African Union for Housing Finance

Stability vs. Access? BASEL III in Southern Africa

Sound Housing Finance around the World | IUHF Joint Congress
Vienna, Austria | 5-7 June 2013

Colin Chimutsa
Chairman, AUHF

African Union for Housing Finance

- Basel I and Basel II
- Towards Basel III
- Stability vs. Access?

African Union for Housing Finance

Basel I

The main objectives were to unify the playing field by introducing capital standards:

- Linking banks' capital requirements to the riskiness of its activities plus Off Balance Sheets risk exposures (risk weights).
- Coordinating the definition of capital, risk assessment and capital adequacy standards across nations.
- Increase integration of financial markets.

But, Basel I did not take account of:

- Risk diversification through portfolio formation.
- Assets maturity profile.
- Risk-mitigating techniques such as collateral.
- Degree of risk standings of individual borrowers.
- Operational and market risks.
- Strength of risk management functions of different banks.

African Union for Housing Finance

Basel II

Basel II encompasses qualitative and quantitative aspects of bank risk.

- Expected to address Basel I shortcomings
- A more comprehensive approach, placing more emphasis on banks' internal risk methodologies, supervisory review and market discipline
- Focuses more on sensitive measures of risk levels involved in a bank's positions & activities.
- More active role of bank supervision
- Harmonization of regulatory and economic approach
- Also took account of additional risk types (e.g. operational risks)

In Zimbabwe the Central Bank issued a guideline requiring banks to implement Pillar 1 by subscribing minimum options for Credit Risk as Modified Standardized Approach, Standardized Approach for Market Risk, and the Alternative Standardized approach for Operational Risk.

Benefits:

- Comprehensive vision of risks
- Higher specialization of functions
- Better allocation of capital and performance measurement
- Intensity of interrelations between units

Challenges:

- Complexity of organizational structure
- Formality of duties and responsibilities
- Lack of external credit ratings
- Needs of appropriate reporting
- Efforts on implementation

Almost 100% of financial institutions in Zimbabwe have now implemented Basel II (deadline was January 2013).

African Union for Housing Finance

Basel III

Basel 11 Ratio	Requirements	Basel 111
8%	Minimum Ratio of Total Capital/ RWAs	10.5%
2%	Minimum Ratio of Common Equity/RWAs	4.5%-7%
4%	Tier 1/ RWAs	6%
none	Capital Conservation buffer/ RWAs	2.5%
none	Leverage Ratio	3%
none	Cyclical buffer Ratio	2.5%

- Strengthens risk management
- Increased capital requirements put pressure on profitability and ROE
- Weaker banks will be crowded out; expect mergers & acquisitions
- Pricing strategies likely to be biased towards long-term arrangements

In Zimbabwe the Central Bank has taken a position to set the minimum capital adequacy ratio at 12%.

African Union for Housing Finance

Basel III: Stability vs. access?

- **Increased costs to consumers**: cost pressures from meeting liquidity requirements will be passed on

+

- **Inherent favoritism of higher value mortgages**: pressure on profitability will reduce attractiveness of smaller, entry-level loans

+

- **Decreased market diversity** as lenders are forced to consolidate under the pressure of regulation

=

- **Pressure on financial inclusion & rising housing backlogs**

In South Africa, one author has suggested that the Basel III could have the impact of doubling the backlogs in the entry-level housing market

African Union for Housing Finance

Basel III: Stability vs. Access?

- Regulatory reform critical to safety and soundness of the banking system
- But this puts pressure on financial inclusion goals
- Lending to low income earners is not by definition sub-prime! No African country has ever had a NINJA loan.
- Sub-market specific data critical to understanding risk
- Mortgage markets in many African countries are in their infancy
- The bulk of the demand is in the entry-level, lower value market
- Lending is critical to the growth of sustainable human settlements
- Appropriate and supportive international frameworks are necessary to enable growth in our markets.

AFRICAN UNION FOR HOUSING FINANCE

Thank you!

Colin Chimutsa

Chairman, AUHF

Executive Director, CBZ Bank, Zimbabwe

For more information, contact

Email: info@housingfinanceafrica.org

Web: **www.auhf.co.za**

Telephone: +2711-447-9581