COURSE: COMESA WORKSHOP ON BASEL III

TOPIC : RISK COVERAGE UNDER BASEL III

DATE: JULY 15, 2016

VENUE: KENYA SCHOOL OF MONETARY STUDIES

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AGENDA

- Enhancing Risk Coverage
- Leverage Ratio
- Incorporating Macro prudential Regulations

A). ENHANCING RISK COVERAGE

- **Current arrangement**

Capital Ratio = $\dfrac{\text{Capital}}{\text{Risk Weighted Assets}}$ $\geq$ 8%

Under Basel III

Setting three minimum standards
Common equity, Tier I and total Capital

Raising the quality of Cap
1. Stricter criteria for inclusion in Ti
2. Internationally harmonized Ded Capital

Capital Ratio = $\dfrac{\text{Capital}}{\text{Risk Weighted Assets}}$

Enhancing Risk Coverage
Securitisation products
Counter party credit Risk

A). ENHANCING RISK COVERAGE

Approaches to measuring risk

- Basel II provided for two different approaches to measuring credit risk
  - The standardized approach, which relies on external credit ratings, and
  - For more sophisticated banks, and only with regulatory approval, the internal-ratings based approach, which allows banks to rely on their internal assessments of credit risks.
- Basel III makes changes to both of these approaches, especially as they relate to:-
  - Securities financing transactions (repurchase agreements, reverse repurchase agreements, securities lending and borrowing arrangements and margin lending arrangements); and
  - Counterparty credit risk (default risk)
  - Banks are subject to capital charge for potential mark-to-market losses as a result of deteriorations in the creditworthiness of their counterparties.
  - Basel III requires stress-testing and scenario analyses to identify risk that is "positively correlated" with counterparty creditworthiness.

B). LEVERAGE RATIO

Objectives:-

- Constrain the build up of leverage in banking sector, thus helping to mitigate the risk of distabilising deleveraging process which can damage the financing system of the economy.

$$\textbf{Leverage Ratio} = \frac{\textbf{Tier 1 Capital (New definition)}}{\textbf{Total Exposure (B/S + Off B/S)}} \geq 3\%$$

C). MACROPRUDENTIAL REGULATION

Objectives:-

- Constrain the build up of leverage in banking sector, thus helping to mitigate the risk of distabilising deleveraging process which can damage the financing system of the economy.

$$\textbf{Leverage Ratio} = \frac{\textbf{Tier 1 Capital (New definition)}}{\textbf{Total Exposure (B/S + Off B/S)}} \geq 3\%$$

Q & A

THANK YOU