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South African Reserve Bank
Prudential Authority

SARB 100 YEARS 1921–2021
A purposeful journey

Ref.: 15/8/1/3

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

Proposed directive issued in terms of section 6(6) of the Banks Act 94 of 1990:

Capital framework for South Africa based on the Basel III framework

Executive summary

The amended Regulations relating to Banks (the Regulations), which set out, among other things, the prescribed minimum required capital ratios and various components of the capital requirements, were implemented with effect from 1 January 2013.

This proposed directive serves to inform all relevant persons of matters related to the prescribed minimum required capital ratios as well as the application of various components of the said capital requirements such as the systemic risk capital requirement (Pillar 2A), the domestic systemically important bank (D-SIB) capital requirement, the countercyclical buffer range and the capital conservation buffer range.

This proposed directive replaces Directive 2/2020, issued in April 2020, and Directive 4/2020, issued in August 2020.

1. Introduction

1.1 In line with the international implementation of the Basel III framework on 1 January 2013, the South African capital framework is set out in the Regulations, which were also implemented with effect from 1 January 2013.

1.2 In order to prevent any potential ambiguity, Annexure A of this directive stipulates the various capital tiers, together with various related elements specified in the Regulations and in the Basel III framework, including the systemic risk capital requirement (Pillar 2A), the bank-specific individual capital requirement (ICR), also known as Pillar 2B, the D-SIB capital requirement and the minimum requirements that must be maintained by all banks. The D-SIB capital requirement is specific to each bank or banking group, based upon criteria related to systemic importance.

2. Minimum capital requirements

2.1 Regulation 38(8)(e)(ii) of the Regulations prescribes that the capital requirement for systemic risk (i.e. Pillar 2A) will be specified by the Prudential Authority (PA). The Pillar 2A requirement may therefore also be revised from time to time.

2.2 The Pillar 2A capital requirement, temporarily reduced to 0% of risk-weighted exposures for all banks at a total capital level, will be reinstated, as set out in Annexure B. In order to assist banks in appropriately managing their capital plans, the PA hereby notifies banks that the combined total capital adequacy requirement in respect of the Pillar 2A and the higher loss absorbency (HLA) requirement for D-SIBs will not exceed 3.5% of a bank's risk-weighted exposure. The aggregate requirement will not exceed 2% for common equity tier 1 (CET 1) and 2.5% for tier 1.

2.3 Furthermore, excluding both bank-specific ICR and the countercyclical buffer requirement, the highest minimum total capital adequacy requirement to be met by any bank or banking group conducting business within South Africa receiving the highest possible HLA requirement for a D-SIB will not exceed 14%.

2.4 The PA will specify the HLA requirement for each individual bank or banking group identified as a D-SIB in terms of regulation 38(8)(e)(vi) of the Regulations. The HLA requirement will accordingly vary between banks identified as D-SIBs. The PA has decided to apply a 'bucketing approach' when assigning the relevant HLA requirement for D-SIBs. The PA reviews the systemic importance of banks and banking groups on a continuous basis and will continue to advise entities identified as D-SIBs in writing of this fact, including the individual HLA requirements assigned to them. The HLA requirement for a D-SIB is regarded as an extension of the capital conservation buffer, and the consequences applicable to breaching the capital adequacy requirement at the capital conservation buffer level will also apply to breaching the combined total of the capital conservation buffer and the HLA requirement for a D-SIB. The first 1% of the specified D-SIB capital requirement, up to a maximum of 1% of a bank's risk-weighted exposures, must be fully met by CET 1 capital and reserve funds. Any additional requirement, up to the first 1.5% of risk-weighted exposures may be met by tier 1 capital and reserve funds. Any additional requirement to the aforementioned requirement, up to 2.5% of risk-weighted exposures, may be met with total capital and reserve funds.

