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SOUTH AFRICAN RESERVE BANK
Prudential Authority

Ref.: 15/8/1/3

To: All banks, branches of foreign institutions, controlling companies (collectively referred to as banks), eligible institutions, and auditors of banks or controlling companies

Proposed directive issued in terms of section 6(6) of the Banks Act 94 of 1990 (Banks Act)

Matters relating to eligible external credit assessment institutions

Executive summary

Regulation 23 of the Regulations relating to Banks (Regulations) allows banks to choose between the internal ratings-based (IRB) approach and the standardised approach (STA) for calculating regulatory capital requirements for credit risk. The STA for credit risk and the treatment of securitisation exposures make extensive use of the ratings issued by external credit assessment institutions (ECAIs) for determining the risk weights of exposures and, ultimately, the calculation of a bank's minimum required regulatory capital. In terms of section 85A of the Banks Act, banks may only use the ratings of eligible ECAIs which are approved by the Prudential Authority (PA) to act as eligible institutions.

The ratings specified in the Regulations to determine the appropriate risk weights to be applied by banks and banking groups that have adopted the STA for credit risk and for the treatment of securitisation exposures relate to the rating symbols on an international scale issued by Standard & Poor's Rating Services (S&P). The rating scales of other ECAIs approved as eligible institutions in South Africa, can be used instead. The mapping of the international scale ratings issued by eligible ECAIs to the risk weights specified in regulation 23 of the Regulations will be monitored by the PA and revised as appropriate.

The purpose of this proposed directive is to (i) inform banks and/or affected persons of the credit rating agencies approved as eligible institutions in South Africa, (ii) require that banks inform the PA of their nominated ECAIs, and (iii) require that banks map the international scale ratings to the specified risk weights in regulation 23 of the Regulations in the manner outlined in this proposed directive.

1. Introduction

- 1.1. In jurisdictions that allow the use of external ratings for regulatory purposes, only credit assessments issued by credit rating agencies approved as eligible ECAIs by national supervisors are allowed. As such, the PA is responsible for determining on a continuous basis whether an ECAI meets the criteria specified in the Regulations, and approval should only be granted in respect of ECAI ratings for specified types of exposure where all criteria and conditions are met. Accordingly, the PA is also responsible for mapping ECAI ratings to the risk weights available under the STA risk weighting framework.
- 1.2. In accordance with the above, the PA had previously issued Banks Act Circular 2 of 2011, Directive 12 of 2013 and Directive 9 of 2015, informing banks of the institutions that are approved as eligible ECAIs and advising banks of the mapping of the international scale ratings issued by eligible ECAIs to the risk weights specified in regulation 23 of the Regulations.
- 1.3. Among other matters, the cancellation of the registration of Fitch Ratings as a credit rating agency in terms of the Credit Rating Services Act 24 of 2012 (CRS Act) and consequent derecognition as an eligible ECAI necessitates a new directive from the PA. This is necessary to formally notify and direct banks and/or affected persons to map the international scale ratings of the remaining ECAIs (listed in paragraph 5 below) to the risk weights specified in regulation 23 of the Regulations in the manner outlined in paragraph 6 below.
- 1.4. This proposed directive replaces Circular 2 of 2011 (dated 8 March 2011), Directive 12 of 2013 (dated 2 August 2013) and Directive 9 of 2015 (dated 22 October 2015).

2. Purpose

- 2.1. Based on the aforesaid, the purpose of this proposed directive is to:
 - 2.1.1. Inform banks and/or affected persons of the ECAIs approved by the PA as eligible institutions in South Africa – listed in paragraph 5 below.
 - 2.1.2. Require banks to notify the PA of their nominated ECAIs from the list of eligible ECAIs.
 - 2.1.3. Require banks to apply the mapping tables outlined below in the calculation of their minimum required capital and reserve funds related to credit risk in terms of the Regulations.

3. References in the Banks Act

- 3.1. Section 1 of the Banks Act defines an eligible institution as an ECAI or an export credit agency that meets the minimum requirements as specified and which institution or agency has been approved in writing by the PA. The process and the related criteria for the approval of an ECAI is set out in regulation 51 of the Regulations.
- 3.2. Section 4(5) of the Banks Act, stipulates that “in order to ensure the appropriate usage of an external credit assessment issued by an eligible institution, by a bank, the PA:
 - (a) shall assign such external credit ratings to such risk weights as may be prescribed from time to time; and

- (b) shall publicly disclose which external credit assessment or rating issued by an ECAI relates to which prescribed risk weight”.

4. References in the Regulations

- 4.1. Regulation 23 of the Regulations stipulates that for the calculation of minimum required capital and reserve funds relating to credit risk under the STA, banks shall apply the ratings or assessments issued by an eligible ECAI of the bank’s choice (as selected or nominated by the bank).
- 4.2. As stated above, regulation 23 of the Regulations specifies, inter alia, risk weights that relate to the ratings on an international scale issued by S&P. However, the rating scales of other ECAIs approved as eligible institutions in South Africa, could have been used instead.
- 4.3. International scale ratings issued by eligible ECAIs are also used to calculate, among other requirements:
- 4.3.1. the capital requirement in respect of securitisation exposures; and
- 4.3.2. the capital requirement in respect of credit derivative instruments under the STA.

