Project: Enhancing Banks' Liquidity Risk Management
Time: Wednesday, 17 June, 2009**,** 14:00
Location: Albanian Association of Banks

Third Working Group Meeting

AGENDA

I. Project Progress Briefing

II. Main Findings of the Bank's suggestion on the new Draft Proposal (Discussion and approval)

III. Presentation of the BoA Updated Draft Proposal (Discussion)

IV. Expert Consultation Session (Discussion)

V. Conclusions and Distribution of Tasks

VI. Closing Remarks

SPI Albania Secretariat
Mrs. Anuela Ristani, Director of Operations, anuela.ristani@spi-albania.eu
Ms. Endrita Xhaferaj, Director Financial Modernization Program and Analytics, endrita.xhaferaj@spi-albania.eu
Address: Twin Tower I, Kati 6, Apt. A3. Tirana, Albania. Tel. +355 42 280 359; Fax. + 355 42 280 371
www.spi-albania.eu

SPI Albania Project:

Enhancing banks' liquidity risk management

DRAFT 16 June 2009

Main Findings on banks' suggestions on the Draft Regulation on Liquidity Risk Management

1. Summary findings

1.1. Bank of Albania is seeking to enhance banks' liquidity risk management by reviewing the regulatory framework according to international guidelines and best practice, including introduction of quantitative prudential ratios, in order to prevent the occurrence of systemic liquidity difficulties.

1.2. BoA has drafted a regulation that sets specific principles for the internal banks' systems for liquidity risk management. It also gives detailed definitions of liquid assets and short-term liabilities and liquidity indicators, and establishes quantitative prudential ratios, for measuring monitoring and managing liquidity risk.

1.3. Six out of sixteen banks gave their suggestions or comments on the draft regulation on Liquidity Risk Management proposed by Bank of Albania. Five out of the six banks gave quantitative assessments.

1.4. The responding banks have given information, based on their historical data on the approach they have towards considering as liquid or less liquid certain balance sheet items such as overdrafts, credit cards, credit lines, current accounts and deposits, securities etc., and off balance sheet items such as warrantees, forward contracts etc.

1.5. Banks have given their opinion on the new liquidity ratio limits introduced by Bank of Albania in the draft proposal of the new regulation.

1.6. Most of the responding banks (4 out of 6) consider the daily generation and monitoring of liquidity ratio indicators very difficult or impossible in the near term, although totally or partially doable in the future.

1.7. In general banks consider the new ratios suitable or partially suitable, and have also given their suggestions on issues that can be better managed.

SPI Albania Secretariat
Anuela Ristani, Director of Operations, anuela.ristani@spi-albania.eu
Ms. Endrita Xhaferaj, Director of Financial Modernization Program & Analytics, endrita.xhaferaj@spi-albania.eu
Address: Twin Tower I, Kati 6, Apt. A3. Tirana, Albania. Tel. +355 42 280 359;Fax. + 355 42 280 371
www.spi-albania.eu

2. Detailed presentation of the survey findings

2.1. Characteristics of the surveyed sample

Total members of AAB (no.):	**16 banks**
Market Share (100%):	**100%**
Total respondent banks (no.):	**6 banks**
Respondent ratio:	**38%**
Market share of the respondent banks: (reference indicator: total assets)	**48%**
Size of the respondent banks:	**medium, large**

6 out of 16 commercial banks operating in Albania gave their comments and suggestions on the Draft Regulation on Liquidity Risk Management. One of the responding banks did not answer to the quantitative data, but nonetheless gave its opinion on issues of the draft regulation.

The composition of the group of respondent by banks of different size is important, since they deal with different situations of liquidity as well as use different policies and strategies to manage liquidity risk.

2.2. Aggregated answers

Question 1. Based on your historical data, please provide information and arguments on:

a. the average percentage of overdrafts and credit cards approved and used in periods:

i. up to 7 days _____ ii. up to 1 month _____

Answer:

The information on historical data and average percentages used by banks for their internal control on liquidity, show that average percentage of the used part of approved overdrafts and credit cards within 7 days varies from 4.5% to 37 %, and within a month from 13% to 44%. This kind of data is not available or not applicable in 2 banks out 5 respondents.

One bank's experience suggest that reports are prepared on contractual expiry basis, therefore Overdrafts are included according to line expiry date, as done with all other BoA items. Under this assumption, this bank has been including more or less 8% in one week.

In the bank's internal scenarios, overdrafts have been considered as 100% rollover, so only interest cash inflows are deriving from them.

