BIS Asian Office

BANK FOR INTERNATIONAL SETTLEMENTS

The Role of Bank Supervisory Authorities under the New Basel Accord

Challenges for Asia

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Goals of Revision of Capital Accord - 1

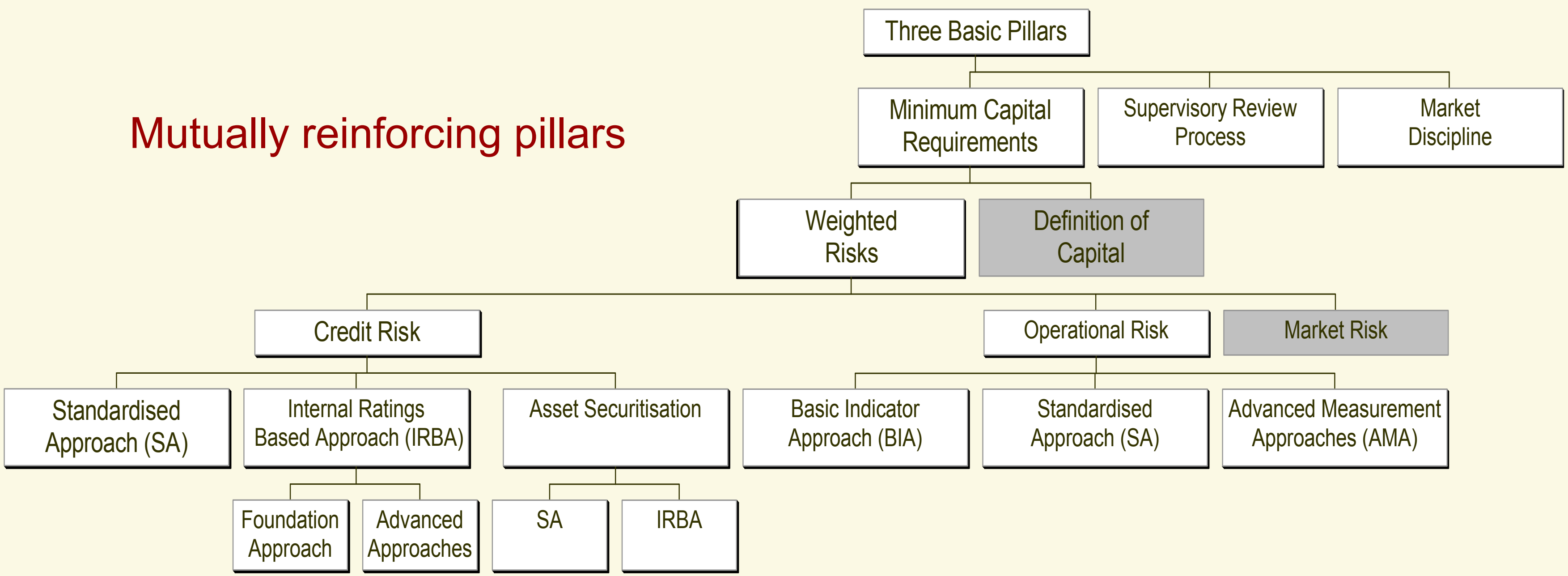
- Enhance the risk sensitivity of capital requirements
  - Accord 1988: Four broad risk weighting categories
- Comprehensive coverage of risks
  - Accord 1988: Credit risk plus market risks in 1996
- Present a menu of options to choose from
  - Accord 1988: One-size-fits-all approach
- Greater focus on banks world-wide
  - Accord 1988: Intended to apply to internationally active banks in G10

