145 LIQUIDITY RISK MANAGEMENT

Policy statement. The Bangko Sentral is cognizant that the viability of financial institutions, particularly banks, is heavily influenced by their ability to manage liquidity, including intraday liquidity positions. Opportunities to expand lending activities, continuous innovations in investment and funding products, growth in off-balance sheet activities, and intense competition for retail and wholesale funds affect the way banks operate. Thus, banks are expected to fully understand, measure, and control the resulting liquidity risk from their operations.

The guidelines in *Appendix 71* shall be used to determine the adequacy and effectiveness of a bank’s liquidity risk management process. The sophistication of the liquidity risk management system shall depend on the size, nature and complexity of a bank’s activities. However, regardless of its size and complexity, a bank must be able to identify, measure, monitor, and control its exposures to liquidity risk in a timely and comprehensive manner, and maintain a structurally sound funding and liquidity profile. Banks shall likewise hold liquidity in accordance with the minimum prudential requirements set by the Bangko Sentral.

Liquidity Coverage Ratio (LCR)

To promote the short-term resilience of the liquidity risk profile of a bank, it shall maintain an adequate stock of unencumbered high-quality liquid assets (HQLAs) that consists of cash or assets that can be converted into cash at little or no loss of value in private markets, to meet its liquidity needs under stressed conditions. The stock of liquid assets should enable the bank to withstand significant liquidity shocks for at least thirty (30) calendar days, which would give time for corrective actions to be taken by the bank management and/or the Bangko Sentral.

The LCR framework shall apply to all UBs/KBs[1] and their subsidiary banks and QBs on both solo (head office plus branches/other offices) and consolidated (parent bank plus subsidiary financial allied undertakings, but excluding insurance companies) bases.

a. *Minimum requirement.* The LCR is the ratio of HQLAs to total net cash outflows. Under a normal situation, the value of the ratio shall not be lower than 100% on an ongoing basis. While the LCR is expected to be met in a single currency (i.e., in peso equivalent terms of all currencies), 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. The detailed LCR framework is provided in *Part 1 of Appendix 72*.

b. *Reporting and monitoring requirements* – Covered banks shall comply with the minimum LCR requirement on a daily basis, and shall have appropriate systems in place to ensure the same.

For reporting purposes, covered banks shall submit a report in accordance with *Appendix 7*.

The LCR Reports shall be accompanied by a certification under oath to the effect that the bank has fully complied with the LCR requirement on all calendar days of the reference period in the form provided under *Appendix 73*. The solo and consolidated LCR Reports, together with the Sworn Certification shall be classified as *Category A-1* reports.

While there is no minimum threshold for LCRs in each significant currency, covered banks shall report the significant currency LCR to the Bangko Sentral for monitoring purposes using the same LCR Report template as of the LCR measurement date. The significant currency LCR shall be reported in the original currency. A currency is considered "*significant*" if the aggregate liabilities denominated in that currency amount to five percent (5%) or more of the banks' total liabilities as of the measurement date.

The submission of the LCR report shall be subject to the governance process on the quality of bank reporting under Sec. 171. Any non-compliance with the reporting standards, or non-submission or delayed submission of the LCR report and the report on significant currency LCRs shall be subject to the monetary and non-monetary sanctions provided under Sec. 171 (*Sanctions on reports for non-compliance with the reporting standards*).

c. *Implementation*. The implementation of the minimum LCR shall be phased in to help ensure that the banks concerned can meet the standard through reasonable measures without disrupting credit extension and financial market activities. In order to facilitate compliance, banks shall undergo an observation period before the LCR becomes a minimum requirement. The timelines are set out in the table below:

<table>
<tr><th></th><th>Observation Period</th><th colspan="2">Minimum LCR</th></tr>
<tr><td>UBs/KBs</td><td>01 July 2016 –
31 December 2017</td><td>01 January 2018 and
thereafter – 90%</td><td rowspan="2">01 January 2019 &
thereafter – 100%</td></tr>
<tr><td>Subsidiary Banks and
QBs
of UBs/KBs</td><td>Until 31 December 2018</td><td></td></tr>
</table>

Requirements during the observation period. For monitoring purposes, banks concerned shall submit the LCR Reports quarterly in single currency and per significant currency, on both solo and consolidated bases following the submission deadlines for consolidated reports set out in Item *"b"*. Any non-submission or delayed submission of the LCR Report during the observation period shall be subject to the monetary and non-monetary sanctions provided under Sec. 171 (*Sanctions on reports for non-compliance with the reporting standards*).

