Implementing Basel III in Russia

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Roundtable discussion

Development of collaboration between Russian and British financial institutions

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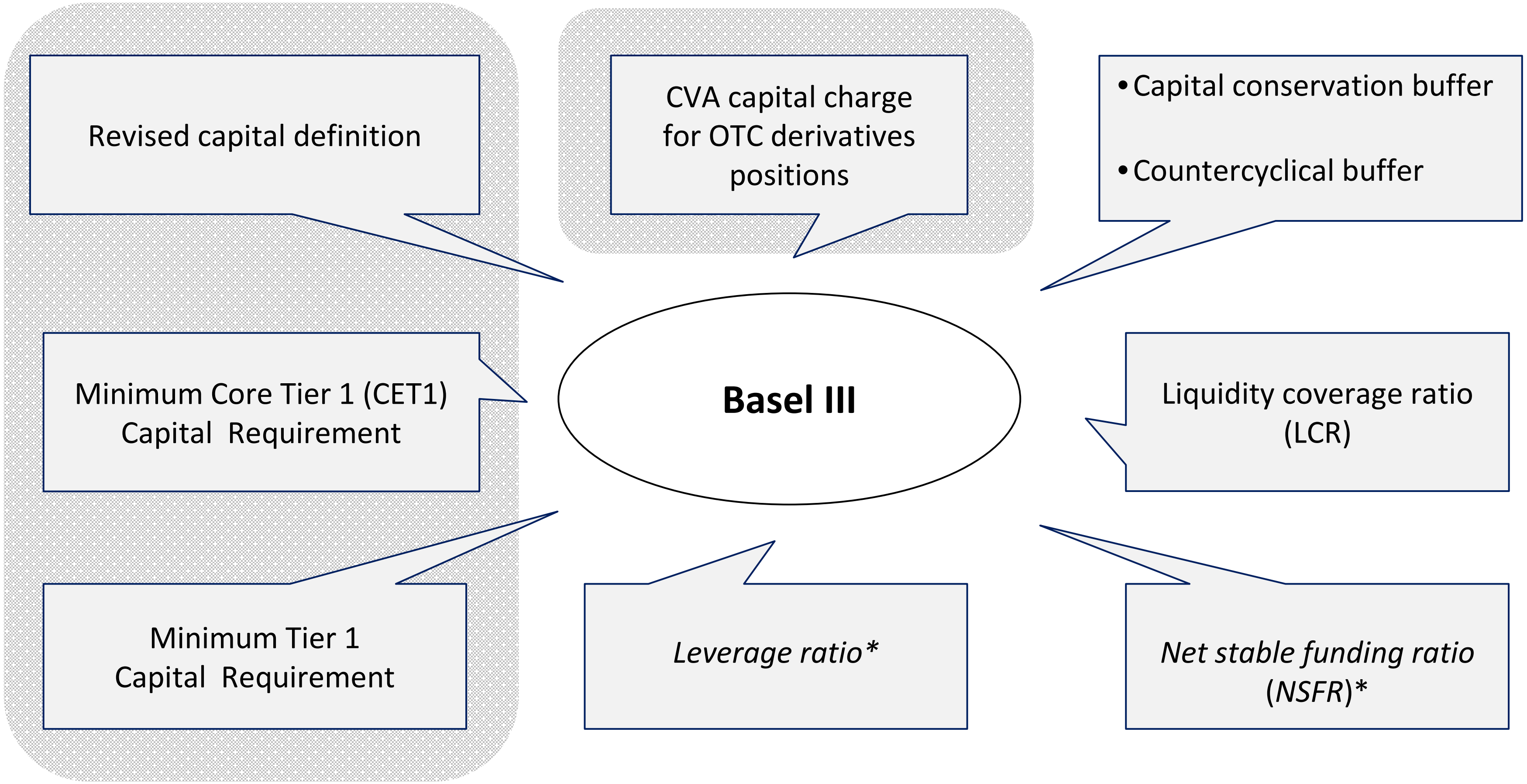
Basel III Overview