This bank's suggestion is that of not including any cash inflow from Overdrafts in the short-term liquidity, but including cash flow from Loans for 2% in 1 week, 3% in 1 month.

b. the average percentage of approved and unused overdrafts that you consider as short term liabilities _____

Answer:

The average percentage of approved and unused overdrafts that banks consider as short-term liabilities is about 12% for the 5 reporting banks. Two of the banks report a zero value for this indicator, while the maximum value is 30%.

c. do you include in short term liabilities any percentage of credit cards?

Answer:

Three out of 5 banks do not include in short term liabilities any percentage of credit cards.

Table 1. Credit Cards percentage as short term liabilities

	Yes	**No**
No. banks	2	3
Market share	22%	21%

d. if not, why?

Answer:

The reason for not including the unused overdrafts in the short term liabilities from the 2 banks is that although increasing, their overdraft portfolios are still minor consisting only on salary accounts and not massive use as a loan type.

In one of the banks, the reason for not including credit cards is that this is an instrument still in development for the bank.

One of the banks explains that for internal monitoring of liquidity, the analysis is included on the assumptions done on Overdrafts/Current accounts linked to the card, and that credit card impact is reflected in the Nostro account, which affects negatively bank's asset side.

Question 2. Based on your historical data, please provide information on:

a. The average of credit lines approved (unused) and irrevocable used in periods:

i. up to 7 days _____ ii. up to 1 month _____

Answer:

On the average of credit lines approved (unused) and irrevocable used, only one of the banks has given quantitative information, that is a range of 15 – 19% for credit lines used up to 7 days, and 12-14% for those used up to one month. In other banks data are either not available, or actually not taken in consideration, since they are usually in small amounts.

b. The percentage of credit lines currently considered as short term liabilities

Answer:

The percentage of credit lines currently considered as short term liabilities varies from bank to bank (on the three banks that have reported a figure) as shown below.

Table 2. Percentage of credit lines considered as short term liabilities

Bank	Percentage of unused credit lines considered as short term liabilities
1.	17-20%
2.	100%
3.	0%

One of the banks has explained their methodology on treating the credit lines as follows:

The bank integrates unutilized committed credit lines in off-balance sheet as cash outflow. The way they calculate the figure is: the monthly average of new loans for the past three months is distributed equally through the following months. In this way, they plan to include almost 100% of their projected new loans. On this bank's experience and suggestion, maturing loan payments normally offset the new loan amounts.

Question 3. Do you find it reasonable to include in liquid assets and short term liabilities the off balance sheet items listed below :

a. Liquid assets:

i. Warrantees Yes No

ii. Credit letters Yes No

iii. Upcoming Forward transactions and other off balance sheet items which can be materialized into *inflows* and will mature in 7 days Yes No

iv. If any of the above answers is No, please give your reasons and alternatives

Answer:

Table 3. Off balance sheet items to be included in liquid assets

Off balance sheet items/ no. of banks	Yes	No	N/A
Warrantees	1	3	1
Credit letters	1	3	1
Upcoming Forward transactions and other off balance sheet items which can be materialized into *inflows* and will mature in 7 days	3	1	1

A reason given for not including warranties and credit letters in liquid assets is that those are customers' transactions and do not affect the liquidity inflow of the bank.

Other items that banks might include as liquid assets are banks' approved credit lines (irrevocable) from counterparts.

b. Short term liabilities:

i. All upcoming Forward transactions Yes No

ii. Open credit uncovered letters of credit Yes No

iii. Credit lines Yes No

iv. Warranties and other off balance sheet items which can be materialized into *outflows* and will mature in 7 days

Yes No

v. If any of the above answers is No, please give your reasons and alternatives

Answer:

Table 4. Off balance sheet items to be included in short term liabilities

Off balance sheet items/ no. of banks	**Yes**	**No**	**N/A**
All upcoming Forward transactions	3	1	1
Open credit uncovered letters of credit	3	1	1
Credit lines	3	1	1
Warranties and other off balance sheet items which can be materialized into *outflows* and will mature in 7 days	3	1	1

For one of the banks, the Head office (parent bank) uses a 5% ratio on the net exposure but they do not have local historical data statistics and in addition, this raises questions on types of collaterals admitted.

Question 4. Based on your historical data, please provide information on the percentage of the used part of current accounts with credit balance.

Up to 7 days _____ Up to 1 month _____

Answer:

The information provided by banks on the percentage of the used part of current accounts, varies significantly from bank to bank, and therefore in the tables below is shown all data collected.

Table 5. Percentage of the used part of current accounts with credit balance

	Within 7 days			**Within 1 month**		
Banks	avg.	min	max	avg.	min	max
1.	28%			22%		
2.	4.40%			5%		
3.	-0.03%	-3.20%	2.20%	-0.05%	-6.40%	4.40%
4.	0.5%			2%		
5.	N/A			N/A		

The worst case scenario reported refers to September – October 2008, with a decrease of -8.8% in one month (only October).

