AUSTRALIAN PRUDENTIAL REGULATION AUTHORITY
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TO: ALL LOCALLY-INCORPORATED ADIs SUBJECT TO APS 210 LIQUIDITY COVERAGE RATIO (LCR) REQUIREMENTS

CONTINGENT LIQUIDITY: FINAL GUIDANCE

The Australian Prudential Regulation Authority (APRA) is today releasing its final guidance on the level of self-securitised assets expected to be maintained by locally-incorporated LCR ADIs on an ongoing basis.

On 14 July 2021, APRA advised its intention to de-link its guidance for self-securitised assets from the Committed Liquidity Facility (CLF), and released for consultation its proposed updated guidance. The proposed guidance stated that it would be prudent for a locally-incorporated LCR ADI to hold self-securitised assets with a cash value equivalent to at least 30 per cent of group net cash outflows (NCOs) as contingency for periods of stress.

Submissions received

APRA received 7 submissions: 6 from ADIs and one from an industry body. Submissions expressed support for the need to maintain contingent liquidity reserves for periods of stress, commenting on five aspects of APRA's proposed guidance:

(i) Some submissions questioned the need to maintain contingent liquidity reserves in the form of self-securitised assets (as opposed to holding loans eligible for securitisation), given ADIs had increased their self-securitised assets quickly during the COVID-19 stress.

APRA's response: *Many ADIs increased their self-securitised assets in a timely manner during the COVID-19 stress. However, there is still a plausible risk of operational issues causing delays in the process of increasing self-securitised assets in a future stress. APRA therefore maintains its view that it would be prudent for ADIs to hold a minimum amount of self-securitised assets at all times.*

(ii) Submissions recommended that APRA's guidance should be based only on an ADI's Australian dollar (AUD) NCOs rather than its group (all currencies) NCOs since the guidance relates to AUD self-securitised assets only and it does not include offshore assets that could be used to access liquidity support from foreign central banks.

APRA's response: *APRA accepts that the guidance should be based on AUD NCOs since it relates to AUD self-securitised assets only.*

(iii) A number of submissions also recommended that the guidance should be sized at less than 30 per cent, arguing that it was unduly conservative to hold contingent liquidity at the level proposed by APRA in addition to the liquid assets held under the LCR.

APRA's response: *APRA does not agree. Given the proposed amount of self-securitised assets would be materially lower than the peak amount held by most ADIs in 2020, the guidance is appropriately sized to provide resilience in stress without being unduly conservative.*

(iv) Submissions noted that a high proportion of mortgages are already in use as collateral for the RBA's Term Funding Facility (TFF) in addition to the CLF. It was argued that using additional mortgages to meet the guidance could limit their availability for secured funding. A phased implementation in line with the TFF maturity dates was therefore recommended.

APRA's response: *APRA does not expect secured funding issuance to be constrained by meeting the guidance, given most ADIs are expected to have sufficient mortgages to achieve both. A phased implementation is therefore not necessary. In the few cases where there are insufficient mortgages, APRA would expect an ADI to prioritise secured funding issuance. This is consistent with the RBA expecting counterparties to have already made reasonable efforts to access private sector liquidity prior to requesting exceptional liquidity assistance*[1]*.*

(v) ADIs requested APRA to clarify how the 12-month average of NCOs on which the guidance is based should be calculated, with annual and quarterly updates of the average being recommended.

APRA's response: *APRA would expect the 12-month average of NCOs to be based on daily NCO observations and to be updated on a quarterly basis.*

Final guidance: APG 210 paragraph 67

APRA has amended the draft guidance as follows:

For a locally-incorporated LCR ADI, it would be prudent to hold self-securitised assets with a cash value equivalent to at least 30 per cent of ~~group~~ Australian dollar net cash outflows as contingency for periods of stress.[1] *APRA would expect the self-securitised assets to be unencumbered, and not held as collateral for any other purpose.*

[1] Using a 12-month average of net cash outflows would reduce the volatility in the level of self-securitised assets that would be held.

APRA will replace APG 210 paragraph 67 with the above guidance and expects to release the updated version of APG 210 on 1 March 2022. APRA expects ADIs to report to the RBA on an ongoing basis the relevant data on the self-securitised assets held to meet the guidance.

Prudential Standard APS 120 Securitisation (APS 120)

APS 120 footnote 5 and Attachment B paragraph 5(e) outline when an ADI may repurchase exposures from a self-securitisation. APRA will not take action under APS 120 as a result of ADIs reducing the size of their self-securitised assets in line with the final guidance. If an ADI is reducing the size of its self-securitised assets for other reasons, it should consult APRA.

If you have any queries regarding this letter, please contact your responsible supervisor.

Yours sincerely,

John Lonsdale
Deputy Chair

[1] Refer to the RBA's website: Domestic Market Operations and Liquidity Facilities | RBA