

Basel II - Challenge for the Future

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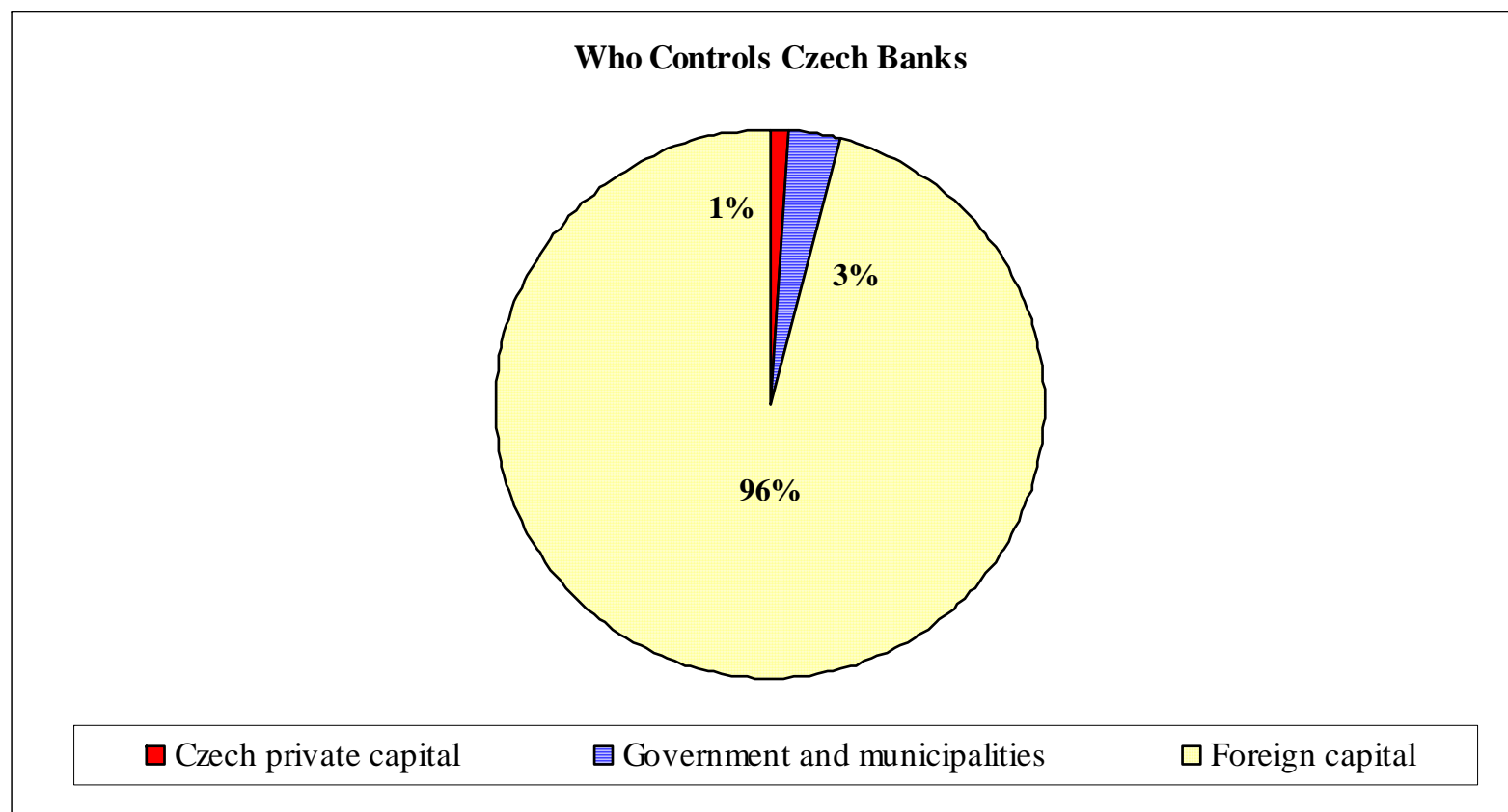
Basel II – What is new?

- Risk sensitive regulatory capital requirements
- Reliance on banks' own models
- Individual risk profile
- Dramatic changes in banking sector – importance of cross-border issues
- Change in supervisory culture

Characteristics of the Czech Banking Sector

- Total of 35 banks (9 of which are branches)
- Total banking assets - approx. 100 billions USD
- Three large banks dominate the sector (approx. 58% of total banking assets)
- Expanding range of products and services: esp. retail business + SME lending
- Capital adequacy around 14%
- Sector mostly controlled by foreign entities

Characteristics of Czech Banking Sector - Ownership Structure



Basel-2 Implementation - Joint Project

Joint Project of the CNB, the Czech Banking Association and the Chamber of Auditors

- Started in September 2002
- Partial participation from Ministry of Finance, SEC
- Project structure - 4 levels: Steering Committee, Working group, Sections (Legislative, Operational risk, Credit risk), 10 expert teams
- Approx. 10 banks actively participating, other passively (access to Project web pages, possibility to comment)
- Timing - preparation phase (until 2004/5, legislative phase 2005/6), implementation phase 2006/7 - subject to periodic review

