Annex-1

Saudi Arabian Banks' Comments on BCBS Paper Entitled "Monitoring Indicators for Intraday Liquidity Management"

BANK # 1

A. GENERAL COMMENTS

In consultation with the Committee on Payment and Settlement Systems (CPSS), the Basel Committee on Banking Supervisors (BCBS) has proposed a set of indicators to monitor banks' intraday liquidity risk, including liquidity requirements, available intraday liquidity, the value of customer payments, critical obligations, credit lines and total payments. The proposed indicators, which are for monitoring purposes only and do not set new standards for intraday liquidity management, are specifically aimed at all internationally active banks but they can also be used to monitor all banks that indirectly access payment and settlement systems.

The Bank supports the aim of the Consultative Document to provide more transparency around intraday liquidity. However, we have some important concerns which we want to share with you; Our comments are as below;

1. **Governance and Control:** The document focuses mainly on monitoring intraday liquidity, but does not address other aspects such as governance and control. These aspects are as important as the monitoring of intraday liquidity and should further be elaborated on.

2. **Who is to provide the indicators**; It's not clear whether payment systems providers or individual banks will develop the systems to monitor intra-day liquidity. Since central banks are often the managers/suppliers of payment systems, we believe that there should be a dialogue between the banks and their respective central banks in the design of the indicators as well as discussions about how best to build the information infrastructure to support them. It might be better for the central banks to gather the information directly from the payment systems rather than the banks build their individual data gathering systems. This will result in economies of scale and will promote transparency and comparability of the information.

3. **Intraday Liquidity Sources**: The 'Available intraday liquidity' covers both normal and stress scenarios, however 'Available intraday liquidity' is not clearly defined. We think it is rather onerous to impose additional liquidity requirements on banks to cover for normal as well as stressed intraday liquidity scenarios. We also believe that the sources for available intraday

liquidity should be enhanced by sources such as unencumbered, non-central bank eligible collateral. Not all jurisdictions work in the same way. In some countries, central bank reserves are usable as intraday liquidity and in others they are not.

4. **Reporting Scope:** The consultative document requires that banks report on direct and indirect market participation. This would lead to a host of new reports and significant investments in MIS infrastructure. Since some of the required data would need to be sourced from the payment and settlement systems (e.g. timing of automated liquidity transfers) as well as from correspondents (timing of outgoing and incoming payments), a vast reporting framework for the banks would be required. We believe it is important that a cost/benefit analysis be undertaken and the results taken into account when defining the scope of the reporting. We also suggest that there should be a provision that would allow for 'materiality' to be agreed between financial institutions and their supervisors with regard to the monitoring of currencies. Managing intraday liquidity on a currency by currency basis will be an onerous task where banks have many (but) insignificant currency exposures. Also, banks will face challenges in addressing the different requirements of home and host supervisors; for example where a bank has a branch or subsidiary overseas, the home supervisor may not be comfortable with it providing such a sensitive information to the host supervisor. The organizational structure scope should thus be limited to the parent entity and the home supervisor.

5. **Confidentiality of Liquidity Data Information:** The proposed monitoring requires highly sensitive data. Liquidity risk data is usually of sensitive nature and can easily be misinterpreted. The document should be enhanced by a section about data confidentiality and disclosure. We suggest that all data be kept within the bank and banks only share this with the supervisors when requested. We also suggest that this be handled by the home supervisor.

6. **Top 5 correspondent banks indicators**. Banks are asked to provide exposure details for each of their "5 largest Financial Institution Customers (by value)".This indicator is dynamic and effectively requires monitoring of exposures to a much wider range of customers. This can be quite difficult if the 'top 5' would keep on changing.

   Whilst we agree bank should report its payment concentration by reporting its high value payments, there should be clarity whether the bank should report its concentration as aggregate of its internalised payments or separate.

7. **Materiality**: Who will determine the definition of materiality in determining what systems, currencies and legal entities to focus on? The data acquisition and MIS challenges for these indicators are material for most banks in our region. It would therefore be advisable if the scope is limited to key areas given the fact that there are many other regulatory developments that would also require investment in IT infrastructure.