Question 5. Based on your historical data, please provide information on the percentage of on sight deposits withdrawals

Up to 7 days _____ **Up to 1 month** _____

Answer:

The information provided by banks on the percentage of the used part of sight deposits with credit balance, varies significantly from bank to bank, and therefore in the tables below is shown all data collected.

Table 6. Percentage of the used part of on sight deposits withdrawals

	Within 7 days			**Within 1 month**		
Bank	avg.	min	max	avg.	min	max
1.	16.5%	14%	19%	26.5%	25%	28%
2.	0.50%			0.50%		
3.	-0.06%	-1.90%	0.70%	-1.20%	-3.90%	1.40%
4.	0.50%			2%		
5.	N/A			N/A		

Question 6. How often are rated the securities your bank holds in its balance sheets?

Answer:

In regards to the frequency of the rating of securities that banks hold in their balance sheets the situation is reported as follows:

- One of the banks up to now has only invested on one-year Government securities.

- One other bank daily monitors the rating available in Bloomberg and related changes for foreign securities but have no knowledge on the policy of the rating agency regarding the assessment frequency.

- Another bank performs monthly rating (reprising) of securities.

- In the forth bank securities booked as “held for trading” (which include all foreign currencies bonds, and part of Lek T-bills/Bonds), are re-evaluated on monthly bases in the banks books, showing the monthly changes in measurements due to market price fluctuations.

- One of the responding banks does not apply any rating and monitoring on securities.

Question 7. The liquidity of securities is related to the active / non active market (which is reflected in the bid-ask spread) where they are traded and worthiness of the issuer. What is your opinion on including the A^+ rating (according to S&P and the equivalent from other rating agencies)?

Answer:

Banks have different opinions regarding this proposal, as is shown below:

One of the banks is not affected by the above restriction since, based on the internal Investment Guidelines, it invests on bonds in foreign currencies issued by sovereigns or multinational banks, with a triple A rating.

Three of the responding banks agree on the use of this type of rating elaborating that such rated securities are always liquid. However, they suggest 2 different options:

1. one bank proposes the limit rating to be A^- and above;
2. - Foreign securities – one bank's opinion is that the latest rating available should be used. This info is easily monitored from all parts. An alternative could be to treat as liquid the whole securities portfolio (traded in international markets) at their market price instead of their book value.

   - Albanian Government Securities. The same bank points out that even these securities can be considered as liquid for local currency purposes, considered the appropriate haircuts, as per regulation. (Based on the Regulation "On credit operation collaterals")

As reported by one of the banks, according to the empirical studies done on the subject of liquidity, it has been concluded that there is no correlation between the credit rating and the liquidity of an instrument. Instead, there are other factors which affect the liquidity such as 1) trading turnover, 2) issue amounts, 3) number of deals, 4) bid-ask spread, 5) time to maturity, which have strong correlation with liquidity. Moreover, none of the Basel II documents gives any reference to the correlation between liquidity and credit rating of a security. Whereas, in the draft regulation it is noted an association of the credit rating with the liquidity of an instruments.

On this bank's opinion, it will not be suitable to consider credit rating of the securities as a measure of their liquidity, so the credit rating shall not be included.

Question 8. What is the level of the ratio of loans in foreign currency / deposits in foreign currency in your bank?

Answer:

The average level of the ratio of loans in foreign currency / deposits in foreign currency of the 5 responding banks is about 103%. The minimum level is 56% and the maximum 204%, and 2 out of the 5 banks have a ratio above 100%.

Question 9. Referring to the above mentioned ratio, how suitable would you consider a maximal limit of 130% (instead of 100% proposed in the draft), with the condition of the existence of a credit line contract (with the mother bank) of non less than one year to cover the amount over 100%.

Agree Disagree Why disagree

Answer:

3 out of the 5 responding banks do not agree with such proposal.

Table 7. Alternative proposal on the ratio loans in foreign currency / deposits in foreign currency

	Agree	Disagree
No. of banks	2	3
Market share	16.6%	26.4%

Reasons for disagreements from banks vary as follows:

- It is too late to turn the situation back;

- Bank of Albania is not permitting the shift of existing loans in Euro to local currency;

- banks have credit line limits of one year maturity (subject to be renewed) according to their liquidity needs;

- If for every loan exceeding the limit of 100 % there is a credit line supporting it, there is no need for such limit (130%);

- 10% of deposits is kept as reserve and some money is kept as cash for liquidity reasons so 100% matching is impossible through same currency so the bank should turn from ALL to FX which means taking foreign exchange risk;

- allowing large exposures in FX loans could increase the credit risk of loan customers who have the biggest part of their incomes in ALL, therefore a ratio above 100 % increases the systemic risk of Albanian banking system.

