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Secretariat of the Basel Committee on Banking Supervision
Bank for International Settlements

Ref.: Revisions to the Basel II market risk framework

The Febraban – Brazilian Banks Federation welcomes the consultative document *Revisions to the Basel II Market Risk Framework* issued in January 2009. It is our belief that the proposed revisions introduce relevant enhancements in market risk management and capital requirement practices.

After a careful analysis of the document, we see that item (j) of section IV.4 - *Quantitative Standards* proposes that capital requirement should be calculated on a daily basis according to the following formula:

$$c = \max(VaR_{t-1}; m_b \times VaR_{avg}) + \max(SVaR_{t-1}; m \times SVaR_{avg})$$

Although we acknowledge that regulatory capital measurement should be concerned with stress conditions, we strongly believe that a more suitable model should weight both VaR and SVaR components, in order to avoid an excessive market risk capital allocation. In our opinion an overestimated capital could render certain banking activities not feasible and could consequently cause negative impact in prevailing economic conditions.

For the weighting of those two components of capital requirement, we suggest the adoption of a weighting factor (p), defined by the local supervisor, ranging from 0 to 1. We further suggest that in low volatility periods a p factor of lesser value should be adopted, in order to emphasize the SVaR component during upswing phases of economic cycles. Additionally, we would like to suggest that multiplication factors m and m_b be the same and equal to m_b .

The suggestions above lead us to the following calculation formula:

$$c = p \times \max(VaR_{t-1}; m_b \times VaR_{avg}) + (1 - p) \times \max(SVaR_{t-1}; m_b \times SVaR_{avg})$$

Concerning the adjustment to the current valuation of less liquid positions related in section VII, we believe that the constitution of reserves would be a better path, and also suggest that preventive measures relative to economic cycles should be considered, such as anticyclical provisions for market risk.

Finally, we would like to congratulate the Basel Committee on the way it has been handling this most challenging issue at such eventful times.

Wilson Roberto Levorato
General Director

Frederico William Wolf
Risk Management Deputy Director