Basel Committee
on Banking Supervision

Regulatory Consistency Assessment Programme (RCAP)

Assessment of Basel NSFR regulations – Kingdom of Saudi Arabia

September 2018

BANK FOR INTERNATIONAL SETTLEMENTS

Note that this report refers to the RCAP grades prior to October 2025. The grade 'materially non-compliant (MNC)', ie one notch above the lowest grade, has since been renamed to 'partially non-compliant (PNC)' for greater clarity

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Glossary

ASF	Available Stable Funding
BCBS	Basel Committee on Banking Supervision
BCL	Banking Control Law
BLR	Banking Liquidity Rules
BIS	Bank for International Settlements
BO	Banking Ordinance
C	Compliant (grade)
CFP	Contingency Funding Plan
D-SIB	Domestically systemically important bank
DNB	Netherlands Bank
FAQs	Frequently asked questions
G-SIB	Global systemically important bank
HQLA	High-quality liquid assets
ILAAP	Internal Liquidity Adequacy Assessment Plan
KSA	Kingdom of Saudi Arabia
LC	Largely compliant (grade)
LCR	Liquidity Coverage Ratio
LDR	Loan-to-deposit ratio
MDB	Multilateral Development Bank
MNC	Materially non-compliant (grade)
NDB	National Development Bank
NC	Non-compliant (grade)
NSFR	Net Stable Funding Ratio
PSE	Public sector entity
RCAP	Regulatory Consistency Assessment Programme
RSF	Required Stable Funding
SAMA	Saudi Arabian Monetary Authority
SAR	Saudi Arabian riyal

Preface

The Basel Committee on Banking Supervision (BCBS or Basel Committee) places a high priority on the implementation of regulatory standards underpinning the Basel III framework. The prudential benefits from adopting Basel standards can only accrue if these are implemented fully, consistently and in a timely manner by all member jurisdictions. The Committee established the Regulatory Consistency Assessment Programme (RCAP) to monitor, assess and evaluate its members' implementation of the Basel framework.

This report presents the findings of an RCAP Assessment Team on the domestic adoption of the Basel Net Stable Funding Ratio (NSFR) standard in the Kingdom of Saudi Arabia (KSA). The assessment focused on the completeness of the domestic regulations in force on 30 June 2018, as applied to the KSA's domestic banks, and their consistency with the Basel NSFR standard. Issues related to prudential outcomes, the adequacy of liquidity, the resilience of the banking system or the supervisory effectiveness of the KSA's authorities were not in the scope of this assessment. The assessment relied on regulations and other information and explanations provided by the KSA's authorities and ultimately reflects the view of the Basel Committee.

The RCAP Assessment Team was led by Olaf Sleijpen, Supervision Policy Director at the Netherlands Bank (DNB). It comprised four technical experts from Mexico, the European Central Bank – Banking Supervision, Indonesia and Turkey (see Annex 1). The main counterpart for the assessment was the Saudi Arabian Monetary Authority (SAMA). The work was coordinated by the Basel Committee Secretariat with the support of staff from the Netherlands Bank.

Starting in February 2018, the assessment comprised three phases: (i) self-assessment by SAMA; (ii) an assessment phase (February to May 2018), including an on-site assessment involving discussions with SAMA and representatives of KSA banks; and (iii) a review phase (June to August 2018), including a technical review of the Assessment Team's findings by a separate RCAP Review Team, the Committee's Supervision and Implementation Group, the RCAP Peer Review Board and the Basel Committee. More information on the RCAP assessment process is available on the Committee's website.[1]

The RCAP Assessment Team acknowledges the cooperation received from SAMA counterparts throughout the assessment process. In particular, the team thanks the staff of SAMA for playing an instrumental role in coordinating the assessment exercise.

[1] See www.bis.org/bcbs/implementation.htm.

Executive summary

SAMA implemented the Basel NSFR standard consistently with the internationally agreed standard. SAMA implemented the NSFR as a minimum standard as of 1 January 2016. The KSA NSFR regulation is applicable to all 12 locally incorporated banks on a consolidated basis. Overall, as of 30 June 2018, the NSFR regulation in the KSA is assessed as compliant with the Basel NSFR standard. This is the highest possible grade. Each component is also assessed as compliant.

The Assessment Team recognises the efforts made by SAMA to improve the consistency of its NSFR regulation throughout the course of the assessment process. These amendments became effective prior to 30 June 2018 (see Annex 5 for a complete list), the cutoff date for the assessment.

