Annex II



GUIDELINES ON THE LIQUIDITY COVERAGE RATIO, NET STABLE FUNDING RATIO AND LEVERAGE RATIO

APRIL 2025

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CENTRAL BANK OF KENYA
GUIDELINES ON LIQUIDITY COVERAGE RATIO, NET STABLE FUNDING RATIO AND LEVERAGE RATIO FOR INSTITUTIONS LICENSED UNDER THE BANKING ACT

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LIQUIDITY COVERAGE RATIO GUIDELINES CBK/LCR/01

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LIST OF ABBREVIATIONS

ABCP	Asset-Backed Commercial Paper
CBK	Central Bank of Kenya
CD	Certificate Of Deposit
CP	Commercial Paper
ECAI	External Credit Assessment Institution
HQLA	High Quality Liquid Assets
LCR	Liquidity Coverage Ratio
LTV	Loan To Value Ratio
NSFR	Net Stable Funding Ratio
OBS	Off-Balance Sheet
PD	Probability Of Default
PSE	Public Sector Entity
RMBS	Residential Mortgage-Backed Securities
SIV	Structured Investment Vehicle
SPE	Special Purpose Entity

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PART I: PRELIMINARY

1.1 **Title:** Liquidity Coverage Ratio Guidelines.

1.2 **Authorization** - This Guideline is issued under Section 33(4) of the Banking Act, which empowers the Central Bank of Kenya to issue guidelines to be adhered to by institutions in order to maintain a stable and efficient banking and financial system.

1.3 **Application** - This Guideline applies to all institutions licensed under the Banking Act (cap 488).

1.4 **Definitions** – the terms used in this guideline are as defined in the Banking Act (cap 488). Other terms used in this guideline shall be taken to have the meaning assigned to them hereunder.

"Aggregated funding" means the gross amount (i.e., not netting any form of credit extended to the legal entity) of all forms of funding (e.g., deposits or debt securities or similar derivative exposure for which the counterparty is known to be a small business customer). In addition, applying the limit on a consolidated basis means that where one or more small business customers are affiliated with each other, they may be considered as a single creditor such that the limit is applied to the total funding received by the bank from this group of customers.

"Beneficiary" means a legal entity that receives, or may become eligible to receive, benefits under a will, insurance policy, retirement plan, annuity, trust, or other contract.

"Cash management relationship" means the provision of cash management services to customers.

"Cash management services" means products and services provided to a customer to manage its cash flows, assets and liabilities and conduct financial transactions necessary to the customer's ongoing operations. Such services are limited to payment remittance, collection and aggregation of funds, payroll administration and control over the disbursement of funds.

"Clearing relationship" means a service arrangement that enables customers to transfer funds (or securities) indirectly through direct participants in domestic settlement systems to final recipients. Such services are limited to the following activities: transmission, reconciliation and confirmation of payment orders, daylight overdraft, overnight financing and maintenance of post-settlement balances, and determination of intra-day and final settlement positions.

"Corporate debt securities" (including commercial paper) means only plain-vanilla assets whose valuation is readily available based on standard methods and does not depend on private knowledge.

"Correspondent banking" means arrangements under which one bank (correspondent) holds deposits owned by other banks (respondents) and provides payment and other services in order to settle foreign currency transactions.

"Custody relationship" means the provision of safekeeping, reporting, processing of assets or the facilitation of the operational and administrative elements of related activities on behalf of customers in the process of their transacting and retaining financial assets. Such services are limited to the settlement of securities transactions, the transfer of contractual payments, the processing of collateral and the provision of custody related cash management services. Also included are the receipt of dividends and other income, client subscriptions and redemptions. Custodial services –

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should further extend to asset and corporate trust servicing, treasury, escrow, funds transfer, stock transfer and agency services, including payment and settlement services (excluding correspondent banking) and depository receipts.

"Fiduciary" means a legal entity that is authorized to manage assets on behalf of a third party. Fiduciaries include asset management entities such as pension funds and other collective investment vehicles.

"Outflow rate" is expected rate at which a bank's liabilities are expected to be redeemed over a given stressed period.

"Public sector entity (PSE)" means a public organization that is a part of the government and delivers public programmes, goods, or services, but exists as a separate organization in its own right, possibly as a legal entity and operates with a partial degree of operational independence. The categorization of PSEs in this guideline is consistent with the categorization in the capital framework for credit risk.

"Re-hypothecation" means the practice by financial institutions of using, for their own purposes, assets that have been posted to them as collateral.

"Retail deposits" means deposits placed by a natural person.

"Run-off rate" refers to the expected rate at which liabilities (e.g. deposits or debt securities) are expected to be called or withdrawn.

"Secured funding" means those liabilities and general obligations that are collateralized by legal rights to specifically designated assets owned by the borrowing institution in the case of bankruptcy, insolvency, liquidation or resolution.

"Special purpose entity" means a corporation, trust, or other entity organized for a specific purpose, the activities of which are limited to those appropriate to accomplish the purpose of the SPE, and the structure of which is intended to isolate the SPE from the credit risk of an originator or seller of exposures. SPEs are commonly used as financing vehicles in which exposures are sold to a trust or similar entity in exchange for cash or other assets funded by debt issued by the trust.

"Total net cash outflows" means the total expected cash outflows minus total expected cash inflows in the LCR stress scenario for the subsequent 30 calendar days. Where applicable, cash inflows and outflows should include interest that is expected to be received and paid during the 30-day time horizon.

"Unencumbered" means free of legal, regulatory, contractual or other restrictions on the ability of the relevant financial institution to liquidate, sell, transfer, or assign the asset. These assets should not be pledged (either explicitly or implicitly) to secure, collateralize or credit-enhance any transaction, nor be designated to cover operational costs (such as rents and salaries).

"Wholesale funding" means any liability or general obligation raised from non-natural persons (i.e., legal entities, including sole proprietorships and partnerships).

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PART II: STATEMENT OF POLICY

2.1 **Introduction** - This Liquidity Coverage Ratio (LCR) guideline[1] presents one of the Basel committee's key reforms to develop a more resilient banking sector. The objective of the LCR is to promote the short-term resilience of the liquidity risk profile of banks. It does this by ensuring that banks have an adequate stock of unencumbered high-quality liquid assets (HQLA) that can be converted easily and immediately into cash to meet their liquidity needs for a 30-calendar day liquidity stress scenario. the LCR will improve the banking sector's ability to absorb shocks arising from financial and economic stress, whatever the source, thus reducing the risk of spillover from the financial sector to the real economy.

The Central Bank of Kenya (CBK) has strengthened its liquidity framework by adopting the LCR as a minimum standard for funding liquidity. This standard aims to promote short-term resilience of a bank's liquidity risk profile by ensuring that it has sufficient HQLA to survive a 30-calendar day stress scenario. The LCR is comprised of specific parameters which are internationally "harmonized" with prescribed values. Certain parameters, however, contain elements of national discretion which has been adopted by Kenya to reflect jurisdiction-specific conditions.

2.2 **Purpose** - This Guideline aims to ensure that a bank has an adequate stock of unencumbered HQLA that consists of cash or assets that can be converted into cash at little or no loss of value, to meet its liquidity needs for a 30-calendar day liquidity stress scenario. At a minimum, the stock of unencumbered HQLA should enable the bank to survive until day 30 of the stress scenario, by which time it is assumed that appropriate corrective actions can be taken by the bank's management and the CBK, or that the bank can be resolved in an orderly way. Banks are also expected to be aware of any potential mismatches within the 30-day period and ensure that sufficient HQLA are available to meet any cash flow gaps throughout the period.

The LCR builds on traditional liquidity "coverage ratio" methodologies used internally by banks to assess exposure to contingent liquidity events. The total net cash outflows for the scenario is to be calculated for 30 calendar days into the future. The Guideline requires that, absent a situation of financial stress, the value of the ratio be no lower than 100 percent (stock of HQLA should at least equal total net cash outflows) on an ongoing basis because the stock of unencumbered HQLA is intended to serve as a defense against the potential onset of liquidity stress.

2.3 **Scope of Application** - The application of the requirements in this document follows the existing scope of application of the Capital Framework. The LCR Guideline and monitoring tools should be applied to banks on a consolidated basis.

A bank should actively monitor and control liquidity risk exposures and funding needs at the level of individual legal entities, foreign branches and subsidiaries, and the group as a whole, taking into account legal, regulatory, and operational limitations to the transferability of liquidity

2.4 **Responsibility of Use and Reporting** – It is the responsibility of banks to use LCR on an ongoing basis to help monitor and control liquidity risk. Banks should report LCR to the CBK on a monthly basis within 10 calendar days after the end of the month, with the operational capacity to increase the frequency to weekly or even daily in stressed situations at the discretion of the CBK.

[1] Reference document: BCBS "Basel III: The Liquidity Coverage Ratio and liquidity risk monitoring tools", January 2013

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Banks are expected to inform the CBK of their LCR and their liquidity profile on an ongoing basis. Banks should also notify the CBK immediately if their LCR has fallen, or is expected to fall, below 100 percent.

2.5 **Treatment of Liquidity Transfer Restrictions** - As noted in paragraph 3.10, as a general principle, no excess liquidity should be recognized by a cross-border banking group in its consolidated LCR if there is reasonable doubt about the availability of such liquidity. Liquidity transfer restrictions (e.g. ring-fencing measures, non-convertibility of local currency, foreign exchange controls, etc.) in jurisdictions in which a banking group operates will affect the availability of liquidity by inhibiting the transfer of HQLA and fund flows within the group. The consolidated LCR should reflect such restrictions in a manner consistent with paragraph 3.11. For example, the eligible HQLA that are held by a legal entity being consolidated to meet its local LCR requirements (where applicable) - should be included in the consolidated LCR to the extent that such HQLA are used to cover the total net cash outflows of that entity, notwithstanding that the assets are subject to liquidity transfer restrictions. If the HQLA held in excess of the total net cash outflows are not transferable, such surplus liquidity should be excluded from the Guideline.

2.6 **Currencies -** As outlined in paragraph 3.13, while the LCR is expected to be met on a consolidated basis and reported in a common currency, banks should also be aware of the liquidity needs in each significant currency. As indicated in the LCR, the currencies of the stock of HQLA should be similar in composition to the operational needs of the bank. Banks cannot assume that currencies will remain transferable and convertible in a stress period, even for currencies that in normal times are freely transferable and highly convertible.

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PART III: DEFINITION OF THE LCR

3.1 The LCR has two components and is expressed as follows:

$$\frac{\textit{Stock of HQLA}}{\textit{Total net cash outflows over the next 30 calendar days}} \geq 100 \text{ percent}$$

A. STOCK OF HQLA

3.2 The numerator of the LCR is the "stock of HQLA". Under the Guideline, banks must hold a stock of unencumbered HQLA to cover the total net cash outflows (as defined below) over a 30-day period under the prescribed stress scenario. In order to qualify as "HQLA", assets should be liquid during a time of stress. The following sets out the characteristics that such assets should generally possess and the operational requirements that they should satisfy.

3 Characteristics of HQLA

3.3 Assets are considered to be HQLA if they can be easily and immediately converted into cash at little or no loss of value. The liquidity of an asset depends on the underlying stress scenario, the volume to be monetized and the timeframe considered. Nevertheless, there are certain assets that are more likely to generate funds without incurring large discounts in short term; loans collateralized with sovereign bonds, sale or repurchase agreement (repo) markets due to fire-sales even in times of stress. This section outlines the factors that influence whether or not the market for an asset can be relied upon to raise liquidity when considered in the context of possible stresses.

(i) Fundamental Characteristics

- Low risk.
- Ease and certainty of valuation.
- Low correlation with risky assets.
- Local sovereign bonds or international assets listed on a developed and recognized exchange.