Question 10. Regarding the indicators in point 4 of article 15 of the proposed draft regulation:

a. **How difficult is for your bank to generate daily data?**

Impossible **Very difficult** **Difficult** **Not difficult**

Answer:

Point 4 of article 15 of the proposed draft regulation defines the liquidity ratio as liquid assets divided by liquid liabilities and banks should monitor it within the following limits:

a) minimum 0.8 – within a working day;
b) minimum 0.9 – in 3 consequent working days;
c) minimum 1 – up to one month (calculated as average of the working days)

3 out of 5 responding banks consider the generation and monitoring of such limits very difficult.

Table 8. How difficult is for your bank to generate daily data?

	Very difficult	Impossible	Not difficult
No. of banks	3	1	1
Market share	17.8%	12.9%	12.3%

b. **What makes it impossible:**

Answer:

Table 9. What makes it difficult / impossible:

	No. of banks	Market share
Existing systems of information management	2	17.2%
Impossibility of daily monitoring	2	16.6%
Impossibility of reporting the next working day	2	22.7%

The existing management information systems can be a holdback especially in regards to the bonds related data that are impossible to be correctly generated from the system.

Daily monitoring is very difficult, especially related to the fact that current tools, which generate the whole financial position of the bank, offer very poor performance and they can be used only with monthly frequency.

In addition, daily frequency of reporting would be logical for internal purposes but not for reporting to BoA.

c. Can these difficulties be overcome within a time frame?

Answer:

The four responding banks that reckon that it is either difficult or impossible to generate and monitor daily data, comment that these difficulties be totally or partially overcome within a time frame. One of the banks has an action plan on liquidity system implementation for the third quarter 2010, in relation to their Group Liquidity policy adoption.

d. Do you consider these indicators as suitable / logical?

Answer:

Overall, 3 out of the responding banks consider these indicators as suitable / logical. One of the banks has not responded and the other believes that they are only partially suitable.

e. Please suggest other alternatives

Answer:

Banks experiences and suggestions:

1. For liquidity monitoring purposes, one of the respondents banks uses a universal logic relying on a liquidity GAP analysis. All assets and liabilities are classified into time buckets according to a specific/agreed logic (cash in/cash out) and once the GAP is obtained, ratios are calculated on it. Limits are set up with relation to such ratios as well and also scenarios utilization could only rely on the same logic.
2. The bank includes contractual interest cash flows and excludes NP receivables.

3. This analysis is performed monthly and provides evidence for all terms, from 1 week to more that 15 years, split in time buckets. Therefore, even though the reporting is monthly, it reflects the forward-looking performance of the bank in all periods.

4. In the very short term (1, 2, 4 weeks) figures are pretty defined. Meanwhile, estimations/assumptions in compliance with agreed criteria are to be done despite of the method used. This is the aim of considering the statistics on historical data requested on this questionnaire. (For internal liquidity system we plan to do more detailed behavioral analysis distinguishing different counterparties).

5. For a base scenario, the bank proposes to keep 82% of Sight deposits as hard core, distributing the 18% in the time buckets 1w, 2w, 1m, 3 m, 6 m and 12m.

Ratios/limits would be calculated on these GAPs, ex. 1w GAP >=0.9, 1m GAP >= 1.

For stress test purposes (maybe is better referring to *scenario analysis* because it is difficult to set up stress test systems), certain assumptions should be defined for all banks in order for the results to be comparable. For ex. higher %-ages of retail funding decay, NP receivables increase, difficulties in wholesale funding markets.

6. It could be better to have longer term monitoring period such as 3 months - 1 year because it is very important to see the prospective liquidity situation not only the current one. It can happen that the bank's liquidity situation seems good in 1 month but the bank might have liquidity problem in the next 6 months period. In order to foresee the situation and take the precautions the proposal is to extend the period.

7. On the indicators (point 4, article 15 of the draft proposal), the liquidity ratio calculated as liquid assets divided by liquid liabilities to be reported only weekly;

8. Regarding the Liquid Assets Ratios - On the ratio of liquid assets in foreign currency to total assets in foreign currency at a minimal level of 30% - proposals are to:
   - clarify whether the indicator refers to all foreign currencies taken together, or to each currency separately;
   - set the limit for each currency if meant otherwise in the draft regulation;
   - decrease the minimal limit to 20%;

