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Basel Committee on Banking Supervision
Bank for International Settlements
Centralbahnplatz 2
CH-4002 Basel
Switzerland

27 March 2015

Dear Sir or Madam

Subject: Consultation Document on Revisions to the Standardised Approach for Credit Risk (December 2014)

China Construction Bank would like to thank the Basel Committee on Banking Supervision (BCBS) for the opportunity to comment on the consultative document: “Revisions to the Standardised Approach for Credit Risk” issued in December 2014. We set out in the annex our detailed comments on the proposals in the consultative document.

We thank you for your consideration. We would be happy to answer any questions on the points enclosed.

Yours sincerely

China Construction Bank

Annex:

In December 2014, Basel Committee issued the *Revisions to the Standardised Approach for Credit Risk (Consultative Document)* (noted "Revision Framework" hereinafter). Our comments are presented as below:

I. It is advisable to refine the measurement criteria for bank exposure

1. Using leverage ratio in lieu of common equity tier 1 capital adequacy ratio as the risk driver. At present, the Revision Framework considers common equity tier 1 capital ratio as one of the main drivers to determine the risk weight of banks. However, the use of capital adequacy ratio as a regulatory requirement and a risk driver concurrently may create conflicts. A systemically important bank has to maintain higher capital adequacy ratio according to the regulatory requirements. But higher capital adequacy ratio may lead to a lower risk weight, thus causing more institutions to choose the bank as their counterparty, consequently further increasing the systematic risks. Besides, since not all banks in the world have implemented Basel III by now, capital adequacy ratio is not completely comparable. Therefore, it is recommended to use the simple and comparable leverage ratio in lieu of CET1 as the risk driver.

2. Permitting national discretionary for information disclosure requirements and reducing the risk weights for small and medium-sized banks. The Revision Framework intends to adopt the punitive weight of 300% for banks which have not disclosed the risk drivers as required by Basel III. Whereas the disclosure requirements of Basel III mainly aim at international active banks, and this criterion is not applicable to all small and medium-sized banks. It is advisable to grant suitable discretionary power to the regulatory authorities of all countries for information disclosure. For small and medium-sized banks which meet the disclosure requirements of the unified information platform established in the country, the punitive weight of 300% need not be applied and their risk weights should be determined according to

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the risk drivers.

3. Adjusting criteria for bank credit by term. The Revision Framework divides bank credit by term into "more than 3 months" and "less than 3 months", where the term of more than 3 months applies to a higher weight. Considering that the term of interbank businesses that serve as a part of bank's liquidity reserve differs across countries, in order to avoid the negative impact on the liquidity of financial market brought by higher weight of these assets, it is advised to adjust the term to "more than 6 months" and "less than 6 months" or give national discretionary power for term division.

II. It is suggested to improve the measurement criteria for corporate exposure

1. Removing the leverage driver or giving differential treatment to countries with underdeveloped capital market. In a country with underdeveloped capital market, bank-based indirect financing usually plays a dominant role and the corporate leverage is generally high. Using leverage as a risk driver to determine risk weights thus is not fair. It is recommended to remove the leverage driver or give differential treatment to countries with developing capital market. Besides, as revenues of enterprises in developing countries are lower than those in developed countries like EU, the weight interval determined as per the level of EU countries is adverse to developing countries. It is advisable to allow developing countries to set their own weight interval based on their actual development levels.

2. Granting country discretionary power for weight of specialized loans. Under the present Revision Framework, the weight of specialized loans is equal to the counterparty's weight or 120% (or 150%, to be determined by the type of specialized loan), whichever is higher. This weight is higher than that of corporate loans. However, criteria on specialized loans differ across countries. For example, the specialized loans in the banking sector of China are characterized by higher requirements for projects, better asset quality, and lower overall risk level than other corporate loans. Therefore, it is not advisable to use a higher weight. It is suggested to allow the countries to determine the weight based on the characteristics of specialized loans and actual risk status in their banking sector.

3. Using total assets instead of operating revenue as the risk driver for management type holding companies. The Revision Framework determines the weight for corporate risk exposure as per revenue and leverage. A parent company, which focuses on group management but has less business operation of its own as shown in relational tree of the group (briefly called “management type holding company), will apply to a higher weight under the Revision Framework since such company is usually not much involved in specific business operation; however, under the internal rating-based approach, such company will normally obtain higher rating because of its strong management capability and risk resistance capacity. The results of these two approaches will show deviation. It is thus proposed to use total assets in lieu of revenue as the risk driver for management type holding companies.

4. Classifying other financial institutions separately. Under the Revision Framework, exposures to non-banking financial institutions, which do not meet the supervision and disclosure requirements, are classified into the category of exposures to corporate, for which the risk weight is uniformly determined as per revenue and leverage. Although the non-banking financial institutions have an inherent feature of high leverage, this does not mean higher risks. It is suggested to split a sub-class of non-banking financial institution under the category of corporate exposure and set a separate risk driver to determine the weight.