2.5 The PA will continue to assess the bank-specific ICR as part of its supervisory review and evaluation processes. These supervisory assessments may attribute ICRs in order to address specific risks identified by the PA in terms of the provisions of regulation 38(8)(e)(iii), read with regulation 38(4) of the Regulations. Any ICR may also be based on the levels of economic capital a bank holds to cover risks not regarded as Pillar 1 risks, as observed in the Internal Capital Adequacy Assessment Process (ICAAP) of a bank. The PA will continue to utilise this supervisory tool to increase or decrease the level of ICR; however, factors that form part of the D-SIB capital framework will no longer form part of the ICR framework.

2.6 In the event that a bank's capital adequacy ratios fall below the levels set out in Annexure A and Annexure B (South African minima, including the countercyclical buffer, the conservation buffer and the HLA requirement for D-SIBs), and in the absence of other remedial actions acceptable to the PA to improve the bank's capital adequacy ratios, capital conservation ratios will be imposed that will limit discretionary payments such as dividend distributions. These limits will be increased as a bank's capital levels approach the specified minimum requirements. Once imposed, capital conservation measures will remain in place until such time as minimum required capital adequacy ratios have been restored.

If a bank seeks to make payments in excess of distribution limits, sufficient capital will have to be raised to fully compensate for the excess distribution. A bank will be required to discuss this alternative with the PA as part of the bank's ICAAP.

2.7 Banks should maintain an additional discretionary capital buffer above the specified minimum requirements, as envisaged in regulation 38(8)(e)(vii) of the Regulations, to ensure that the execution of internal business objectives or the occurrence of adverse external environmental factors do not prevent banks from operating above the relevant minima. The PA will continue to monitor and assess the adequacy of this internal buffer against a bank's strategy, risk profile and levels of capital.

2.8 As is standard practice in most international jurisdictions and to ensure that no confusion exists in the market, banks are required to refrain from disclosing to the public their ICR (Pillar 2B) requirement that is based on a combination of various qualitative and quantitative factors that are not directly comparable across banks.

2.9 Banks are required to publicly disclose their D-SIB capital add-on as part of their composition of regulatory capital disclosure.

3. Invitation for comments

3.1 Banks and all other interested persons are hereby invited to submit their comments in respect of the proposed directive to SARB-PA@resbank.co.za and to Jaco.Vermeulen@resbank.co.za, for the attention of Mr J Vermeulen, by no later than 19 March 2021.

Kuben Naidoo
Deputy Governor and CEO: Prudential Authority

Date: 18 February 2021

Encl. 2

ANNEXURE A: Capital Framework for South Africa based on the Basel III framework

Capital tiers	Reference in the proposed amended Regulations	CET 1 Capital Requirement	Tier 1 Capital Requirement	Total Capital Requirement
BCBS Basel III minima		4,5%	6,0%	8,0%
South African minima	**Reg 38(8)(b) & Reg 38(8)(e)(i)**	**4,5%**	**6,0%**	**8,0%**
Systemic risk add-on[1] (Total Pillar 2A range 0,5% to 2,0%)	Reg 38(8)(e)(ii)	$A_1 \geq$ 50% of P2A	$A_2 \geq$ 75% of P2A	P2A (≤2.0%)
South African base minima	**Reg 38(9)(a)(i) to (iii)**	**4,5% + A_1**	**6,0% + A_2**	**8,0% + P2A**
Bank-specific ICR add-on (Pillar 2B)	Reg 38(8)(e)(iii) & Reg 38(4)	B_1 = 50% of ICR	B_2 = 75% of ICR	ICR
South African minima (prudential minima)		**4,5% + A_1 + B_1**	**6,0% + A_2 + B_2**	**8,0% + P2A + ICR**
Domestic Systemically-Important Bank capital add-on[1] (0% to 2.5%)	Reg 38(8)(e)(vi)	$\mathbf{C_1}$ = up to the first 1%	$\mathbf{C_2}$ =up to the first 1,5%	DSIB (max of 2,5%)
Conservation buffer range (0% to 2.5%)	Reg 38(8)(e)(iv) & Reg 38(8)(f)	D_1 = 100% of CB	D_2 = 100% of CB	CB (≤2.5%)
Countercyclical buffer range[2] (0% to 2.5%)	Reg 38(8)(e)(v) & Reg 38(8)(g)	E_1 = 100% of CCyB	E_2 = 100% of CCyB	CCyB
SA minima including countercyclical buffer, conservation buffer and D-SIB requirements[3]		**7,0% + B_1 + E_1 + min(2,0% or (A_1 + C_1))**	**8,5% + B_2 + E_2+ min(2,5% or (A_2 + C_2))**	**10,5% + ICR + CCyB + min(3,5% or (P2A + DSIB))**