3. Implications of the findings for regulatory design

Main issues of the new regulatory proposal and banks' suggestions

ISSUE	REGULATORY PROPOSAL	BANKS' EXPERIENCES AND SUGGESTIONS	CONSIDERATIONS FOR FINAL REGULATION DRAFTING
	Systems for liquidity risk management		
Organizational framework for liquidity risk management **(Article 5 of the Draft Regulation "On Liquidity Risk Management" proposed by Bank of Albania)**	Banks should have in place effective organizational structure for liquidity risk management with a clear set of procedures and polices on liquidity risk management, defined competences, power and responsibility of the bank's bodies. Banks' boards should mainly: - Approve the Strategy and policies for liquidity risk management, including contingency plans - Review the appropriateness of the Strategy and policies ***annually;*** - Approve internal limits for liquidity management, - Review stress tests reports	Banks do have already structures and strategies for the management of liquidity risk, therefore the requirements of the new proposed regulation are well accepted.	
Stress-testing **(Article 8 of the Draft Regulation**	Banks should perform periodical stress tests and / or scenarios analysis, to identify situations that influence its liquidity position The frequency of stress tests is chosen by the	Most of banks already perform stress testing for their internal control on liquidity. The issue raised by banks is that there should be a clear definition in the regulation about	BoA may consider the option of defining 1 or 2 base scenarios for stress testing with certain assumptions defined for all banks in order for the

ISSUE	REGULATORY PROPOSAL	BANKS' EXPERIENCES AND SUGGESTIONS	CONSIDERATIONS FOR FINAL REGULATION DRAFTING
proposed by BoA)	bank but should ***not be less than twice in a year***. Bank of Albania can require more frequent stress tests. The results of stress tests are reviewed by the banks' Board and used to improve the strategy, identify main issues, and develop effective contingency plans. Scenarios could be developed as bank specific, based on factors within the banks, and scenarios arising from market or macro economical conditions (exogenous factors). The proposed regulation gives several possible scenarios that banks can use; however, it is up to banks to use the scenarios that better fit them. Banks should define the methodology of performing stress tests including the periodicity, the scenarios used, the periodical revision of assumptions used, the form and reporting of the results, and the actions to be undertaken based on the stress tests results.	the required number and formats of the basic scenarios to be followed for the stress tests. For a base scenario, the bank proposes to keep 82% of Sight deposits as hard core, distributing the 18% in the time buckets 1w, 2w, 1m, 3 m, 6 m and 12m. Ratios/limits would be calculated on these GAPs, ex. 1w GAP >=0.9, 1m GAP >= 1.	results to be comparable.
	Indicators for measuring monitoring and managing liquidity risk		
Liquidity Indicators	The liquidity ratio is calculated as liquid assets divided by liquid liabilities and banks	3 out of 5 responding banks consider the generation and monitoring of such limits very	It is still to be discussed whether the daily limits should

ISSUE	REGULATORY PROPOSAL	BANKS' EXPERIENCES AND SUGGESTIONS	CONSIDERATIONS FOR FINAL REGULATION DRAFTING
(Article 15, point 4 of the Draft Regulation proposed by BoA)	should monitor it within the following limits: a) minimum 0.8 – within a working day; b) minimum 0.9 – in 3 consequent working days; c) minimum 1 – up to one month (calculated as average of the working days) In case of failure to meet the established limits, the banks should report to the Bank of Albania not later than the following working day.	difficult. The existing management information systems can be a holdback especially in regards to the bonds related data that are impossible to be correctly generated from the system. Daily monitoring is very difficult, especially related to the fact that current tools, which generate the whole financial position of the bank, offer very poor performance and they can be used only with monthly frequency. In addition, daily frequency of reporting would be logical for internal purposes but not for reporting to BoA. The four responding banks that reckon that it is either difficult or impossible to generate and monitor daily data, comment that these difficulties be totally or partially overcome within a time frame.	only be indicative, and whether the reporting period in case of failure to meet the limits should be extended. One of the possible alternatives is for the liquidity ratio calculated as liquid assets divided by liquid liabilities to be reported only weekly.
Liquid Assets Ratios **(Article 15, point 6 of the Draft Regulation**	The bank should monitor and respect in every moment the following limits: a. ratio of liquid assets to total assets at a minimal level of 20%; b. ratio of liquid assets in foreign currency to total assets in foreign currency at a minimal level of 30%;	The average level of the ratio of loans in foreign currency / deposits in foreign currency of the 5 responding banks is about 103%. The minimum level is 56% and the maximum 204%, and 2 out of the 5 banks have a ratio above 100%.	Bank of Albania may reconsider the ratios with the aim to accommodate all banks and their specifics, holding to the best practices of liquidity risk management. In particular, BoA may consider decreasing