Goals of Revision of Capital Accord - 2

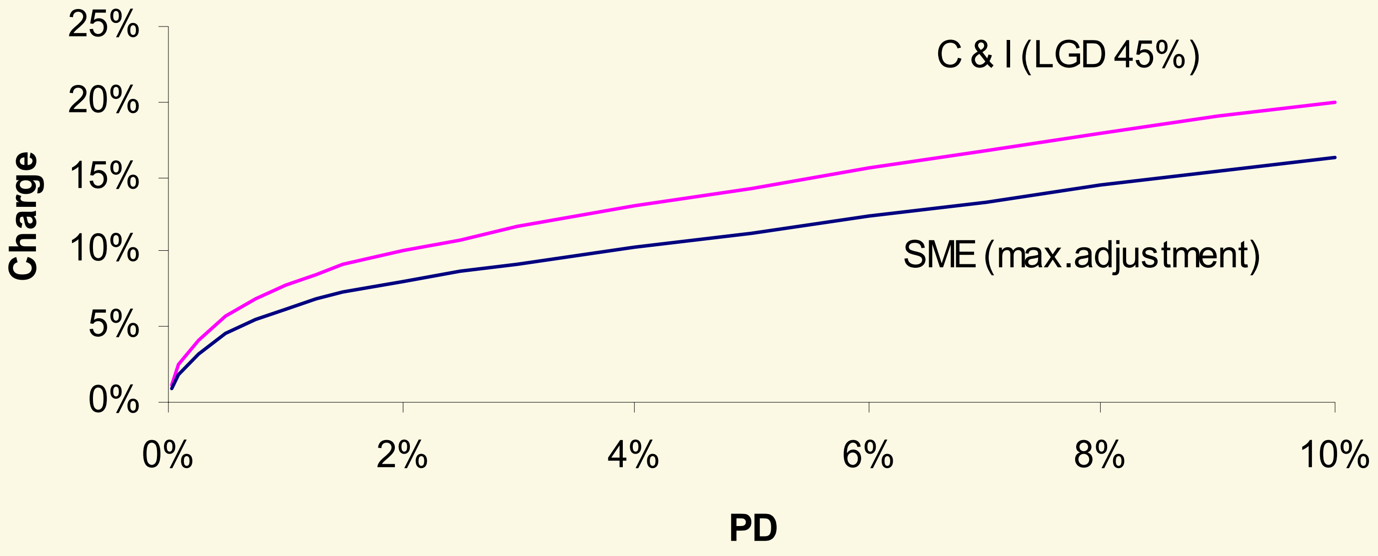
- More power to supervisors and the market
  - Accord 1988: Focused on minimum capital requirements
- Maintain overall level of capital in the banking system
- Implications
  - Complexity?
  - Cyclicality?

