BASEL III REFORMS (BASEL IV):
FOUNDATIONS FOR A RESILIENT BANKING SYSTEM
A CLOSER LOOK AT THE IMPLICATIONS OF THE CREDIT RISK CHANGES

MONOCLE
CONSULT. DESIGN. DELIVER.

1 ABOUT MONOCLE

Established in 2002, Monocle is a large independent management consulting firm specialising in banking and insurance, employing highly skilled consultants at offices in London, Amsterdam, Johannesburg and Cape Town.

Monocle has 18 years of experience working with industry-leading banks and insurance companies around the world, including institutions in the United Kingdom, Iceland, Denmark, Philippines, Singapore, Luxembourg, Thailand, South Africa, and throughout sub-Saharan Africa.

Monocle has extensive experience in implementing regulatory risk requirement projects for large, multi-juristic financial institutions and we have deep subject matter expertise specifically related to the requirements of Basel II, III and IV.

2 AN OVERVIEW

The purpose of the Basel III Reforms published by the Basel Committee on Banking Supervision (BCBS) in December 2017 – a package of reforms commonly known as 'Basel IV' – is to provide confidence in the banking system by improving the comparability of banks' capital ratios.

From a credit risk perspective, this is primarily to be achieved by the implementation of an output floor – designed to reduce the variation in RWAs across banks resulting from their internal models.

- Mandatory implementation of revised standardised approach
- Reduce reliance on external ratings
- Changes to methodology to remove the option to use A-IRB
- Application of regulatory minimum input levels (e.g. PD)

**The 5-year phase in period, originally due to start in 2022, will be revised following the global COVID-19 pandemic.*

3 FIRST STEPS

- Calculate a high-level estimate of future capital requirements on an asset class basis to prepare your organisation for future capital needs.
- Map existing processes and outputs to new regulatory reporting/ QIS formats to automate these processes and reduce reliance on already constraint resources during a period of dual reporting.
- Perform a gap analysis of data required to implement the revised standardised approach.
- Initiate data sourcing process for additional elements required under the standardised approach.
- If a new system is required for the calculation of the standardised approach, gather requirements for the new strategic system and initiate your organisation's RFP process.
- Implement a simplified standardised approach calculation using proven technology to facilitate the transition and test the strategic solution.

4 KEY CHALLENGES

- Recognising the potential increase in capital requirements as a result of the capital floor
- Calculating credit RWA using multiple methodologies (e.g. IRB approach and standardised approach)
- Understanding and mapping regulatory reporting changes
- Identifying and sourcing new data items required for the standardised approach
- Implementing the mandatory rule-based standardised calculations, as well as internal variations
- Designing automated reporting to compare RWA under the IRB and the standardised approach on an asset class level

5 HOW MONOCLE CAN ASSIST

- Monocle assists institutions with the **strategic design of regulatory risk reporting systems**, utilising a strong understanding of calculation engine changes, additional data derivations and updated reporting requirements.
- Monocle has substantial experience in designing, **building and implementing standardised credit risk engines** under the Basel II guidelines and a sound understanding of the requirements of the Basel IV standardised approach.
- Monocle has established an **extensive data dictionary of attributes** required for the standardised approach. This will fast-track the performance of a gap analysis, enabling organisations to source new data early on.
- Monocle is, at present, **involved in multiple ongoing Basel IV implementations** and can leverage lessons learnt in these projects.
- Monocle consultants are equipped with **a deep understanding of the subject matter**, extensive experience in the finance domain and rigorous technical training. Our team takes a hands-on approach to the management of the organisation's data and offers pragmatic assistance in solving any challenges.

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