   Daily maximum liquidity requirement: This is most significant indicator in the document which requires Banks to monitor and report net cumulative intraday liquidity position calculated on settlement time basis. Whilst this indicator attempts to monitor whether a bank significantly relies on payments to be received to fund its outgoings, under normal market conditions, it is a common model of managing intraday liquidity to fund or invest the end of day gap or excess respectively. Therefore reliance on funding the outgoings through payments received could significantly vary on a daily basis depending on the ratio of outgoings over payments received on a certain day. Imposing this specific indicator would encourage banks to actively manage this indicator by deliberately delaying the payments (time) in order to reduce the daily maximum liquidity requirement. Active management of the indicator by all market participants could thus lead to the following:

   a) A 'theoretical' no settlement in early hours of operations and could increase volumes in the last couple of hours of the operations which could unnecessarily increase the operational risk.
   b) Evolve the market towards time specific settlements which could results in additional cost as normal settlements could delay the payment due to above.
   c) Would requires investment in IT and Human resources to build the infrastructure as currently majority of the market operates on value date basis rather than value time and date basis.

B. COMMENTS ON SPECIFIC QUESTIONS RAISED IN THE CONSULTATIVE DOCUMENT

Below is our response to the specific questions the committee seeks comments on the design of the proposed indicators and on the supporting regulatory reporting regime.

<u>(i) Do the proposed indicators adequately capture the intraday liquidity risk run by banks?</u>
We believe that the indicators reflect the risks associated with intraday liquidity. We however believe that there is a need to also focus on the governance process associated with managing intraday liquidity.

(ii) Are the stress scenarios identified in the paper comprehensive?
We believe the stress scenarios are fairly comprehensive and we welcome the fact that the stress scenarios will be agreed with the supervisors.

In addition, there should be an additional indicator defined to quantify the concentration of the incoming payments from the financial institutions in order to monitor and stress test counterparty stress as stated in paragraph 35 of the document.

(iii) Is the proposed scope of application of the indicators clear?
We believe the scope of application is clear. We however suggest that there should be a provision that would allow for 'materiality' to be agreed between financial institutions and their supervisors with regard to the monitoring of intraday liquidity on a currency by currency basis.

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

In cases where a bank is a participant in the payment system and hence is required to report its intraday exposures, it would be difficult for it to also report activities relating to correspondent banking services that it provides to other banks (indirect participation). Another challenge will be to address the different requirements of home and host supervisors in that where a bank has a branch or subsidiary overseas, the home supervisor may not be comfortable with it providing sensitive information to the host supervisor. In any case, central banks and systems providers have the information that regulators are looking for.

Banks will also feel burdened depending on the timeframe given to implement this requirement. At a time when the banks are in the process of implementing the recently introduced global liquidity standards, it would be a big challenge if they were required to meet these standards within a short timeframe.

(v) Are the different monitoring and reporting requirements for direct and indirect payment and settlement system participants clear?
We believe there is a need to further clarify how the exposures arising from direct and indirect payment and settlement participants would be aggregated. Will this be done on the basis of legal entities, currency or payment systems? It would be difficult to compare the regulatory returns across jurisdictions and we believe it would be difficult to be able to audit figures reported by banks intraday.

BANK # 2

We concur that intraday liquidity management is a key part of a bank's overall liquidity risk management framework. In our view, regulatory oversight of this function and additional rules and guidance might usefully focus initially on governance and controls rather than initiating additional regulation of the area with detailed intraday liquidity reporting - all be it that this reporting is stated to be for monitoring purposes only.

At a practical level, in the domestic context the bulk of transactions are denominated in local currency. Requiring reporting for all other currencies without a materiality assessment would impose a significant resource burden on banks for little obvious benefit. As regard Saudi Riyal payments, the larger part of the data suggested to be reported by banks for Saudi Riyal flows might more efficiently be collated centrally through SARIE.

Finally, whilst the paper suggests the reporting will be purely for monitoring purposes, we assume this monitoring will ultimately be for the purpose of assisting in the formulation of further regulation, possibly including some form of limit structure and / or could prompt regulatory action if a given bank's reported intraday liquidity position or trend was perceived to be unfavourable. This gives rise to two issues: first, greater clarity as to the ultimate purpose of the monitoring regime would be beneficial to all stakeholders in evaluating the effectiveness of the proposals; second, since banks have discretion as to the intraday timing of the bulk of payments made, banks may be driven to postpone payments to the latest possible time in order to present flattering intraday liquidity numbers. Far from improving intraday liquidity risk management, this would result in heightened risk of a payment failure due to the clustering of payments late in the day and the lack of time to resolve any operational or other issues that may arise.