ISSUE	REGULATORY PROPOSAL	BANKS' EXPERIENCES AND SUGGESTIONS	CONSIDERATIONS FOR FINAL REGULATION DRAFTING
proposed by BoA)	c. ratio of loans in foreign currency to deposits in foreign currency at a maximum level of 100%.	Bank of Albania has proposed another alternative: a maximal limit of 130%, with the condition of the existence of a credit line contract (with the parent bank) of non less than one year to cover the amount over 100%. 3 out of the 5 responding banks do not agree with such proposal. Reasons for disagreements from banks vary as follows: - It is too late to turn the situation back; - Bank of Albania is not permitting the shift of existing loans in Euro to local currency; - banks have credit line limits of one year maturity (subject to be renewed) according to their liquidity needs; - If for every loan exceeding the limit of 100 % there is a credit line supporting it, there is no need for such limit (130%); - 10% of deposits is kept as reserve and some money is kept as cash for liquidity reasons so 100% matching is impossible through same currency so the bank should turn from ALL to FX which means taking foreign exchange risk;	the ratio of liquid assets in foreign currency to total assets in foreign currency and increasing the ratio of loans in foreign currency to deposits in foreign currency. Regarding the ratio of liquid assets in foreign currency to total assets in foreign currency, the regulation should clarify whether the indicator refers to all foreign currencies taken together or to each currency separately.

ISSUE	REGULATORY PROPOSAL	BANKS' EXPERIENCES AND SUGGESTIONS	CONSIDERATIONS FOR FINAL REGULATION DRAFTING
		- allowing large exposures in FX loans could increase the credit risk of loan customers who have the biggest part of their incomes in ALL, therefore a ratio above 100 % increases the systemic risk of Albanian banking system.	
Liquid Assets Definition **(Article 15, point 7 of the Draft Regulation proposed by BoA)**	a. Cash; b. Accounts with Bank of Albania including the legal reserve up to 50% of its usable amount; c. Treasury Bills (up to 80%) and obligations issued by BoA or Government of Republic of Albania; d. other re-financing bills accepted by the central bank; e. Current accounts with banks, credit institutions and other financial institutions; f. Deposits with banks, credit institutions and other financial institutions with remaining maturity up to 7 days; g. Loans to banks, credit institutions and other financial institutions with remaining maturity up to 7 days (excluding subaccount 157); h. securities issued by central government and central banks with rating assigned by internationally recognized rating agency	3 out of 5 responding banks do not consider as reasonable including in liquid assets the following off balance sheet items: - Warrantees - Credit letters but do consider reasonable including in liquid assets the upcoming Forward transactions and other off balance sheet items which can be materialized into *inflows* and will mature in 7 days Banks have different opinions regarding this proposal, as is shown below: One of the banks is not affected by the above restriction since, based on the internal Investment Guidelines, it invests on bonds in foreign currencies issued by sovereigns or	

ISSUE	REGULATORY PROPOSAL	BANKS' EXPERIENCES AND SUGGESTIONS	CONSIDERATIONS FOR FINAL REGULATION DRAFTING
	equivalent to rating of S&P not less then BBB^- (investment grade); i. securities issued by financial institution with rating assigned by internationally recognized rating agency equivalent to rating of S&P not less then A^+, assessed not earlier than 6 months from the reporting period; j. securities that have not been rated but issued by international development banks listed in the regulation of Bank of Albania "On risk management arising from the large exposures of Banks"; k. Securities with remaining maturity up to one month; l. Securities purchased in a repurchase agreement with a remaining maturity up to one month; m. irrevocable credit facilities approved to the bank. Liquid assets are included on a net basis excluding accrued interest and subtracting provisions.	multinational banks, with a triple A rating. Three of the responding banks agree on the use of this type of rating elaborating that such rated securities are always liquid. However, they suggest 2 different options: 3. one bank proposes the limit rating to be A^- and above; 4. - Foreign securities – one bank's opinion is that the latest rating available should be used. This info is easily monitored from all parts. An alternative could be to treat as liquid the whole securities portfolio (traded in international markets) at their market price instead of their book value. - Albanian Government Securities. The same bank points out that even these securities can be considered as liquid for local currency purposes, considered the appropriate haircuts, as per regulation. (Based on the Regulation "On credit operation collaterals") On one bank's opinion, it will not be suitable to consider credit rating of the securities as a measure of their liquidity, so the credit rating	

