

**BANKING INSTITUTIONS ACT, 1998 (ACT NO. 2 OF
1998), AS AMENDED**

CIRCULAR – BIA 1/16

TO: **ALL BANKING INSTITUTIONS**

DATE: **16 FEBRUARY 2016**

BASEL III – IMPLEMENTATION FOR NAMIBIA

1. PURPOSE

This Circular is issued in line with the provisions of section 3 of the Banking Institutions Act, 1998 (Act No. 2 of 1998), as amended. The purpose is mainly to provide guidance and clarity on the implementation of the new capital accord – Basel III in Namibia. This Circular spells out the elements of Basel III to be adopted, major changes in the statutory limits and requirements, the implementation plan, phases and timelines of the Basel III accord in Namibia.

2. BACKGROUND

The Basel Committee on Banking Supervision (BCBS) in December 2010 released a package of reform initiatives called Basel III to strengthen the global quality of capital and liquidity rules, following the peak of the global financial crisis with the aim of promoting a more resilient banking and financial sector. The objectives of Basel III reforms are:

- (i) to improve the ability of the banking sector to absorb shocks arising from financial and economic sector;
- (ii) to improve the risk management and governance practices of banking institutions;
- (iii) to strengthen the resolution of systemically significant cross-border banks; and
- (iv) to strengthen the transparency and disclosure of capital and liquidity of banking institutions.

The Basel III Framework was developed in response to the deficiencies in financial regulation revealed during the world financial crisis. These measures are set out in *Basel III: A global regulatory framework for more resilient banks and banking systems* also known as 'Basel III'

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The Bank took a decision to adopt the Basel III Capital Framework in Namibia during 2015, which decision was subsequently communicated to the banking industry. This decision was informed by position paper, which assessed the feasibility and applicability of the underlying components of the Basel III Capital Adequacy Framework for Namibia, the impacts it may bring and the readiness of banking institutions to adopt and implement Basel III. The Bank is convinced that the implementation of Basel III Capital Framework will not only ensure consistency with international best practices, but also enhance the quality of domestic banking institution's capital.

The implementation of Basel III will, among others, introduce the following major requirements or changes capital requirements:

- a) **Risk-weighted capital adequacy** - In terms of the new capital requirements, **Tier 1 capital** shall comprise of: Common Equity of 5.5%; Additional Tier 1 capital equal to 1.5%; Capital Conservation Buffer of 2.5%. Tier 2 capital will amount to 3%. This is expected to bring the proposed total Risk-Weighted Capital Adequacy ratio (RWCR) for the industry to a possible level of 12.5%.

These reforms will therefore raise both the quality and quantity of the regulatory capital base and enhance the risk coverage of the capital framework.

- b) **Minimum Leverage Ratio** – all banking institutions are expected to maintain the leverage ratio in excess of 3%. This leverage ratio is expected to serve as a backstop to the risk-based capital measures and is intended to constrain excess leverage in the banking system.
- c) **Liquidity ratios** – all banking institutions will be required to comply with two new liquidity ratios, namely the **Liquidity Coverage Ratio (100%)**, which requires banking institutions to hold sufficient high-quality liquid assets to cover its total net cash outflows over 30 days; and the **Net Stable Funding Ratio (100%)** that requires the available amount of stable funding to exceed the required amount of stable funding over a 30-day period of extended stress.
- d) Apart from the above mentioned changes, the Basel III proposes some adjustments to be made to the calculation of total risk-weighted assets and gross assets for the purposes of calculating the risk-weighted capital and the leverage ratios. For example, it proposes risk-weightings of certain exposures at 1250%, which are currently deducted from the elements of capital. Further, it proposes the inclusion of off-balance sheet items as part of total exposures for the purposes of calculating minimum capital ratios.

Kindly, note that the Bank will be introducing these new requirements in phases as set out in **Table 2** below. This approach taken is expected to lessen the potential impact that these strong regulatory requirements may have on the banking industry.

3. APPLICATION

The Bank of Namibia Basel III Implementation Program is expected to be both pragmatic and flexible, thus taking into account the different profiles of all banking institutions in Namibia. The scope of application will include all banking institutions considered to be Domestic Systemically Important Banks (DSIBs) in Namibia. Smaller banking institutions, branches of foreign banking institutions operating within this jurisdiction are excluded from the strict rules of the Basel III Capital Adequacy Framework, which does not imply that their risk profiles will not be measured against capital adequacy standards.