The New Capital Accord in a Nutshell

Mutually reinforcing pillars

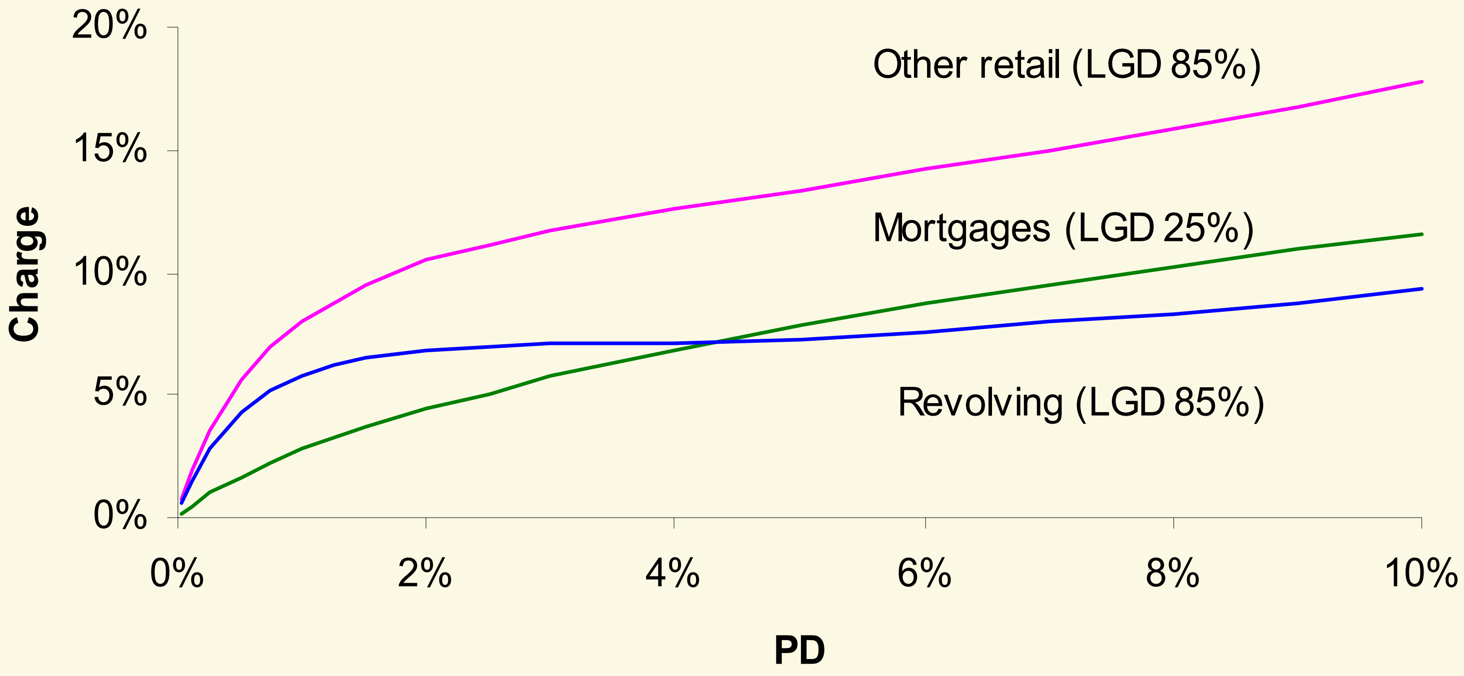


Capital charges for corporate and SME exposures



"IRB"* certainly does not *always mean lower capital requirements

Capital charges for retail exposures



"IRB" certainly does not ***always mean lower capital requirements***

Future time table

- May 2003: Consultative Document III
- Fall 2003: Final Accord
- End-2004: IRBA banks start data warehousing of PD observations to benefit from transitional arrangements
  - Without exception, banks adopting the advanced IRBA are required to have at least five years of data for PDs, and seven years for LGDs and EADs
- End-2005: parallel calculation (old and new) for IRB banks
- End-2006: Accord comes into force
- From 2007 through 2008: declining floor (90%, 80%)

Implementation - Challenges for Asia

- Assessing national priorities important first step
- Effective implementation does not necessarily require application of the New Accord to all banks in a jurisdiction
- However, implementing key elements Pillar 2 and Pillar 3 even if Pillar 1 is not fully implemented after year-end 2006 seems reasonable

Implementation - What needs to be done?

- Overarching policy considerations
- Assessing national priorities versus benefits of implementation in end 2006
  - Core Principles implemented?
  - Legal and regulatory infrastructure?
  - Role of market discipline?
  - Accounting standards?
  - Human resources?
  - Soundness of corporate governance structure?

Implementation considerations – Phase 1

Determining the Scope of Application

- Assess current status/needs of banking system
- Determine range of approaches which banks could reasonably be expected to implement
  - Identify significant banks (size, complexity, international presence, systemic importance)
- Implementation/Timing
  - National considerations
  - Phased approach (different approaches, different dates)

Implementation considerations - Phase 2

Assessment of Banks' Capabilities

- Assess risk management capabilities of significant banks
  - Early communication with banks
  - Determine current status
  - Determine quantitative impact
  - Discuss national discretion
- Supervisory efforts to assist banks in their process
  - Guidance of what models will be acceptable
  - Data collection specifications
- Discuss validation of internal assessments

Implementation considerations - Phase 3

Assessing Supervisory Preparedness

- Translate findings of phase 2 into legislation and supervisory framework
- Give national guidance including timeframe
- Assess supervisory resource and training requirements
  - Internal resources and/or new staff
  - Consultants
- Infrastructure requirements (IT, reporting, …)
- Dialogue between supervisors crucial

Implementation considerations - Phase 4

Implementation

- Pass legislation
- Perhaps adjust to national conditions of Accord
- Run of old and new system in parallel
- Continue dialogue with other supervisors

What has been done?