The Assessment Team identified one non-material finding with regard to the definition of required stable funding. This finding refers to the definition of Level 1 assets subject to a 5% stable funding requirement in the NSFR. Differing from paragraph 50(c) of the Basel Liquidity Coverage Ratio (LCR) standard, SAMA defines 0% risk-weighted local government bonds as Level 1 assets despite the absence of a large, deep and active private market. While the wording in the KSA NSFR regulation does not differ from the Basel NSFR standard with regard to the treatment of Level 1 assets, this deviation in the LCR affects the NSFR since the definitions used in the NSFR regulation mirror those outlined in the LCR regulation (unless otherwise specified).

However, the Assessment Team considers this finding non-material. KSA government debt securities, currently rated as A, do not benefit from a 0% risk weight under the Basel credit risk standardised approach. As such, these assets do not qualify as Level 1 assets as per the KSA equivalent of paragraph 50(c) of the Basel LCR standard. Instead, these securities qualify as Level 1 assets as per the KSA equivalent of paragraph 50(d) of the Basel LCR standard, which, however, does not require the securities to be traded in large, deep and active private markets.

SAMA and other governmental entities of the KSA have undertaken actions to create an active and deep market for government debt securities as well as for other financial instruments. SAMA also created the financial infrastructure necessary for this objective. SAMA expects these initiatives to be completed within the next three to five years. In the opinion of the Assessment Team, these actions may establish the adequate conditions to meet the requirements provided in paragraph 50(c) of the Basel LCR standard for the use of local government bonds and other local assets to be classified as Level 1 assets in the LCR (and the NSFR).

The Assessment Team recommends a follow-up on this finding at a later stage. This follow-up should also take into consideration potential guidance or revisions issued by the Basel Committee on the treatment of illiquid (in terms of not being traded on large, deep and active private markets) but 0% risk-weighted government securities in the LCR. Furthermore, progress regarding the targeted strengthening of the market for government debt securities in the KSA should be taken into account.

The Assessment Team believes it would be helpful to review paragraph 50(c) of the Basel LCR standard and to re-assess whether or not it is appropriate to exclude from the LCR liquidity buffer (domestic) securities that are assigned a 0% risk weight but are not traded on large, deep, active and liquid markets. This issue was also raised in the KSA RCAP-LCR as an area for further guidance from the Basel Committee.

The KSA NSFR regulation is super-equivalent to the Basel NSFR standard in several areas. SAMA introduced the NSFR as a binding minimum standard as of 1 January 2016, two years ahead of the implementation date provided in the Basel standard. SAMA does not permit the use of Level 2B assets for the purpose of the LCR. As such, for the NSFR, those assets are treated as non-liquid securities subject to a stable funding requirement of 50% for assets with a residual maturity or encumbrance period less than one year or 85% for all other assets. The stricter rules have not been taken into account as mitigants for the overall or component-level assessment of compliance.

Response from SAMA

SAMA welcomes the opportunity to be the first jurisdiction to be assessed under the RCAP for the implementation of the Basel III Net Stable Funding Ratio standard, and to respond to the findings and comments of the RCAP Assessment Team. SAMA also wishes to acknowledge and appreciate the commitment, professionalism and expertise of the RCAP Assessment Team, under the leadership of Mr Olaf Sleijpen, and would like to thank the Assessment Team for the proficiency with which the entire RCAP exercise for Saudi Arabia was completed.

This assessment has provided a comprehensive and thorough review of the implementation of the Basel Net Stable Funding Ratio standard in Saudi Arabia, and we are pleased that Saudi Arabia has received an overall compliant rating.

SAMA has always considered a strong liquidity adequacy framework to be the cornerstone of a sound banking system. This important principle was embedded in the Banking Control Law, which provided for a SAMA liquidity ratio for Saudi banks as far back as 1966. In the following years, SAMA led the way in this region, introducing the Basel Liquidity Coverage Ratio as a binding minimum requirement in 2015 in accordance with the Basel-agreed time line and introducing the Basel Net Stable Funding Ratio standard as a binding minimum requirement in 2016, two years ahead of the Basel implementation date.

Based on SAMA's self-assessment and as identified by the Assessment Team, SAMA has carried out 21 modifications to the existing regulations and guidelines before the agreed cutoff date of 30 June 2018. We believe that these modifications will further strengthen the implementation of the Basel liquidity framework in Saudi Arabia and will confirm our commitment to the work of the Basel Committee and the consistent implementation of regulatory standards underpinning the Basel III framework.

Overall, SAMA considers the RCAP process a very useful exercise, and is supportive of the Basel objectives to promote consistency of implementation of rules among member countries. SAMA also concurs that the RCAP process promotes a level playing field among Basel member jurisdictions, which reduces regulatory arbitrage and promotes the safety, soundness and stability of the global financial system.