During the observation period, the Bangko Sentral is not precluded from assessing the covered bank's compliance with the LCR requirement. Banks with LCRs that are already at or near the prescribed minimum should not view the transition period as an opportunity to reduce their liquidity coverage. Where a subsidiary bank/QB of a UB/KB is unable to meet the minimum LCR for two (2) consecutive weeks during the observation period, the bank shall immediately adopt a board-approved liquidity build-up plan. The plan should clearly articulate the bank's defined strategies and timelines for meeting the required LCR by 1 January 2019, and should include estimates of the liquidity ratio at every quarter prior to the effectivity date. The build-up plan shall be submitted to the appropriate supervising department of the Bangko Sentral, within ten (10) banking days after it is approved by the board. The appropriate supervising department of the Bangko Sentral will evaluate the continuing compliance of the bank with the said plan. In case of non-compliance, the Bangko Sentral may require the covered bank to undertake a set of actions. The Bangko Sentral may likewise impose enforcement actions as provided under this Section.

LCR disclosure requirements. To improve the transparency of the regulatory liquidity requirement, enhance market discipline, and reduce uncertainty in the market, covered banks shall publicly disclose information related to the LCR on solo and consolidated bases as prescribed under *Part II of Appendix 72* starting year 2019. The mandatory disclosure requirements in single currency should be published in the quarterly published balance sheet, as well as in the annual reports or published financial reports (e.g., the audited financial statements).

Minimum Liquidity Ratio (MLR) for Stand-Alone TBs, RBs and Coop Banks. To promote short-term resilience to liquidity shocks, banks shall maintain a stock of liquid assets proportionate to their on- and off-balance sheet liabilities. The prudential MLR requirement applies to all TBs, RBs and Coop Banks and QBs that are not subsidiaries of UBs/KBs.

a. *Minimum requirement* – A prudential MLR of twenty percent (20%) shall apply to banks on an ongoing basis absent a period of financial stress. The liquidity ratio is expressed as a percentage of a bank's eligible stock of liquid assets to its total qualifying liabilities.

(1) The stock of liquid assets shall consist of:

(a) Cash on hand;
(b) Reserves in the Bangko Sentral;
(c) Overnight and term deposits[2] with the Bangko Sentral, including reverse repos where the Bangko Sentral is the counterparty;
(d) Eligible debt securities representing claims on or guaranteed by-

(i) The Philippine national government (NG) and the Bangko Sentral; or

(ii) Sovereigns, central banks of foreign countries, or by multilateral organizations that are assigned a zero percent risk weight under *Part III of Appendix 62*; and

(e) Deposits in other banks:

Provided, That the amounts to be included in the stock of liquid assets are immediately liquefiable and free from encumbrances.

(2) The qualifying liabilities shall consist of the following:

(a) Total liabilities; and
(b) Irrevocable obligations under off-balance sheet items, such as:

(i) Guarantees issued;
(ii) Trade related guarantees;
(iii) Letters of credit; and
(iv) Other committed credit lines.

b. *Reporting and monitoring requirements.* Covered banks shall comply with the MLR on a daily basis, and shall have the appropriate systems in place to ensure the same. For reporting purposes, covered banks shall submit a monthly report on their compliance with the MLR to the appropriate supervising department of the Bangko Sentral. The report shall be submitted on solo basis in peso-equivalent terms using the prescribed form within fifteen (15) banking days after the end of the reference period, effective 1 January 2019.

The reports shall be accompanied by a certification under oath to the effect that the bank has fully complied with the MLR requirement on all calendar days of the reference period shown under *Appendix 129*. In cases when the MLR is not met but the same do not warrant the submission of a notification to the Bangko Sentral under Item *"b"* of this Section (*Supervisory framework for the minimum prudential liquidity requirements*), the specific date of the occurrence of the shortfall/s shall likewise be indicated in the certification. These reports shall be considered as *Category A-1* reports.

In addition, banks shall use the MLR template to internally measure and monitor their compliance with the prudential requirement for each currency in which they have significant activities. For this purpose, a currency is considered significant if the aggregate liabilities denominated in that currency amount to five percent (5%) or more of the total liabilities as of the MLR measurement date. Banks are expected to be able to meet their liquidity needs in each currency and maintain a stock of eligible liquid assets consistent with the distribution of their liquidity needs by currency to ensure that risks arising from currency mismatch are properly mitigated.