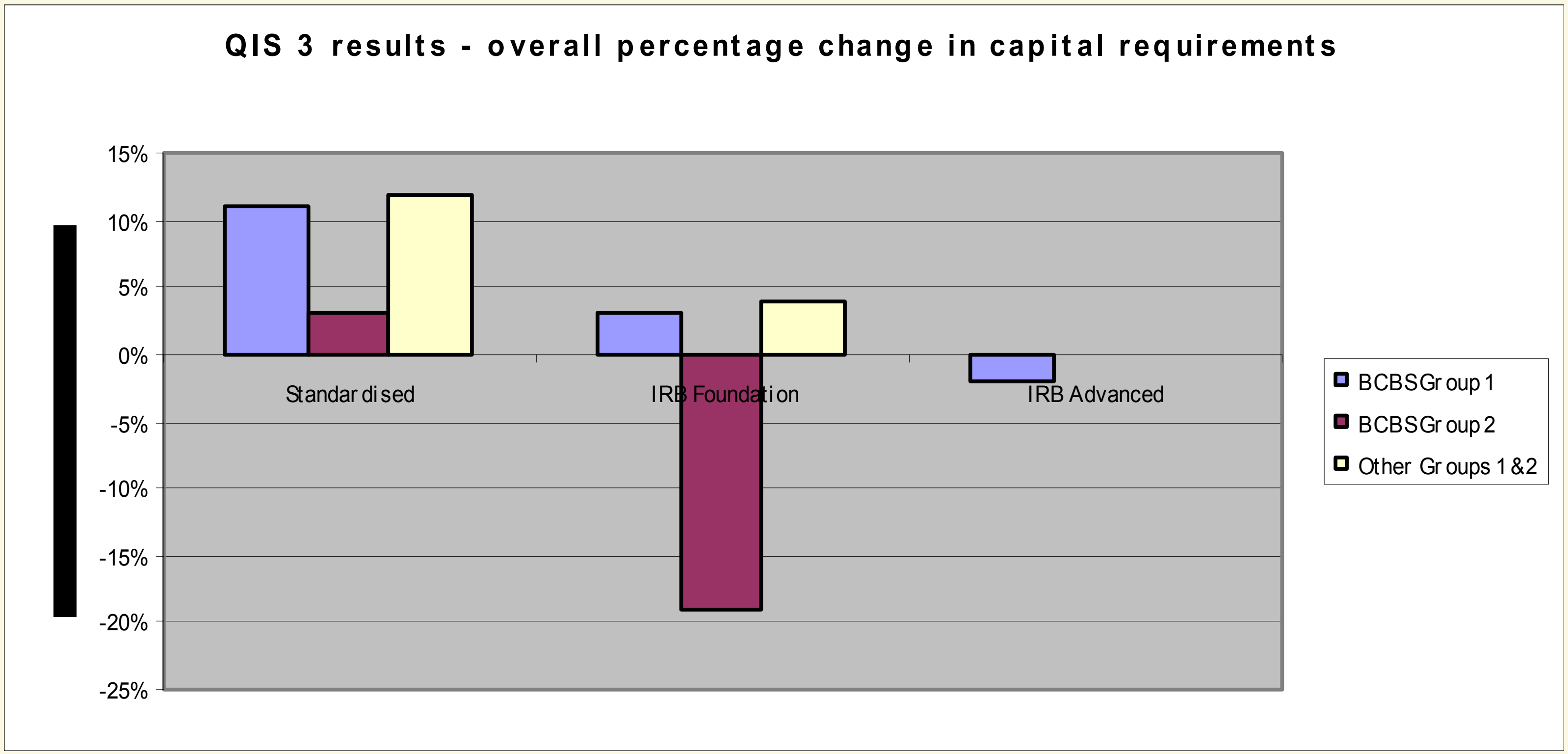
- All BCBS member countries, plus EU and some countries (Australia, Singapore, …?) have indicated to implement by end 2006
  - Largest banks on IRB (US only on Advanced IRB)
  - Most will have many banks on the Standardised Approach (probably US is exemption)
  - With explicit Pillar 1 charge for Operational Risk
  - But, implementation of pillars 2 & 3 will vary
- Impact analysis – Quantitative Impact Study 3
  - Strong participation in Asia

Quantitative Impact Study - QIS 3

- Launched on 1st October 2002 with participating banks
  - BCBS* - 188 banks
  - Other countries - 177 banks
    - 18 EME countries including
      - Australia, China, Hongkong, Indonesia, Japan, Korea, Malaysia, Philippines, Singapore, Thailand
      - Coordinated by APRA and BIS Asian Office
    - 5 EU accession countries and 7 non-G10 EU
- Group 1 banks are large, diversified, internationally active with Tier 1 capital > €3bn
- Group 2 banks are smaller, sometimes specialized institutions

