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Basel Committee on Banking Supervision
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Re: Consultation paper on revisions to the credit valuation adjustment risk framework

We thank you for the opportunity to provide comments on the consultative document “*Credit Valuation Adjustment: target final revisions*”, published November 2019.

We have captured our industry comments below on **Annexure A**.

We support the fact that the revisions aim to align relevant parts of the revised CVA risk framework with the *Minimum Capital Requirements for Mark Risk* published in January 2019 as well as *The Capital Requirements for Banks Exposure to Central Counterparties*.

Yours sincerely



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Prudential Division

ANNEXURE A

Reference	Specific revisions arising from the consultative document on CVA risk	Comments	Recommendations
General		➤ Since the intention of these regulations is to base the capital charge on the underlying sensitivity of the portfolio, and the definition of sensitivities given thus far can be interpreted as the derivative of the risk factor, can we get explicit mention of whether or not the usage of AAD (automatic algorithmic differentiation) is permissible?	
MAR50.5 (2)	SFT's and CCT included in the CVA capital calculations	We believe that client cleared transactions (CCT) and securities financing transactions (SFT), should be removed from the scope of CVA for the following reasons: a) CCT's are not accounted for on the bank's balance sheet as the bank does not assume principal risk in this transaction. The bank rather acts as a clearing member in an agency capacity to facilitate the clearing of trades for the client. The only scenario where the bank could incur a loss from its client clearing activity would be where the client defaults, which is captured through the separate CCR charge. - This has a significant impact on the Prime Banking Services business whereby banks transact on behalf of clients with an equity listed exchange b) SFT's are transacted on a principal basis and therefore recorded on the balance sheet. However, curves used by banks to mark SFTs don't generally reflect the counterparty credit risk of the counterparty due to significant overcollateralization. Rather, the valuation of an SFT is primarily driven by the curve associated	➤ Consistent with the overall aim to align the CVA framework more closely with industry practices for accounting purposes, we recommend to removing CCTs and SFTs from the scope of CVA capital charge.

		with supply and demand factors of the underlying collateral. Hence, a bank would not incur any losses from a deterioration of the counterparty prior to any default and therefore a CVA charge is not warranted. c) Including CCTs in the calculation of CVA capital, will be system intensive due to the large volumes of transactions executed.	
MAR50.14	Adjusting the calibration of the BA-CVA via a general scalar commensurately to any changes to the SA-CVA	We understand that regulators may want BA-CVA to yield on average higher capital requirements than SA-CVA as the latter reflects CVA risks more comprehensively. To strike an overall balance between the need for a more conservative calibration for BA-CVA to account for missing risk factors but also preserve BA-CVA as an effective fallback to SA-CVA, we believe that BA-CVA's capital charge should not be more than 50% of SA-CVA's.	➤ We support the introduction of a scalar for BA-CVA as the most effective way to ensure a coherently calibrated CVA framework.
MAR50.16	Granular Risk Weights for Financial Counterparties	We welcome the proposed change to the risk weight bucket relating to HY and NR credit quality of sovereign counterparties from 3.0% to 2.0%. We would like to draw attention to the following: I. In the revised CVA framework, all financial sector entities are given the same risk weight, irrespective of the type of financial sector entity. II. Furthermore, there are only two risk weights to reflect credit quality. This bucket is very broad and captures a diverse set of entities, which includes highly regulated institutions, unregulated and highly leveraged institutions.	We believe that using more granular credit risk buckets, risk sensitivity for financials could be improved by specifying different risk weights for different types of financial institutions, which will be more representative of the underlying CVA risk. Furthermore, it would be more consistent with other areas of the Basel framework, e.g. the Treatment of the Regulated and Unregulated Financials in the Standardised Approach for Default