1 Assessment context

1.1 Status of NSFR implementation

SAMA is responsible for the regulation and supervision of the banking sector in the KSA. SAMA is empowered by the Banking Control Law (BCL) 1966 and the SAMA Charter 1957 to issue banking regulations, rules and guidance to licensed banks in the KSA. The Basel NSFR standard was implemented via the issuance of circulars (see Annex 2) and has been in effect from 1 January 2016 (NSFR minimum requirement) and 1 January 2018 (NSFR disclosure requirements).

The NSFR minimum requirement was first introduced through Circular #3610000036260 (29 December 2014) to be applicable as of 1 January 2018. Subsequently, SAMA issued Circular #361000141528 (26 August 2015), which provided for the earlier introduction of the NSFR as a binding minimum requirement by 1 January 2016. Final revisions to the NSFR standard entered into force on 8 February 2018 through Circular #391000059160, reflecting SAMA's decision not to exercise the national discretion to lower the Required Stable Funding requirement (RSF) factor applied to gross derivative liabilities. The NSFR disclosure requirements were introduced through Circular #361000130698 (28 July 2015) and completed with Circular #381000088967 (18 May 2017) by implementing the consolidated and enhanced Pillar 3 disclosure requirements published by the Basel Committee in March 2017. SAMA updated the KSA NSFR regulation during the RCAP review through Circular #6041/41 dated June 2018. SAMA publishes the regulation in English with a cover letter in Arabic, which ensures the enforceability of the regulation per local requirements.

1.2 Regulatory system

In the KSA, all locally incorporated banks are subject to the local implementation of the Basel III NSFR standard. SAMA is responsible for issuing and enforcing the NSFR regulation in the KSA. The circular and guidance on NSFR issued by SAMA include a data collection template with the information required from each bank to calculate the NSFR. The submitted NSFR and accompanying data are reported to and reviewed by SAMA on a quarterly basis. If the NSFR regulation is breached, SAMA has powers to impose corrective measures and penalties, as detailed in the BCL.

In the area of liquidity risk, banks in the KSA also have to comply with other requirements:

- The SAMA liquidity ratio requires banks in the KSA to maintain a minimum percentage of their liquidity reserve relative to their deposit liabilities. The requirement was introduced in 1966 and is currently set at 20%.
- The loan-to-deposit ratio (LDR) requires banks not to exceed a certain percentage of loans relative to their deposit liabilities. The metric was introduced in the 1970s and is flexibly applied by SAMA, keeping in view the needs of individual banks and the banking system. The maximum requirement for this ratio increased from 60% to 85% on 1 September 2006 and from 85% to 90% in February 2016 in response to the liquidity situation in the KSA.
- The LCR requires banks to maintain a minimum amount of liquid assets to cover net cash outflows under a 30-day stress scenario. The minimum requirement was set at 60% from 1 January 2015 and will be gradually increased, reaching 100% by January 2019. As of 30 June 2018, banks in the KSA must comply with a 90% LCR requirement.

Beyond quantitative minimum requirements, SAMA introduced requirements for banks in the KSA to produce a standalone internal liquidity adequacy assessment plan (ILAAP). This document contains information on liquidity risk stress testing along with a contingency funding plan (CFP). The ILAAP is effective from 1 January 2018 based on 31 December 2017 data and projections for the year 2018.

Throughout this process, banks must provide evidence that they have robust strategies, policies, processes and systems for the identification, measurement, management and monitoring of liquidity risk.

1.3 Structure of the banking sector

Twenty-five institutions are licensed by SAMA to carry out banking functions in SAMA. Twelve of these are domestic and thirteen are foreign bank branches. Banks provide a range of core banking functions but not exotic products of the type that may be offered by global systemically important banks (G-SIBs) or in advanced economies. Most of the banking activities are focused within the KSA or in the general region. As noted in the July 2017 International Monetary Fund's Financial Sector Assessment Program report, "[KSA] banks follow a simple business model, mainly intermediating private sector deposits for lending to corporates and households. Among the latter, mortgage loans comprise only about one-fourth of the total while the remainder is consumer and credit card loans. Direct exposure to the government is limited."[2]

In assessing the materiality of deviations, the Assessment Team focused on a sample of the five largest banks in the KSA.[3] Together, these banks account for about 63% of the total assets of the banking sector and 65% of the assets of internationally active banks in the KSA (in terms of leverage ratio exposure data as of 30 September 2017). Annex 3 provides further information on the banking system in the KSA and the NSFR of the sample banks.

SAMA applies the NSFR regulation to all commercial banks and regulated entities in the KSA on a consolidated level with the exception of foreign bank branches.