(ii) Market-related characteristics (other than local sovereign bonds)

- Active and sizable market.
- Low volatility of asset prices.
- Tendencies to move into these types of assets in a systemic crisis.

3.4 As outlined by these characteristics, the test of whether liquid assets are of "high-quality" is that, by way of sale or repo, their liquidity-generating capacity is assumed to remain intact even in periods of severe idiosyncratic and market stress.

4 Operational Requirements

3.5 All assets in the stock of HQLA are subject to specific operational requirements as indicated in (3.6 to 3.13). These operational requirements are designed to ensure that the stock of HQLA is managed in such a way that the bank can, and is able to demonstrate that it can, immediately use the stock of assets as a source of contingent funds that is available for the bank to convert into cash through the interbank market by means of collateralized loans, outright sale or repo, to fill funding

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gaps between cash inflows and outflows at any time during the 30-day stress period, with no restriction on the use of the liquidity generated.

3.6 All assets in the stock should be unencumbered. Assets which qualify for the stock of HQLA that have been pre-positioned or deposited with, or pledged to, the CBK but have not been used to generate liquidity may be included in the stock.

3.7 A bank should exclude from the stock those assets that, although meeting the definition of "unencumbered", the bank would not have the operational capability to monetize to meet outflows during the stress period.

3.8 The stock should be under the control of the function charged with managing the liquidity of the bank, meaning the function has the continuous authority, and legal and operational capability, to monetize any asset in the stock.

3.9 A bank should monitor the legal entity and physical location where collateral is held and how it may be mobilized in a timely manner. Specifically, it should have a policy in place that identifies legal entities, geographical locations, currencies and specific custodial or bank accounts where HQLA are held.

3.10 Qualifying HQLA that are held to meet statutory liquidity requirements at the legal entity or sub-consolidated level, where applicable, may only be included in the stock at the consolidated level to the extent that the related risks (as measured by the legal entity's or sub-consolidated group's net cash outflows in the LCR) are also reflected in the consolidated LCR.

3.11 In assessing whether assets are freely transferable for regulatory purposes, banks should be aware that assets may not be freely available to the consolidated entity due to regulatory, legal, tax, accounting or other impediments.

3.12 A bank should exclude from the stock of HQLA those assets where there are impediments to sale or use as collateral for a loan through the interbank market.

3.13 While the LCR is expected to be met and reported in a single currency, banks are expected to be able to meet their liquidity needs in each currency and maintain HQLA consistent with the distribution of their liquidity needs by currency.

5 Diversification of the Stock of HQLA

3.14 The stock of HQLA should be well diversified within the asset classes themselves. Banks should have policies and limits in place in order to avoid concentration with respect to asset types, issue and issuer types, and currency (consistent with the distribution of net cash outflows by currency) within asset classes.

6 Definition of HQLA

3.15 The stock of HQLA should comprise assets with the characteristics outlined in paragraphs 3.3. This section describes the type of assets that meet these characteristics and- should therefore be included in the stock.

3.16 There are two categories of assets (Level 1 and Level 2) that should be included in the stock. Assets

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to be included in each category are those that the bank is holding on the first day of the stress period, irrespective of their residual maturity. Level 1 assets - should be included without limit, while Level 2 assets - should only comprise a maximum of 40 percent of the total stock of HQLA.

3.17 Level 2 A comprises an additional class of assets, Level 2B assets, these assets should comprise no more than 15 percent of the total stock of HQLA. They must also be included within the overall 40 percent cap on Level 2 A assets.

3.18 The 40 percent cap on Level 2 assets and the 15 percent cap on Level 2B assets should be determined after the application of required haircuts, and after taking into account the unwind of short-term securities financing transactions maturing within 30 calendar days that involve the exchange of HQLA. In this context, short-term transactions are transactions with a maturity date up to and including 30 calendar days.

(i) Level 1 Assets

3.19 Level 1 assets – should comprise an unlimited share of the pool and are not subject to a haircut under the LCR. For the purpose of calculating the LCR, Level 1 assets in the stock of HQLA should be measured at an amount no greater than their current market value.

3.20 Level 1 assets are limited to:

(a) coins and banknotes;

(b) balances with the CBK (including required reserves);

(c) balances with other banks (local and foreign)

(d) marketable securities representing claims on or guaranteed by sovereigns, central banks, PSEs, the International Monetary Fund, the European Central Bank and European Community, or multilateral development banks, and satisfying all of the following conditions:

- assigned a 0 percent risk-weight under the capital framework for credit risk;
- have a proven record as a reliable source of liquidity in the markets (repo or sale) even during stressed market conditions; and
- not an obligation of a financial institution or any of its affiliated entities.

(e) where the sovereign has a non 0 percent risk weight, sovereign or central bank debt securities issued in domestic currencies by the sovereign or central bank in the country in which the liquidity risk is being taken or in the bank's home country; and

(f) where the sovereign has a non-0 percent risk weight, domestic sovereign or central bank debt security issued in foreign currencies are eligible up to the amount of the bank's stressed net cash outflows in that specific foreign currency stemming from the bank's operations in the jurisdiction where the bank's liquidity risk is being taken.

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(ii) Level 2 Assets

3.21 Level 2 assets (comprising Level 2A assets and any Level 2B assets -recommended by the CBK) – should be included in the stock of HQLA, subject to the requirement that they comprise no more than 40 percent of the overall stock after haircuts have been applied. The method for calculating the cap on Level 2 A assets and the cap on Level 2B assets is set out in paragraph 3.18.

3.22 A 15 percent haircut is applied to the current market value of each Level 2A asset held in the stock of HQLA. Level 2A assets are limited to the following:

(a) Marketable securities representing claims on or guaranteed by sovereigns, central banks, PSEs or multilateral development banks that satisfy all of the following conditions:

- assigned a 20 percent risk weight under the capital framework;
- have a proven record as a reliable source of liquidity in the markets (repo or sale) even during stressed market conditions; and
- not an obligation of a financial institution or any of its affiliated entities.

(b) Corporate debt securities (including commercial paper) and covered bonds that satisfy all of the following conditions:

- in the case of corporate debt securities: not issued by a financial institution or any of its affiliated entities;
- In the case of covered bonds: not issued by the bank itself or any of its affiliated entities;
- either (i) have a long-term credit rating from a recognized external credit assessment institution (ECAI) of at least AA- or in the absence of a long term rating, a short-term rating equivalent in quality to the long-term rating; or (ii) do not have a credit assessment by a recognized ECAI but are internally rated as having a probability of default (PD) corresponding to a credit rating of at least AA-;
- traded in large, deep and active repo or cash markets characterized by a low level of concentration; and
- have a proven record as a reliable source of liquidity in the markets (repo or sale) even during stressed market conditions: i.e., maximum decline of price or increase in haircut over a 30-day period during a relevant period of significant liquidity stress not exceeding 10 percent.

(iii) Level 2B Assets

3.23 Level 2B assets are limited to the following:

(a) Residential mortgage-backed securities (RMBS), with the prior approval of the CBK, which satisfy all of the following conditions may be included in Level 2B, subject to a 25 percent haircut:

- not issued by, and the underlying assets have not been originated by the bank itself or any of its affiliated entities;

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- have a long-term credit rating from a recognized ECAI of AA or higher, or in the absence of a long-term rating, a short-term rating equivalent in quality to the long-term rating;
- traded in large, deep, and active repo or cash markets characterized by a low level of concentration;
- have a proven record as a reliable source of liquidity in the markets (repo or sale) even during stressed market conditions;
- the underlying asset pool is restricted to residential mortgages and cannot contain structured products;
- the underlying mortgages are "full recourse" loans (i.e., in the case of foreclosure the mortgage owner remains liable for any shortfall in sales proceeds from the property) and have a maximum loan-to-value ratio (LTV) of 80 percent on average at issuance.

(b) Corporate debt securities (including commercial paper) that satisfy all of the following conditions may be included in Level 2B, subject to a 50 percent haircut:

- not issued by a financial institution or any of its affiliated entities;
- either (i) have a long-term credit rating from a recognized ECAI between A+ and BBB- or in the absence of a long term rating, a short-term rating equivalent in quality to the long-term rating; or (ii) do not have a credit assessment by a recognized ECAI and are internally rated as having a PD corresponding to a credit rating of between A+ and BBB; and
- have a proven record as a reliable source of liquidity in the markets (repo or sale) even during stressed market conditions, i.e., a maximum decline of price not exceeding 20 percent or increase in haircut over a 30-day period not exceeding 20 percentage points during a relevant period of significant liquidity stress.

(c) Common equity shares that satisfy all of the following conditions may be included in Level 2B, subject to a 50 percent haircut:

- not issued by a financial institution or any of its affiliated entities;
- exchange traded and centrally cleared;
- is listed on a major stock index in the home jurisdiction or where the liquidity risk is taken;
- denominated in the domestic currency of a bank's home jurisdiction or in the currency of the jurisdiction where a bank's liquidity risk is taken; and
- have a proven record as a reliable source of liquidity in the markets (repo or sale) even during stressed market conditions.

B. Total Net Cash Outflows

3.24 The term total net cash outflows[2] is defined as the total expected cash outflows minus total expected cash inflows in the specified stress scenario for the subsequent 30 calendar days. Total expected cash outflows are calculated by multiplying the outstanding balances of various categories or types of liabilities and off-balance sheet commitments by the rates at which they are expected to run off or be drawn down. Total expected cash inflows are calculated by multiplying the outstanding

[2] Where applicable, cash inflows and outflows should include interest that is expected to be received and paid.

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balances of various categories of contractual receivables by the rates at which they are expected to flow in under the scenario up to an aggregate cap of 75 percent of total expected cash outflows.

Total net cash outflows over the next 30 calendar days =
Total expected cash outflows – (the lesser of: (i) Total expected cash inflows and 75 percent of total expected cash outflow)

3.25 Banks will not be permitted to double count items, i.e., if an asset is included as part of the "stock of HQLA", the associated cash inflows cannot also be counted as cash inflows. Where there is potential that an item could be counted in multiple outflow categories, (e.g., committed liquidity facilities granted to cover debt maturing within the 30-calendar day period), a bank only has to assume up to the maximum contractual outflow for that product.

I. Cash Outflows

(i) Retail Deposits

3.26 Retail deposits are defined as deposits placed with a bank by a natural person. These retail deposits are divided into “stable” and “less stable” portions of funds as described below, with minimum run-off rates listed for each category. Stable deposits are the amount of the deposits below KES 500,000 that are fully insured by the Kenya Deposit Insurance Corporation.

3.27 Stable deposits in Kenyan Shillings (KES) will receive a run-off factor of 5 percent, whilst stable deposits in foreign currency will receive a run-off factor of 10 percent.

3.28 The remaining retail (also called less stable) deposits in KES will receive a run-off factor of 10 percent, whilst less stable deposits in foreign currency will receive a run-off factor of 20 percent.

3.29 Cash outflows related to retail term deposits with a residual maturity or withdrawal notice period of greater than 30 days will be excluded from total expected cash outflows if the depositor has no legal right to withdraw deposits within the 30-day horizon of the LCR, or if early withdrawal results in a significant penalty that is materially greater than the loss of interest.

(ii) ***Unsecured wholesale funding run-off***

3.30 For the purposes of the LCR, "unsecured wholesale funding" is defined as those liabilities and general obligations that are raised from non-natural persons (i.e., legal entities, including sole proprietorships and partnerships) and are not collateralized by legal rights to specifically designated assets owned by the borrowing institution in the case of bankruptcy, insolvency, liquidation, or resolution. Obligations related to derivative contracts are explicitly excluded from this definition.

3.31 The wholesale funding included in the LCR is defined as all funding that is callable within the LCR's horizon of 30 days or that has its earliest possible contractual maturity date situated within this horizon (such as maturing term deposits and unsecured debt securities) as well as funding with an undetermined maturity. This should include all funding with options that are exercisable at the investor's discretion within the 30-calendar day horizon.

