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# Deloitte Banking Alert

## December 2020

## 9.4 billion EUR of additional Tier 1 capital to be added by EU banks to comply with final Basel III

The European Banking Authority (EBA) published a **Report on the impact of implementing the final Basel III reforms in the European Union**. According to the report, the **full Basel III implementation, in 2028, would result in an average increase of 15.4% on the current Tier 1 minimum required capital of EU banks**. The results do not reflect the economic impact of the COVID-19 pandemic on participating banks as the reference date of this impact assessment is December 2019.

**To comply with the new framework EU banks would need EUR 9.4 billion of additional Tier 1 capital.** These estimates are based on the assumption that Basel III requirements are implemented in full.

## Banks need to increase their capital

The cumulative impact analysis of the present report uses a sample of 106 banks, split between 40 Group 1 banks and 66 Group 2 banks.

The weighted average change of total T1 minimum required capital (MRC) after full implementation of the reform is 15.4% (for the reduced estimation bias sample) across all 106 banks, 16.2% for the large and internationally active banks (Group 1) and 11.1% for the other banks (Group 2). It is to be mentioned that **for the G-SIIs there is expected an average increase on the current Tier 1 minimum required capital of 23.0%.**

| Bank group | Credit risk | | | MR | CVA | Op Risk | Other Pillar 1 | Output floor | Total risk-based | LR | Total |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | SA | RB | Securitisation | | | | | | | | |
| **All banks** | 2.2 | 2.4 | 0.4 | 0.6 | 3.0 | 3.8 | -0.3 | 6.2 | 18.3 | -2.8 | 15.4 |
| **Group 1** | 1.9 | 2.2 | 0.4 | 0.7 | 3.2 | 4.1 | -0.4 | 7.0 | 19.1 | -2.9 | 16.2 |
| Of which: G-SIIs | 2.1 | 3.5 | 0.6 | 0.5 | 3.1 | 6.2 | -0.2 | 6.8 | 22.6 | 0.4 | 23.0 |
| **Group 2** | 4.4 | 3.3 | 0.0 | 0.4 | 1.5 | 2.3 | 0.0 | 1.9 | 13.8 | -2.7 | 11.1 |

***Source****: EBA Report on the impact of implementing the final Basel III reforms in the EU*

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Based on the constant sample of 87 banks that have been consistently submitting data from December 2018 to December 2019, and applying the latest methodology (as of December 2019), **the results show that the impact in December 2019 is slightly reduced compared with the previous references dates**.

Beyond the results of the present report, the EBA will also publish, on 15 December 2020, a more detailed ad hoc report, which will respond to the European Commission's Call for Advice (CfA) on Basel III, based on the same reference date (December 2019).

## Net stable funding ratio (NSFR) and Operational risk impact

In addition to the estimation of the impact of the implementation of the Basel III reforms, as finalised in December 2017, the current monitoring exercise report also assesses the impact of implementing the net stable funding ratio (NSFR) framework. **The results show that, in December 2019, EU banks required additional stable funding of EUR 24.3 billion to fulfil the minimum NSFR requirement of 100%.**

**Compared with the June 2019 exercise, the shortfall of stable funding decreased by EUR 9.4 billion.** The improvement is mainly attributable to Group 1 banks (EUR 16.4 billion vs EUR 29.3 billion in previous report), which compensate for a slight worsening for Group 2 banks (EUR 8 billion vs EUR 4.3 billion). **Taking a longer-term perspective, for the constant sample of banks over time, it can be observed that the compliance with the NSFR has steadily improved since the start of the monitoring exercise in June 2011.**

**As regards operational risk**, **the final Basel III framework replaces all existing approaches**, including the model-driven advanced measurement approach (AMA), with a new approach, the standardised measurement approach (SMA). **Under the new operational risk framework, banks can use only the SMA.**

**The revisions to the framework generate an aggregate increase in operational risk MRC of approximately 40.9% for Group 1 banks and 28.6% for Group 2 banks.**

## Earlier this year, Basel III implementation has been delayed by one year due to COVID-19 pandemics

A press release published on March 27 announced **deferral of Basel III implementation to increase operational capacity of banks and supervisors to respond to COVID-19**.

"**It is important that banks and supervisors are able to commit their full resources to respond to the impact of COVID-19.** This includes providing critical services to the real economy and ensuring that the banking system remains financially and operationally resilient." said François Villeroy de Galhau, Chairman of the GHOS and Governor of the Bank of France.

**The revised timeline is therefore not expected to dilute the capital strength of the global banking system,** but will provide banks and supervisors additional capacity to respond immediately and effectively to the impact of COVID-19.

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| Standard | Original implementation date | Revised implementation date |
|---|---|---|
| Revised leverage ratio framework and G-SIB buffer | 1 January 2022 | 1 January 2023 |
| Revised standardised approach for credit risk | 1 January 2022 | 1 January 2023 |
| Revised IRB approach for credit risk | 1 January 2022 | 1 January 2023 |
| Revised operational risk framework | 1 January 2022 | 1 January 2023 |
| Revised CVA framework | 1 January 2022 | 1 January 2023 |
| Revised market risk framework | 1 January 2022 | 1 January 2023 |
| Output floor | 1 January 2022; transitional arrangements to 1 January 2027 | 1 January 2023; transitional arrangements to 1 January 2028 |
| Revised Pillar 3 disclosure framework | 1 January 2022 | 1 January 2023 |

IRB = internal ratings-based approach; CVA = credit valuation adjustment.

**Link to the full Report:**

**https://eba.europa.eu/sites/default/documents/files/document_library/Publications/Reports/2020/960797/Basel%20III%20monitoring%20report%20-%20Dec%202020.pdf**

**For further questions regarding the aspects mentioned in this alert, please don't hesitate to contact us.**

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