Basel-2 Implementation - Joint Project

Main Goals

- Understanding of the concept, in-house education
- The exchange of information - banks and regulator statements
- The identification of problems
- Mutual "language" and definitions
- Analyzing merits of pooling data among banks
- The implementation of Basle 2 and the EU Directive into Czech law

Basel-2 Implementation - Joint Project

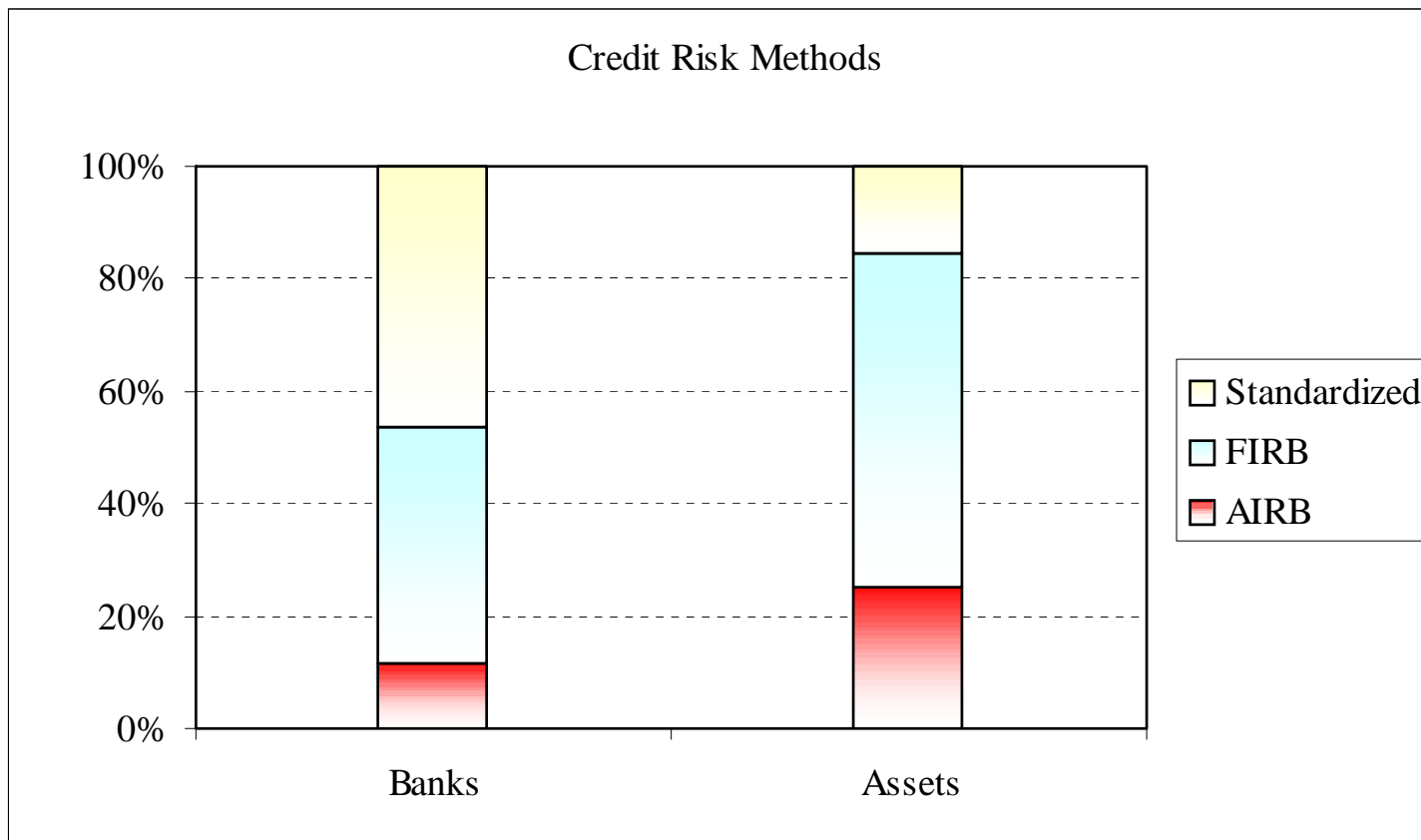
Results up to now

- Comments on BCBS and EC Proposals (CP3)
- Presentations on the New Accord
- Materials explaining definitions - credit and operational risk
- Ten expert teams - identification of problems, national discretions, legal issues

