New liquidity rules effective from the beginning of the year

The Central Bank set new rules for the liquidity ratio of credit institutions subject to reserve requirements in the Central Bank in December which came into effect on the 31st of that month. Earlier rules on liquidity of credit institutions with required reserves were rescinded at the same time and the reference period ending on December 20 was the last in which they were in effect. An adjustment period is given whereby penalties for non-compliance with the new rules are not applied in full until after three months.

Work on drafting the new rules took place from spring 1999 onwards, in collaboration with credit institutions and the Financial Supervisory Agency. In order for them to take effect, provisions on liquidity of credit institutions in the Central Bank Act had to be amended, and a bill to this effect was passed by the parliament just before Christmas.

The new liquidity rules are modelled on those of the Deutsche Bundesbank, the EU's "Groupe de Contact" and BIS. Based on different principles from the earlier rules, they involve an overall assessment of liquid assets and liquid liabilities on the credit institutions' balance sheets, along with non-balance sheet items. The former rules, however, only took into account domestic and foreign credit institutions' claims and liabilities among themselves, and their dealings with the Central Bank. Thus the new rules are even better designed to ensure that credit institutions have adequate liquidity for meeting their liabilities. They do not involve less restraint on the liquidity position of credit institutions, and will reduce the negative impact that the earlier rules had on interest rate formation in the money and securities markets.

Highlights of the new rules:

1. Liquidity is classified into four time-bands within the following twelve months. These are: Liquid within one month, from one and up to three months, from three and up to six months, and from six and up to twelve months.
2. The liquidity ratio (ratio of liquid claims to liquid liabilities) as defined in the rules shall be calculated monthly on the basis of end-of-month data.
3. Assessment includes the liquid value of all claims and liabilities that may have either a market value or a specified income or expenditure flow.
4. Individual balance sheet items and non-balance sheet items have been assessed with respect to the ease and security of liquidating them. An item is assessed at 100% if it has a full effect, but as not having any effect if it is highly uncertain whether it can be liquidated.
5. According to the weighting of each item, liquidity is assessed at the end of each month, taking into account each item's market worth, position and income or expenditure flow.
6. Liquid claims are required to be greater than liquid liabilities during the first two periods (cf. item 1), i.e. the ratio of claims to liabilities must not be lower than one for each period. A surplus during the first period may be carried over to the second.
7. If the liquidity ratio does not reach specified minimum levels, penalties are calculated on the amount of the shortfall, corresponding to 30-day penalty interest at any time.