BANK # 3

Bank Comments

1) **Paragraph 12 Page 3- Definition and constituent elements of intraday liquidity**

The paper provides the constituent elements of a bank's intraday liquidity sources and needs. The bank wishes to add this list other of Sources for available intraday liquidity which may include unencumbered securities of sound ratings as well.

2) **Paragraph 15, Page 5- Daily maximum liquidity requirement**

This indicator will show a bank's daily maximum requirement for intraday liquidity in normal times by establishing its net cumulative intraday liquidity position over a period of time. The net cumulative intraday liquidity position of a bank is the difference between the value of its payments received and the value of its payments made at any point in the day. The bank's largest negative net cumulative position during the day will determine its maximum intraday liquidity requirement on that day.

Bank Comments:

In an attempt to improve this indicator and to make their net exposure positive banks might make efforts to delay their intraday payments till end of day which might lead to a potential payment gridlock in the payment and settlement system which would potentially lead to a liquidity risk for the whole system.

3) **Paragraph 58, Page 13- Reporting frequency and granularity**

Banks are expected to report the monitoring indicators to their supervisor on a monthly basis in line with proposed LCR reporting requirements. A template reporting form can be found in Annex 2. As noted above, the indicators have been designed to apply to all banks, but it will be left to local supervisors to determine the scope of firms required to report the indicators.

Bank Comments:

Reporting requirements cover a wide range of indicators of intraday liquidity and the results of a series of stress tests. The reporting is required for each payment and settlement system the bank participates in - for each currency - and for each significant legal entity in a group. It will result into a whole new set of reports and a major investment to further improve the reporting infrastructure.

On the whole, focus of the document remains on monitoring and reporting of intraday liquidity risk; we are of the opinion that guidelines should also be given on the control and governance framework for the intraday liquidity management.

BANK # 4

It is noted that the Consultation paper considers six operational elements that should be part of a bank's strategy for managing intraday liquidity risk, including all the monitoring indicators and stress testing metrics.

The key recommendations from Bank would be as follows:

Consider which monitoring ratios are most relevant for the domestic market and focus reporting on those metrics such as the "Available Intraday Liquidity /Daily Maximum Liquidity Requirement"; Encourage the enhancement of Real Time Gross Settlement (RTGS) systems, to provide the relevant indicators on a daily basis to assist direct participants with monitoring intraday liquid risk;

The Consultation Paper requested that banks respond to five specific questions.

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

Whilst the indicators proposed are considered adequate, not all indicators are considered material for the Saudi Market.

As discussed within the Consultation Paper, not all measures will be appropriate to all sites and any inclusion within a regulatory monitoring report should consider factors such as materiality, relevance, and whether a combined set of stress scenarios provide a more meaningful measure. Thus it is recommended for local regulatory discretion to be retained to define which of the metrics are relevant and required to be reported.

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

The four distinct categories of stress test scenarios are considered sufficient.

Whereby three involve changes in banks' payment profile, which in turn affect their intraday liquidity needs and the forth involves a change in the value of the assets that a bank has to support its intraday liquidity needs.

Preparing stress scenarios in combination with the monitoring indicators will require subjective inputs making comparisons of results difficult across real-time gross settlement (RTGS) systems unless a consistent set of assumptions are applied.

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

The scope of application is clear and there are no further comments in this area.

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

Implementation challenges appear significant requiring enhancements to RTGS systems such to be able to generate on a real time basis the necessary consolidated liquidity information as well as the integration with internal Bank specific systems used for liquidity management to facilitate timely analysis and reporting.

The following indicators would be recommendations for RTGS systems to include in the daily batch report:

The daily maximum liquidity requirement against specific time intervals as a measure of total receipts and payments recorded at regular time intervals;

The inclusion of payment throughput % on an hourly basis even where central banks have not set targets;
Total gross payments made for the day by the bank; and Average daily settlement time of transactions once they enter the RTGS system.

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

There are no further observations on the different monitoring and reporting requirements at this stage.

Overall, the Bank welcomes the changes being proposed and believes that these revisions will over time lead to a more comprehensive level of understanding for liquidity management.

BANK # 5

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

Bank's Comments: Yes

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

Bank's Comments: Yes, the stress scenarios are comprehensive. However, the assumptions adopted for each scenario are not well defined, which may lead to differing interpretation and result in dissimilar indicator levels.

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

Bank's Comments: Yes.

