ISSN 2616-5902 Vol. 3, Issue 7: 107-110, DOI: 10.25236/AJBM.2021.030718

Suggestions on the implementation of Basel III under the COVID-19

Li Yusheng

Xinzhou Teachers University

Abstract: *Affected by the sudden outbreak of COVID-19 in early 2020, the global economic recession and financial fluctuations have had a huge impact on the asset quality and daily operations of banks, and also challenged the banks to support the recovery of the real economy. In order to maintain the stability of the global banking industry and the recovery of the economy, the Basel Committee delayed the implementation of Basel III standards for one year at the end of March 2020, and further strengthened the supervision of the global banking industry. This paper attempts to show that the implementation of Basel III under the COVID-19, and then put forward suggestions for the next step of implementation.*

Keywords: *Basel III, COVID-19, suggestions*

1. Background

In 1974, several international banks in Britain, the United States and Germany successively went bankrupt and settled accounts, which shocked the international banking regulators. People begin to realize that the internationalization of banks, the innovation of financial instruments and the development of off balance sheet business of banks have seriously weakened the supervision of commercial banks in various countries, but the risks borne by commercial banks themselves have greatly increased, which seriously threatens the normal operation and healthy development of the international financial system and national economy. Therefore, the supervision of international banking has been put on the schedule. In September 1974, at the suggestion of the president of the Bank of England and under the initiative and auspices of the Bank for International Settlements(BIS), representatives of central banks from 12 countries such as the United States, Britain and France met in Basel, Switzerland to discuss the international supervision and management of banks, and then established the Basel Committee on Banking Supervisory(BCBS).

The propose of the Basel record is to improve the worldwide bank regulatory framework. The Basel I was fully implemented in 1988, it has been adopted by more than 100 countries or regions around the world in different forms. However, with technological progress and financial innovation, many contents of the Basel I can not meet the requirements of the new situation. At the same time, many financial innovations are often used to avoid the rules of the Basel I. The emergence of financial innovation reduces the effectiveness of the agreement. Therefore, in developed countries, the Basel I has gradually lost its binding force. On the basis of soliciting opinions, the Basel Committee officially issued Basel II in June 2004. The New Basel Accord consists of three pillars: Minimum Capital Requirements、Supervisory Review Process and Market Discipline.

The global financial crisis triggered by the mortgage crisis in the United States in 2008 has brought huge economic losses to the international community, and various major economies have experienced economic recession. The outbreak of the financial crisis has fully exposed the defects of the previous financial supervision system, and the deficiencies of the Basel II, as an important document of international supervision, have also emerged. For example, in the original regulatory rules, the requirements for the core capital adequacy ratio are too low, which makes commercial banks suffer serious losses in front of the financial crisis. On December 8, 2017, the Basel Committee published Basel III. The core content of this agreement is to improve the minimum capital regulatory standards of the global banking industry, to improve the quantity and quality of capital, and expand the risk coverage of the capital framework. At the same time, The standard of leverage ratio and liquidity management of commercial banks are added.

In 2020, the COVID-19 has had a great impact on the economic and social operation all over the

ISSN 2616-5902 Vol. 3, Issue 7: 107-110, DOI: 10.25236/AJBM.2021.030718

world. Many industries have been affected, including the finance and banking. In order to provide sufficient liquidity to financial institutions, help enterprises maintain operations, maintain the stability of the global banking industry and economic recovery, the Basel Committee delayed the implementation of Basel III related standards by one year at the end of March 2020, further strengthened the challenges to the global banking system, and continuously evaluated the post crisis reform.

2. Main content of Basel III

On December 8, 2017, the Basel Committee announced *Basel III: Finalising Post-crisis Reforms*. The Basel III final plan determines the both macro and micro prudential supervision system. Systemic risk management and systemically important bank supervision are the new development of the concept of financial supervision. Basel III has put forward new requirements for major risk areas, which will promote profound changes in bank risk strategic decision-making, risk measurement methods and risk management processes. For example, in terms of credit risk, for new business scenarios such as online credit, it is necessary to build a risk weighting engine under the new standard method, and the group level should cover the risk jurisdiction to its subsidiaries; In terms of market risk, reconstruct the market risk measurement engine, implement the new standard method and internal model method risk measurement based on Basel III rules, and support the risk factor sensitivity model to replace the historical simulation model; In terms of operational risk, implement the new standard method, optimize the risk monitoring report, and establish a new measurement system based on business model. For more, Basel III has greatly expanded the collection requirements of new indicators and new business data, and the operation requirements and complexity of data processing have increased significantly.

3. Progress of Basel III

In July 2020, the Basel Committee released the 18th Basel III Standard Implementation Test Report, which statistically analyzed the implementation of its 27 member states as of May 2020 (Table 1). Overall, the implementation of Basel III in various countries has made some progress. Among them, these regulatory standards, such as capital definition, liquidity coverage ratio, reserve capital buffer and counter cyclical capital buffer, which were formulated relatively early and implemented relatively early, were implemented in all Member States. Some regulatory requirements, such as the proportion of net stable funds and large amount risk exposure framework, which are relatively late in policy formulation and implementation, have not been implemented by many member states. Furthermore, the credit risk, market risk and operational risk frameworks we mentioned earlier will come into force in 2023.

