NATIONAL RESEARCH UNIVERSITY
HIGHER SCHOOL OF ECONOMICS

Henry Penikas

BCBS Consultative Document Monitoring Indicators for Intraday Liquidity Management

POSITION PAPER No. 2012-03

HIGHER SCHOOL OF ECONOMICS
National Research University
(Moscow, Russia)
http://www.hse.ru/en/

September 14, 2012

Basel Committee on Banking Supervision
Email: baselcommittee@bis.org

Dear Sirs,

Basel Committee on Banking Supervision Consultative Document
Monitoring Indicators for Intraday Liquidity Management

On behalf of the National Research University Higher School of Economics (NRU HSE), and particularly the International Laboratory of Decision Choice and Analysis we would like to thank the Basel Committee on Banking Supervision for the opportunity to deliver our opinion on the Consultative Document óMonitoring Indicators for Intraday Liquidity Managementô published by the Basel Committee on Banking Supervision on July 02, 2012 at http://www.bis.org/publ/bcbs225.htm.

The position paper consists of two groups of comments:
(1) Specific (answers to questions raised);
(2) Paragraph-wise (general comments).
We hope our comments would be of use for further development of the prudent international regulatory framework.

In case of further questions, please, do not hesitate to get in touch through email (dhm-econ@hse.ru), telephone (+7.495.772.95.90, ext. 26162).

Dr. Henry Penikas
Senior Research Fellow
International Laboratory of
Decision Choice and Analysis
Higher School of Economics
E-mail: Penikas@gmail.com
URL: http://www.hse.ru/en/org/persons/245889
Web-site: http://www.hse.ru/en/DeCAn/

Specific Comments (answers to questions raised on p. 3, paragraph 9)

(i) Do the proposed indicators adequately capture the intraday liquidity risk run by banks?

- Yes, the proposed indicators capture a wide liquidity environment the bank operates in.
- Though only *monitoring* purposes are stated for indicators their regular estimation would need material CapEx investments to calculation modules and data storages.
- *It is proposed to limit the set of indicators to liquidity inflows and outflows (i.e. indicator 1 and equivalent to inflows) and their probabilistic measures discussed in paragraphs 59 and 60 with respect to below comments.*

(ii) Are the stress scenarios identified in the paper comprehensive?

- Yes, the proposed scenarios are sufficient and well detailed.
- To facilitate banksô transition to the proposed ways of monitoring intraday liquidity it is proposed *to keep the scenarios mentioned as the ideal ones and allow banks to go with the ones the use for Basel II Pillar II (ICAAP) purpose.*
- Otherwise effort duplication might happen.

(iii) Is the proposed scope of application of the indicators clear?

- Yes, the proposed scope of indicators is clear.
- Never-the-less, a lot of effort would be demanded to *localize* them by national regulators given local accounting standards specifics.

(iv) What, if any, implementation challenges would the proposed reporting requirements present to banks?

- Several challenges might be thought of, including the above mentioned:
  - Additional CapEx for *respective data storage and back-up*;
  - Methodological issues of calculating liquidity risk for several branches located in different countries and particularly in different time zones (please, see comment to paragraph 11 below on business day definition).
- I would also add challenges on the regulatorsô side:
  - Additional staff and IT resources would be needed to be able to verify the accuracy of all indicator dynamics without delays to accepted terms of banksô reports review.

(v) Are the different monitoring and reporting requirements for direct and indirect payment and settlement system participants clear?

- Yes, the distinction between the direct and non-direct participants is clear and adequate.

Paragraph-wise Comments

p. 2, paragraph 4 ï ñThe aim of the proposed indicators is to enable banking supervisors to monitor a bankôs intraday liquidity risk management and its ability to meet payment and settlement obligations on a timely basis, *both in normal times and in stressed scenarios*.ò

- We propose to amend the statement after ñin normal times and in stressed scenariosò with the following text ñ*and given the growth of business aligned with strategic objectives of the institution*ò.
- The add-on is important to underline that even in normal times there might be problems experienced because of liquidity demands given the significant launch of new products etc.
- Thus it needs special treatment.

p. 3, paragraph 11 ï ñFor the purpose of this document, óbusiness dayô is defined as the opening hours of the payment and settlement system (or group of systems) during which it is possible for a bank to receive and make payments.ò

- Though correct the óbusiness dayô definition needs clarification in operational terms.
- Consider a large bank operating in several time zones (layers). Such a bank would have larger óbusiness dayô from the start of the earliest branch in the East till the latest branch at the West.
- Particular treatment is needed for global systemically important banks that operate throughout the world. The actually have an online (non-stop) business-day.
- Because of the cases described it is proposed *to align* ***ó****business day****ô*** *definition with the working hours of the local available interbank market open hours*.

p. 5, table 1 ï ñThe proposed set of indicatorsò.

- When the document on fundamental review of trading book by BCBS would be finalized it is proposed to align the methodology with the current document, i.e.

when it would be certainly decided to continue with the expected shortfall, not Value-at-Risk, and when confidence levels would be announced they should be applied to the indicators from the table (respective review would be needed for paragraphs 59 and 60).

p. 5, paragraph 15 ï ñThis indicator will show a bankôs daily *maximum* requirement for intraday liquidity in normal times by establishing its net cumulative intraday liquidity position over a *period of time*ò.

- As mentioned above the maximum value might not correspond to the most important or most probable situation. Following the logic of Annex 4 to Basel II it is proposed to extend the concept to EPE, i.e. the *effective positive exposure to liquidity risk, or effective liquidity exposure (ELE).*
- It is proposed to define the notion of a óperiod of timeô. For consistence with market risk framework the period of 10 business days is proposed to be fixed in.

p. 6, paragraph 19 ï ñThe larger the positive net cumulative position, the greater a bankôs usage of incoming payments to *fund its own payment obligations*ò.

- It is proposed to specially focus on the maximum of inflows and outflows the institution is subject to in case its counterparties fail.

p. 13, paragraph 59 ï ñIn addition, they are expected to report the 5^{th} percentile for the indicator of available intraday liquidity and the 95^{th} percentile figure for the following indicatorsò.

- To be consistent with the current Basel II market risk framework (until the confidence level is announced for the expected shortfall within the fundamental review of the trading book) it is proposed to *use 1% and 99% percentiles.*
- It is proposed to add that ñ*these probabilistic measures should be evaluated using 1-year history****ò***. Currently it is not explicitly stated. It is clear that using longer history the particular negative event would be mostly diluted. That is why common data window is proposed.

p. 13, paragraph 60 ï ñThey are also expected to report the 5th percentile for the indicator of available intraday liquidity and the 95th percentile figure for the following indicatorsò.

- Please, see the above comment to paragraph 59.

p. 16, bullet (vi) ï ñTiming of intraday paymentsò

- Using calendar time seems to be inconvenient.
- Extending the logic of comment to paragraph 11 on business day definition it is proposed to use time from zero and continue by adding minutes (min) within the accepted óbusiness dayô to arrive at the time in minutes (min).