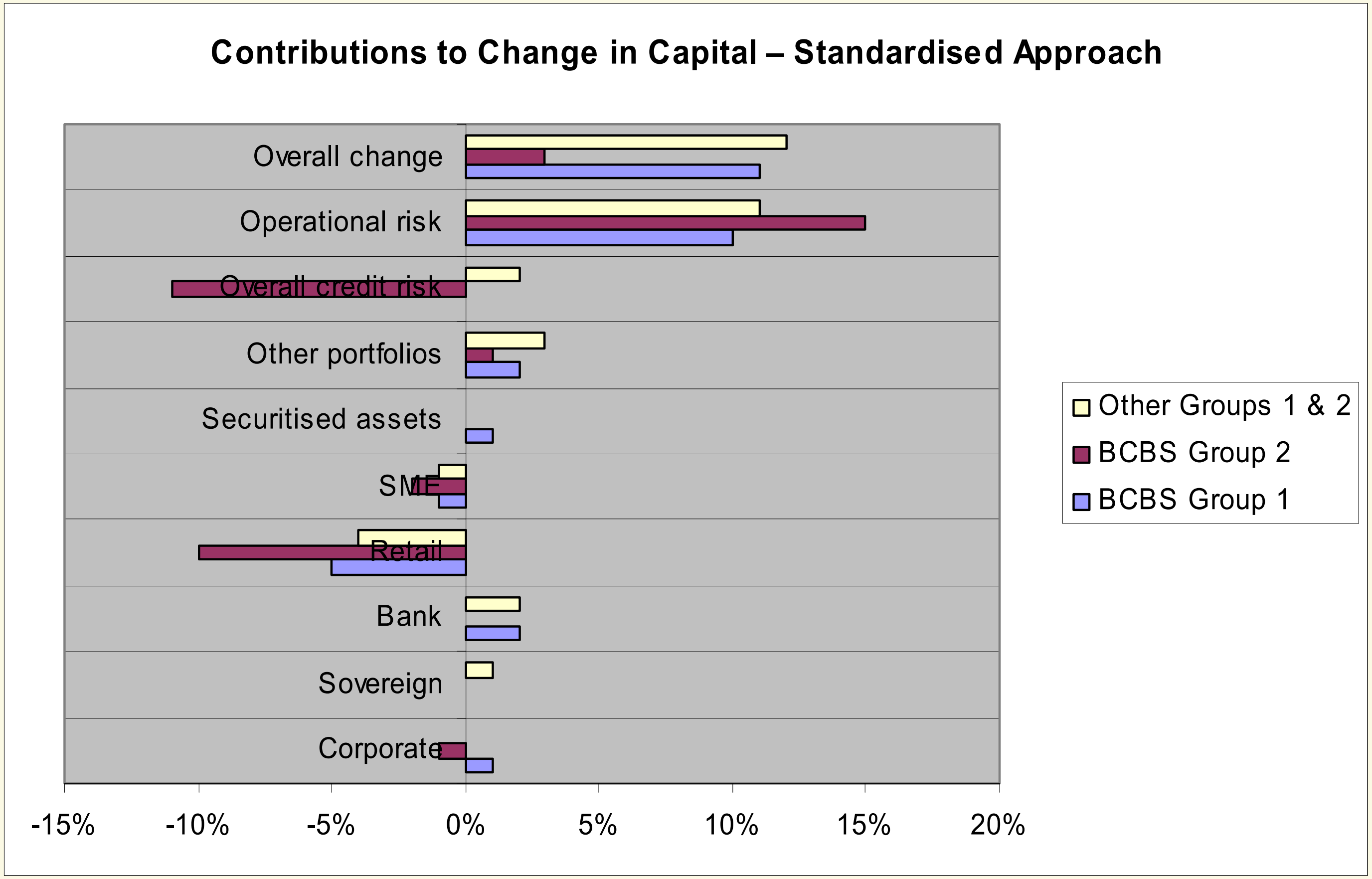
* BCBS – Basel Committee for Banking Supervision (13 countries)