Table 1 The progress of Basel III in 27 member countries

Basel regulatory standards	Implementation time	The implementation of progress		
		Implementation draft issued	Release the final plan (but not implemented)	The final plan has been implemented
Capital definition	January, 2013	—	—	27
Reserve capital buffer	January, 2016	—	—	27
counter cyclical capital buffer	January, 2016	—	—	27
Total loss absorption capacity(TLAC)	January, 2019	4	1	18
Counterparty credit risk standard method	January, 2017	3	12	11
Asset securitization framework	January, 2018	1	—	21
Liquidity Coverage Ratio(LCR)	January, 2015	—	—	27
Net Stable Funding Ratio(NSFR)	January, 2018	4	11	12
Global systemically important bank(G-SIB)	January, 2016	—	—	18
Domestic systemically important banks(D-SIB)	January, 2016	—	—	26
Leverage rate of systemically important banks	January, 2018	—	—	26
Large risk exposure framework(LEX)	January, 2019	4	10	12

In the specific implementation of Basel III international standards in countries around the world, it not only pays attention to the degree of synchronization of implementation progress, but also pays attention to the consistency of national banking regulatory rules and international standards, and more

ISSN 2616-5902 Vol. 3, Issue 7: 107-110, DOI: 10.25236/AJBM.2021.030718

importantly, enhances the comparability of the results of regulatory capital ratios in various countries. Therefore, the Basel Committee comprehensively tracked the implementation of Basel III through the regulatory compliance assessment project(RCAP). The BCBS originally planned to complete the consistency assessment of the Net Stable Funding Ratio(NSFR) and the large risk exposure framework(LEX) in all countries in 2021. However, in March 2020, they decided to suspend the implementation of consistency assessment in member states in 2020, so as to allow national regulators and banks to dealing with the impact of the COVID-19. Currently, they plans to complete the consistency assessment of the NSFR and the LEX by the end of 2022. At the same time, they also planning to start the consistency assessment of the final reform of Basel III.

4. The delay of Basel III under the COVID-19

On March 27, 2020, GHOS approved a series of measures to provide banks and regulatory agencies with additional operational capabilities, hoping to assist institutions in achieving financial stability goals under the COVID-19. The measures also adjusted the implementation time of Basel III, including 1) postponing the implementation date of the Basel III standard finalized in December 2017 to January 1, 2023; 2) The implementation date of the market risk framework (revised opinions) finalized in January 2019 is postponed to January 1, 2023； 3) The implementation date of the third pillar disclosure requirements (revised opinions) finalized in December 2018 was postponed to January 1, 2023.

There are two main reasons for the GHOS postponed the implementation date of Basel III: First of all, the global economy is currently walking downward, financial market volatility has intensified, the global banking business environment has further deteriorated, and the banking industry is under greater pressure. Secondly, the COVID-19 exacerbated the impact on banking system. From the perspective of various countries, the current epidemic has a major impact on the real economy, and it will impact on the banking industry. If Basel III is implemented as scheduled, there may be a conflict between serving the real economy and building regulatory requirements in the short term, that is hard for banks. Therefore, delaying the implementation of Basel III may help alleviate the pressure on banks to meet regulatory standards and reduce the regulatory cost of banks.

5. Conclusion

From the development trend, the implementation of the Basel Accord is a long-term project. The member states of BCBS and IMF are obliged to implement these international agreements. The banking industry should continue to follow up the regulatory dynamics and actively promote the implementation of the Basel Accord. In the implementation process, we can focus on the following aspects:

1) The implementation of Basel III should be closely combined with the strategy of banks.

The implementation of the Basel Agreement is not only to calculate capital and meet compliance requirements, but the basic positioning of this work must be closely integrated with the bank's overall strategic transformation and the bank's establishment of a new development model.

We should select the most critical areas for bank development to promote the realization of the bank's strategic objectives. For example, banks should develop retail business. In the process of implementing the Basel III, we should combine the development strategy of retail business with the specific requirements of the business in the accord to promote the realization of business objectives.

2) The implementation of Basel III should further strengthen the prevention of systemic financial risks.

With the development of world economy and finance, it has become the top priority of financial supervision in most countries to firmly guard against systemic financial risks and effectively maintain financial stability. On the one hand, we should further strengthen the supervision of systematic financial institutions in accordance with the standards of Basel III and in combination with reality. On the other hand, we should comprehensively evaluate and deal with the systemic risks that may brought by the rapid development of financial technology.

3) The implement of Basel III should strengthen the coordination mechanism between capital and risk.

In the long run, the current development model relying on the rapid growth of credit scale will be restricted by leverage ratio and capital adequacy ratio, which is difficult to sustain. The main trend of banking management in the future is to establish the concept of capital constraints, gradually change the business model of high capital consumption, accurately and scientifically measure the capital, improve the level of risk pricing, and gradually establish an intensive business model.

References

[1] Yang Jun. Risk Management and Basel Accord [M]. Beijing: China finance Press,2020.
[2] Zhu Minru, Gao Xiaoguang. Management of Commercial Bank [M]. Dalian: Dongbei University of Finance&Economics Press, 2018.
[3] Ba Shusong, Zhu Yuanqian, Gao Ying. The progress and challenges of Basel III under the COVID-19 [J].China Finance, 2021(02): 56-58.
[4] Xu Qian. Challenges and suggestions in the implementation of Basel III [J]. Banker, 2020(02): 91-93.
[5] Xiong Qiyue. What's the impact of Basel III on the banking industry [J]. Financial View,2021(01): 52-54.