ISSUE	REGULATORY PROPOSAL	BANKS' EXPERIENCES AND SUGGESTIONS	CONSIDERATIONS FOR FINAL REGULATION DRAFTING
		shall not be included.	
Short Term Liabilities Definition **(Article 15, point 8 of the Draft Regulation proposed by BoA)**	a. Liabilities to the Central Bank (including current accounts, on sight deposits and deposits with remaining maturity up to 7 days, loans from the central bank refinanced by an international financial institution and not financed by an international financial institution with remaining maturity up to 7 days, and other accounts with the central bank with remaining maturity up to 7 days); b. Treasury bills and other bonds suitable for refinancing with the Central Bank; c. Current accounts with banks, credit institutions and other financial institutions; d. Deposits with banks, credit institutions and other financial institutions with remaining maturity up to 7 days; e. Loans from banks, credit institutions and other financial institutions with remaining maturity up to 7 days; f. Other accounts with banks, credit institutions and other financial institutions with remaining maturity up to 7 days; g. Current accounts and on sight deposits of the Albanian Government and public administration and time deposits with remaining maturity up to 7 days;	The average percentage of the used part of approved overdrafts and credit cards within 7 days varies from 4.5% to 37 %, and within a month from 13% to 44%. The average percentage of approved and unused overdrafts that banks consider as short-term liabilities is about 12% for the 5 reporting banks. Two of the banks report a zero value for this indicator, while the maximum value is 30%. Three out of 5 banks do not include in short term liabilities any percentage of credit cards. On the average of credit lines approved (unused) and irrevocable used, only one of the banks has given quantitative information, that is a range of 15 – 19% for credit lines used up to 7 days, and 12-14% for those used up to one month. In other banks data are either not available, or actually not taken in consideration, since they are usually in small amounts. The information provided by banks on the percentage of the used part of current	Bank of Albania might reconsider the percentage of current accounts and on sight deposits to be considered as short term liabilities (items (i) and (j)) of article 8 of the draft regulation.

ISSUE	REGULATORY PROPOSAL	BANKS' EXPERIENCES AND SUGGESTIONS	CONSIDERATIONS FOR FINAL REGULATION DRAFTING
	h. Securities sold in a reverse repurchase agreement with a remaining maturity up to one month; i. 30% of current accounts with credit balance; j. 30% of on sight deposits; k. 10% of time deposits; l. 5% of guarantees and other commitments (off balance sheet); m. 20% of irrevocable unused approved credit lines.	accounts and on sight deposits, varies significantly from bank to bank. 3 out of 5 responding banks believe that off balance sheets such as the following, should be included in short term liabilities. - Upcoming Forward transactions - Open credit uncovered letters of credit - Credit lines - Warranties and other off balance sheet items which can be materialized into outflows and will mature in 7 days	
Other Indicators **(Article 15, point 9 of the Draft Regulation proposed by BoA)**	a. Cumulative GAP up to one month / liquid assets; b. Cumulative GAP up to three months / liquid assets; c. Loans / Deposits (calculated in total and separately in Lek and foreign currency) d. Loans / Deposits and financing lines e. Liquid Assets / Total Deposits f. Cash / Short Term Liabilities g. Liquidity Ratio by maturity bands; h. Ratio of maturity transformation of short term sources in long term placements;	Banks require a clearer definition of the composition and maturities of the assets composing the buckets used to calculate GAPs.	The new regulation should provide clearer definitions of the assets that will compose the buckets, and an indicative table to cover for different types of maturity buckets.

ISSUE	REGULATORY PROPOSAL	BANKS' EXPERIENCES AND SUGGESTIONS	CONSIDERATIONS FOR FINAL REGULATION DRAFTING
	i. Indicator of deposits concentration (by type of depositor, currency, sector, ect.) and their volatility; j. Weighted average interest rate on assets and liabilities; k. Average marginal cost of liquidity l. Limits of placements in other banks; m. Forecasting future needs for liquidity (disposable liquid assets – necessary liquid).		

SPI Project on Enhancing Banks' Liquidity Risk Management

Project Objective

To enhance banks' liquidity risk management by reviewing the current regulatory framework according to international guidelines and best practice, including introduction of quantitative prudential ratios, in order to prevent the occurrence of systemic liquidity difficulties.

Project Management Team

Project Owner (PO): Indrit Banka, Supervision Director, BoA
Project Manager (PM): Miranda Ramaj, Supervision Deputy Director, BoA
Deputy Project Manger (DPM): Enkelejda Bargjo, TB, Market and Liquidity Risk Coordinator

Minutes

Third meeting
June 17, 2009—AAB premises

Attendees:

Ermira Curri, BoA (Acting PM)
Elvana Troqe, BoA
Julia Manushi, RB
Ornela Dino, RB
Albana Grillo, RB
Bledar Shella, BP
Erjon Tace, BP
Niko Kotonika, NBG
Shpetim Hereni, UBA
Admir Ramadani, FIB
Donata Totokoci, PCB
Erida Mele, PCB
Miranda Citozi, BKT
Artan Koci, CB
Erjona Poro, CB
Dimitrios Kakounis, AB
Entela Marga, AB