3.32 Wholesale funding that is callable by the funds provider subject to a contractually defined and binding notice period surpassing the 30-day horizon is not included.

3.33 For the purposes of the LCR, unsecured wholesale funding is to be categorized as detailed below, based on the assumed sensitivity of the funds providers to the rate offered and the credit quality

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and solvency of the borrowing bank. This is determined by the type of funds providers and their level of sophistication, as well as their operational relationships with the bank. The run-off rates for the scenario are listed for each category.

(a) Unsecured Wholesale Funding Provided by Small Business Customers (Run-off = 10 percent)

3.34 Unsecured wholesale funding provided by small business customers is treated the same way as retail deposits for the purposes of this Guideline, effectively distinguishing between a "stable" portion of funding provided by small business customers and different buckets of less stable funding. The same bucket definitions and associated run-off factors apply as for retail deposits.

3.35 This category consists of deposits and other extensions of funds made by non-financial small business customers. "Small business customers" are managed as retail exposures and are generally considered as having similar liquidity risk characteristics to retail accounts provided the total aggregated funding raised from one small business customer is less than KES 500,000 (on a consolidated basis, where applicable).

3.36 Cash outflows related to term deposits from small business customers with a residual maturity or withdrawal notice period of greater than 30 days will be excluded from total expected cash outflow.

(b) Operational deposits generated by Clearing, Custody and Cash Management Activities: (Run-off = 25 percent)

3.37 Certain activities lead to financial and non-financial customers needing to place, or leave, deposits with a bank in order to facilitate their access and ability to use payment and settlement systems and otherwise make payments. These funds will receive a 25 percent run-off factor only if the customer has a substantive dependency with the bank and the deposit is required for such activities. The CBK's approval would have to be given to banks that choose to utilize this treatment.

3.38 Any excess balances that could be withdrawn and would still leave enough funds to fulfil these clearing, custody and cash management activities do not qualify for the 25 percent run-off rate. In other words, only that part of the deposit balance with the service provider that is proven to serve a customer's operational needs -should qualify as stable. Excess balances should be treated in the appropriate category for non-operational deposits. If banks are unable to determine the amount of the excess balance, then the entire deposit should be assumed to be excess to requirements and, therefore, considered non-operational.

3.39 Operational deposits would receive a 0 percent inflow assumption for the depositing bank given that these deposits are required for operational reasons and are therefore not available to the depositing bank to repay other outflows.

3.40 Notwithstanding these operational categories, if the deposit under consideration arises out of correspondent banking or from the provision of prime brokerage services, it will be treated as if there were no operational activity for the purpose of determining run-off factors.

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(c) Unsecured Wholesale Funding Provided by Non-Financial Corporates and Sovereigns, Central Banks, Multilateral Development Banks, and PSEs (Run-off = 40 percent)

3.41 This category comprises all deposits and other extensions of unsecured funding from non-financial corporate customers (that are not categorized as small business customers) and (both domestic and foreign) sovereign, central bank, multilateral development bank, and PSE customers that are not specifically held for operational purposes (as defined above). The run-off factor for these funds is 40 percent.

(d) Unsecured Wholesale Funding Provided by Other Legal Entity Customers: (Run-off = 100 percent)

3.42 This category consists of all deposits and other funding from other institutions (including banks, securities firms, insurance companies, etc.), fiduciaries, beneficiaries, conduits and special purpose vehicles, affiliated entities of the bank and other entities that are not specifically held for operational purposes and not included in the prior three categories. The run-off factor for these funds is 100 percent.

3.43 All notes, bonds and other debt securities issued by the bank are included in this category regardless of the holder.

(iii) *Secured funding run-off*

3.44 For the purposes of this Guideline, "secured funding" is defined as those liabilities and general obligations that are collateralized by legal rights to specifically designated assets owned by the borrowing institution in the case of bankruptcy, insolvency, liquidation, administration or resolution.

3.45 In this case, the ability to continue to transact repurchase, reverse repurchase, and other securities financing transactions is limited to transactions backed by HQLA or with the bank's domestic, sovereign, PSE, or central bank.[3] The amount of outflow is calculated based on the amount of funds raised through the transaction, and not the value of the underlying collateral.

3.46 Due to the high-quality of Level 1 assets, no reduction in funding availability against these assets is assumed to occur. Moreover, no reduction in funding availability is expected for any maturing secured funding transactions with the bank's domestic central bank. A reduction in funding availability will be assigned to maturing transactions backed by Level 2 assets equivalent to the required haircuts. A 25 percent factor is applied for maturing secured funding transactions with the bank's domestic sovereign, multilateral development banks, or domestic PSEs that have a 20 percent or lower risk weight, when the transactions are backed by assets other than Level 1 or Level 2A assets, in recognition that these entities are unlikely to withdraw secured funding from banks in a time of market-wide stress. This, however, gives credit only for outstanding secured funding transactions, and not for unused collateral or merely the capacity to borrow.

3.47 For all other maturing transactions, the run-off factor is 100 percent. The table below summarizes the applicable standards:

[3] In this context, PSEs that receive this treatment should be limited to those that are 20 percent risk weighted or better, and "domestic" can be defined as a jurisdiction where a bank is legally incorporated.

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Categories for outstanding maturing secured funding transactions	Amount to add to cash outflows
• Backed by Level 1 assets or with central banks.	0 percent
• Backed by Level 2A assets.	15 percent
• Secured funding transactions with domestic sovereign, PSEs, or multilateral development banks that are not backed by Level 1 or 2A assets. PSEs that receive this treatment are limited to those that have a risk weight of 20 percent or lower. • Backed by RMBS eligible for inclusion in Level 2B	25 percent
• Backed by other Level 2B assets	50 percent
• All others	100 percent

(iv) ***Additional requirements***

3.48 **Derivatives cash outflows:** the sum of all net cash outflows should receive a 100 percent factor.

3.49 **Additional Requirements to be met before a bank increases liquidity needs and asset backed securities**, see Annex I.

3.50 **Drawdowns on committed credit and liquidity facilities:** For the purpose of the Guideline, credit and liquidity facilities are defined as explicit contractual agreements or obligations to extend funds at a future date to retail or wholesale counterparties. For the purpose of the Guideline, these facilities only include contractually irrevocable ("committed") or conditionally revocable agreements to extend funds in the future. Unconditionally revocable facilities that are unconditionally cancellable by the bank (in particular, those without a precondition of a material change in the credit condition of the borrower) are excluded from this section and included in "Other Contingent Funding Liabilities". These off-balance sheet facilities or funding commitments - should have long or short-term maturities, with short-term facilities frequently renewing or automatically rolling-over. In a stressed environment, it will likely be difficult for customers drawing on facilities of any maturity, even short-term maturities, to be able to quickly pay back the borrowings. Therefore, for purposes of this Guideline, all facilities that are assumed to be drawn (as outlined in the paragraphs below) will remain outstanding at the amounts assigned throughout the duration of the test, regardless of maturity.

3.51 For the purposes of this Guideline, the currently undrawn portion of these facilities is calculated net of any HQLA eligible for the stock of HQLA, if:

- the HQLA have already been posted as collateral by the counterparty to secure the facilities or that are contractually obliged to be posted when the counterparty will draw down the facility (e.g. a liquidity facility structured as a repo facility),
- the bank is legally entitled and operationally capable to re-use the collateral in new cash raising transactions once the facility is drawn, and
- there is no undue correlation between the probability of drawing the facility and the market

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value of the collateral.

The collateral - should be netted against the outstanding amount of the facility to the extent that this collateral is not already counted in the stock of HQLA, in line with the principle in paragraph 3.25 that items cannot be double counted in the Guideline.

3.52 A liquidity facility is defined as any committed, undrawn back-up facility that would be utilized to refinance the debt obligations of a customer in situations where such a customer is unable to rollover that debt in financial markets (e.g., pursuant to a commercial paper program, secured financing transactions, obligations to redeem units, etc.). For the purpose of this Guideline, the amount of the commitment to be treated as a liquidity facility is the amount of the currently outstanding debt issued by the customer (or proportionate share, if a syndicated facility) maturing within a 30-day period that is backstopped by the facility. The portion of a liquidity facility that is backing debt that does not mature within the 30-day window is excluded from the scope of the definition of a facility. Any additional capacity of the facility (i.e., the remaining commitment) would be treated as a committed credit facility with its associated drawdown rate as specified in paragraph 3.54. General working capital facilities for corporate entities (e.g., revolving credit facilities in place for general corporate or working capital purposes) will not be classified as liquidity facilities, but as credit facilities.

3.53 For that portion of financing programs that are captured in requirements 7 and 8 of Annex I (i.e., are maturing or have liquidity that may be exercised in the 30-day horizon), banks that are providers of associated liquidity facilities do not need to double count the maturing financing instrument and the liquidity facility for consolidated programs.

3.54 Any contractual loan drawdowns from committed facilities[4] and estimated drawdowns from revocable facilities within the 30-day period should be fully reflected as outflows.

(a) *Committed credit and liquidity facilities to retail and small business customers:* Banks should assume a 5 percent drawdown of the undrawn portion of these facilities.

(b) *Committed credit facilities to non-financial corporates, sovereigns and central banks, PSEs and multilateral development banks:* Banks should assume a 10 percent drawdown of the undrawn portion of these credit facilities.

(c) *Committed credit and liquidity facilities extended to banks subject to prudential supervision:* Banks should assume a 40 percent drawdown of the undrawn portion of these facilities.

(d) *Committed credit facilities to other financial institutions including securities firms, insurance companies, fiduciaries, and beneficiaries* Banks should assume a 40 percent drawdown of the undrawn portion of these credit facilities.

(e) *Committed liquidity facilities to other financial institutions, including securities firms, insurance companies, fiduciaries, and beneficiaries:* Banks should assume a 100 percent drawdown of the undrawn portion of these liquidity facilities.

(f) C*ommitted credit and liquidity facilities to other legal entities, conduits and special purpose vehicles, and other entities not included in the prior categories:* Banks should assume a 100 percent drawdown of the undrawn portion of these facilities.

3.55 Contractual obligations to extend funds within a 30-day period**.** Any contractual lending obligations to financial institutions not captured elsewhere in this Guideline should be captured here at a 100 percent outflow rate.

[4] Committed facilities refer to those which are irrevocable.

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3.56 If the total of all contractual obligations to extend funds to retail and non-financial corporate clients within the next 30 calendar days (not captured in the prior categories) exceeds 50 percent of the total contractual inflows due in the next 30 calendar days from these clients, the difference should be reported as a 100 percent outflow.

(v) *Other contingent funding obligations:*

3.57 These contingent funding obligations may be either contractual or non-contractual and are not lending commitments. Non-contractual contingent funding obligations include associations with, or sponsorship of, products sold, or services provided that may require the support or extension of funds in the future under stressed conditions. Non-contractual obligations may be embedded in financial products and instruments sold, sponsored, or originated by the institution that can give rise to unplanned balance sheet growth arising from support given for reputational risk considerations. These include products and instruments for which the customer or holder has specific expectations regarding the liquidity and marketability of the product or instrument and for which failure to satisfy customer expectations in a commercially reasonable manner would likely cause material reputational damage to the institution or otherwise impair ongoing viability.

3.58 Some of these contingent funding obligations are explicitly contingent upon a creditor other event that is not always related to the liquidity events simulated in the stress scenario but may nevertheless have the potential to cause significant liquidity drains in times of stress. For this Guideline, the bank should consider which of these "other contingent funding obligations" may materialize under the assumed stress events. The potential liquidity exposures to these contingent funding obligations are to be treated as a behavioral assumption. All identified contractual and non-contractual contingent liabilities and their assumptions should be reported, along with their related triggers. Banks should, at a minimum, use historical behavior in determining appropriate outflows.