Phased-in implementation to start in 2014

** Final rules to be released by Basel Committee on Banking Supervision*

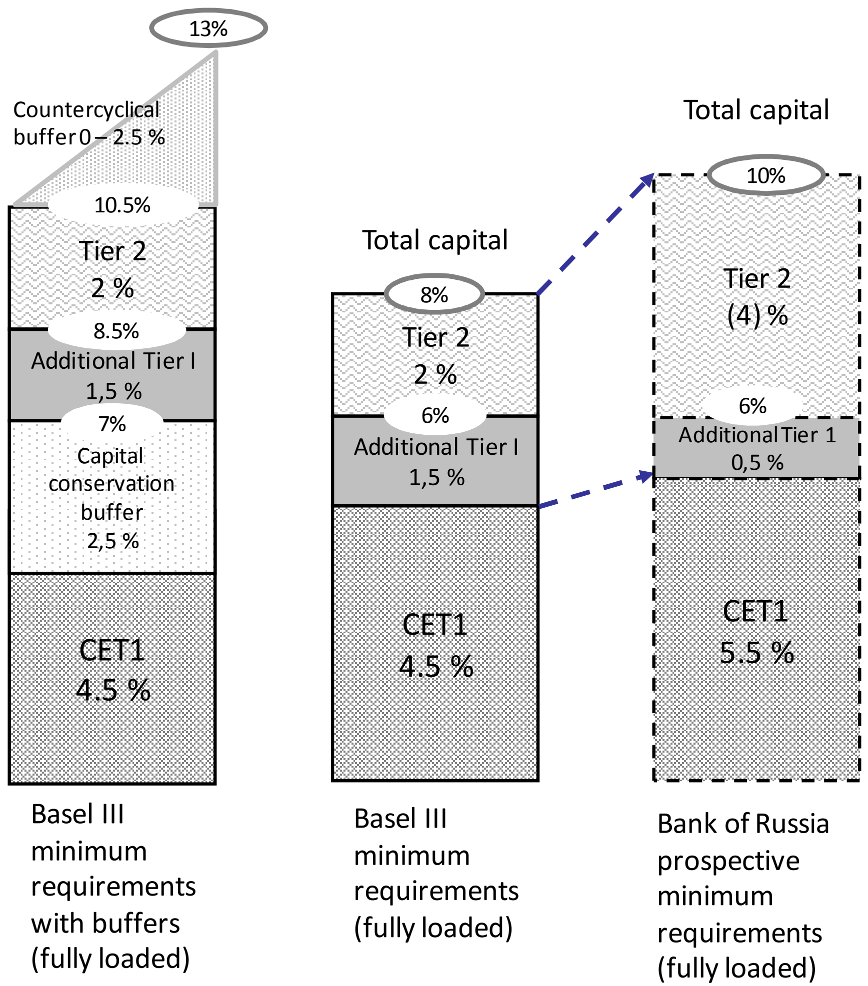
Revised Capital Adequacy Requirements

Current situation

- Total capital $\geq$ 10 percent of RWA
- Tier 2 capital $\leq$ 100% Tier 1 Capital
- Tier 3 capital not present
- Scarce hybrid capital instruments (e.g. perpetual debt instruments not allowed under Russian law), hence little additional Tier 1 capital
- CET1 $\approx$ Tier 1 Capital

Basel III implementation issues

- Scaling up CET1 needed to account for difference in total capital requirements
- Cap on Tier 2 capital to be removed
- CET1 should not be < 5 percent of RWA
- Conversion/write-off triggers to be customized
- Legislative amendments needed to introduce capital conservation buffer and countercyclical buffer



New Liquidity Requirements: LCR

Current situation

- Regulatory liquidity requirements in force since mid-1990s (Ratios N2, N3, and N4 in Regulation 139-I)

Basel III implementation issues

- Insufficient supply of high-quality liquid assets (HQLA)
- Scope of monitoring/application
- Use of alternative approach 1 requires introducing contractual committed liquidity facility from Bank of Russia

Bank of Russia proposals for BCBS

- ✗ All central-bank eligible assets should be recognized as HQLA
- ✓ Outflow rate on unsecured funding from sovereigns and CBs down from 75 % to 45 % (finally at 40%)
- ✓ Outflow rate on secured funding from sovereigns CBs down from 100% for some collateral types (finally at 0% for all collateral)
- ✓ Corporate bonds with ratings up to BBB- to be included in Level 2 HQLA
- ? CBs' committed liquidity facilities to be recognized as HQLA not only in times of stress

Alternative Liquidity Approaches

1. Contractual committed liquidity facilities from central bank
2. FX HQLA to cover domestic currency liquidity needs
3. Additional use of Level 2 assets with higher haircut

Credit Valuation Adjustment

Current situation

- 60 percent cap on unrealized profits from derivatives positions in Tier II capital (Regulations 215-P, 395-P)
- Exchange-traded derivatives market shrank in 2012
  - Daily turnover down by 17.6 percent to RUB 201.7 bln (RUB 230.1 bln in 2011)
- OTC derivatives market presumably thin
- OTC counterparties often unrated

Basel III implementation issues

- Risk weight not specified for unrated counterparties under standardized approach in Basel III
- Risk weight for unrated counterparties set at 4 percent

Basel III CVA risk weights under standardized approach

Credit rating	Risk weight, percent
AAA	0.7
AA	0.7
A	0.8
BBB	1
BB	2
B	3
Unrated	4
CCC	10

Leverage Ratio

Current situation

- No capital adequacy requirements other than N1 risk-weighted CaR (Regulation 139-I)
- Leverage ratio to be based on final rules for Tier 1 capital calculation (Regulation 395-P)
- Recommendations on calculating leverage ratio published in July 2013 (Letter 142-T)
- Disclosure requirements for Russian banks to be released in 2014

Basel III implementation issues

- Accounting issues, e.g.
  - Credit derivatives not identified as separate type of financial instruments
- Data issues, e.g.
  - Exposures on exchange-traded derivatives transactions
  - Unconditionally cancellable off-balance-sheet commitments subject to CCF = 10%
  - Counterparty risk on repo-style transactions
- Standard and disclosure template to be finalized by BCBS
- Bank to start quarterly reporting from 1st Oct, 2013
- Leverage ratio to be calculated be Bank of Russia based on banks’ reporting data

Basel III: Implementation Timeline