The submission of the MLR report shall be subject to the governance process on the quality of bank reporting under *Sec. 171*. Any non-compliance with the reporting standards, or non-submission or delayed submission of the MLR report and the report on significant currency MLRs shall be subject to the monetary and non-monetary sanctions provided under Sec. 171 (*Sanctions on reports for non-compliance with the reporting standards*).

c. *Implementation*. In order to facilitate compliance with the MLR, stand-alone TBs, RBs, Coop Banks and QBs shall undergo a one-year observation period beginning 1 January 2018 until the MLR takes effect on 1 January 2019.

Requirements during the observation period. During this period, banks shall submit the MLR report quarterly on a solo basis to the appropriate supervising department of the Bangko Sentral. Each quarterly submission shall consist of the MLR reports for each month-end within a reference quarter. The report shall be submitted within thirty (30) banking days after the end of each reference quarter. For example, a bank's submission for the reference period covering 1 January to 31 March 2018 shall consist of the MLR on solo basis as of end-January, end-February and end-March. The report shall be submitted within thirty (30) banking days after end-March 2018.

The Bangko Sentral is not precluded from assessing a bank's compliance with the MLR during the observation period. Banks with liquidity ratios that are already at or near the prescribed minimum should not view the transition period as an opportunity to reduce their liquidity coverage. Where a bank is unable to meet the MLR for two (2) consecutive weeks during the observation period, the bank shall immediately adopt a board-approved liquidity build-up plan. The plan should clearly articulate the bank's defined strategies and timelines for meeting the required MLR by 1 January 2019, and should include estimates of the liquidity ratio at every quarter prior to the effectivity date. The build-up plan shall be submitted to the appropriate supervising department of the Bangko Sentral, within ten (10) banking days after it is approved by the board. The appropriate supervising department of the Bangko Sentral will evaluate the continuing compliance of the bank with the said plan. In case of non-compliance, the Bangko Sentral may require the covered bank to undertake a set of actions. The Bangko Sentral may likewise impose enforcement actions as provided under this Sec. 145.

MLR disclosure requirements. A bank shall disclose its MLR on a solo basis in its annual report or audited financial statement (AFS), as well as in the quarterly Published Balance Sheet (PBS) starting year 2019.

Net Stable Funding Ratio (NSFR). To promote long-term resilience of a bank against liquidity risk, it shall maintain a stable funding profile in relation to the composition of its assets and off-balance sheet activities. The NSFR seeks to meet this objective by limiting overreliance on short-term wholesale funding and promoting enhanced assessment of funding risk across all on- and off-balance sheet accounts. The NSFR complements the LCR, which promotes short term resilience of a bank's liquidity profile.

The NSFR framework shall apply to all UBs/KBs and their subsidiary banks and QBs hereinafter referred to as "covered banks", on both solo (head office plus branches) and consolidated (parent bank plus subsidiary financial allied undertakings, but excluding insurance companies) bases.

a. *Minimum requirement.* The NSFR is the ratio of a covered bank's available stable funding (ASF) to its required stable funding (RSF), as shown below:

$$\text{Basel III NSFR (0\%)} = \frac{\text{Available stable funding (ASF)}}{\text{Required stable funding (RSF)}}$$

The covered bank shall maintain an NSFR of at least 100% at all times.

The NSFR shall be computed and reported in a single currency, i.e., in peso equivalent terms of all currencies. Notwithstanding this requirement, a covered bank shall internally measure and monitor NSFR per significant currency. A currency is considered *significant* if the aggregate liabilities denominated in that currency amount to five percent (5%) or more of the covered banks' total liabilities as of NSFR measurement date. The guidelines implementing the NSFR are provided in *Appendix 130*.

b. *Reporting and monitoring requirements*. Covered banks shall comply with the minimum NSFR on a daily basis, and shall have appropriate systems in place to ensure the same. For reporting purposes, the covered banks shall submit a report of their NSFR to the Bangko Sentral in accordance with *Appendix 7*.

The NSFR reports shall be accompanied by a certification under oath to the effect that a covered bank has fully complied with the NSFR requirement on all calendar days of the reference period in the form provided under *Appendix 131*. This requirement shall take effect on 1 January 2019. The solo and consolidated NSFR reports, together with the Sworn Certification, shall be classified as *Category A-1* reports.

