennial Central Banks Survey on Foreign Exchange Turnover, as published by the Bank of International Settlements from time to time. This foreign currency denominated HQLA shall be subject to an 8% haircut. Banks are also reminded to continue to comply with the net open position limits as specified from time to time when managing foreign currency mismatches.

2.1.5 Retail deposits: less-stable deposits

i. Banks must apply a 10 per cent run-off factor for less-stable retail deposits.

2.1.6 Retail term deposits

i. The run-off factor for all retail term deposits with a residual maturity or notice period greater than 30 days, as contemplated in regulation 26(12)(d)(ii) of the Regulations, shall be 3 per cent. This is in accordance with paragraph 84 of the Basel III LCR standard. As such, no retail term deposits shall be excluded from the LCR calculation. The determination of early withdrawal penalty fees relating to retail term deposits is at each bank’s discretion.

2.1.7 Foreign-currency deposits

i. Foreign-currency deposits shall receive the same treatment as rand-denominated deposits for each type of deposit and deposit counterparty as specified in the LCR framework read with the related Regulations.

2.1.8 Other contingent funding obligations

i. The following run-off factors shall apply to revocable liquidity and credit facilities related to specified counterparties:
   a. retail and small business clients shall be subject to a 2,5 per cent run-off factor;
   b. all other credit and liquidity facilities shall be subject to a 5 per cent run-off factor.

ii. Contingent funding obligations shall be assigned the following run-off factors:
   a. guarantees shall be subject to a 5 per cent run-off factor;
   b. letters of credit shall be subject to a 5 per cent run-off factor;
   c. non-contractual obligations
      i. potential debt buy-back requests of the bank's own debt or that of related conduits (including but not limited to negotiable certificates of deposits and instruments with similar characteristics) shall be subject to a 5 per cent run-off factor;
      ii. structured products shall be subject to a 5 per cent run-off factor;
      iii. managed funds shall be subject to a 5 per cent run-off factor;
      iv. other non-contractual obligations shall be subject to a 5 per cent run-off factor;
      v. for issuers with an affiliated dealer or market maker, the amount of outstanding debt securities with a remaining maturity of greater than 30 days shall be subject to a 5 per cent run-off factor to cover the potential repurchase of such outstanding securities; and
      vi. non-contractual obligations where other customer's collateral covers customer short positions shall be subject to a 50 per cent run-off factor.

2.1.9. Trade finance instruments

i. Contingent funding obligations relating to trade finance instruments shall be subject to a run-off rate of 2,5 per cent.

2.1.10. The PA reserves the right to reassess and revise any of the aforementioned factors or requirements should it be deemed appropriate.

3. Acknowledgement of receipt

3.1. Kindly ensure that a copy of this Directive is made available to your institution's external auditors. In addition, 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: 14/12/22

The previous Directive issued was Directive 10/2022, dated 30 September 2022.