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

Bank's Comments

It is expected that most of the indicators are based on actual timing of payments in **various** systems **where it is expected at international banks** there **would be** no process in place to receive such information on a daily or more frequent basis. Hence, appropriate IT applications needs to be developed in conjunction with **national payment system** not only to capture these details on a daily basis but also to perform required analyses for computing the indicator values.

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

Bank's comments: Reporting requirements are clear.

BANK # 6

Please find below our post review comments:

I. The indicators proposed vis-a-vis Liquidity Coverage Ratio (LCR) and Net Stable Funding Ratio (NSFR) appear appropriate for the purpose of capturing intraday liquidity risk run by the bank both under normal and stressed conditions.

II. The proposed stress scenarios encapsulated in the document are sufficient for stress analysis purposes and are expected to provide insight to banks as regards managing their liquidity profile from intra-day and also strategic perspective.

III. The scope of application for stress scenarios at different levels, in terms of currency, organizational structure and home / host supervisor would entail and expect banks to have robust systems architecture enabling them not only to cater to Business As Usual requirements but also to run stress scenarios simultaneously at both, stand alone and consolidated levels and to be able to communicate results thereof at appropriate management levels.

IV. The proposed requirements may pose the following implementation challenges to the banks:

- A robust IT infrastructure would be required with capabilities of providing granular data for real-time analysis and reporting as envisaged in the document. Scoping and planning the IT infrastructure will require additional time and may present additional challenges that we will need to work around before we can commit to implement.

- The monitoring of delivery and payment will play a critical role whilst determining actual / real time intra-day liquidity requirement, therefore, banks will be required to develop appropriate system capability to comprehensively capture delivery and payments data.

- In Annexure, banks are expected to report in future, average intraday liquidity, however, additional clarity is required as regards calculation methodology of such average i.e. whether the average would be calculated as a sum total of daily average intraday liquidity figure or would be calculated as a simple average of daily intraday liquidity.

- Where banks have a tacit understanding with the regulator, without any formal agreements, with respect to extension of credit facilities for intraday liquidity management for national payment systems, would the banks be permitted to include such facilities as part of their own sources of intraday liquidity.

- Further, we seek clarity with reference to Islamic Banks' transactions including, Murabaha transactions, which by their nature, double up

cash flows for each transaction due to the involvement of commodity brokers/agents. There may be a requirement to off-set some of these flows, which should be feasible because the flows and their timing are controlled by the bank.

- The availability of suitable collateral to service intraday liquidity remains a significant issue for some banking system, as it does in the context of all liquidity measures. This is particularly the case for the Islamic banks. (Should relevant central bank require collateral to be posted then there would be a need for such central bank to officially recognize the commodity murabaha based investments that the Islamic banks have.)

BANK # 7

- Our primary concern relates to the assumptions that are imbedded in the recommended monitoring.

- The first assumption is that the cash flow management systems have the instantaneous capability of resolving cash in bank accounts with a time resolution of hourly basis. Moreover, it assumes that the information and cash flow certainty is symmetrical across facing institutions, and all banks will have online cash flow management systems that can allow continuous management of cash.

- The multi-currency issues are assumed that different jurisdictions will have online time alignment across time zones.

- Not enough discussion and thinking is represented in the consultative document on these underlying assumptions and furthermore, what are the potential costs and timelines that it will take for the global banking industry to be able to meet these requirements?

- In addition, there is also an implied assumption that the derivatives are centrally cleared in all jurisdictions. As you may be aware that the central clearing system has a fundamental disconnect in the Islamic legal jurisdictions which are non-netting jurisdictions. The non-netting jurisdictions have to first figure out how they can comply with central clearing architecture with a non-netting legal framework.

- The section "Reporting frequency and granularity" on page 13 is unclear because it seems to suggest that the reporting will be on a monthly basis; however the example states that the cash flow picture will be hourly.

  - Does that mean the reporting is backward looking or forward looking?
  - Assuming it is forward looking, which is what we believe a regulator would want how do we know on a particular day; let's say 15 days in future a payment of USD 200Mio from a bank e.g. Citibank is to arrive in our account and what time it will be exactly credited?
  - These are some observations on the practical implementation which need more analysis, understanding as well as clarity for all stakeholders.

- We also have the issue of branches in other countries where the relationships of home Vs host supervisors are very important factor. This has some fundamental implications for Saudi jurisdiction where the sharing of data regulations might come into contradiction with the requirement of mutual and full reporting between supervisors. This is something that has to be better explained and understood in terms of disclosures obligations between supervisors.