

It's final: RBI tells banks to keep 60% liquidity coverage ratio from January 2015

The Reserve Bank of India has finalised banks' liquidity coverage ratio plan and told them to keep 60% coverage from January 2015 and raise the level to 100% in phases.

Liquidity coverage ratio is a concept aimed at ensuring availability of short term liquidity with banks and financial institutions. It was conceived by the Basel Committee on Banking Supervision after Lehman Brothers collapsed in 2008 leading to the most severe global financial crisis after great depression in 1930.

The concept says that financial institutions should have 100% assets back-up to ride out short-term liquidity disruptions. Accordingly, banks are required to hold an amount of highly-liquid assets, such as cash or treasury bills, equal to or greater than their net cash over a 30 day period.

RBI is a member of the Basel Committee and is fully committed to the objective of the Basel III reform package.

It said the liquidity coverage ratio would be on Indian banks from January 1, 2015 and it would be 60% for the entire 2015. Banks will have to raise the level to 70% from January 2016, to 80% from January 2017, to 90% from January 2018 and to 100% from January 2019.

RBI has finalized the plan after consulting with banks to smoothen the transition.

The sector regulator placed the draft transition plan in 2012 and sought banks' views on that.

Liquidity is a bank's capacity to fund rise in assets and meet both expected and unexpected cash and collateral obligations. The global financial crisis re-emphasised the importance of sound liquidity risk management framework to smooth functioning of financial institutions and markets.

RBI told banks to develop process for identifying, measuring, monitoring and controlling liquidity risk, including a robust framework for comprehensively projecting cash flows arising from assets, liabilities and off-balance sheet items over an appropriate time horizon.

"A bank should actively monitor and manage liquidity risk exposure and funding needs within and across legal entities, business lines and currencies, taking into account legal, regulatory and operational limitations to transferability of liquidity," RBI said.

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