QIS 3 – overall results

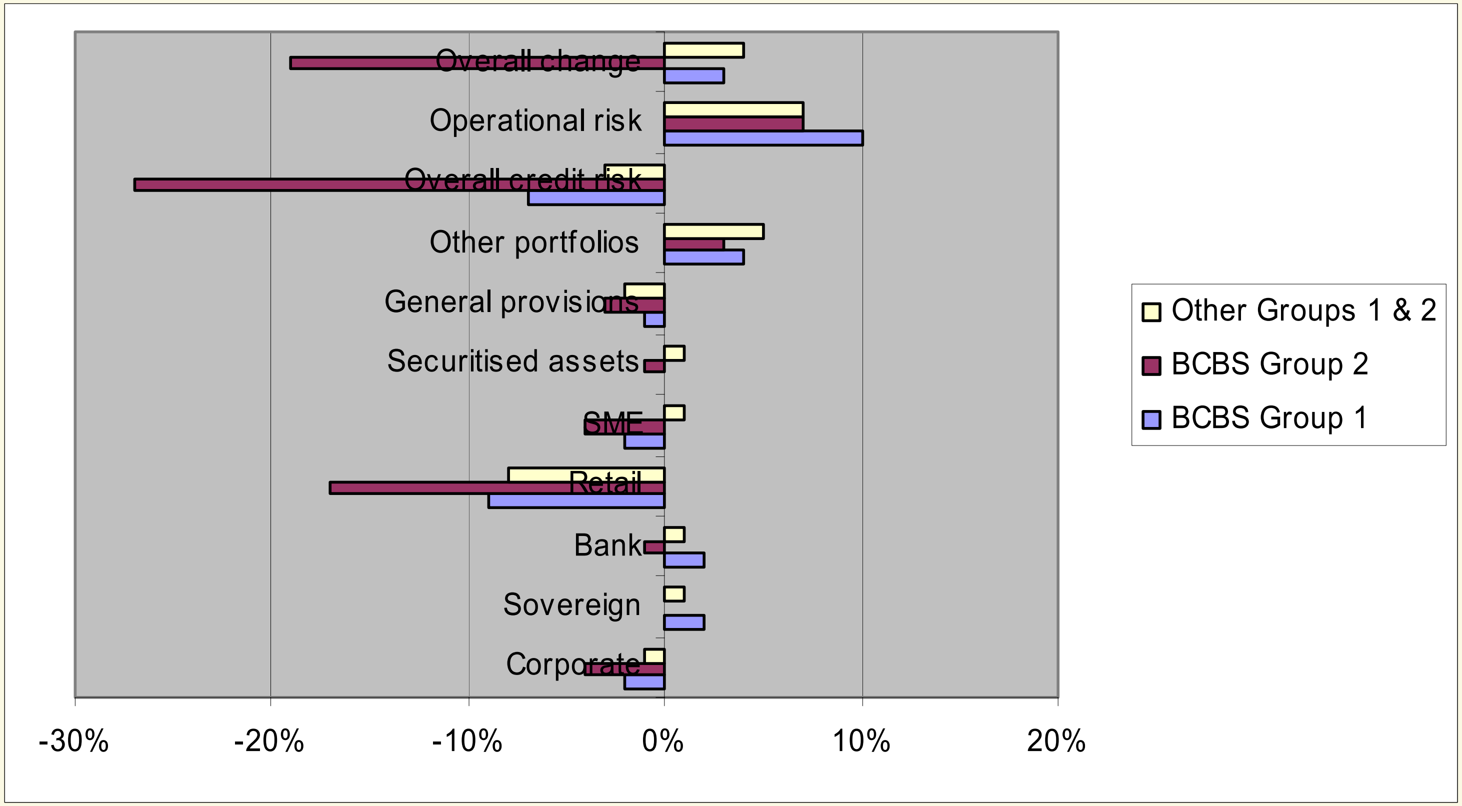


Other represents 17 EME countries

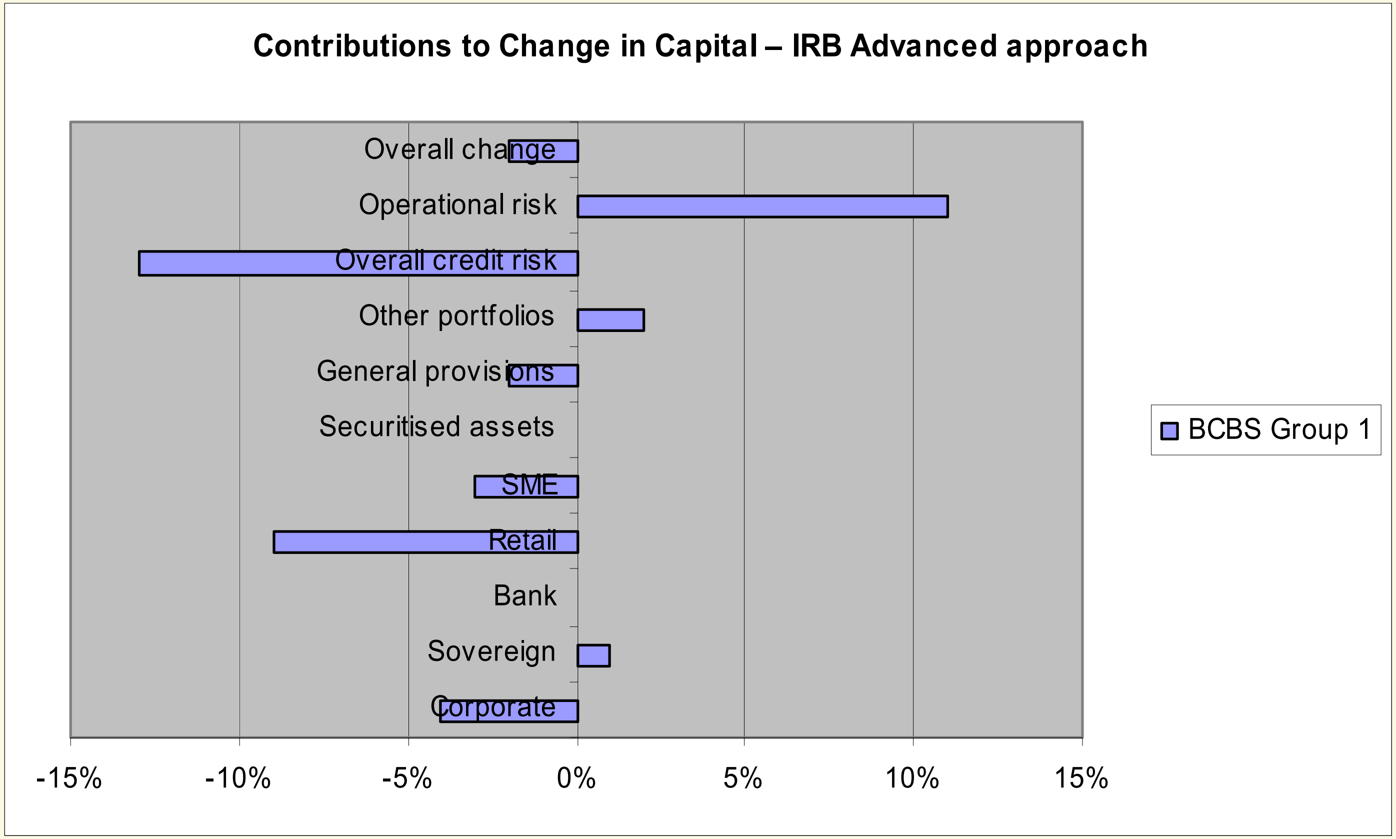
QIS 3 – SA contributions



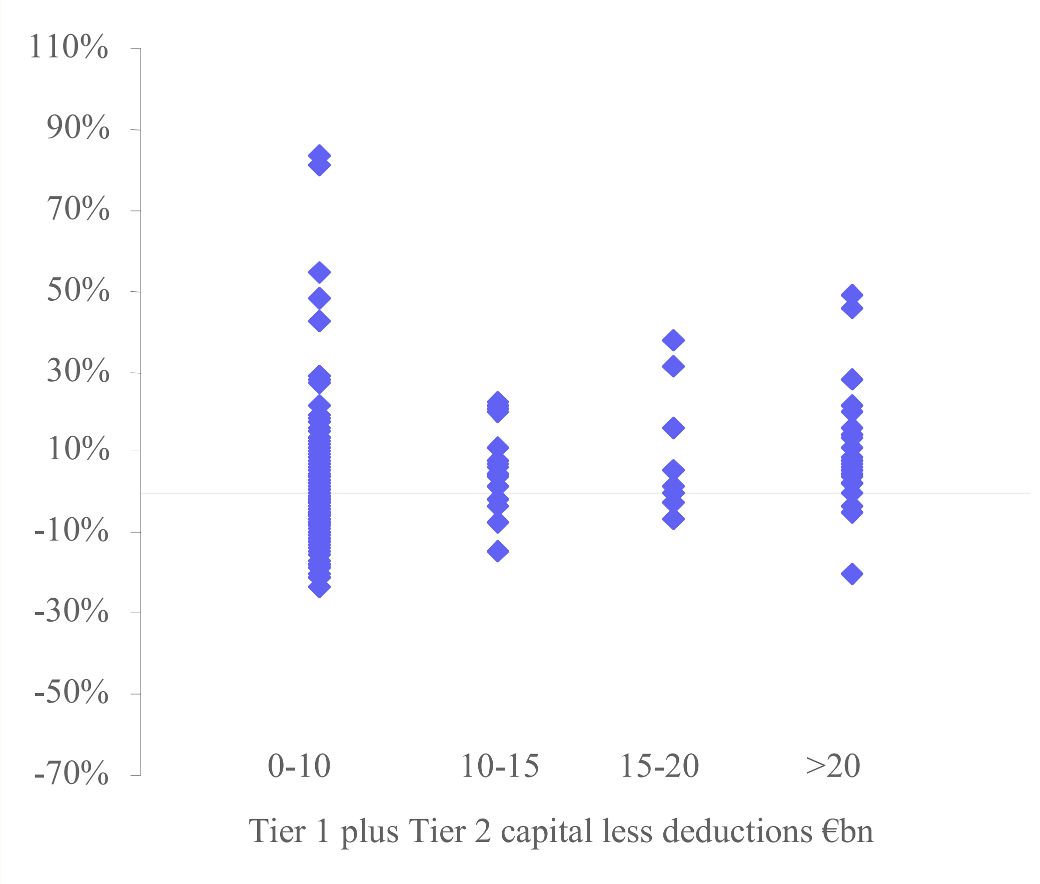
QIS 3 – Foundation IRB contributions



QIS 3 – Advanced IRB contributions

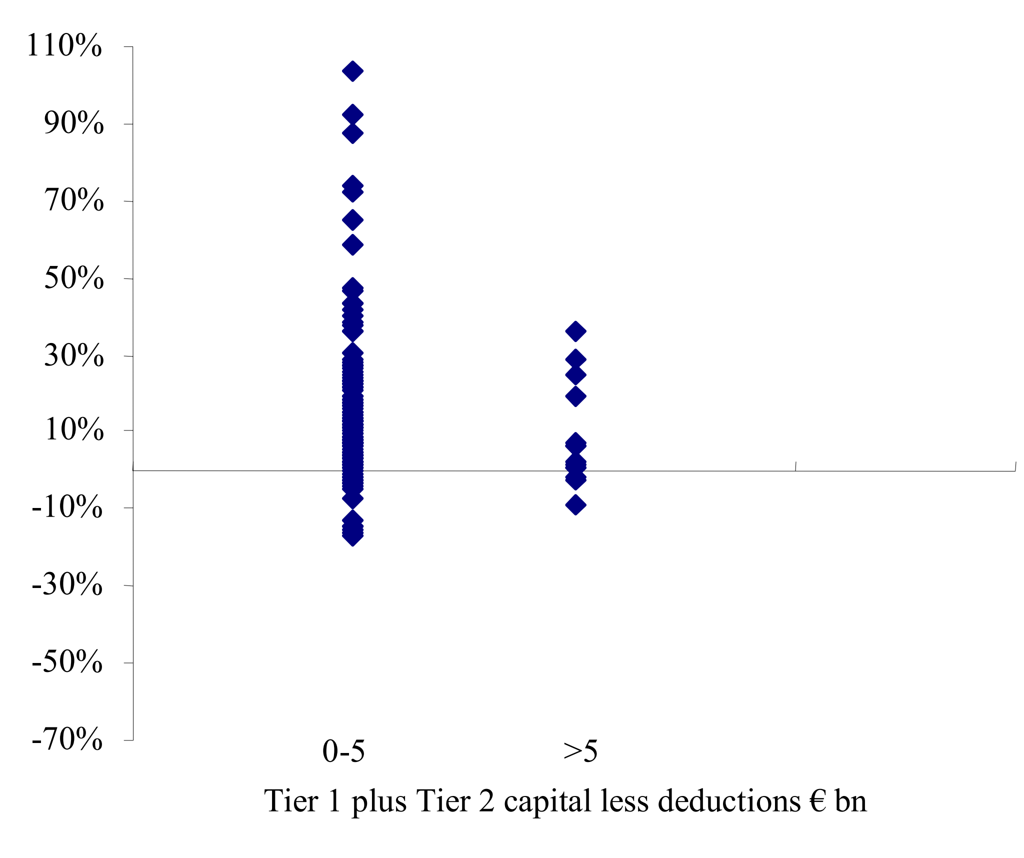


SA – variation for BCBS banks



% change in minimum capital requirements versus current Accord

SA – variation for “other” banks



% change in minimum capital requirements versus current Accord

QIS 3 – BCBS major impacts (Group 1)

	Standardised[1]	FIRB[1]
• Sovereign	+ 19	+ 47
• Bank	+ 43	+ 45
• Retail mortgages	- 20	- 56

[1] % change in risk-weighted assets to current approach, in contrast to contributions

Concluding Thoughts

- IRBA is most risk sensitive, but SA equally important
- New Accord encourages banks to refine their risk measurement and risk management over time
- Implementation challenges for all countries
  - Appropriate capital adequacy framework should be implemented to ensure safety and soundness of the banking system and encourage improvements in risk management.
  - Effective implementation requires a framework suited national circumstances
- Supervisors should ensure that, over time, they can permit their significant banks the possibility to move to more advanced methodologies