4. IMPLEMENTATION TIMELINES

Since the Basel III Capital Adequacy Framework intends to introduce critical buffers and significant capital outlays, the key aspects of the Basel III Framework will be implemented in Phases, which start with briefing the banking industry during 2015. For more details, the banking industry is requested to note the Basel III project milestones and the respective timelines in Table 1.

Table 1 – Project Plan (Milestones)

Main Activities	Due Date
Basel III Capital and Leverage ratio requirements	
(i) Informing banking institutions of the implementation of Basel III Capital Rules;	30 June 2015
(ii) Training - Basel III Capital Rules;	30 September 2015
(iii) Draft Amendment to Determination on Measurement and Calculation of Credit Risk, Market and Operational Risk (BID-5) ;	31 March 2016
(iv) Workshop/Training by Consultants of Afritac South (IMF);	15 April 2016
(v) Draft Determination on Measurement and Calculation of Credit Risk, Market and Operational Risk (BID-5) and Phasing Schedule issued to the industry for consultation;	30 June 2016
(vi) Conduct Quantitative Impact Study on implementation of the Basel III Standards and obtain feedback from the banking industry;	1 July - 31 October 2016
(vii) Issue Final Determination on Measurement and Calculation of Credit Risk, Market and Operational Risk (BID-5);	31 December 2016
(viii) Implementation of the parallel – run.	1 July 2017
Liquidity requirements	
(i) Inform banking institutions of the implementation of Basel III Liquidity Rules;	30 June 2016
(ii) Draft Amendments to Determination on Minimum Liquidity Requirements (BID-6);	31 March 2017
(iii) Draft Determination on Minimum Liquidity Requirements (BID-6) and Phasing Schedule issued to the industry for	31 March 2017

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consultation;		
(iv)	Conduct Quantitative Impact Study on implementation of the Basel III Liquidity rules – (Liquidity Coverage Ratio and Net Stable Funding Ratio) and obtain feedback from banking industry;	1 April – 31 August 2017
(v)	Issue Determination on Minimum Liquidity Requirements (BID-6);	30 September 2017
(vi)	Implementation parallel – run.	1 July 2018

In addition, in Table 2 below the Bank presents the phase-in arrangement for the implementation of the Basel III Capital Framework. This Capital Adequacy Framework is expected to become effect by 2021, which has a two year time lag behind the recommended date envisaged by the Basel Committee. In terms of the Basel Committee timelines banking intuitions are expected to comply with the new capital and liquidity rules by 2019, while they have to comply with new capital and liquidity requirements for Namibia only by 2021.

Table 2: Namibia Basel III implementation plan phases:

	Current		Phased-in Arrangement				
	2015	2016	2017	2018	2019	2020	2021
Minimum Common Equity Capital Ratio	7.0%	7.0%	5.5%	5.5%	5.5%		
Additional Tier 1 Capital (maximum)			1.5%	1.5%	1.5%		
Common Equity Tier 1 Capital	7.0%	7.0%	7.0%	7.0%	7.0%		
Capital Conservation Buffer			1.0%	2.0%	2.5%		
Total Minimum Tier 1 Capital Ratio	7.0%	7.0%	8.0%	9.0%	9.5%		
Maximum Tier 2 Capital	3.0%	3.0%	3.0%	3.0%	3.0%		
Total Risk-weighted Capital ratio	10%	10%	11%	12%	12.5%		
Leverage Ratio	6%	6%	3.0%	4.0%	5.0%		
Liquidity Coverage Ratio				60%	75%	90%	100%
Net Stable Funding Ratio				60%	75%	90%	100%

*The shaded areas in the above table represent the transitional periods – all dates are as of 1 January

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5. Project Governance Principles

The decision taken by the Bank is that the Banking Supervision Department will draft the required amendments to the relevant documents (the Determination on the Measurement and Calculation of Credit, Market and Operation Risk (BID-5), the Determination on Liquidity the Statutory Returns and the related Directives and Instructions for Completion) and engage the banking industry through consultation on the contents of the Draft Amendments.

The Bank regards the banking industry as the key stakeholder for the purposes of this project. In this regard, banking industry is expected to have dedicated Team who will be contacted or engaged by the Bank in the drafting process of the required amendments to the relevant Determinations.

These teams or officials will be expected to attend meetings or workshops that the Bank will arrange relating to the implementation of the Basel III Capital Framework.

6. ACKNOWLEDGEMENT OF RECEIPT

Two additional copies of this circular are enclosed for the use of your banking institution's independent auditors. The attached acknowledgement of receipt should be returned to the Bank as soon as possible, duly completed and signed by both the Chief Executive Officer/Managing Director of the institution and the said auditors.

Questions relating to this circular should be addressed to the:


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