1.4 Scope of the assessment

The Assessment Team considered the NSFR regulation applicable to all of the 12 locally incorporated banks in the KSA as of 30 June 2018. The assessment had two dimensions:

- A comparison of the domestic regulation with the Basel NSFR standard to ascertain that all the required provisions have been adopted (*completeness* of the regulation); and
- Whether there are any differences in substance between the domestic regulation and the Basel NSFR standard and, if so, their significance (*consistency* of the regulation).

In its assessment, the RCAP Assessment Team considered all binding documents that effectively implement the Basel NSFR standard in the KSA. Annex 2 lists the Basel requirements used as the basis for the assessment. The assessment did not evaluate the adequacy of liquidity or the resilience of the banking system in the KSA or the supervisory effectiveness of the KSA's authorities.

As set out in the RCAP methodology, the Assessment Team evaluated the materiality of identified deviations between the Basel NSFR standard and the domestic regulation. The quantification was limited to the sample of banks. In addition, the Assessment Team reviewed the non-quantifiable aspects of identified deviations and applied expert judgment as to whether the domestic regulation meets the Basel framework in letter and in spirit. The materiality analysis is summarised in Annex 4.

The Assessment Team noted that, in some areas, the KSA's rules go beyond the minimum Basel NSFR requirements. Although these elements (listed in Annex 8) provide for a more rigorous implementation of the Basel NSFR standard, they have not been taken into account for the assessment of compliance.

[2] See www.imf.org/~/media/Files/Publications/CR/2017/cr17318.ashx.

[3] National Commercial Bank, AlRajhi Bank, Riyad Bank, SAMBA and Bank Saudi Fransi.

The outcome of the assessment is summarised using a four-grade scale, both at the level of each of the four key components of the Basel NSFR standard and the overall assessment of compliance. The four grades are compliant, largely compliant, materially non-compliant and non-compliant.

2 Assessment findings

2.1 Assessment grades and summary of findings

Overall, the Assessment Team finds the implementation of the NSFR in the KSA to be compliant with the Basel standard. This grade is based on the materiality assessment (summarised in Annex 4) and takes into account the rectifications issued by SAMA in June 2018, as described in Annex 5.

Assessment grades

Table 1

Component of the Basel NSFR standard	Grade
Overall grade	C
Scope, minimum requirement and application issues	C
Available Stable Funding (numerator)	C
Required Stable Funding (denominator)	C
NSFR disclosure requirements	C

Assessment scale: C (compliant), LC (largely compliant), MNC (materially non-compliant) and NC (non-compliant).

2.1.1 Scope, minimum requirement and application issues

The SAMA regulation on the scope, minimum requirement and applications issues is compliant with the Basel standard.

The Assessment Team did not find any differences between the KSA NSFR regulation and the Basel NSFR standard with regard to the scope, minimum requirements and application issues.

The Basel NSFR framework is applicable to all internationally active banks on a consolidated basis. SAMA applies the standard to all commercial banks and regulated entities in the KSA on a consolidated level with the exception of foreign bank branches. Currently, 12 locally incorporated banks and 13 foreign branches are registered in the KSA.

SAMA implemented the NSFR as a minimum standard as of 1 January 2016, which is two years ahead of the implementation date stipulated in the Basel standard. The early implementation was due to the positive experience with the NSFR during the monitoring period between 2012 and 2015, with reported banks' ratios being well above 100%. Furthermore, SAMA chose an earlier introduction of the NSFR as it was considering additional metrics within the existing SAMA monetary policy toolbox.

2.1.2 Available Stable Funding (numerator)

The SAMA definition of Available Stable Funding (ASF) is compliant with the Basel standard.

The Assessment Team did not find any differences between the KSA NSFR regulation and the Basel NSFR standard with regard to the definition of Available Stable Funding.

2.1.3 Required Stable Funding (denominator)

The SAMA definition of Required Stable Funding is compliant with the Basel standard.

The KSA RCAP-LCR assessment notes that KSA government debt securities and other domestic Level 1-type claims are recognised by SAMA as high-quality liquid assets (HQLA) for the calculation of the LCR, even though these assets are not traded in liquid and active private markets as required under paragraph 50(c)of the Basel LCR standard. Since the definitions used in the NSFR regulations generally mirror those outlined in the LCR regulations, this finding applies for the RCAP-NSFR assessment as well. This finding is non-material.

2.1.4 Disclosure requirements

The SAMA disclosure requirements are compliant with the Basel standard.

The Assessment Team did not find any differences between the KSA NSFR regulation and the Basel NSFR standard with regard to the disclosure requirements.

SAMA has implemented all the Basel NSFR disclosure requirements (2015) as well as the subsequent consolidated Basel framework on Pillar 3 disclosure requirements (2017) via the issuance of circulars. As such, banks in the KSA are required to disclose the NSFR at a consolidated level and at the same frequency, and concurrently with, the publication of financial statements.