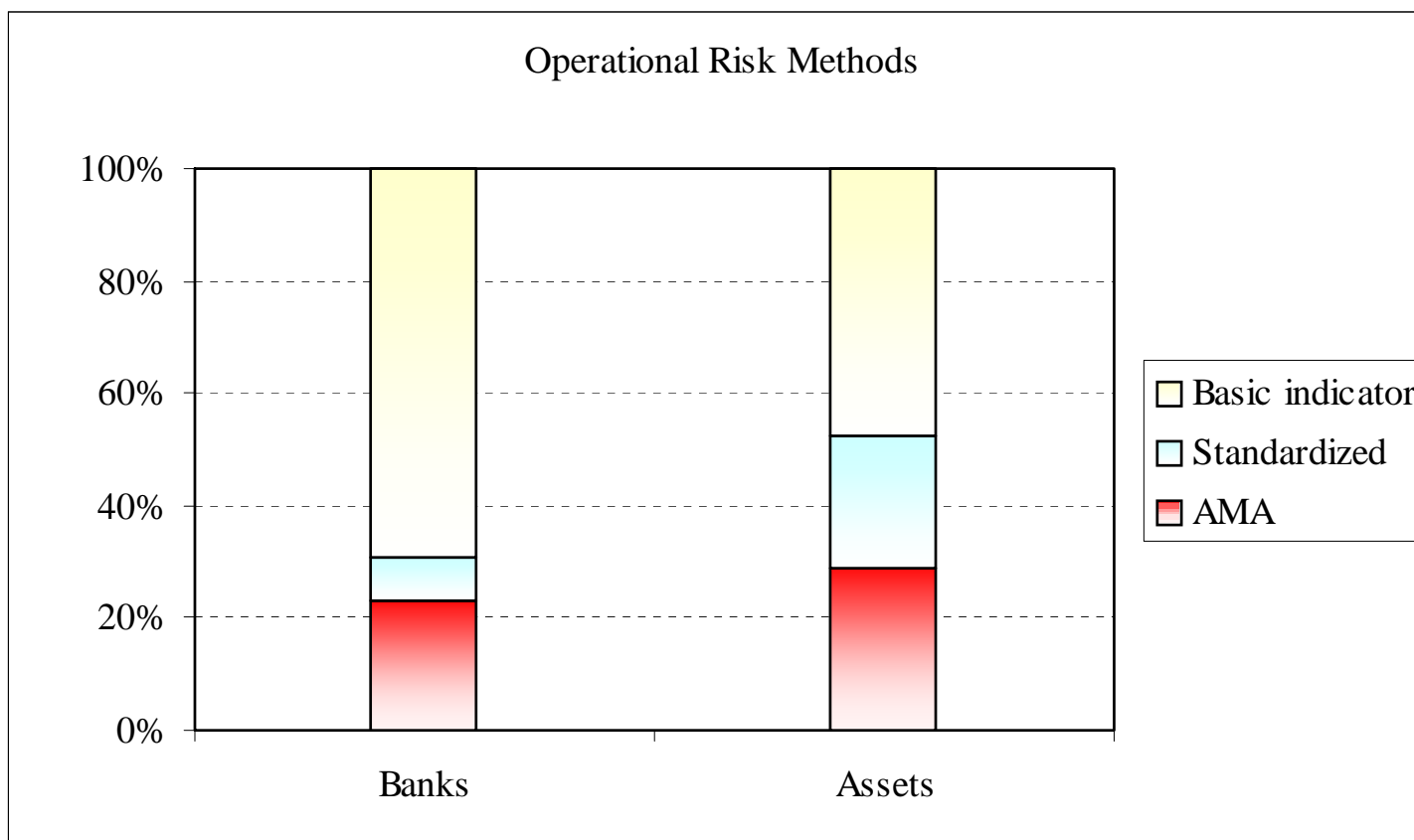
Basel-2 Implementation - Banks' Planned Approaches

- **Credit risk:**
 - ◆ 3 banks potentially AIRB (all of them are subsidiaries of foreign banking groups)
 - ◆ 11 banks (8 groups) FIRB
 - ◆ 12 banks STA
- **Operational risk:**
 - ◆ 5-6 banks AMA
 - ◆ 2 banks STA
 - ◆ 18 banks BIA

Basel-2 Implementation - Banks' Planned Approaches



Basel-2 Implementation - Banks' Planned Approaches



Basel-2 Implementation - Current Stage of Preparation

- **CNB in close individual contacts with banks**
- Banking groups mostly manage Basel-2 projects that are headed by parent banks
- Methodologies mostly developed by parents (exceptionally purchased), partially with local set ups (e.g. retail)
- Implementation costs not exactly quantifiable
- Banks mostly head towards advanced approaches but with different timing
- Banks expect benefits in improved risk management and capital savings

Basel-2 Implementation-the Main Issues

1. Home/host issues

- Running discussions on EU level + with individual home supervisors
- Approaches range from soft co-ordination, to “consolidated” or a full-scale “lead supervisor”
- Powers and responsibilities not clear
- Need of convergence of approaches
- CNB = host regulator, 7 related home regulators
- Different views of hosts - importance of subsidiaries on domestic market
- Burden on banks? Burden on supervisors?

Basel-2 Implementation-the Main Issues

2. Data and validation methods

- Lack of data
- Non-statistical methods of validation?
- Data pooling across banking groups? reliable estimates? LGD - even different jurisdictions?

3. Demands on banks and regulators

- Human and technical resources \Rightarrow cost burden
- Supervisory teams for approvals
- Postponement of final documents
- Time shortage (legislative process critical)

Thank you for your attention.

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