[1] The aggregate requirement for Pillar 2A and D-SIB will not exceed 2,0 per cent for CET1, 2,5 per cent for Tier 1 and 3,5 per cent in respect of the total capital-adequacy ratio.

[2] In line with the BCBS's paper released in December 2010, entitled "Basel III: Global Regulatory Framework for more Resilient Banks and Banking Systems", revised June 2011, under paragraph 137, the countercyclical buffer is likely to be imposed on an infrequent basis in order to serve its intended purpose.

[3] As specified in regulation 38(9)(a) of the proposed amended Regulations, the South African minima ratios, including the HLA requirement for D-SIBs, the capital conservation buffer and the countercyclical buffer, shall not be lower than 6,5 per cent for CET1, 8 per cent for Tier 1 and 10 per cent in respect of the total capital-adequacy ratio.

ANNEXURE B: Phase-in Arrangements for the minimum requirements

Shading indicates transition periods - all dates are as of 1 January unless otherwise stated

	Basel III	2013	2014	2015	2016	2017	2018	2019	6 Apr 2020	2022
Common Equity Tier 1 requirements (CET1)										
Minimum CET1 Ratio (per Basel III)	4,5%	3,5%	4,0%	4,5%	4,5%	4,5%	4,5%	4,5%	4,5%	4,5%
Pillar 2A for CET1		1,0%	1,5%	2,0%	1,75%	1,50%	1,0%	0,50%	0,0%	0,50%
Minimum CET1 plus Pillar 2A		4,5%	5,5%	6,5%	6,25%	6,0%	5,5%	5,0%	4.5%	5,0%
Phasing in of D-SIB requirements at CET1 level [1]					25%	50%	75%	100%	100%	100%
Capital Conservation buffer [2]	2,5%				0,625%	1,25%	1,875%	2,5%	2,5%	2,5%
Countercyclical buffer (maximum per cent, if imposed) [2]	2,5%				0,625%	1,25%	1,875%	2,5%	2,5%	2,5%
Tier 1 requirements (T1)										
Minimum Tier 1 Ratio (per Basel III)	6,0%	4,5%	5,5%	6,0%	6,0%	6,0%	6,0%	6,0%	6,0%	6,0%
Pillar 2A for T1		1,5%	1,5%	2,0%	1,5%	1,25%	1,0%	0,75%	0,0%	0,75%
Minimum T1 plus Pillar 2A		6,0%	7,0%	8,0%	7,5%	7,25%	7,0%	6,75%	6,0%	6,75%
Phasing in of D-SIB requirements at Tier 1 level [1]					25%	50%	75%	100%	100%	100%
Total capital requirements										
Minimum Total Capital Ratio (per Basel III)	8,0%	8,0%	8,0%	8,0%	8,0%	8,0%	8,0%	8,0%	8,0%	8,0%
Pillar 2A for Total Capital (maximum 2.0%)		1,5%	2,0%	2,0%	1,75%	1,50%	1,25%	1,0%	0,0%	1,0%
Minimum Total Capital plus Pillar 2A		9,5%	10,0%	10,0%	9,75%	9,5%	9,25%	9,0%	8,0%	9,0%
Phasing in of specified D-SIB charge at Total Capital level [1]					25%	50%	75%	100%	100%	100%

[1] The aggregate requirement for Pillar 2A and D-SIB will not exceed 2,0 per cent for CET1, 2,5 per cent for Tier 1 and 3,5 per cent in respect of the total capital-adequacy ratio

[2] The capital conservation buffer together with the countercyclical buffer will be applied at CET1 level and will also be required to be met at both a Tier 1 and Total capital level.