

Ref.: 15/8/1/3

To: All banks, branches of foreign institutions, controlling companies, 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

National discretion related to the liquidity coverage ratio

Executive summary

The amended Regulations relating to Banks (the Regulations), in which the framework for the liquidity coverage ratio (LCR) was included, were implemented with effect from 1 January 2013.

Directive 7/2014 was issued by the Prudential Authority (previously the Bank Supervision Department) to communicate to 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 LCR

Provision was made by the Basel III LCR framework¹ for supervisors to specify factors relating to national discretion items.

Due to sufficient high-quality liquid assets (HQLA) in its economy, South Africa no longer meets the requirements to make use of any of the alternative liquidity approaches (ALA) as stipulated in the Basel III LCR framework¹. Accordingly, further guidance is also provided regarding the treatment of retail term deposits when calculating the LCR.

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

1. Introduction

- 1.1 On 12 December 2012, the amended Regulations were published in Government Gazette No. 35950. The majority of amendments were made to incorporate the Basel III framework. The Regulations became effective on 1 January 2013.
- 1.2 On 7 January 2013, the Basel Committee on Banking Supervision released an updated framework for calculating and implementing the LCR.
- 1.3 Directive 7/2014 was released on 28 October 2014 to address national discretion items relating to the LCR.
- 1.4 Guidance Note 5/2017 was issued to phase out the Committed Liquidity Facility (CLF).

- 1.5 Paragraphs 55 and 56 of the Basel III LCR framework set out the conditions for jurisdictions to make ALA options available to banks.
- 1.6 During recent years, the shortage of high-quality liquid assets (HQLA) within the South African environment has continued to decrease to such an extent that the provision of the ALA options no longer meets the qualifying criteria set out in the Basel III LCR framework.
- 1.7 As such, banks will no longer be allowed to include foreign-currency denominated HQLA to cover any domestic currency liquidity needs when calculating the bank's LCR as of 1 September 2022.
- 1.8 In the event that market conditions change, the Prudential Authority (PA) may re-evaluate its decision to remove the ALA options available to banks.
- 1.9 In order to ensure level playing field amongst banks and Basel III LCR compliance, further guidance regarding the treatment of retail term deposits are provided.
- 1.10 This proposed 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 Inclusion of cash reserves as part of level 1 HQLA

- i. As previously communicated in Guidance Note 6/2013, banks' cash reserves may be included as part of their level 1 HQLA, excluding cash reserves utilised for square-off operations in SAMOS at the close of a business day.

2.1.2 Haircuts on level 1 HQLA

- i. The 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 for 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, subject to the limits, haircuts and qualifying criteria specified for these assets in the revised Basel liquidity framework read with the related amended Regulations.
- ii. Regarding 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 Retail deposits- less-stable deposits

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

2.1.5 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 amended Regulations.

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), shall be 3 per cent. This is in accordance with paragraph 84 of the Basel III LCR standard¹. No retail term deposits can be excluded from the LCR calculation.

2.1.7 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.
- ii. The PA reserves the right to reassess and revise the aforementioned factors should it be deemed appropriate.

3. Invitation for comment

- 3.1. Banks are hereby invited to submit their comments with respect to the proposed Directive directly to SARB-PA@resbank.co.za and Cristel.Bakker@resbank.co.za for the attention of Ms Cristel Bakker by no later than 28 April 2022.
- 3.2. All comments received from banks may be published on the website of the PA unless a respondent bank specifically requests confidential treatment.



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