3.59 Non contractual contingent funding obligations related to potential liquidity draws from joint ventures or minority investments in entities, which are not consolidated per paragraph 4.3 should be captured where there is the expectation that the bank will be the main liquidity provider when the entity is in need of liquidity.

3.60 In the case of contingent funding obligations stemming from trade finance instruments, a run-off rate of 5 percent is applied. Trade finance instruments consist of trade-related obligations directly underpinned by the movement of goods or the provision of services, such as:

- documentary trade letters of credit, documentary and clean collection, import bills, and export bills; and
- guarantees directly related to trade finance obligations, such as shipping guarantees.

3.61 Lending commitments, such as direct import or export financing for non-financial corporate firms, are excluded from this treatment and banks will apply the draw-down rates specified in paragraph 3.54.

3.62 Other contingent funding obligations include products and instruments such as:

- unconditionally revocable "uncommitted" credit and liquidity facilities (2 percent run-off rate);
- guarantees and letters of credit unrelated to trade finance obligations (as described in paragraph 3.60) (10 percent run-off rate);

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3.63 **Other contractual cash outflows:** (100 percent). Any other contractual cash outflows within the next 30 calendar days should be captured in this Guideline, such as outflows to cover unsecured collateral borrowings, uncovered short positions, dividends or contractual interest payments, with explanation given as to what comprises this bucket. Outflows related to operating costs, however, are not included in this Guideline.

II. Cash Inflows

3.64 When considering its available cash inflows, the bank should only include contractual inflows (including interest payments) from outstanding exposures that are fully performing and for which the bank has no reason to expect a default within the 30-day time horizon. Contingent inflows are not included in total net cash inflows.

3.65 Banks need to monitor the concentration of expected inflows across wholesale counterparties in the context of banks' liquidity management in order to ensure that their liquidity position is not overly dependent on the arrival of expected inflows from one or a limited number of wholesale counterparties.

3.66 *Cap on total inflows:* In order to prevent banks from relying solely on anticipated inflows to meet their liquidity requirement, and also to ensure a minimum level of HQLA holdings, the amount of inflows that can offset outflows is capped at 75 percent of total expected cash outflows as calculated in the Guideline. This requires that a bank must maintain a minimum amount of stock of HQLA equal to 25 percent of the total cash outflows.

(i) *Secured lending, including reverse repos and securities borrowing*

3.67 The table shows the inflow rates to be applied:

Maturing secured lending transactions backed by the following asset category:	**Inflow rate (if collateral is not used to cover short positions):**	**Inflow rate (if collateral is used to cover short positions):**
Level 1 assets	0 percent	0 percent
Level 2A assets	15 percent	0 percent
Level 2B assets		
Eligible RMBS	25 percent	0 percent
Other Level 2B assets	50 percent	0 percent
Margin lending backed by all other collateral	50 percent	0 percent
Other collateral	100 percent	0 percent

(ii) *Committed facilities*

3.68 No credit facilities, liquidity facilities or other contingent funding facilities that the bank holds at other institutions for its own purposes are assumed to be able to be drawn. Such facilities receive a 0 percent inflow rate, meaning that this scenario does not consider inflows from committed credit or liquidity facilities. This is to reduce the contagion risk of liquidity shortages at one bank causing shortages at other banks and to reflect the risk that other banks may not be in a position to honor

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credit facilities, or may decide to incur the legal and reputational risk involved in not honoring the commitment, in order to conserve their own liquidity or reduce their exposure to that bank.

(iii) *Other inflows by counterparty*

3.69 For all other types of transactions, either secured or unsecured, the inflow rate will be determined by counterparty. In order to reflect the need for a bank to conduct ongoing loan origination/roll-over with different types of counterparties, even during a time of stress, a set of limits on contractual inflows by counterparty type is applied.

3.70 When considering loan payments, the bank should only include inflows from fully performing loans. Further, inflows should only be taken at the latest possible date, based on the contractual rights available to counterparties. For revolving credit facilities, this assumes that the existing loan is rolled over and that any remaining balances are treated in the same way as a committed facility according to paragraph 3.54.

3.71 Inflows from loans that have no specific maturity (i.e., have non-defined or open maturity) should not be included; therefore, no assumptions should be applied as to when maturity of such loans would occur. An exception to this would be minimum payments of principal, fee or interest associated with an open maturity loan, provided that such payments are contractually due within 30 days. These minimum payment amounts should be captured as inflows at the rates prescribed in paragraphs 3.72 and 3.73.

(iv) *Retail and small business customer inflows*

3.72 This scenario assumes that banks will receive all payments (including interest payments and instalments) from retail and small business customers that are fully performing and contractually due within a 30-day horizon. At the same time, however, banks are assumed to continue to extend loans to retail and small business customers, at a rate of 50 percent of contractual inflows. This results in a net inflow number of 50 percent of the contractual amount.

(v) *Other wholesale inflows*

3.73 This scenario assumes that banks will receive all payments (including interest payments and instalments) from wholesale customers that are fully performing and contractually due within the 30-day horizon. In addition, banks are assumed to continue to extend loans to wholesale clients, at a rate of 0 percent of inflows for financial institutions and central banks, and 50 percent for all others, including non-financial corporates, sovereigns, multilateral development banks, and PSEs. This will result in an inflow percentage of:

- 100 percent for financial institution and central bank counterparties; and
- 50 percent for non-financial wholesale counterparties.

3.74 Inflows from securities maturing within 30 days not included in the stock of HQLA should be treated in the same category as inflows from financial institutions (i.e., 100 percent inflow). Banks may also recognize in this category inflows from the release of balances held in segregated accounts in accordance with regulatory requirements for the protection of customer trading assets, provided that these segregated balances are maintained in HQLA. This inflow should be calculated in line with the treatment of other related outflows and inflows covered in this Guideline. Level 1 and Level 2 securities maturing within 30 days should be included in the stock of liquid assets, provided that they meet all operational and definitional requirements, as laid out in paragraphs 3.5

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to 3.23.

3.75 Operational deposits: Deposits held at other financial institutions for operational purposes, as outlined in paragraphs 3.34 to 3.40, such as for clearing, custody, and cash management purposes, are assumed to stay at those institutions, and no inflows - should be counted for these funds - i.e., they will receive a 0 percent inflow rate, as noted in paragraph 3.38.

(vi) ***Other cash inflows***

3.76 Derivatives cash inflows: the sum of all net cash inflows should receive a 100 percent inflow factor.

3.77 Where derivatives are collateralized by HQLA, cash inflows should be calculated net of any corresponding cash or contractual collateral outflows that would result, all other things being equal, from contractual obligations for cash or collateral to be posted by the bank, given these contractual obligations would reduce the stock of HQLA. This is in accordance with the principle that banks should not double-count liquidity inflows or outflows.

3.78 Other contractual cash inflows: Other contractual cash inflows should be captured here, with explanation given to what comprises this bucket. Cash inflows related to non-financial revenues are not taken into account in the calculation of the net cash outflows for the purposes of this Guideline.

PART IV: EFFECTIVE DATE

4. **Effective date:** The effective date of this Guideline shall be 1st October 2025.

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ANNEX I

Operational deposits generated by Clearing, Custody and Cash Management Activities

1. Qualifying activities in this context refer to clearing, custody or cash management activities that meet the following criteria:
   - The customer is reliant on the bank to perform these services as an independent third-party intermediary in order to fulfil its normal banking activities over the next 30 days. For example, this condition would not be met if the bank is aware that the customer has adequate back-up arrangements;
   - It must be provided under a legally binding agreement to institutional customers; and
   - The termination of such agreements shall be subject either to a notice period of at least 30 days or significant switching costs (such as those related to transaction, information technology, early termination, or legal costs) to be borne by the customer if the operational deposits are moved before 30 days.
2. Qualifying operational deposits generated by such an activity are ones where:
   - The deposits are by-products of the underlying services provided by the banking organization and not sought out in the wholesale market in the sole interest of offering interest income.
   - The deposits are held in specifically designated accounts and priced without giving an economic incentive to the customer (not limited to paying market interest rates) to leave any excess funds on these accounts.
3. The following describe the types of activities that may generate operational deposits. A bank should assess whether the presence of such an activity does indeed generate an operational deposit as not all such activities qualify due to differences in customer dependency, activity, and practices:
   - A **clearing relationship** refers to a service arrangement that enables customers to transfer funds (or securities) indirectly through direct participants in domestic settlement systems to final recipients. Such services are limited to the following activities: transmission, reconciliation and confirmation of payment orders; daylight overdraft, overnight financing and maintenance of post-settlement balances; and determination of intra-day and final settlement positions.
   - A **custody relationship** refers to the provision of safekeeping, reporting, processing of assets or the facilitation of the operational and administrative elements of related activities on behalf of customers in the process of their transacting and retaining financial assets. Such services are limited to the settlement of securities transactions, the transfer of contractual payments, the processing of collateral, and the provision of custody related cash management services. Also included are the receipt of dividends and other income, client subscriptions and redemptions. Custodial services – should furthermore extend to asset and corporate trust servicing, treasury, escrow, funds transfer, stock transfer and agency services, including payment and settlement services (excluding correspondent banking), and depository receipts.
   - A **cash management relationship** refers to the provision of cash management and related services to customers. Cash management services, in this context, refers to those products and services provided to a customer to manage its cash flows, assets and liabilities, and conduct financial transactions necessary to the customer's ongoing operations. Such services are limited to payment remittance, collection and aggregation of funds, payroll administration, and control over the disbursement of funds.

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ANNEX II

Cash Outflows: Additional Requirements for banks to increase liquidity needs and asset backed securities

4. **Increased liquidity needs related to downgrade triggers embedded in financing transactions, derivatives, and other contracts:** (100 percent of the amount of collateral that would be posted for, or contractual cash outflows associated with, any downgrade up to and including a 3-notch downgrade).

5. **Increased liquidity needs related to the potential for valuation changes on posted collateral securing derivative and other transactions**: (20 percent of the value of non- Level 1 posted collateral).

6. **Increased liquidity needs related to excess non-segregated collateral held by the bank that could contractually be called at any time by the counterparty:** 100 percent of the non-segregated collateral that could contractually be recalled by the counterparty because the collateral is in excess of the counterparty's current collateral requirements.

7. **Increased liquidity needs related to contractually required collateral on transactions for which the counterparty has not yet demanded the collateral be posted:** 100 percent of the collateral that is contractually due but where the counterparty has not yet demanded the posting of such collateral.

8. **Increased liquidity needs related to contracts that allow collateral substitution to non-HQLA assets:** 100 percent of the amount of HQLA collateral that– should be substituted for non-HQLA assets without the bank's consent that have been received to secure transactions that have not been segregated.

9. **Increased liquidity needs related to market valuation changes on derivative or other transactions:** As market practice requires collateralization of mark-to-market exposures on derivative and other transactions, banks face potentially substantial liquidity risk exposures to these valuation changes. Inflows and outflows of transactions executed under the same master netting agreement – should be treated on a net basis. Any outflow generated by increased needs related to market valuation changes should be included in the LCR calculated by identifying the largest absolute net 30-day collateral flow realized during the preceding 24 months. The absolute net collateral flow is based on both realized outflows and inflows.

10. **Loss of funding on asset-backed securities,5covered bonds and other structured financing instruments:** The scenario assumes the outflow of 100 percent of the funding transaction maturing within the 30-day period, when these instruments are issued by the bank itself (as this assumes that the re-financing market will not exist).

11. **Loss of funding on asset-backed commercial paper, conduits, securities investment vehicles and other such financing facilities:** (100 percent of maturing amount and 100 percent of returnable assets).

[5] To the extent that sponsored conduits/SPVs are required to be consolidated under liquidity requirements, their assets and liabilities will be taken into account.