The submission of the NSFR report shall be subject to the governance process on the quality of bank reporting under *Sec. 171*. Any non-compliance with the reporting standards, or non-submission or delayed submission of the NSFR report shall be subject to the monetary and non-monetary sanctions provided under Sec. 171 (*Sanctions on reports for non-compliance with the reporting standards*).

c. *Implementation*. The implementation of the minimum NSFR shall be phased in to help ensure that the covered banks can meet the standard through reasonable measures without disrupting credit extension and financial market activities. In order to facilitate compliance, covered banks, shall undergo an observation period before the minimum NSFR becomes a requirement. The timelines are set out in the table below:

	Timelines
Observation period	01 July 2018 – 31 December 2018
Actual implementation	01 January 2019 and thereafter – 100%

Requirements during the observation period. Consistent with the expectations set out on the governance process for an effective reporting system, the Board and Senior Management shall ensure the generation of complete, accurate, consistent, and reliable reports that are timely submitted to the Bangko Sentral. For monitoring purposes, covered banks shall submit the solo and consolidated NSFR Reprts in accordance with the following timelines.

	Reporting Details
Frequency	Quarterly
Measurement Date	End-of-quarter
Submission Deadlines	30 banking days from measurement date

Any non-submission or delayed submission of the NSFR Reports during the observation period shall be subject to monetary and non-monetary sanctions provided under Sec. 171 (*Sanctions on reports for non-compliance with the reporting standards*).

During the observation period, the Bangko Sentral is not precluded from assessing the covered bank's compliance with the NSFR requirement. The covered banks with NSFRs that are already at or near the prescribed minimum should not view the transition period as an opportunity to reduce their stable funding profile. Where a covered bank is unable to meet the minimum NSFR for two (2) consecutive weeks during the observation period, the covered bank shall immediately adopt a board-approved stable funding build-up plan. The plan should clearly articulate the covered bank's defined strategies and timelines for meeting the required NSFR by 01 January 2019, and should include estimates of the NSFR at every quarter prior to the effectivity date. In modifying its stable funding profile, the covered bank should ensure that all other minimum liquidity requirements shall be complied with. The build-up plan shall be submitted to the Bangko Sentral through the appropriate supervisory department, within ten (10) banking days after it is approved by the board. The appropriate supervisory department concerned will evaluate the continuing compliance of the covered bank with the said plan. In case of non-submission of, or non-compliance with, the said build-up plan, the Bangko Sentral may require the covered bank to undertake a set of actions. The Bangko Sentral may likewise impose enforcement actions as provided under this Section (*Supervisory enforcement actions*).

Supervisory framework for the minimum prudential liquidity requirements.

a. General Provisions

(1) While the minimum prudential liquidity requirements establish common parameters for stress testing, they should be viewed as minimum supervisory requirements. Covered banks are expected to conduct their own stress tests in accordance with *Part IX of Appendix 71* as part of their liquidity risk management process in order to identify the risk drivers that may lead to drastic fluctuations in their liquidity positions. Accordingly, banks should be able to assess the level of liquidity they should hold, which could possibly go beyond the regulatory minimum.

Where the Bangko Sentral is not satisfied with the adequacy of a bank's liquidity management framework or where it has particular concerns about a bank's liquidity exposures, it may require the bank to comply with a higher liquidity requirement.

(2) It shall be the responsibility of the board of directors and senior management, or the equivalent governing bodies in the case of foreign bank branches, to institute a system that would ensure compliance with the minimum liquidity requirements, the accuracy of their calculations, and the integrity of the related monitoring and reporting system. It is likewise the responsibility of senior management to report shortfalls in the minimum liquidity requirements both to their board of directors immediately and to the Bangko Sentral within the prescribed timelines.

(3) As the stock of liquid assets is intended to serve as a defense against the potential onset of liquidity stress, banks are allowed to use their stock of liquid assets as necessary during a period of financial stress in order to meet unforeseen liquidity needs, thereby causing the LCR to temporarily fall below the minimum requirement or the MLR to be breached. This may also alter the stable funding profile of banks and result in non-compliance with the required NSFR.

Under this condition, the Bangko Sentral will assess the situation to determine the extent to which the reported decline in the LCR or NSFR/non-compliance with the MLR is due to a bank-specific or market-wide shock and will accordingly provide the supervisory response necessary to address the circumstances. The action of the Bangko Sentral shall be proportionate to the drivers, magnitude, duration and frequency of the reported liquidity deficit.