			Risk, where lower risk weights are applied to prudentially regulated banks compared to other financials that are treated as corporates, with higher risk weights.
MAR50.32 (9)	Reduce the floor for the margin period of risk for client cleared derivatives	We support the proposed change to set the MPOR floor at 4+n for client cleared transactions. We would like to draw your attention to the following: i. We strongly believe that the MPOR floor should be revisited for all transactions, which is set at a minimum of 9+N business days, irrespective of master agreement documentation, jurisdiction legal differences, or type of counterparty, under the revised framework. We are concerned that a 10-day MPOR leads to an overstatement of regulatory CVA, when compared to accounting CVA for collateralized counterparties. - Since banks hedge based on economic CVA risk rather than regulatory CVA the impact of hedges is reduced in the CVA charge, if the floor is increased, compared to how hedges would reduce actual CVA losses. ii. The MPOR proposed, should align and take into consideration the BCBS standard on Margin requirements for non-centrally cleared derivatives.	➤ The legal terms negotiated between parties should form the basis in determining the MPOR.
MAR50.40 to MAR50.41	Revision of the CVA Multiplier (mCVA) from 1.25 to a range between 1 to 1.25	We support the revision of the CVA multiplier and the Committee's efforts in seeking to resolve the calibration of the capital requirement for CVA risk, being disproportionate relative to the underlying economic risk to the associated counterparty default risk.	➤ We recommend that the mCVA multiplier be set to one. - A case-by-case approach that considers the model risk management framework of the bank is a more

		We would like to draw attention to the following: i. We believe that the calculation of CVA sensitivities is not a significantly more complex process than the sensitivity calculation of trading book instruments. This process is inherently like the Market Risk sensitivity calculation process. - We are not aware of any quantitative analysis that would indicate a 25% increase in model risk for computation of CVA risk sensitivities, when compared to Market Risk sensitivities.	proportionate and targeted supervisory approach to managing model risk. This would also increase the incentives for banks to improve CVA models and mitigate model risk
MAR50.50	Introduction of index buckets for counterparty credit spread and reference credit spread and equity risks	We support the proposed introduction of index buckets.	
MAR50.56	Revision of interest rate risk weights We note: The interest rate delta risk factors for a bank's reporting currency and for the following currencies USD, EUR, GBP, AUD, CAD, SEK or JPY.	Sensitivity calculations are mentioned with respect to risk-free rates. Are we to assume that all current IBOR curves are to be represented as a spread over a suitable risk-free curve? - This would also apply to other bucketing requirements (i.e. credit spreads).	
MAR50.57	Revision of the risk-free yield curve and inflation rate risk weights from 2.25% to 1.58%	We support the proposed reduction in the risk weights.	
MAR50.58	Revision of the interest rate volatilities and inflation rate volatilities rate risk weights.	We support the proposed reduction in the risk weights.	
MAR50.61	Revision of the risk weight for all exchange rates between the bank's reporting currency and another currency from 21% to 11%	We support the proposed reduction in the risk weights.	
MAR50.62	Revision of the FX volatility risk weights.	We support the proposed reduction in the risk weights.	

MAR50.64	Correlations between Sovereigns and other credits	The new CVA (and revisions) materially improve the recognition of proxy hedges but fail to address a concern with the recognition of such hedges in a non-developed market context. Emerging market systemic risk is generally dominated by the sovereign of each market concerned. This is often the best proxy hedge for hedging CVA risk (being a systemic risk, primarily), and is generally one of the few tradable counters. The revisions maintain a very low correlation between sovereign and other risk types. This leaves banks running EM CVA with the choice of either entering a reasonable economic hedge (the sovereign) or a reasonable regulatory hedge (a credit in an equivalent industry with no economic relation). This penalises the pricing of emerging market derivative risks, creating an unnecessary barrier to corporate hedging which is directly at odds with emerging markets immaterial impact on systemic risk. ➤ We would recommend increasing the correlation for sovereign in an EM/HY context when hedging corporates with the sovereign credit of their own sovereign.
MAR50.68	Revision to the Reference credit spread delta risk weights.	We support the proposed reduction in the risk weights.
MAR50.69	Revision to the Reference credit spread volatility risk weights.	We support the proposed reduction in the risk weights.
MAR50.73	Revision to the equity volatility risk weights.	We support the proposed reduction in the risk weights.
MAR50.77	Revision to the commodity volatility risk weights.	We support the proposed reduction in the risk weights.