2.2 Detailed assessment findings

2.2.1 Scope, minimum requirement and application issues

This component is judged to be compliant with the Basel framework. No findings were identified.

2.2.2 Available Stable Funding

This component is judged to be compliant with the Basel framework. No findings were identified.

2.2.3 Required Stable Funding

Section grade	Compliant
Basel paragraph number	Paragraphs 27 and 37 of the Basel NSFR standards
Reference in the domestic regulation	SAMA's *Guidance Document Concerning Basel III: The Net Stable Funding Ratio (NSFR)* – Based on BCBS document of October 2014: Section 5, page 7, General Guidance Part B, Definition of Required Stable Funding for assets and off-balance sheet exposures and Section 7, page 12, Specific Guidance Notes-Assets, Assets assigned a 5% Required Stable Funding (RSF) factor.
Finding	In accordance with paragraph 50(c) of the Basel LCR standard, marketable securities assigned a 0% risk-weight may be classified as Level 1 HQLA without any restriction, although only where these securities are, among others, traded in large, deep and active repo or cash markets characterised by a low level of concentration. As reported in the KSA RCAP-LCR, SAMA has made repo-ability with the central bank a sufficient requirement to satisfy the "large, deep and active market" condition in the LCR. As a consequence, KSA government debt securities (and other local Level 1-type assets) are accepted as Level 1 HQLA for the purpose of the LCR despite the absence of a large, deep and active private market for those securities. This finding was noted as a material deviation from the Basel standard in the KSA RCAP-LCR. The Basel NSFR standard states that the definitions for Level 1 HQLA must mirror those from the LCR standard though without regard to the LCR operational requirements and without consideration of the caps on Level 2 and Level 2B assets that may otherwise limit the ability of some HQLA to be included as eligible HQLA in the LCR. While the KSA's NSFR rules do not differ from the Basel NSFR standard with regard to the treatment of Level 1 HQLA, a relevant deviation from the local LCR regulation also affects the NSFR. As such, the Assessment Team notes that the deviation in the KSA's LCR rules applies in the context of the RCAP-NSFR as well.

	The finding is currently not material. KSA government debt securities are rated as A and therefore qualify as Level 1 HQLA under the KSA's equivalent of paragraph 50(d) of the Basel LCR standard, which, however, does not require the securities to be traded in large, deep and active private markets. Nevertheless, there is a certain probability of KSA government debt securities (and other local Level 1-type assets) being upgraded to a 0% risk weight within the next three years. Consequently, paragraph 50(c) of the Basel LCR standard would become applicable and KSA government debt securities (and other local Level 1-type assets) would no longer be eligible as Level 1 HQLA under the Basel LCR and NSFR standard, whereas those assets would still be treated as Level 1 HQLA under local rules. This deviation would then also be relevant for the NSFR, where those assets would be subject to different (lower) Required Stable Funding factors under the SAMA NSFR regulation than the Basel NSFR standard. The expected impact of KSA government debt securities and other local Level 1-type assets being upgraded to a 0% risk weight would be a 1.5 percentage points decrease in the weighted average NSFR of the sample of banks provided. The expected impact for the most affected bank would be a 2.5 percent point decrease in the NSFR. This takes into consideration the likelihood of such an event and assumes the application of the Basel NSFR standard. Since 2014, SAMA and other KSA governmental entities have undertaken concrete actions to create an active and deep market for government debt securities as well as for other financial instruments. Among others, these include the listing of government debt on Tadawal (the Saudi Arabian stock exchange) and the establishment of a debt management office that will provide opportunities to banks and investment firms to underwrite future debt issuances. This may establish conditions that are adequate to meet the general requirements provided in paragraph 50(c) of the Basel LCR standard for the use of local government bonds and other local Level 1-type assets to be classified as Level 1 assets in the LCR (and the NSFR). Considering both of these forward-looking assessments of potential materiality, the assessment team concludes that the finding is non-material.
Materiality	Not material

2.2.4 Disclosure requirements

This component is judged to be compliant with the Basel framework. No findings were identified.