Penesta Gjoka, TB
Rajmond Pavaci TB
Albana Aleksi, BIS
Eralda Tafaj, EB
Ornela Konti, EB
Altin Koci , ICB
Jola Dima, ISBA,
Gerona Ziu, BoA,
Aida Deliu, BoA,
Brisilda Bala, BoA,
Endrita Xhaferaj, SPI Albania, Director of Financial Modernization and Analytics
Anuela Ristani, SPI Albania, Director of Operations

AGENDA

I. Project Progress Briefing

II. Discussion of the main issues brought by the banks on the first BoA Draft

III. Conclusions and Distribution of Tasks

IV. Closing Remarks

I. Project Progress Briefing

SPI Secretariat welcomed the PWG members and other participants present mentioning the fact that the participation in this meeting (nearly 30 participants) is a record high for all SPI Albania PWG meetings. This is also due to the persistence of BoA for a complete banking community discussion in such an important matter as the new Regulation on Liquidity Risk Management. SPI Secretariat, in consultation with the PWG members from BoA, summarized all the issues discussed in the meeting with regards to the BoA's proposal in order to facilitate the opinion issuing by the participating PWG banks. Consequently SPI Secretariat sent all the questions for which PWG's opinion was needed with regards to the proposal and the cost-benefit questionnaire. After collecting the individual inputs, SPI Secretariat presented them in a structured approach to BoA team which reflected the suggestions into a revised drat for discussion in the third PWG meeting.

II. Discussion of the main issues brought by the banks on the first BoA Draft

BoA representatives lead the PWG members in a discussion on the newly revised articles of the regulatory draft as follows:

Article 1. The object has changed: The regulation establishes the minimal requirements (main requirements in the old version) on content, shape, accounting and reporting method that banks and branches of foreign banks shall meet for a rather sound liquidity management.

Article 4: Paragraph 1, gives the definition of the concept of illiquidity instead of that of liquidity as in the old version.

Article 5. The article on the regulative framework was added in the new version, and it establishes the obligation of banks for at least a strategy of liquidity risk management. Banks discussed on whether they should provide detailed information on customers structure, as well as on the internal limits they should apply. BoA will consider revising the point 4/b of the article with the aim to cover for foreign banks with strategies set up by their parent banks.

Article 6 (Paragraph 3). Banks suggested that the regulation should be clearer in terms of internal Liquidity Risk Committee that banks should create to manage liquidity risk, and the functions it should have.

Article 9. Establishes that Banks should perform periodical stress tests and / or scenarios analysis, to identify situations that influence their liquidity position. However, BoA does not set any obligatory scenario for running such stress testing, as was proposed in the 2nd PWG meeting by banks.

Article 11. This is a new article introduced in the revised draft, which sets some general principles for better management of liquidity risk.

Article 12. The article on planning and monitoring of inflows and outflows funds, has been further detailed in the revised draft regulation, to include more comprehensive definitions of inflows and outflows of funds.

Article 13. Has not changed from the previous draft, although banks still have some reserves on the achievable realization of daily gap analysis. BoA might reconsider and establish as obligatory only weekly gap analysis.

Article 17. Liquidity ratios.

- Pargraph 3. In the revised draft, instead of the limits of the liquid assets divided by liquid liabilities of : a) minimum 0.8 – within a working day; b) minimum 0.9 – in 3 consequent working days; c) minimum 1 – up to one month (calculated as average of the working days), there are only two limits to be followed: on 10 days basis not lower than 20 %, and on daily basis the average not lower than 10%.

- Pargraph 4/i. Banks suggested that the rating of securities to be included in liquid assets, to be considered should be the latest available rather that performed no earlier than six months from the reporting period;

- Paragraph 4/h. Included in short term assets will be securities issued by central government and central banks with rating assigned by internationally recognized rating agency equivalent to rating of S&P not less then A+ (investment grade) instead of BBB^{-} that was in the original draft.

BoA has prepared a table based on the newly introduced ratios to deliver to the banks so that they have a preliminary assessment of the reporting that will be generated through this new regulation from the data that the banks will provide as of January 2008.

IV. Cost Benefit Questionnaire Draft

SPI Secretariat presented the qualitative draft of the cost benefit questionnaire that will be delivered to the banks together with the BoA ratios table. The SPI Secretariat will aggregate the banks' answers and structure them in the qualitative impact assessment document.

VII. Conclusions and distribution of tasks

- PWG members representing the banks will complete the excel table drafted by BoA with the data from January 2008 as well as the SPI Secretariat qualitative cost benefit questionnaire
- SPI Secretariat will aggregate the answers and will forward them to BoA for consideration in the drafting of their final regulatory proposal

VII. Closing Remarks

The fourth PWG meeting is preliminarily scheduled to take place in mid July 2009.