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ANNEX III

Illustrative Summary of the LCR

(Percentages are factors to be multiplied by the total amount of each item)

Item	Factor
Stock of HQLA	
A. Level 1 assets:	
• Coins and bank notes • Qualifying marketable securities from sovereigns, central banks, PSEs, and multilateral development banks • Qualifying central bank reserves • Domestic sovereign or central bank debt for non-0 percent risk-weighted sovereigns	100 percent
B. Level 2 assets (maximum of 40 percent of HQLA):	
Level 2A assets • Sovereign, central bank, multilateral development banks, and PSE assets qualifying for 20 percent risk weighting • Qualifying corporate debt securities rated AA- or higher • Qualifying covered bonds rated AA- or higher	85 percent
Level 2B assets (maximum of 15 percent of HQLA) • Qualifying RMBS • Qualifying corporate debt securities rated between A+ and BBB- • Qualifying common equity shares	75 percent 50 percent 50 percent
Total value of stock of HQLA	

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Cash Outflows	
A. Retail deposits:	
Local demand deposits and term deposits (less than 30 days maturity)	5 percent
Foreign demand deposits and term deposits (less than 30 days maturity)	10 percent
Term deposits with residual maturity greater than 30 days	0 percent
B. Unsecured wholesale funding:	
Demand and term deposits (less than 30 days maturity) provided by small business customers:	12 percent
Operational deposits generated by clearing, custody and cash management activities	25 percent
Non-financial corporates, sovereigns, central banks, multilateral development banks, and PSEs	40 percent
Other legal entity customers	100 percent
C. Secured funding:	
• Secured funding transactions with a central bank counterparty or backed by Level 1 assets with any counterparty.	0 percent
• Secured funding transactions backed by Level 2A assets, with any counterparty	15 percent
• Secured funding transactions backed by non-Level 1 or non-Level 2A assets, with domestic sovereigns, multilateral development banks, or domestic PSEs as a counterparty	25 percent
• Backed by RMBS eligible for inclusion in Level 2B	25 percent
• Backed by other Level 2B assets	50 percent
• All other secured funding transactions	100 percent
D. Additional requirements:	
Liquidity needs (e.g., collateral calls) related to financing transactions, derivatives and other contracts	3-notch downgrade
Market valuation changes on derivatives transactions (largest absolute net 30-day collateral flows realized during the preceding 24 months)	Look back approach
Valuation changes on non-Level 1 posted collateral securing derivatives	20 percent
Excess collateral held by a bank related to derivative transactions that could contractually be called at any time by its counterparty	100 percent
Liquidity needs related to collateral contractually due from the reporting bank on derivatives transactions	100 percent

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Increased liquidity needs related to derivative transactions that allow collateral substitution to non-HQLA assets	100 percent
ABCP, SIVs, conduits, SPVs, etc.: • Liabilities from maturing ABCP, SIVs, SPVs, etc. (applied to maturing amounts and returnable assets) • Asset Backed Securities (including covered bonds) applied to maturing amounts	 100 percent 100 percent
Currently undrawn committed credit and liquidity facilities provided to: • retail and small business clients • non-financial corporates, sovereigns, and central banks, multilateral development banks, and PSEs • banks subject to prudential supervision • other financial institutions (include securities firms, insurance companies) • other legal entity customers, credit, and liquidity facilities	 5 percent 10 percent for credit 30 percent for liquidity 40 percent 40 percent for credit 100 percent for liquidity 100 percent
Other contingent funding liabilities (such as guarantees, letters of credit, revocable credit and liquidity facilities, etc.)	
• Trade finance • Customer short positions covered by other customers' collateral	5 percent 50 percent
Any additional contractual outflows	100 percent
Net derivative cash outflows	100 percent
Any other contractual cash outflows	100 percent
Total cash outflows	

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Cash Inflows	
Maturing secured lending transactions backed by the following collateral:	
Level 1 assets	0 percent
Level 2A assets	15 percent
Level 2B assets	
• Eligible RMBS	25 percent
• Other assets	50 percent
Margin lending backed by all other collateral	50 percent
All other assets	100 percent
Credit or liquidity facilities provided to the reporting bank	0 percent
Operational deposits held at other financial institutions (include deposits held at centralized institution of network of co-operative banks)	0 percent
Other inflows by counterparty:	
• Amounts to be received from retail counterparties	50 percent
• Amounts to be received from non-financial wholesale counterparties, from transactions other than those listed in above inflow categories	50 percent
• Amounts to be received from financial institutions and central banks, from transactions other than those listed in above inflow categories.	100 percent
Net derivative cash inflows	100 percent
Other contractual cash inflows	50 percent
Total cash inflows	
Total net cash outflows = Total cash outflows minus min [total cash inflows, 75 percent of gross outflows]	
LCR = Stock of HQLA / Total net cash outflows	

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NET STABLE FUNDING RATIO GUIDELINE CBK/NSFR/02

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LIST OF ABBREVIATIONS

AFS	Available Stable Funding
BCBS	Basel Committee on Banking Supervision
HQLA	High Quality Liquid Assets
LCR	Liquidity Coverage Ratio
NSFR	Net Stable Funding Ratio
OBS	Off-Balance Sheet
PSE	Public Sector Entity
RMBS	Residential Mortgage-Backed Securities
RSF	Required Stable Funding
CCP	Central Counter Parties

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PART I: PRELIMINARY

1.1 **Title:** Net Stable Funding Ratio Guidelines.

1.2 **Authorization** - This Guideline is issued under Section 33(4) of the Banking Act, which empowers the Central Bank of Kenya to issue guidelines to be adhered to by institutions in order to maintain a stable and efficient banking and financial system.

1.3 **Application** - This Guideline applies to all institutions licensed under the Banking Act (cap 488).

1.4 **Definitions** – the terms used in this guideline are as defined in the Banking Act (cap 488). Other terms used in this guideline shall be taken to have the meaning assigned to them hereunder.

"Available Stable Funding" - capital and liabilities not susceptible to fluctuations and are readily available to the Bank at minimal cost and for a longer period of time of at least one (1) year.

"Required Stable Funding" is measured based on the broad characteristics of the liquidity risk profile of an institution's assets and OBS exposures.

"Secured financing transactions" are transactions such as repurchase agreements, reverse repurchase agreements, security lending and borrowing, and margin lending transactions, where the value of the transactions depends on the market valuations and the transactions are often subject to margin agreements.

"Secured funding" means those liabilities and general obligations that are collateralized by legal rights to specifically designated assets owned by the borrowing institution in the case of bankruptcy, insolvency, liquidation or resolution.

"Unencumbered" means free of legal, regulatory, contractual or other restrictions on the ability of the relevant financial institution to liquidate, sell, transfer, or assign the asset. These assets should not be pledged (either explicitly or implicitly) to secure, collateralize or credit-enhance any transaction, nor be designated to cover operational costs (such as rents and salaries).

"Wholesale funding" means any liability or general obligation raised from non-natural persons (i.e., legal entities, including sole proprietorships and partnerships).

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PART II: STATEMENT OF POLICY

2.1 Purpose - The net stable funding ratio (NSFR) guideline presents one of the Basel Committee's key reforms to promote a more resilient banking sector. The NSFR will require banks to maintain a stable funding profile in relation to the composition of their assets and off-balance sheet activities. A sustainable funding structure is intended to reduce the likelihood that disruptions to a bank's regular sources of funding will erode its liquidity position in a way that would increase the risk of its failure and potentially lead to broader systemic stress. The NSFR limits overreliance on short-term wholesale funding, encourages better assessment of funding risk across all on- and off-balance sheet items, and promotes funding stability.

The Central Bank of Kenya has strengthened its liquidity framework by adopting the NSFR as a minimum standard for funding liquidity. This standard aims at reducing funding risk over a longer time horizon by requiring banks to fund their activities with sufficiently stable sources of funding in order to mitigate the risk of future funding stress. The NSFR is comprised of specific parameters which are internationally "harmonized" with prescribed values. Certain parameters, however, contain elements of national discretion which has been adopted by Kenya to reflect jurisdiction-specific conditions.

2.2 Scope - The application of the requirements in this document follows the existing scope of application of the Capital Framework. The NSFR Guideline should be applied to banks on a consolidated basis.

2.3 Responsibility - Banks are expected to meet the NSFR requirement on an ongoing basis. The NSFR should be reported semi-annually.

Banks should actively monitor and control liquidity risk exposures and funding needs at the level of individual legal entities, foreign branches and subsidiaries, and the group as a whole, taking into account legal, regulatory, and operational limitations to the transferability of liquidity.

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PART III: DEFINITION AND MINIMUM REQUIREMENTS

3.1 The NSFR is defined as the amount of available stable funding relative to the amount of required stable funding. This ratio should be equal to at least 100 percent on an ongoing basis. "Available stable funding" is defined as the portion of capital and liabilities expected to be reliable over the time horizon considered by the NSFR, which extends to one year. The amount of such stable funding required ("Required stable funding") of a specific institution is a function of the liquidity characteristics and residual maturities of the various assets held by that institution as well as those of its off-balance sheet (OBS) exposures.

$$\frac{\textbf{Available amount of stable funding}}{\textbf{Required amount of stable funding}} \quad \geq \textbf{100 percent}$$

3.2 The amounts of available and required stable funding specified in the Guideline are calibrated to reflect the presumed degree of stability of liabilities and liquidity of assets. The calibration reflects the stability of liabilities across two dimensions:

(a) *Funding tenor* – The NSFR is generally calibrated such that longer-term liabilities are assumed to be more stable than short-term liabilities.

(b) *Funding type and counterparty* – The NSFR is calibrated under the assumption that short-term (maturing in less than one year) deposits provided by retail customers and funding provided by small business customers are behaviorally more stable than wholesale funding of the same maturity from other counterparties.

3.3 In determining the appropriate amounts of required stable funding for various assets, the following criteria were taken into consideration, recognizing the potential trade-offs between these criteria:

(a) *Resilient credit creation* – The NSFR requires stable funding for some proportion of lending to the real economy in order to ensure the continuity of this type of intermediation.

(b) *Bank behaviour* – The NSFR is calibrated under the assumption that banks may seek to roll over a significant proportion of maturing loans to preserve customer relationships.

(c) *Asset tenor* – The NSFR assumes that some short-dated assets (maturing in less than one year) require a smaller proportion of stable funding because banks would be able to allow some proportion of those assets to mature instead of rolling them over.

(d) *Asset quality and liquidity value* – The NSFR assumes that unencumbered, high-quality assets that can be securitized or traded, and thus can be readily used as collateral to secure additional funding or sold in the market, do not need to be wholly financed with stable funding.

3.4 Additional stable funding sources are also required to support at least a small portion of the potential calls on liquidity arising from OBS commitments and contingent funding obligations.

3.5 NSFR definitions mirror those outlined in the LCR Guideline, unless otherwise specified. For the purposes of calculating the NSFR, HQLA are defined as all HQLA without regard to LCR operational requirements and LCR caps on Level 2 and Level 2B assets that may otherwise limit the ability of some HQLA to be included as eligible HQLA in calculation of the LCR.

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A. Definition of Available Stable Funding

3.6 The amount of available stable funding (ASF) is measured based on the broad characteristics of the relative stability of a bank's funding sources, including the contractual maturity of its liabilities and the differences in the propensity of different types of funding providers to withdraw their funding. The amount of ASF is calculated by first assigning the carrying value of a bank's capital and liabilities to one of five categories as presented below. The amount assigned to each category is then multiplied by an ASF factor, and the total ASF is the sum of the weighted amounts. Carrying value represents the amount at which a liability or equity instrument is recorded before the application of any regulatory deductions, filters or other adjustments.