5. Considering that some group customers do not have consolidated financial statements, **it is suggested that the corporate exposure risk driver is calculated on a single customer basis**.

III. It is recommended to keep the definition and scope of various exposures consistent with the internal rating-based approach

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The classification of exposures under the Revision Framework is inclined towards the internal rating-based approach, but shows difference. It is advised to keep the classification as consistent as possible, thus to avoid any confusion of the scope or impact on the reform of IT system. The specific suggestions are given as below.

1. It is proposed to give differential treatment to corporate exposure of general companies and small and medium-sized enterprises. Under the Revision Framework, SMEs and other enterprises are not differentiated. Considering that SMEs have different characteristics from larger-sized enterprises, it is not fair to compare their risk drivers such as revenue with general companies at the same standard. The suggestion is to differentiate general companies and SMEs and set different risk drivers to determine the weight, so as to further improve the risk sensitivity.

2. It is recommended to give differential treatment to qualified revolving retail risk exposure and other qualified retail risk exposure. Considering that qualified revolving retail risk exposure (mainly credit card business) has smaller amount and is better in risk diversification, it is suggested to make separate classification by referring to the internal rating-based approach and give a lower weight to qualified revolving retail risk exposure.

IV. It is advised to improve the measurement criteria for claims secured by real estate

1. Properly loosing the requirements on eligible real estate property. In real estate exposure under the Revision Framework, the property securing a mortgage must be fully completed. Since different countries have varied real estate markets, regulations and policies, the mortgage loan requirements and policies for *completion* of mortgaged property are not exactly the same. It is recommended to loose the requirements on eligible real estate property according to the actual situation of different countries and allow the countries to define eligible real estate on their own.

2. Removing the use of debt service coverage ratio as a risk driver. The

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Revision Framework considers debt service coverage ratio (DSC) as one of the risk drivers for residential real estate exposure. Due to the difference of credit systems, it is hard to obtain true and complete personal income and debt information in many countries; even if the required data can be obtained when applying for a loan, it is difficult to update such data on a timely basis after the loan is granted. Over time, the initial DSC will hardly have any guiding role as the term of a residential real estate is usually long. In addition, this indicator may introduce cyclical effects. It is advisable to remove the use of DSC as risk driver for exposures secured by real estate.

3. Further clarifying the criteria for exposures secured by real estate. Except residential mortgage loans, various mortgage loans, it is necessary to specify whether the loan containing a portion of risk mitigation of real estate is identified as real estate exposure (for example, to identify as real estate exposure, the minimum proportion of risk mitigation of the real estate should meet).

V. It is proposed to maintain the existing measurement criteria for investment in capital instruments of financial institutions

Under the Revision Framework, a unified weight of 250% applies to both subordinated debt and capital instruments investment. Considering that Basel III already sets stringent provisions for capital instrument investment and has not been implementing for long, it is suggested to maintain the existing measurement criteria and continue using the method of threshold deduction for investment in equity and other capital instruments of financial institutions.

VI. It is advisable to give national discretionary power for commitment made through credit card

Under the Revision Framework, the credit conversion factor (CCF) in commitment is no longer based on the maturity but uniformly increased to 75%; and no preferential weight is assigned to commitments from credit cards. However, credit card markets that are still developing have a large gap from matured credit card markets. For example, the credit limit utilization rate is usually much lower. Therefore, despite the plentiful commitment made through credit cards, the proportion of credit limit actually converted into loans (thereby creating risks) is small. 75% of the CCF can not reasonably reflect the credit risk status of credit cards for developing markets, which is adverse to long-term development of the sector. It is advised to permit national discretion to determine the CCF of credit commitment made through credit cards, based on the development stage and characteristics of credit card business in each country.

VII. It is suggested to set a reasonable transitional period in order to provide sufficient time for optimization of banking business processes, reform of systems, and adjustment of internal policies

VIII. It is proposed to give national discretionary power in risk weights for businesses with which the identification of risks does not rely on financial information

Under the Revision Framework, determining the weight of corporate and retail risk exposure mainly relies on the financial information of counterparties. But banks have many asset businesses whose risks are not dependent on the financial status of counterparties. For instance, some loans to SMEs based on big data are granted and subject to risk evaluation considering factors such as transaction settlement and activeness of settlement accounts, without giving too much consideration to the financial indicators such as revenue and leverage. In the future, businesses based on big data will gradually increase. If the punitive weight of 300% is applied to such businesses due to the lack of relevant financial indicators, the risk assets of banks will be over-estimated. It is recommended to give national discretionary power to determine risk weights of such businesses.

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