Domestic-Systemically Important Banks (D-SIBs) in Mauritius

1.0 Introduction

G-SIBs

The Global-Systemically Important Banks ("G-SIBs") Framework was recommended by the Financial Stability Board (FSB)[1] in the wake of the recent global financial crisis to address the systemic risks[2] and reduce the moral hazard, posed by these financial institutions in case of failure.

Subsequently, in November 2011, the Basel Committee on Banking Supervision ("BCBS") published a framework for assessing G-SIBs. G-SIBs are financial institutions of such size, complexity and systemic interconnectedness whose distress or failure would hamper the functioning of the financial system and in turn negatively impact the real economy.

The G-SIBs Framework covers the assessment methodology for identifying G-SIBs and the higher additional loss absorbency (i.e. additional capital requirements) which G-SIBs must hold on top of Basel III capital requirements.

D-SIBs

BCBS's view is that the "too big to fail" problem does not exist only at global level but at national level also. BCBS thus adapted the G-SIB Framework to Domestic-Systemically Important Banks (D-SIBs), which can also significantly impact the domestic financial system and the economy.

In October 2012, the BCBS published a paper on "A Framework for dealing with D-SIBs". The paper comprises of policy frameworks established to address the risks posed by D-SIBs following the adverse effects which these banks would create in case of failure.

The aim of the framework is to impose stricter capital requirements for D-SIBs in order to reduce the probability of their failure and their impact on the national economy.

2.0 The Case for Mauritius

2.1 Consultation Paper on "A Framework for dealing with D-SIBs"

In line with these international developments, in August 2013, the Bank of Mauritius (BoM) released a Consultation Paper on "A Framework for dealing with D-SIBs" for the Mauritian banking industry.

The Framework discusses the methodology to be adopted by BoM for identifying D-SIBs in Mauritius and the higher loss absorbency (HLA), i.e. additional capital requirements, which D-SIBs would be subjected to.

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[1] FSB is an international body that monitors and makes recommendations about the global financial system.
[2] Systemic risk is risk that the failure of one financial institution could cause other interconnected institutions to fail and eventually harm the economy as a whole.

The framework consists of the assessment methodology for D-SIBs based on a set of Principles focusing on, firstly, the Indicator-Based Approach and secondly, the Bucketing Approach. Banks whose Segment A assets represent at least 3.5% of the total GDP would be assessed.

The Indicator Based Approach is based on 5 criteria to determine a bank's systemic importance namely: *Size, Exposure to large groups, Interconnectedness, Substitutability* and *Complexity*, where an equal weight of 20% is given to each criterion.

BoM would be collecting data from banks on a yearly basis to calculate their respective scores of systemic importance and these scores would be revised every 3 years.

Based on the above scores of systemic importance, banks classified as D-SIBS would then be segregated into different buckets with varying levels of additional loss absorbency requirements. The buckets determine the level of additional capital requirements, ranging from 1% to 2.5% Common Equity Tier 1 (CET1)[3] capital, which a bank would have to maintain. This would be on top of the capital conservation buffer[4] of 2.5% which is another requirement of the Basel III framework imposed by BCBS.

A D-SIB in a lower bucket will attract lower capital surcharge whilst a D-SIB in a higher bucket will attract higher capital surcharge.

2.2 Guideline for dealing with D-SIBs

Following consultations with the MBA and Member banks likely to be concerned, BoM issued a Guideline for dealing with D-SIBs in June 2014 with an effective date of 30 June 2014.

The data collection from banks started in June 2014 and following this exercise, 5 banks were identified as D-SIBs by BoM and subject to a capital surcharge as from 1 January 2016 brought in a phased manner. These banks are expected to fully comply with the capital surcharge as from 1 January 2019. *(Click here to view BoM's Communiqué on D-SIBs dated 31 Dec' 2014)*

A second exercise has been conducted on the basis of figures as at end-June 2015 and the list of systemically important banks has remained unchanged. *(Click here to view BoM's Communiqué on D-SIBs dated 21 Jan' 2016)*

3.0 Conclusion

While the aim of the D-SIBs Framework is to make the banking sector stronger and better-capitalised, in order to withstand shocks and ensure proper functioning of the financial system, the implementation of the D-SIBs Framework poses various challenges for these banks in terms of additional capital buffers, costs, data and risk management.

Mauritius Bankers Association Limited, 28 January 2016

[3] CET 1 is recognised as the highest quality component of capital under Basel III.

[4] Capital Conservation Buffer is a buffer designed to be used in times of stress and to protect the banking systems against risks involved with excess credit growth.