3.7 When determining the maturity of an equity or liability instrument, investors are assumed to redeem a call option at the earliest possible date. For funding with options exercisable at the bank's discretion, reputational factors should be taken into account that may limit a bank's ability not to exercise the option.[6] In particular, where the market expects certain liabilities to be redeemed before their legal final maturity date, banks should assume such behaviour for the purpose of the NSFR and include these liabilities in the corresponding ASF category. For long-dated liabilities, only the portion of cash flows falling at or beyond the six-month and one-year time horizons should be treated as having an effective residual maturity of six months or more and one year or more, respectively.

Calculation of derivative liability amounts

3.8 Derivative liabilities are calculated first based on the replacement cost for derivative contracts (obtained by marking to market) where the contract has a negative value. In calculating NSFR derivative liabilities, collateral posted in the form of variation margin in connection with derivative contracts, regardless of the asset type, must be deducted from the negative replacement cost.[7,8]

Liabilities and capital receiving a 100 percent ASF factor

3.9 Liabilities and capital instruments receiving a 100 percent ASF factor comprise:

(a) the total amount of regulatory capital, before the application of capital deductions, excluding the proportion of Tier 2 instruments with residual maturity of less than one year;

(b) the total amount of any capital instrument not included in (a) that has an effective residual maturity of one year or more, but excluding any instruments with explicit or embedded options that, if exercised, would reduce the expected maturity to less than one year; and

(c) the total amount of secured and unsecured borrowings and liabilities (including term deposits) with effective residual maturities of one year or more (cash flows falling below the one-year horizon but arising from liabilities with a final maturity greater than one year do notqualify for the 100 percent ASF factor).

[1] This could reflect a case where a bank may imply that it would be subject to funding risk if it did not exercise an option on its own funding

[2] NSFR derivative liabilities = (derivative liabilities) – (total collateral posted as variation margin on derivative liabilities).

[3] To the extent that the bank's accounting framework reflects on-balance sheet, in connection with a derivative contract, an asset associated with collateral posted as variation margin that is deducted from the replacement cost amount for purposes of the NSFR, that asset should not be included in the calculation of a bank's required stable funding (RSF) to avoid any double-counting.

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Liabilities in Kenyan Shillings (KES) receiving a 95 percent ASF factor

3.10 Stable non-maturity (demand) deposits and term deposits with residual maturity of less than one year provided by retail and small business customers in KES.

Liabilities in Kenyan Shillings (KES) receiving a 90 percent ASF factor

3.11 Less stable non-maturity deposits and term deposits with residual maturity of less than one year provided by retail and small business customers in KES.

Liabilities in foreign currency receiving a 90 percent ASF factor

3.12 Stable non-maturity deposits and term deposits with residual maturity of less than one year provided by retail and small business customers in foreign currency.

Liabilities in foreign currency receiving a 80 percent ASF factor

3.13 Less stable non-maturity deposits and term deposits with residual maturity of less than one year provided by retail and small business customers in foreign currency.

Liabilities receiving a 50 percent ASF factor

3.14 Liabilities receiving a 50 percent ASF factor comprise:

(a) funding (secured and unsecured) with a residual maturity of less than one year provided by non-financial corporate customers;

(b) operational deposits generated by clearing, custody and cash management activities;

(c) funding with residual maturity of less than one year from sovereigns, public sector entities (PSEs), and multilateral and national development banks; and

(d) other funding (secured and unsecured) not included in the categories above with residual maturity between six months to less than one year, including funding from central banks and financial institutions.

Liabilities receiving a 0 percent ASF factor

3.15 Liabilities receiving a 0 percent ASF factor comprise:

(a) all other liabilities and equity categories not included in the above categories, including other funding with residual maturity of less than six months from central banks and financial institutions;

(b) other liabilities without a stated maturity. This category may include short positions and open maturity positions. Two exceptions – should be recognized for liabilities without a stated maturity:

- first, deferred tax liabilities, which should be treated according to the nearest possible date on which such liabilities could be realized; and

- second, minority interest, which should be treated according to the term of the instrument, usually in perpetuity.

These liabilities would then be assigned either a 100 percent ASF factor if the effective maturity is one year or greater, or 50 percent, if the effective maturity is between six months and less than

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one year; and

(c) NSFR derivative liabilities net of NSFR derivative assets, if NSFR derivative liabilities are greater than NSFR derivative assets.

3.16 Table 1 below summarizes the components of each of the ASF categories and the associated maximum ASF factor to be applied in calculating an institution's total amount of available stable funding under the standard.

Table 1: Summary of liability categories and associated ASF factors

ASF factor	Components of ASF category
100 percent	• Total regulatory capital (excluding Tier 2 instruments with residual maturity of less than one year) • Other capital instruments and liabilities with effective residual maturity of one year or more
95 percent	• Stable non-maturity (demand) deposits and term deposits with residual maturity of less than one year provided by retail and small business customers in KES.
90 percent	• Less stable non-maturity deposits and term deposits with residual maturity of less than one year provided by retail and small business customers in KES. • Less stable non-maturity deposits and term deposits with residual maturity of less than one year provided by retail and small business customers in foreign currency
80 percent	• Less stable non-maturity deposits and term deposits with residual maturity of less than one year provided by retail and small business customers in foreign currency.
50 percent	• Funding with residual maturity of less than one year provided by non-financial corporate customers • Operational deposits • Funding with residual maturity of less than one year from sovereigns, PSEs, and multilateral and national development banks • Other funding with residual maturity between six months and less than one year not included in the above categories, including funding provided by central banks and financial institutions
0 percent	• All other liabilities and equity not included in the above categories, including liabilities without a stated maturity (with a specific treatment for deferred tax liabilities and minority interests) • NSFR derivative liabilities net of NSFR derivative assets if NSFR derivative liabilities are greaterthan NSFR derivative assets

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B. Definition of Required Stable Funding For Assets and Off-Balance Sheet Exposures

3.17 The amount of required stable funding is measured based on the broad characteristics of the liquidity risk profile of an institution's assets and OBS exposures. The amount of required stable funding is calculated by first assigning the carrying value of an institution's assets to the categories listed. The amount assigned to each category is then multiplied by its associated required stable funding (RSF) factor, and the total RSF is the sum of the weighted amounts added to the amount of OBS activity (or potential liquidity exposure) multiplied by its associated RSF factor.

3.18 The RSF factors assigned to various types of assets are intended to approximate the amount of a particular asset that would have to be funded, either because it will be rolled over, or because it could not be monetized through sale or used as collateral in a secured borrowing transaction over the course of one year without significant expense. Under the standard, such amounts are expected to be supported by stable funding.

3.19 Assets should be allocated to the appropriate RSF factor based on their residual maturity or liquidity value. When determining the maturity of an instrument, investors should be assumed to exercise any option to extend maturity. For assets with options exercisable at the bank's discretion, reputational factors should be taken into account that may limit a bank's ability not to exercise the option. In particular, where the market expects certain assets to be extended in their maturity, banks should assume such behaviour for the purpose of the NSFR and include these assets in the corresponding RSF category. For amortizing loans, the portion that comes due within the one-year horizon – should be treated in the less-than-one-year residual maturity category.

3.20 For purposes of determining its RSF, a bank should (i) include financial instruments, foreign currencies and commodities for which a purchase order has been executed, and (ii) exclude financial instruments, foreign currencies and commodities for which a sales order has been executed, even if such transactions have not been reflected in the balance sheet under a settlement-date accounting model, provided that (i) such transactions are not reflected as derivatives or secured financing transactions in the institution's balance sheet, and (ii) the effects of such transactions will be reflected in the institution's balance sheet when settled.

Encumbered assets

3.21 Assets on the balance sheet that are encumbered for one year or more receive a 100 percent RSF factor. Assets encumbered for a period of between six months and less than one year that would, if unencumbered, receive an RSF factor lower than or equal to 50 percent -. Assets encumbered for between six months and less than one year that would, if unencumbered, receive an RSF factor higher than 50 percent retain that higher RSF factor. Where assets have less than six months remaining in the encumbrance period, those assets may receive the same RSF factor as an equivalent asset that is unencumbered.

Secured financing transactions

3.22 For secured funding arrangements, use of balance sheet and accounting treatments should generally result in banks excluding, from their assets, securities which they have borrowed in securities financing transactions (such as reverse repos) where they do not have beneficial ownership. In contrast, banks should include securities they have lent in securities financing transactions where they retain beneficial ownership. Where banks have encumbered securities in repos or other securities financing transactions, but have retained beneficial ownership and those assets remain on the bank's balance sheet, the bank should allocate such securities to the appropriate RSF category.

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3.23 Securities financing transactions with a single counterparty may be measured net when calculating the NSFR, provided that the netting conditions are met[9].

Calculation of derivative asset amounts

3.24 Derivative assets are calculated first based on the replacement cost for derivative contracts (obtained by marking to market) where the contract has a positive value.

3.25 In calculating NSFR derivative assets, collateral received in connection with derivative contracts may not offset the positive replacement cost amount, regardless of whether or not netting is permitted under the bank's operative accounting or risk-based framework, unless it is received in the form of cash variation margin. Any remaining balance sheet liability associated with (a) variation margin received that does not meet the criteria above or (b) initial margin received may not offset derivative assets and should be assigned a 0 percent ASF factor.

Assets assigned a 0 percent RSF factor

3.26 Assets assigned a 0 percent RSF factor comprise:

(a) coins and banknotes immediately available to meet obligations;

(b) all central bank reserves (including required reserves and excess reserves); and

(c) all claims on central banks with residual maturities of less than six months.

Assets assigned a 5 percent RSF factor

3.27 Assets assigned a 5 percent RSF factor comprise unencumbered Level 1 assets as defined in LCR guideline, excluding assets receiving a 0 percent RSF as specified above, and including:

- marketable securities representing claims on or guaranteed by sovereigns, central banks, PSEs, the International Monetary Fund, the European Central Bank and the European Community, or multilateral development banks that are assigned a 0 percent risk weight under the Basel II/II capital framework for credit risk; and

- certain non-0 percent risk-weighted sovereign or central bank debt securities as specified in theLCR guideline.

Assets assigned a 10 percent RSF factor

3.28 Unencumbered loans to financial institutions with residual maturities of less than six months, where the loan is secured against Level 1 assets as defined in the LCR guideline, and where the bank has the ability to freely rehypothecate the received collateral for the life of the loan.

Assets assigned a 15 percent RSF factor

3.29 Assets assigned a 15 percent RSF factor comprise:

(a) unencumbered Level 2A assets as defined in the LCR guideline, including:

[9] See BCBS: p.33i of "Basel III leverage ratio framework and disclosure requirements", January 2014

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- marketable securities representing claims on or guaranteed by sovereigns, central banks, PSEs or multilateral development banks that are assigned a 20 percent risk weight under the Basel II/III capital framework for credit risk; and

- corporate debt securities (including commercial paper) and covered bonds with a credit rating equal or equivalent to at least AA–;

(b) all other unencumbered loans to financial institutions with residual maturities of less than six months not included in paragraph 3.28

Assets assigned a 50 percent RSF factor

3.30 Assets assigned a 50 percent RSF factor comprise:

(a) unencumbered Level 2B assets as defined and subject to the conditions set forth in the LCR Guideline, including:

- residential mortgage-backed securities (RMBS) with a credit rating of at least AA;

- corporate debt securities (including commercial paper) with a credit rating of between A+ and BBB–; and

- exchange-traded common equity shares not issued by financial institutions or their affiliates;

(b) any HQLA as defined in the LCR Guideline that are encumbered for a period of between six months and less than one year;

(c) all loans to financial institutions and central banks with residual maturity of between six months and less than one year;

(d) deposits held at other financial institutions for operational purposes, as outlined in the LCR guideline, that are subject to the 50 percent ASF factor in paragraph 3.14 and

(e) all other non-HQLA not included in the above categories that have a residual maturity of less than one year, including loans to non-financial corporate clients, loans to retail customers (ie natural persons) and small business customers, and loans to sovereigns and PSEs.