Annexes

Annex 1: RCAP Assessment Team and Review Team

Assessment Team Leader

Mr Olaf Sleijpen	Netherlands Bank

Assessment Team members

Mr Alberto Munguía Cisneros	National Banking and Securities Commission of Mexico
Mr Maximilian Dinse	European Central Bank – Banking Supervision
Mr Enrico Hariantoro	Financial Services Authority of Indonesia
Mr Mahmut Kutlukaya	Banking Regulation and Supervision Agency of Turkey

Supporting members

Mr Marijn de Jong	Netherlands Bank
Ms Louise Eggett	Basel Committee Secretariat
Mr Mark Pocock	Basel Committee Secretariat
Mr Olivier Prato	Basel Committee Secretariat

Review Team members

Mr Toshio Tsuiki	Basel Committee Secretariat
Mr Saurav Sinha	Reserve Bank of India
Ms Joanne Marsden	Office of the Superintendent of Financial Institutions, Canada
Ms Camilla Hellgren	Financial Supervisory Authority, Sweden

Annex 2: List of Basel standards and implementing regulations issued by SAMA

The following Basel standards were used as the basis of this RCAP assessment:

- *Basel III: the Net Stable Funding Ratio*, October 2014
- *Pillar 3 disclosure requirements – consolidated and enhanced framework*, March 2017
- *Implementation of the Net Stable Funding Ratio and treatment of derivative liabilities*, October 2017
- *Basel III – The Net Stable Funding Ratio: frequently asked questions*, February 2018

Table A.1 lists the regulations issued by SAMA to implement the NSFR. Previous RCAP assessments of SAMA's implementation of the Basel standards considered the binding nature of regulatory documents in the KSA.[4] This RCAP Assessment Team did not repeat that assessment, but instead relied on the previous assessment's findings. Those assessments concluded that the types of instrument described in Table A.1 could be considered as binding on banks and supervisors for the purposes of an RCAP assessment.

Overview of relevant liquidity regulations in the KSA — Table A.1

Domestic regulations	Type, version and date
Banking Ordinance (BO)	(1) Liquid assets to be maintained by Banks at SAMA under the provisions of BCL Article #7 (law issued in 1966). (2) SAMA's Regulatory Requirement concerning the loan-to-deposit ratio was introduced in the 1970s. SAMA ensures that banks maintain a loan-to-deposit ratio of less than 90%.
Banking (Liquidity) Rules (BLR) with regard to the implementation of the NSFR in the KSA	(1) Circular #3610000036260 introducing NSFR standards with the NSFR to be introduced as minimum requirement by 1 January 2018 (circular published on 29 December 2014). (2) Circular #361000130698 introducing NSFR disclosure requirements to be effective by 1 January 2018 (circular published on 28 July 2015). (3) Circular #361000141528 providing for earlier introduction of NSFR as minimum requirement by 1 January 2016 (circular published on 26 August 2015). (4) Circular #381000079331 passing on NSFR FAQs published by the Basel Committee in February 2017 (circular published on 24 April 2017). (5) Circular #381000088967 passing on the entire consolidated Pillar 3 framework published by the Basel Committee in March 2017 (circular published on 18 May 2017). (6) Circular #391000059160, which reflects SAMA's decision regarding national discretion to lower the RSF factor applied to gross derivative liabilities (circular published on 8 February 2018). (7) Circular #6041/41 which has updates from the RCAP exercise (published June 2018)[5]

Source: SAMA.

[4] Annex 3 of the BCBS RCAP-LCR report for the Kingdom of Saudi Arabia, www.bis.org/bcbs/publ/d390.pdf.

[5] See www.sama.gov.sa/en-US/Laws/BankingRules/Guidance%20Document%20Concerning%20BASEL%20III%20THE%20NET%20STABLE%20FUNDING%20RATIO%20(NSFR)%20-%20Based%20on%20BCBS%20Document%20of%20October%202014.pdf.

Annex 3: Key liquidity indicators of the KSA's banking system

Overview of KSA banking sector liquidity as of September 2017

Table A.2

Size of banking sector (SAR, millions)		
Total exposures of all banks operating in KSA (including off-balance sheet exposures)	2,601,960	
Total assets of all locally incorporated internationally active banks	2,524,269	
Total assets of locally incorporated banks to which liquidity standards under the Basel framework are applied	2,524,269	
Number of banks		
Number of banks operating in the KSA (excl. local representative offices)[a]	26	
Number of global systemically important banks (G-SIBs)	0	
Number of domestically systemically important banks (D-SIBs)	6	
Number of banks which are internationally active	12	
Number of banks required to implement Basel III liquidity standards	12	
Number of banks required to implement domestic liquidity standards[a]	26	
Breakdown of NSFR for KSA RCAP sample banks (SAR, millions)[b]	**Unweighted**	**Weighted**
Capital	249,070	249,070
Stable deposits from retail and small business customers	0	0
Less stable deposits from retail and small business customers	684,425	616,113
Unsecured funding from non-financial corporates	250,072	125,036
Unsecured funding from central banks, sovereigns, PSEs, MDBs and NDBs	60,432	30,216
Unsecured funding from financials (other legal entities)	30,724	2,428
Secured funding (all counterparties)	26,713	0
Other liabilities	119,552	48,259
Total Available Stable Funding	1,420,989	1,071,123
Cash and central bank reserves	120,014	0
Loans to financial institutions	31,224	8,786
Securities eligible as Level 1 HQLA	193,222	13,256
Securities eligible as Level 2A HQLA	27,064	4,060
Securities eligible as Level 2B HQLA	0	0
All residential mortgages	0	0
Loans, <1 year	407,559	201,432
Other loans, >1 year, risk weight<=35%	0	0
Loans, risk weight>35%	278,529	233,611
Derivatives	1,634	1,634
All other assets	372,673	368,097
Off-balance sheet	499,829	1,703
Total Required Stable Funding	1,931,748	832,579
NSFR		128%

