

Warsaw, 16 April 2010

KNF – Polish Financial Supervision Authority

Response to

“International framework for liquidity risk measurement, standards and monitoring”
Consultative Document
presented by Basel Committee on Banking Supervision

REMARKS TO THE TECHNICAL PROVISIONS

1. The Basel Committee on Banking Supervision’s proposals on liquidity requirements have been elaborated in the wake of the financial crisis that almost cut funding of banks in many countries. This experience has left a distinctive impression on many regulatory initiatives of the past months, including the consultative document presented by the BCBS. While the risks the world had to face during the crisis can hardly be underestimated, we should not forget about other threats to banking sector stability that fortunately did not materialize in 2008-2009. And the document seems to pass them over. One of the dangers that were generally avoided is a bank run. The consultative document proposes some assumed percentages for various categories of deposits that are expected to run-off (paragraph 41), but these percentages are adequate to normal conditions rather than to a situation of reduced customers’ confidence.
2. Similarly, some other elements of the LCR and NSFR ratios may raise doubts, too. For instance, it is questionable that in times of a crisis a bank receives 100% of planned inflows from amounts receivable from retail and wholesale counterparties from performing assets (annex 1). What also needs explanation is why the run-off factor for unsecured wholesale funding provided by non-financial corporate customers was estimated for the purposes of the LCR at 75% (paragraph 54), while the same category was attributed 50% stability factor for the purposes of the NSFR (paragraph 86).
3. The NSFR, as it is proposed by the Committee, may make it more attractive for banks to buy bonds of highly-rated nonfinancial companies than to offer them credits. Eventually, banks may also decide to substitute existing credits with bonds. Consequences of this development should be further analyzed.
4. What may need further attention is the fact that it will be hard to meet the NSFR requirement for banks that depend overwhelmingly on wholesale funding, like those specializing in car or mortgage loans.

5. Generally, the proposed outflow and inflow factors for both the LCR and NSFR, being crucial for the ratios to achieve their goal, should be calibrated very carefully. Any estimates must be preceded by thorough analysis (verification of statistical data).
6. Among the monitoring tools, the contractual maturity mismatch profile (95-103) is an acknowledged, noncontroversial metric, while the concentration-of-funding metric (paragraphs 104-116) may also reduce vulnerability of the banking sector to liquidity shocks.
7. To the contrary, the metric of available unencumbered assets (117-122) is not commonly accepted. Although it does provide some information, without reference to cash flows or other balance sheet and off-balance sheet positions, it gives supervisors no value added.
8. Within the monitoring framework stated in the document it would be advisable to standardise the liquidity gap so that banks in every country report their positions using detailed, identical buckets thus ensuring comparable data for supervisors on a global scale.
9. The document proposes that the metrics be calculated and reported at least monthly (paragraph 132). Experiences from the Polish market demonstrate that better effects would be secured by making it obligatory to calculate and report the ratios on a daily basis. This will help us avoid a situation of banks adjusting their liquidity management to given reporting dates.
10. It should be reconsidered if disclosure of information such sensitive as liquidity position (paragraph 135) would not trigger unnecessary risk for the banking sector. Misinterpretation of the data could undermine confidence in a given bank and, in consequence, result in massive deposit withdrawal.
11. It is important that the Committee, together with designing the two standardised ratios, provide as many accompanying technical parameters as possible. Otherwise national supervisors may calculate these parameters differently, which could give some banks a competitive advantage. This could, in turn, encourage regulatory arbitrage. The Committee does not necessarily have to propose exact numbers, but, for instance, consistent methodology to calculate them.

REMARKS CONCERNING THE SCOPE OF APPLICATION

12. The BCBS' proposals on liquidity rules provide a useful toolbox for countries that have not yet in place similar arrangements. They should not, however, be a priori deemed superior to those adopted by several countries, which are specifically designed to fit local conditions. In Poland, for instance, the existing liquidity regulations proved effective during the financial crisis. The Polish framework is flexible, that is adjusted to the size and legal form of a bank, with specific requirements for banks, branches of credit institutions and cooperative banks. This approach is based on an assumption that many factors determine liquidity position, some of them institution-specific and, thus, analysis of liquidity and liquidity ratios should vary depending on a bank. In line with paragraph 5, we think that the liquidity standards authored by the Committee should serve as a regulatory minimum, with national supervisors free to adopt more rigorous norms.

13. **It is of paramount importance that the liquidity rules are applied at the level of individual institutions**, although they can additionally be applied also on a group basis. It is legal entities, not groups, that are obliged to repay their liabilities and that are exposed to liquidity shortfalls. If a group has liquidity problems, they must have originated in one of the companies that form it. Historical experiences, including those of the recent crisis, demonstrate clearly that liquidity must be protected and supervised at the level of individual institutions.

14. It should also be noted that shifting liquidity requirements to the group level may lead to overreliance on liquidity held by one company within a group and, in consequence, to problems of the whole group should this company face an unexpected crisis. Moreover, if we want to solve the problem posed by institutions that are “too big to fail”, we can not eradicate one of the last barriers to unlimited consolidation of banks. Of course, if a home country supervisor is willing to apply the standards on a consolidated basis, this could serve as an additional safeguard – but not as a substitute.

15. **It should be ensured, thus, that national supervisors will be able to require all local banks – whether belonging to cross-border groups or not - to meet the Basel or national liquidity standards (whichever more stringent).** Host supervisors should have total discretion over the decision to apply liquidity rules at the local level. We are glad that paragraphs 5 and 133 indicate that the Committee is ready to implement this principle.