FiSer Regulatory Roadmap – Basel IV

Regulation	Details	Key elements and impacts
Basel IV- Credit Risk	The key objectives of revising both the Standardised and Advanced Based approaches to credit risk are:: i) reduce the complexity of the credit risk framework, ii) improve comparability among banks and (iii) reduce the variation in risk weights across banks. The overall aim is not to increase the total required capital.	The key proposed changes impact as follows:i) recalibration of risk weights for standardised approach, ii) higher due diligence requirements to use external ratings and quality of collateral in using the standardised approach, iii) removal of the option to use internal rating-based models for certain exposure classes e.g. banks and (iv) IRB models to be subject to capital floors and parameter restrictions.
Basel IV- Market Risk (incorporates the FRTB)	Over the years a number of structural flaws in the market risk framework have remained unaddressed. The Fundamental Review of the Trading Book (FRTB) was conducted as a result of this at the beginning of 2016. New revisions were put in place, namely: i) a revised banking book vs trading book boundary, ii) a revised internal models approach (IMA) to focus on tail risk, iii) desk level IMA approval process with P&L attribution analysis requirements and iv) a revised standardised approach (SA) to make it more risk-sensitive.	The purpose of the revisions is to deliver credible capital outcomes and to promote consistent implementation of the standards across jurisdictions. The implications of the revisions are significant. Total market risk capital requirement can increase by 40% on a weighted average basis. In addition to increased capital requirements, compliance with the revised framework may entail significant changes to the business model, governance and technology, which requires additional effort and investment at a time when most institutions are under fire to reduce costs. Sector consolidation may be an option to cope with the increasing costs of compliance for trading desks.
Basel IV- Operational Risk	A new approach to operational risk is proposed, termed the Standardised Measurement Approach (SMA). It replaces the existing approaches and may facilitate the withdrawal of internal modelling for operational risk regulatory capital purposes. The measure combines both the simplicity and comparability of a standardised approach with bank-specific loss data, resulting in a more risk-sensitive, yet standardised measure of operational risk.	The key objectives of SMA are to: i) reduce the model complexity of the current modelling approach, (ii) promote the comparability of risk-based capital measures and (iii) reduce the variability in RWA calculations and capital ratios across banks. The overall impact remains significant for some banks. Larger banks would be allowed some recognition of bank-specific loss data similar to current internal models. However they would not be able to base calculations on external data, forward-looking scenario analyses or data on business environment and internal controls. Smaller banks would have to cope with increasing model complexity and loss data requirements. However, their risk measurement may increase in terms of accuracy.
Basel IV- IRRBB	BCBS has decided that the interest rate risk principles and methods used to measure, manage, monitor and control such risks need to be updated to reflect changes in market and supervisory practices. The key updates are: i) greater guidance on the expectations for a bank's IRRBB management; ii) extended disclosure requirements to promote consistency, transparency and comparability in the measurement and management of IRRBB; iii) elaborated supervisory review process on the factors to consider when assessing the bank's level and management of IRRBB exposures; iv) a stricter threshold for identifying outlier banks, from 20% of a bank's total capital to 15% of a bank's tier 1 capital.	IRRBB currently remains part of Pillar 2 requirements. The revisions will stimulate to reflect IRRBB in Pillar 2 capital requirements, thereby enhancing supervisory focus on how banks manage IRRBB. Banks can continue with internal models, but can expect more exhaustive supervisory review. Further, banks may need to, on top of their own model, apply a standardised shock scenario and/or the standardised measurement framework. Inadequate management or excessive risk taking could result in supervisory and/or regulatory capital add ons.