In all cases, the Bangko Sentral will be cognizant of the procyclicality of supervisory actions if applied in circumstances of market-wide stress. Likewise, the Bangko Sentral will consider the potential for contagion to the financial system and the additional restricted flow of credit or reduced market liquidity due to actions to maintain a minimum LCR, NSFR or the MLR. Overall, the supervisory response will be based on a forward-looking assessment of macroeconomic and financial conditions of the financial system as a whole.

b. Liquidity ratios below the minimum

(1) In the event that a shortfall in the stock of HQLA/eligible liquid assets/available stable funding occurs on three (3) banking days within any two-week rolling calendar period, thereby causing the LCR or NSFR to fall below the minimum threshold/the MLR to be breached on such days, the bank must notify the appropriate supervising department of the Bangko Sentral, of such non-compliance within the banking day immediately following the occurrence of the third liquidity/stable funding shortfall, notwithstanding the restoration of the LCR or NSFR/compliance with the MLR on the day that the shortfall must be reported.

The shortfall notice shall be signed by the bank President or officer of equivalent rank, and by the officer charged with managing the liquidity of the bank. It shall contain the following minimum information:

(a) The dates the shortfalls occurred;
(b) The reason/s or factor/s leading to the utilization of the stock of liquid assets and non-compliance with the minimum LCR/MLR/NSFR;
(c) The action/s the bank has taken and/or will take to achieve full compliance with the minimum requirement;
(d) The expected duration and possible extent of the shortfall (although this may no longer be applicable if the LCR or NSFR has been restored/MLR has been met); and
(e) A commitment to submit its LCR/MLR/NSFR Report weekly until the bank is able to comply with the required LCR/NSFR/MLR.

A shortfall will not necessarily result in supervisory or enforcement action; at a minimum, it will entail heightened supervisory monitoring. The shortfall notice, together with the information gathered from the latest report of examination, regular prudential reports, available market information, and, if available, the internal management reports of the bank, will serve as the basis of the Bangko Sentral in making an assessment of the extent of the liquidity deficit. The Bangko Sentral will also assess whether the non-compliance with the minimum requirement is temporary, part of a regular pattern or practice, or caused by an unusual event.

(2) The Bangko Sentral will require effective and timely remedial action from the bank to address the deficiency in its liquidity position within a committed timeline under the following circumstances:

(a) The liquidity requirement is not met for a prolonged period of time or if the Bangko Sentral has determined that the bank is otherwise materially non-compliant with the minimum LCR, NSFR or the MLR; or

(b) The reported shortfall is caused by a firm-specific stress situation, i.e., based on operational issues of the bank which are part of an outstanding supervisory concern (such as imprudent management of liquidity consisting of material and/or persistent breaches of liquidity policies and limits, large funding mismatches and/or concentrations, undue reliance on high cost funds).

Subject to the approval of the Monetary Board, banks may continue to have access to the credit and liquidity facilities of the Bangko Sentral during the period that the liquidity requirement is being restored notwithstanding non-compliance with standard conditions of access to such facilities that pertain to a bank's liquidity position.

Supervisory enforcement actions. Consistent with *Sec. 002*, the Bangko Sentral may deploy enforcement actions to promote adherence with the requirements set forth in these guidelines and bring about timely corrective actions. If a bank's risk exposures are not well managed, the Bangko Sentral may direct the bank to augment its funds management practices and the level of its liquid assets, reduce its liquidity risk exposures, and/or strengthen its risk management system. The Bangko Sentral may likewise impose sanctions to limit the level of or suspend any business activity that has adverse effects on the safety or soundness of the bank, among others. Sanctions may likewise be imposed on a bank and/or its directors, officers and/or employees.

The Bangko Sentral reserves the right, upon authority of the Deputy Governor of the appropriate sector of the Bangko Sentral, to require the submission of reports and information prescribed under Item *"b"* of this Section (*LCR and MLR for Stand-Alone TBs, RBs and Coop Banks, and NSFR*) outside the regular reporting periods, and to conduct on-site inspections outside of regular or special examinations, for the purpose of ascertaining the accuracy of calculations of the minimum liquidity requirement/s as well as the integrity of the related monitoring and reporting systems.

If a bank experiences a shortfall in respect of its minimum prudential liquidity requirement and fails to restore its liquidity position within the committed timeline, the Bangko Sentral may deploy more stringent enforcement actions. In cases where a bank's liquidity problem is deemed to be exceptionally serious from the outset, or when the bank refuses to restore the required liquidity position, the Bangko Sentral may employ more drastic measures based on existing laws, rules and regulations.

(Circular Nos. 1007 dated 6 June 2018, 996 dated 8 February 2018, 981 dated 3 November 2017, and 903 dated 29 February 2016)

Footnotes

1. Including branches of foreign banks
2. To the extent allowed to be drawn down in times of stress.