Assets assigned a 65 percent RSF factor

3.31 Assets assigned a 65 percent RSF factor comprise:

(a) unencumbered residential mortgages with a residual maturity of one year or more that would qualify for a 50 percent or lower risk weight under the Basel II/III capital framework; and

(b) other unencumbered loans not included in the above categories, excluding loans to financial institutions, with a residual maturity of one year or more that would qualify for a 50 percent or lower risk weight under the Basel II/III capital framework.

Assets assigned an 85 percent RSF factor

3.32 Assets assigned an 85 percent RSF factor comprise:

(a) cash, securities or other assets posted as initial margin for derivative contracts. Where securities or other assets posted as initial margin for derivative contracts would otherwise receive a higher RSF factor, they should retain that higher factor.

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(b) other unencumbered performing loans that do not qualify for the 50 percent or lower risk weight under the Basel II/III capital framework and have residual maturities of one year or more, excluding loans to financial institutions;

(c) unencumbered securities with a remaining maturity of one year or more and exchange- traded equities, that are not in default and do not qualify as HQLA according to the LCR guideline; and

(d) physical traded commodities, including gold.

Assets assigned a 100 percent RSF factor

3.33 Assets assigned a 100 percent RSF factor comprise:

(a) all assets that are encumbered for a period of one year or more;

(b) NSFR derivative assets as calculated according to paragraphs 3.24 and 3.25 net of NSFR derivative liabilities as calculated according to paragraph 3.8, if NSFR derivative assetsare greater than NSFR derivative liabilities;

(c) all other assets not included in the above categories, including non-performing loans, loans to financial institutions with a residual maturity of one year or more, non-exchange-traded equities, fixed assets, items deducted from regulatory capital, retained interest, insurance assets, subsidiary interests and defaulted securities; and

(d) 20 percent of derivative liabilities (ie negative replacement cost amounts) as calculated according toparagraph 3.8 (before deducting variation margin posted).

3.34 Table 2 summarizes the specific types of assets to be assigned to each asset category and their associated RSF factor.

Table 2. Summary of asset categories and associated RSF factors

RSF factor	Components of RSF category
0 percent	• Coins and banknotes • All central bank reserves • All claims on central banks with residual maturities of less than six months
5 percent	• Unencumbered Level 1 assets, excluding coins, banknotes and central bank reserves
10 percent	• Unencumbered loans to financial institutions with residual maturities of less than six months, where the loan is secured against Level 1 assets as defined in LCR Guideline, and where the bank has the ability to freely rehypothecate the received collateral for the life of the loan
15 percent	• All other unencumbered loans to financial institutions with residual maturities of less than six months not included in the above categories • Unencumbered Level 2A assets

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RSF factor	Components of RSF category
50 percent	• Unencumbered Level 2B assets • HQLA encumbered for a period of six months or more and less than one year • Loans to financial institutions and central banks with residual maturities between six months and less than one year • Deposits held at other financial institutions for operational purposes • All other assets not included in the above categories with residual maturity of less than one year, including loans to non-financial corporate clients, loans to retail and small business customers, and loans to sovereigns and PSEs
65 percent	• Unencumbered residential mortgages with a residual maturity of one year or more and with a risk weight of less than or equal to 50 percent under the Basel II/II Capital Framework. • Other unencumbered loans not included in the above categories, excluding loans to financial institutions, with a residual maturity of one year or more and with a risk weight of less than or equal to 50 percent under the Basel II/II Capital Framework.
85 percent	• Cash, securities or other assets posted as initial margin for derivative contracts and cash or other assets provided to contribute to the default fund of a CCP • Other unencumbered performing loans with risk weights greater than 50 percent under the Basel II/II Capital Framework and residual maturities of one year or more, excluding loans to financial institutions • Unencumbered securities that are not in default and do not qualify as HQLA with a remaining maturity of one year or more and exchange-traded equities • Physical traded commodities, including gold
100 percent	• All assets that are encumbered for a period of one year or more • NSFR derivative assets net of NSFR derivative liabilities if NSFR derivative assets are greater than NSFR derivative liabilities • 20 percent of derivative liabilities as calculated according to 2.8 • All other assets not included in the above categories, including non-performing loans, loans to financial institutions with a residual maturity of one year or more, non-exchange-traded equities, fixed assets, items deducted from regulatory capital, retained interest, insurance assets, subsidiary interests and defaulted securities

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Off-balance sheet exposures

3.35 Many potential OBS liquidity exposures require little direct or immediate funding but can lead to significant liquidity drains over a longer time horizon. The NSFR assigns an RSF factor to various OBS activities in order to ensure that institutions hold stable funding for the portion of OBS exposures that may be expected to require funding within a one-year horizon.

3.36 Consistent with the LCR, the NSFR identifies OBS exposure categories based broadly on whether the commitment is a credit or liquidity facility or some other contingent funding obligation. Table 3 identifies the specific types of OBS exposures to be assigned to each OBS category and their associated RSF factor.

Table 3. Summary of off-balance sheet categories and associated RSF factors

RSF factor	RSF category
5 percent of currently undrawn portion	• Irrevocable and conditionally revocable credit and liquidity facilities to any client
5 percent of currently undrawn portion	• Trade finance-related obligations (including guarantees and letters of credit)
10 percent of currently undrawn portion	Other contingent funding obligations, including products and instruments such as: • Unconditionally revocable credit and liquidity facilities • Guarantees and letters of credit unrelated to trade finance obligations • Other Non-contractual obligations 10 percent

PART IV EFFECTIVE DATE

4.1 **Effective date:** The effective date of this Guideline shall be 1st October 2025.

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Leverage Ratio Guideline CBK/LR/03

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LIST OF ABBREVIATIONS

CBK	Central Bank of Kenya
CCP	Central Counterparty
CM	Clearing Member
MNA	Master Netting Agreement
OBS	Off-Balance Sheet
OTC	Over the Counter
PFE	Potential Future Exposure
QCCP	Qualified Central Counterparty
RC	Replacement Cost
SFT	Security Financing Transactions

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PART I: PRELIMINARY

1.2 **Title:** Leverage Ratio Guidelines.

2.2 **Authorization** - This Guideline is issued under Section 33(4) of the Banking Act, which empowers the Central Bank of Kenya to issue guidelines to be adhered to by institutions in order to maintain a stable and efficient banking and financial system.

2.3 **Application** - This Guideline applies to all institutions licensed under the Banking Act (cap 488).

2.4 **Definitions** – the terms used in this guideline are as defined in the Banking Act (cap 488). Other terms used in this guideline shall be taken to have the meaning assigned to them hereunder.

"Bilateral netting" means the consolidation of agreements between a financial organization and a counterparty, which results in a single legally enforceable arrangement between a financial organization and a counterparty covering all, included individual contracts including master netting agreements.

"Counterparty credit risk (CCR)" is the risk that the counterparty to a transaction could default before the final settlement of the transaction's cash flows. An economic loss would occur if the transactions or portfolio of transactions with the counterparty has a positive economic value at the time of default. Unlike a firm's exposure to credit risk through a loan, where the exposure to credit risk is unilateral and only the lending bank faces the risk of loss, CCR creates a bilateral risk of loss: the market value of the transaction can be positive or negative to either counterparty to the transaction. The market value is uncertain and can vary over time with the movement of underlying market factors.

"Central counterparty (CCP)" is a clearing house that interposes itself between counterparties to contracts traded in one or more financial markets, becoming the buyer to every seller and the seller to every buyer and thereby ensuring the future performance of open contracts. A CCP becomes counterparty to trades with market participants through novation, an open offer system, or another legally binding arrangement. For the purposes of the capital framework, a CCP is a financial institution.

"Clearing member" is a member of, or a direct participant in, a CCP that is entitled to enter into a transaction with the CCP, regardless of whether it enters into trades with a CCP for its own hedging, investment or speculative purposes or whether it also enters into trades as a financial intermediary between the CCP and other market participants.

"Clearing relationship" means a service arrangement that enables customers to transfer funds (or securities) indirectly through direct participants in domestic settlement systems to final recipients. Such services are limited to the following activities: transmission, reconciliation and confirmation of payment orders, daylight overdraft, overnight financing and maintenance of post-settlement balances, and determination of intra-day and final settlement positions.

"Qualifying central counterparty (QCCP)" is an entity that is licensed to operate as a CCP (including a license granted by way of confirming an exemption), and is permitted by the

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appropriate regulator/overseer to operate as such with respect to the products offered. This is subject to the provision that the CCP is based and prudentially supervised in a jurisdiction where the relevant regulator/overseer has established, and publicly indicated that it applies to the CCP on an ongoing basis, domestic rules and regulations that are consistent with the Principles for Financial Market Infrastructures issued by the Committee on Payments and Market Infrastructures and the International Organization of Securities Commissions.

"Initial margin" means a clearing member's or client's funded collateral posted to the CCP to mitigate the potential future exposure (PFE) of the CCP to the clearing member arising from the possible future change in the value of their transactions. Initial margin includes collateral deposited by a clearing member or client in excess of the minimum amount required, provided the CCP or clearing member may, in appropriate cases, prevent the clearing member or client from withdrawing such excess collateral.

"Variation margin" means a clearing member's or client's funded collateral posted on a daily or intraday basis to a CCP based upon price movements of their transactions.

"Security financing transaction (SFT)" are transactions such as repurchase agreements, reverse repurchase agreements, security lending and borrowing, and margin lending transactions, where the value of the transactions depends on market valuations and the transactions are often subject to margin agreements.

"Long settlement transactions" are transactions where a counterparty undertakes to deliver a security, a commodity, or a foreign exchange amount against cash, other financial instruments, or commodities, or vice versa, at a settlement or delivery date that is contractually specified as more than the lower of the market standard for this particular instrument and five business days after the date on which the bank enters into the transaction.

"Margin lending transactions" are transactions in which a bank extends credit in connection with the purchase, sale, carrying or trading of securities. Margin lending transactions do not include other loans that happen to be secured by securities collateral. Generally, in margin lending transactions, the loan amount is
collateralised by securities whose value is greater than the amount of the loan.

"Netting set" is a group of transactions with a single counterparty that are subject to a legally enforceable bilateral netting arrangement and for which netting is recognised for regulatory capital purposes that are applicable to the group of transactions. Each transaction that is not subject to a legally enforceable bilateral netting arrangement that is recognised for regulatory capital purposes should be interpreted as its own netting set for the purpose of these rules.

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PART II STATEMENT OF POLICY

2.1 **Purpose -** The Leverage Ratio is a simple, transparent, non-risk-based measure that is calibrated to act as a credible supplementary measure to the risk-based capital requirements. the leverage ratio is intended to achieve the following objectives:

- constrain the build-up of leverage in the banking sector, helping avoid destabilizing deleveraging processes which can damage the broader financial system and the economy; and
- reinforce the risk-based requirements with a simple, non-risk based "backstop" measure.

2.2 Scope of Application - The Leverage Ratio framework follows the same scope of regulatory consolidation, including consolidation criteria, as is used for the risk-based capital framework. where a banking, financial, insurance or commercial entity is outside the scope of regulatory consolidation, only the investment in the capital of such entities is to be included in the leverage ratio exposure measure. however, investments in the capital of such entities that are deducted from tier 1 capital may be excluded from the leverage ratio exposure measure.

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PART III: CALCULATION

3.1 The leverage ratio is defined as the capital measure (the numerator) divided by the exposure measure (the denominator), with this ratio expressed as a percentage:

$$Leverage\ ratio = \frac{Capital\ measure}{Exposure\ measure}$$

3.2 The capital measure for the leverage- - ratio is core capital (Tier 1 capital) measure' applicable at that time under the risk-based framework. The exposure measure for the leverage ratio is defined in the next section.