Source: SAMA. Notes: [a] One foreign branch ceased operations before early 2018. [b] The totals may contain rounding differences.

Annex 4: Materiality assessment

The outcome of the RCAP assessment is based on the materiality of the findings described in Section 2.2 and summarised in Table A.3. Assessment Teams evaluate the materiality of findings quantitatively where possible, or using expert judgment when the impact cannot be quantified.

The materiality assessment for quantifiable gaps is based on the cumulative impact of the identified deviations on the reported NSFR of banks in the RCAP sample. These banks are listed in Table A.4.

Number of deviations by component

Table A.3

Component	Not material	Potentially material	Material
Scope, minimum requirement and application issues	0	0	0
Available Stable Funding (numerator)	0	0	0
Required Stable Funding (denominator)	1	0	0
NSFR disclosure requirements	0	0	0

RCAP sample banks

Table A.4

Banking group	Share of banks' assets in the total assets of the KSA banking system (per cent)
Bank 1	18.91%
Bank 2	13.41%
Bank 3	10.95%
Bank 4	10.10%
Bank 5	9.34%
Total	62.71%

Source: SAMA. For this purpose, banking assets are based on the measure of total exposures used in the leverage ratio, which includes both on- and off-balance sheet exposures. Per confidentiality requirements of SAMA, bank names are not provided.

The Assessment Team assessed the impact of the finding regarding the definition of Level 1 HQLA to be non-material as of the cutoff date, 30 June 2018. KSA government debt securities are rated as A and therefore qualify as Level 1 HQLA under the KSA's equivalent of paragraph 50(d) of the Basel LCR standard, which does not require the securities to be traded in large, deep and active private markets. Nevertheless, there is a certain probability of KSA government debt securities (and other local Level 1-type assets) being upgraded to a 0% risk weight within the next three years. As a consequence, paragraph 50(c) of the Basel LCR standard would become applicable and KSA government debt securities (and other local Level 1-type assets) would no longer be eligible as Level 1 HQLA under the Basel LCR and NSFR standard, whereas those assets would still be treated as Level 1 HQLA under local rules. This deviation would then also be relevant for the NSFR, where those assets would be subject to different Required Stable Funding factors under the SAMA NSFR regulation than the Basel NSFR standard.

Currently, KSA government debt securities comprise 62.2% of all Level 1 HQLA. Assuming an upgrade of the KSA's credit rating, those assets would be treated as non-HQLA securities for the purpose of the NSFR. The expected impact of the deviation (by also taking into consideration the likelihood of an upgrade of the KSA's credit rating) would be a 1.5 percentage point decrease in the weighted average

NSFR of the sample of banks provided, and the expected impact for the most affected bank would be a 2.5 percent points decrease in the NSFR.[6]

Since 2014, SAMA and other KSA governmental entities have undertaken concrete actions to create an active and deep market for government debt securities and other financial instruments. SAMA has also created the financial infrastructure necessary for the success of this project. SAMA expects the results of the initiatives to develop within the next three to five years. In the opinion of the Assessment Team, this may establish conditions that are adequate to meet the general requirements set out in paragraph 50(c) of the Basel LCR standards for the use of local government bonds and other local Level 1-type assets to be classified as Level 1 HQLA in the LCR (and the NSFR).

Considering both of these forward-looking assessments of potential materiality, the Assessment Team concludes that the finding is non-material.

[6] The assessment of the potential materiality of the deviation of the SAMA NSFR rules was estimated as the *Expected impact = Impact of scenario x Probability of scenario.* Regarding the impact of the scenario, it is assumed that KSA government debt securities (and other local Level 1-type assets) will become eligible for a 0% risk weight. As a consequence, and assuming the application of the Basel NSFR standard, those securities would no longer be eligible as Level 1 HQLA under the Basel LCR and NSFR standard and would have to be treated as non-liquid securities (being subject to higher stable funding requirements in the NSFR). The impact of this scenario would be a 12.9% decrease in the weighted average NSFR for the sample of banks provided and a 22.3% decrease in the NSFR of the most affected bank. Regarding the probability of the scenario, the likelihood of the scenario is based on the transition rates of the 2016 Annual Sovereign Default Study and Rating Transitions of S&P that estimates an average three-year transition rate from a grade of A to AA and AAA of 11.2%. Lastly, the expected impact for the entire sample of banks is 12.9% x 11.2%= 1.5% and for the most affected bank is 22.3% x 11.2% = 2.5%.

