Association of Supervisors of Banks of The Americas

ASBA

Asociación de Supervisores Bancarios de las Américas

Association of Supervisors of Banks of the Americas

LIQUIDITY MANAGEMENT ALTERNATIVES

Rudy V. Araujo Medinacelli

Secretary General

August 26, 2013

Prague, Czech Republic

REGIONAL ASSESSMENT

- Liquidity risk regulatory frameworks with different degrees of depth:
  - Several jurisdictions combine regulatory limits and best practices
  - Some jurisdictions **only** have qualitative requirements
    - *Most regulated and supervised: contingency funding plans; liquidity mismatches; stress testing; operative liquidity internal assessment.*

- Most jurisdictions expect liquidity rules to impact their domestic financial markets and the supply of credit, especially, when the NSFR comes into rule.
  - *Greater reliance on retail deposits*
  - *Greater diversification of funding sources and liquid assets (HQLA)*
  - *Manage maturities to meet cut off NSFR requirements*

POTENTIAL UNINTENDED CONSEQUENCES

- Higher requirements to comply with liquidity requirements:
  - Both supervisors and supervised entities would need to develop or adapt their data processing and IT infrastructure to obtain information in the detail required by Basel III
- Given the development of financial markets, banks would hold HQLA portfolios concentrated in few assets, thus generating vulnerabilities for banks
  - Mainly concentrated on EMSEs government paper and central bank reserves
- Due to public paper's lower returns, banks may increase their risk in search of better returns for their liquid reserves.

REGULATORY GUIDANCE

Preconditions for the effective management of liquidity risk:

- A financial security system for the mitigation of systemic risk
  - A macro prudential monitoring system
  - Effective off site early warning systems
  - Clear protocols for the management of liquidity insufficiencies and crisis
- Identification and design of liquidity support instruments
  - Creation of a special fund for confidence preservation and restoration with public and private participation
- Ad hoc regulation for liquidity risk management
- Public disclosure on the availability of funding sources public or private (to curve moral hazard private resources must be committed in crisis events)

SUPERVISORY GUIDANCE

Liquidity risk regulatory and supervisory activities require to:

•Assess if the new liquidity requirements are less stringent than current ones – if so, run impact studies before considering the adoption of the newer recommendations. If not, analyze a gradual transition process to not choke off financial intermediaries.

•Set a credible and flexible framework for the LCR as a buffer and define its scope of application – a general standard is recommended. If entities are going to be left out of this requirement, simpler but demanding limits may be set not to alter the level playing field

•Admit tier 2 liquid assets only if they are acceptable in monetary policy operations; exceptions could only be made if and only if it could be proven that the proposed asset has a liquid market.

•Define if the reserve requirement could be admitted as part of the liquid assets of the bank and its extent.

SUPERVISORY GUIDANCE

Liquidity risk regulatory and supervisory activities require to:

•Consider alternatives to the current assets that are admissible by the LCR, such as mutual funds that invest only on high quality liquid assets according to the Basel definition so long as the resources may available the same day.

•Clarify the use of the options made available by the standard for cases of liquidity insufficiency.

- Option 1 is recommendable for countries with low Tier 1 Assets and scarce tier 2.
- Option 2 is recommendable for countries with an important foreign exchange presence in their markets.
- Option 3 is recommendable for countries with insufficient Tier 1 assets and with a lot of Tier 2 Assets

•Define if the accounting classification between AFS, HTM and trading assets, will affect the definition of HQLA.

SUPERVISORY GUIDANCE

Liquidity risk regulatory and supervisory activities require to:

•Define the disclosure requirements; especially, what institution is responsible and if the supervisor could restrict it.

•Adopt a well structured implementation plan


ASBA
Asociación de Supervisores
Bancarios de las Américas
Association of Supervisors
of Banks of the Americas

Thank you!