3.3 Banks must meet a 4 percent leverage ratio minimum requirement at all times.

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PART IV: EXPOSURE MEASURE

4.1 A bank's total leverage ratio exposure measure is the sum of the following exposures:

a. On-balance sheet exposures (excluding on-balance sheet derivative and SFTs exposures);

b. derivative exposures;

c. Securities financing transaction exposures; and

d. Off-balance sheet items.

4.2 The leverage ratio exposure measure generally follows gross accounting values.

4.3 Unless specified differently below, banks must not take account of physical or financial collateral, guarantees or other credit risk mitigation techniques to reduce the leverage ratio exposure measure, nor may banks net assets and liabilities.

4.4 To ensure consistency, any item deducted from Tier 1 capital according to the Basel framework and regulatory adjustments other than those related to liabilities may be deducted from the leverage ratio exposure measure. For example, where a banking, financial or insurance entity is not included in the regulatory scope of consolidation, the amount of any investment in the capital of that entity that is totally or partially deducted from Tier 1 capital of the bank may also be deducted from the leverage ratio exposure measure.

4.5 Liability items must not be deducted from the leverage ratio exposure measure. For example, gains/losses on fair valued liabilities or accounting value adjustments must not be deducted from the leverage ratio exposure measure.

I. On-balance sheet exposures

4.6 Banks must include all balance sheet assets in their leverage ratio exposure measure, including on-balance sheet derivatives collateral and collateral for SFTs, with the exception of on-balance sheet derivative and SFT assets that are covered under section II. Derivatives exposures.

4.7 On-balance sheet, non-derivative assets are included in the leverage ratio exposure measure at their accounting values less deductions for associated specific provisions. In addition, general provisions or general loan-loss reserves which have reduced Tier 1 capital may be deducted from the leverage ratio exposure measure.

II. Derivative exposures

4.8 For the purpose of the leverage ratio exposure measure, exposures to derivatives are included by means of two components:

a. replacement cost (RC); and

b. potential future exposure (PFE).

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4.9 Banks must calculate their exposures associated with all derivative transactions as a scalar multiplier alpha set at 1.4 times the sum of the RC and the PFE[10]. If the derivative exposure is covered by an eligible bilateral netting contract, a specific treatment may be applied.

4.10 The amount to be included in the leverage ratio exposure measure is calculated according to:

$$Exposure\ measure = 1.4 \cdot (RC + PFE)$$ (See Capital Adequacy section 4.3.1.3).

4.11 For derivative transactions not covered by an eligible bilateral netting contract[11], the amount to be included in the leverage ratio exposure measure is determined, for each transaction separately. When an eligible bilateral netting contract is in place, the formula below is applied at the netting set level.

4.12 When calculating the exposure amount, a bank must not reduce the leverage ratio exposure measure amount by any collateral received from the counterparty. Similarly, with regard to collateral provided, banks must gross up their leverage ratio exposure measure by the amount of any derivatives collateral provided where the provision of that collateral has reduced the value of their balance sheet assets under their operative accounting framework.

4.13 Where a bank acting as clearing member (CM) offers clearing services to clients, the CM's trade exposures to the CCP that arise when the CM is obligated to reimburse the client for any losses suffered due to changes in the value of its transactions in the event that the CCP defaults must be captured by applying the same treatment that applies to any other type of derivative transaction. However, if the CM, based on the contractual arrangements with the client, is not obligated to reimburse the client for any losses suffered in the event that a QCCP defaults, the CM need not recognize the resulting trade exposures to the QCCP in the leverage ratio exposure measure.

4.14 For derivative exposures associated with the bank's offering of client clearing services, the RC and the PFE of the exposure to the client may be calculated according to the rules set out in the Capital Adequacy prudential Guidelines for CCR.

4.15 Where a client enters directly into a derivative transaction with the CCP and the CM guarantees the performance of its client's derivative trade exposures to the CCP, the bank acting as the CM for the client to the CCP must calculate its related leverage ratio exposure resulting from the guarantee as a derivative exposure, as if it had entered directly into the transaction with the client, including with regard to the receipt or provision of cash variation margin.

4.16 For the purposes of 4.12 and 4.14, an entity affiliated to the bank acting as a CM may be considered a client if it is outside the relevant scope of regulatory consolidation at the level at which the leverage ratio is applied. In contrast, if an affiliate entity falls within the regulatory scope of consolidation, the trade between the affiliate entity and the CM is eliminated in the course of consolidation but the CM

[10] Or "PFE Add-on" as renamed under the Basel III SA-CCR standard.
[11] See the conditions under which bilateral netting will be allowed under the Capital Adequacy Prudential guidelines (section 4.3.1.3 subsection on Bilateral Netting).

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still has a trade exposure to the CCP. In this case, the transaction with the CCP will be considered proprietary and the exemption in 4.12 will not apply.

4.17 In the treatment of derivative exposures for the purpose of the leverage ratio exposure measure, the cash portion of variation margin exchanged between counterparties may be viewed as a form of pre-settlement payment if the following conditions are met:

a. For trades not cleared through a qualifying central counterparty (QCCP) the cash received by the recipient counterparty is not segregated.
b. Variation margin is calculated and exchanged on at least a daily basis based on mark-to-market valuation of derivative positions.
c. The variation margin is received in a currency specified in the derivative contract, governing master netting agreement (MNA), credit support annex to the qualifying MNA or as defined by any netting agreement with a CCP.
d. Variation margin exchanged is the full amount that would be necessary to extinguish the mark-to-market exposure of the derivative subject to the threshold and minimum transfer amounts applicable to the counterparty.
e. Derivative transactions and variation margins are covered by a single MNA between the legal entities that are the counterparties in the derivative transaction.

4.18 If the conditions in 4.16 are met, the cash portion of variation margin received may be used to reduce the replacement cost portion of the leverage ratio exposure measure, and the receivables assets from cash variation margin provided may be deducted from the leverage ratio exposure measure.

4.19 Banks won't be allowed to use credit derivatives without prior authorization of the CBK.

III. Securities financing transaction exposures

4.20 SFTs are an important source of leverage and therefore should be included in the exposure measure SFTs are included in the leverage ratio exposure measure according to the treatment described below.

4.21 For a bank acting as principal the sum of the amounts in (1) and (2) is to be included in the leverage ratio exposure measure:

(1) Gross SFT assets recognized for accounting purposes[12], adjusted as follows:

a) excluding from the leverage ratio exposure measure the value of any securities received under an SFT, where the bank has recognized the securities as an asset on its balance sheet;

b) cash payables and cash receivables in SFTs with the same counterparty may be measured net if all the following criteria are met:

i. Transactions have the same explicit final settlement date;

[12] Gross SFT assets recognized for accounting purposes must not recognize any accounting netting of cash payables against cash receivables (e.g. as currently permitted under the IFRS).

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ii. The right to set off the amount owed to the counterparty with the amount owed by the counterparty is legally enforceable both currently in the normal course of business and in the event of the counterparty's default, insolvency, or bankruptcy; and

iii. The counterparties intend to settle net, settle simultaneously, or the transactions are subject to a settlement mechanism that results in the functional equivalent of net settlement, that is, the cash flows of the transactions are equivalent, in effect, to a single net amount on the settlement date.

(2) A measure of CCR calculated as the current exposure without an add-on for PFE calculated as follows. For the purposes of this subparagraph, the term "counterparty" includes not only the counterparty of the bilateral repo transactions but also triparty repo agents that receive collateral in deposit and manage the collateral in the case of triparty repo transactions. Therefore, securities deposited at triparty repo agents are included in "total value of securities and cash lent to a counterparty" (E) up to the amount effectively lent to the counterparty in a repo transaction. However, excess collateral that has been deposited at triparty agents but that has not been lent out may be excluded.

a) Where a qualifying MNA[13] is in place, the current exposure (E*) is the greater of zero and the total fair value of securities and cash lent to a counterparty for all transactions included in the qualifying MNA (ΣE_i), less the total fair value of cash and securities received from the counterparty for those transactions (ΣC_i). This is illustrated in the following formula: $E^* = \max(0, \Sigma E_i - \Sigma C_i)$.

b) Where no qualifying MNA is in place, the current exposure for transactions with a counterparty must be calculated on a transaction-by-transaction basis - that is, each transaction i is treated as its own netting set, as shown in the following formula: $E^* = \max(0, (E_i - C_i))$.

c) E_i^* may be set to zero if:

i. E_i is the cash lent to a counterparty;

ii. this transaction is treated as its own netting set; and

iii. the associated cash receivable is not eligible for the netting treatment in (1).

4.22 The effects of bilateral netting agreements for covering SFTs should be recognized on a counterparty-by-counterparty basis if the agreements are legally enforceable in each relevant jurisdiction upon the occurrence of an event of default and regardless of whether the counterparty is insolvent or bankrupt. In addition, netting agreements must:

a) provide the non-defaulting party with the right to terminate and close out in a timely manner all transactions under the agreement upon an event of default, including in the event of insolvency or bankruptcy of the counterparty;

b) provide for the netting of gains and losses on transactions (including the value of any collateral) terminated and closed out under it so that a single net amount is owed by one

[13] A qualifying MNA is the one that meets the requirements under 4.21 and 4.22.

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party to the other;

c) allow for the prompt liquidation or setoff of collateral upon the event of default; and

d) be, together with the rights arising from provisions required in (1) and (3) above, legally enforceable in each relevant jurisdiction upon the occurrence of an event of default regardless of the counterparty's insolvency or bankruptcy.

4.23 Netting across SFT positions held in the banking book and trading book shall only be recognized when the netted transactions fulfil the following conditions:

a. all transactions are marked to market daily; and

b. the collateral instruments used in the transactions are recognized as eligible financial collateral in the banking book.

4.24 Where a bank acting as agent in an SFT provides an indemnity or guarantee to a customer or counterparty for any difference between the value of the security or cash the customer has lent and the value of collateral the borrower has provided, then the bank will be required to calculate its exposure measure by applying only a measure of CCR calculated as the current exposure without an add-on for PFE. Where a bank acting as an agent in an SFT does not provide an indemnity or guarantee to any of the involved parties, the bank is not exposed to the SFT and therefore need not recognize those SFTs in its exposure measure.

IV. Off-balance-sheet exposures

4.25 OBS items include commitments (including liquidity facilities), whether or not unconditionally cancellable, direct credit substitutes, acceptances, standby letters of credit and trade letters of credit.

4.26 For the purposes of the leverage ratio, OBS items will be converted into credit exposures by multiplying the committed but undrawn amount by a CCF set out in the prudential guidelines (Capital Adequacy section 4.3.1.3). Commitment means any contractual arrangement that has been offered by the bank and accepted by the client to extend credit, purchase assets or issue credit substitutes. It includes any such arrangement that can be unconditionally cancelled by the bank at any time without prior notice to the obligor. It also includes any such arrangement that can be cancelled by the bank if the obligor fails to meet conditions set out in the facility document, including conditions that must be met by the obligor prior to any initial or subsequent drawdown arrangement.

4.27 Specific and general provisions set aside against OBS exposures that have decreased Tier 1 capital may be deducted from the credit exposure equivalent amount of those exposures (ie the exposure amount after the application of the relevant CCF). However, the resulting total off-balance-sheet equivalent amount for OBS exposures cannot be less than zero.

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PART V: REPORTING REQUIREMENT AND TRANSITIONAL ARRANGEMENTS

5.1 Banks are required, at a minimum, to report both the capital measure and the exposure measure on a quarterly basis. They should also be able to calculate and report the leverage ratio on a quarterly basis, 30 days after the end of the quarter for internal monitoring purposes to ensure ongoing compliance with internal limits.

5.2 Banks are required to provide an explanation for the key drivers of material changes in their Basel III leverage ratio observed from the end of the previous reporting period to the end of the current reporting period.

PART VI: EFFECTIVE DATE

6.1 Effective date: The effective date of this Guideline shall be 1st October 2025.

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