Annex 5: Rectifications made by SAMA

List of rectifications by SAMA — Table A.5

Basel paragraph	Reference in KSAS regulations	Description of the rectification
Various	Various	Updated references to SAMA regulations instead of Basel standards, thereby explicitly covering the specific provisions and national discretions as adopted in the local rules.

Source: SAMA.

Annex 6: Areas for further guidance from the Basel Committee

The Assessment Team listed the following issue for further guidance from the Basel Committee.

Required Stable Funding: Active market for securities under LCR paragraph 50(c)

The Assessment Team believes it would be helpful to review paragraph 50(c) of the Basel LCR standard and to re-assess whether it is appropriate or not to exclude from the LCR liquidity buffer (domestic) securities that are assigned a 0% risk weight but that are not traded on large, deep, active and liquid markets. This issue was also raised in the KSA RCAP-LCR as an area for further guidance from the Basel Committee.[7]

In accordance with paragraph 50(c) of the Basel LCR standard, marketable securities assigned a 0% risk-weight may be classified as Level 1 assets without any restriction, although only where these securities are, among others, traded in large, deep and active repo or cash markets. If these conditions are not fulfilled, the asset is not eligible as a Level 1 asset for the LCR liquidity buffer.

However, such a qualitative requirement is not provided for assets referred to under paragraphs 50(d) and (e), which include sovereign and central bank debt securities (either issued in domestic or foreign currency) where the sovereign is not assigned a 0% risk-weight. Those assets can also be included without any restriction if they comprise domestic securities issued by the sovereign or central bank in the bank's home country. Other non-domestic sovereign or central bank debt securities (issued in domestic or foreign currency) not assigned a 0% risk-weight may only be included as Level 1 assets up to the amount of net cash outflows in the relevant jurisdiction and in that currency.

Therefore, domestic marketable securities representing claims by sovereigns or central banks in the bank's home country that are assigned a 0% risk-weight referred to under paragraph 50(c) for which there is no active market are not eligible for the LCR liquidity buffer, whereas they would become eligible as per paragraph 50(d) if the sovereign were to lose its eligibility for a 0% risk weight (eg as a consequence of a rating downgrade).

[7] See RCAP-Saudi Arabia, LCR, page 34, www.bis.org/bcbs/publ/d336.pdf.

Annex 7: Issues for follow-up RCAP assessments

The Assessment Team identified the following issue for follow-up.

Required Stable Funding (denominator)

The Assessment Team recommends a follow-up on the Required Stable Funding finding. Currently, the KSA government debt securities are internationally rated as A and are therefore not subject to a 0% risk weight under the Basel II standardised approach for credit risk and the finding is non-material.[8] However, the finding may become material if the KSA's rating is upgraded. Progress in the planned strengthening of the market for government debt securities should also be taken into account.

8 The KSA's long-term foreign and local currency issuer default ratings (April 2018): A1 (Moody's); A+ (Fitch); A– (S&P).

Annex 8: Areas where the KSA's rules are stricter than the Basel standard

In some areas, SAMA has adopted a stricter approach than the minimum standards prescribed by the Basel Committee. These are listed below for information. The stricter rules have not been taken into account as mitigants for the overall or component-level assessment of compliance.

- SAMA introduced the NSFR as a binding minimum standard as of 1 January 2016, two years ahead of the implementation date provided in the Basel standard.
- SAMA does not permit the use of Level 2B assets for the purpose of the LCR. As such, for the NSFR, those assets are treated as non-liquid securities subject to a stable funding requirement of 50% for assets with a residual maturity or encumbrance period of less than one year or 85% for all other assets.

Annex 9: Elements of the NSFR subject to national discretion

Implementation of national discretions by SAMA — Table A.6

Basel paragraph	Description	National implementation
36	RSF factor for required central bank reserves	Application of a 0% Required Stable Funding factor
47	RSF factors for other contingent funding obligations[9]	Application of a 0% Required Stable Funding factor

Source: SAMA.

9 Excluding irrevocable and conditionally revocable credit and liquidity facilities (to any client) for which SAMA applies a 5% stable funding requirement in line with paragraph 47 of the Basel NSFR standard.