5. Eligible institutions

- 5.1. Banks and other affected persons are hereby informed that the following rating agencies remain eligible institutions as approved by the PA in terms of section 85A of the Banks Act:
- 5.1.1. Global Credit Rating Co. (Pty) Ltd (GCR).
- 5.1.2. Moody’s Investors Service (Moody’s).
- 5.1.3. Standard & Poor’s Rating Services (S&P).
- 5.2. Banks are required to notify the PA in writing of their nominated ECAIs within two months from the date of issue of this [proposed] directive.
- 5.3. In relation to export credit agencies’ ratings, banks that wish to adopt the simplified, standardised method for the calculation of minimum required capital and reserve funds relating to credit risk may use a rating issued by an export credit agency approved by the PA. The banks may also use the consensus country risk scores of export credit agencies participating in the “Arrangement on Officially Supported Export Credits”. The consensus country risk scores are available on the website of the Organisation for Economic Co-operation and Development at www.oecd.org.

6. International scale ratings of GCR and Moody's assigned to prescribed risk weights

6.1. The PA hereby directs that the international scale ratings of GCR and Moody's shall be mapped in the manner outlined below.

6.1.1. *Tables 1 and 2* below sets out the mapping of the corresponding long and short-term credit assessments of GCR and Moody's, respectively, to the relevant risk weights specified under the STA as outlined in Table 8 in regulation 23(8)(a) of the Regulations.

Table 1: Long-term credit assessments and corresponding risk weights

Institution			Claims in respect of:					
S&P assessments	Moody's assessments	GCR assessments	Sovereigns (including the Central Bank of that particular country)	Public-sector entities	Banks	Securities Firms	Banks: short-term claims	Securities Firms: short-term claims
AAA to AA-	Aaa to Aa3	AAA to AA-	0%	20%	20%	20%	20%	20%
A+ to A-	A1 to A3	A+ to A-	20%	50%	50%	50%	20%	20%
BBB+ to BBB-	Baa1 to Baa3	BBB+ to BBB-	50%	50%	50%	50%	20%	20%
BB+ to B-	Ba1 to B3	BB+ to B-	100%	100%	100%	100%	50%	50%
Below B-	Below B3	Below B-	150%	150%	150%	150%	150%	150%
Unrated	Unrated	Unrated	100%	50%	50%	50%	20%	20%

Continuation of Table 1: Claims in respect of corporate entities

S & P assessments	Moody's assessments	GCR assessments	Risk weights
AAA to AA-	Aaa to Aa3	AAA to AA-	20%
A+ to A-	A1 to A3	A+ to A-	50%
BBB+ to BB-	Baa1 to Ba3	BBB+ to BB-	100%
Below BB-	Below Ba3	Below BB-	150%
Unrated	Unrated	Unrated	100%

Table 2 below sets out the short-term credit assessments and corresponding risk weights.

S & P assessments	Moody's assessments	GCR assessments	Risk weights
A-1	P-1	A1	20%
A-2	P-2	A2	50%
A-3	P-3	A3	100%
All other ratings or unrated	All other ratings or unrated	All other ratings or unrated	150%

6.1.2. Securitisation

6.1.2.1 With reference to Table 7a and 7b in the securitisation regulation 23(6)(k)(i&ii) of the Regulations, Tables 3 and 4 below set out the long and short-term ratings categories and corresponding risk-weight categories of securitisation exposures to be used by banks when an inferred rating based on an external credit rating is available.

Table 3: Long-term ratings and corresponding risk weights for securitisation exposures

Credit Assessments			Risk weights:			
S&P	Moody's	GCR	Senior tranche		Non-senior (thin) tranche	
			Tranche maturity (M _T)		Tranche maturity (M _T)	
			1 year	5 years	1 year	5 years
AAA	Aaa	AAA	15%	20%	15%	70%
AA+	Aa1	AA+	15%	30%	15%	90%
AA	Aa2	AA	25%	40%	30%	90%
AA-	Aa3	AA-	30%	45%	40%	120%
A+	A1	A+	40%	50%	60%	140%
A	A2	A	50%	65%	80%	160%
A-	A3	A-	60%	70%	120%	180%
BBB+	Baa1	BBB+	75%	90%	170%	260%
BBB	Baa2	BBB	90%	105%	220%	310%
BBB-	Baa3	BBB-	120%	140%	330%	420%
BB+	Ba1	BB+	140%	160%	470%	580%
BB	Ba2	BB	160%	180%	620%	760%
BB-	Ba3	BB-	200%	225%	750%	860%
B+	B1	B+	250%	280%	900%	950%
B	B2	B	310%	340%	1050%	1050%
B-	B3	B-	380%	420%	1130%	1130%
CCC+/CCC /CCC-	Caa1/Caa2/ Caa3	CCC+/CCC /CCC-	460%	505%	1250%	1250%
Below CCC-	Below Caa3	Below CCC-	1250%	1250%	1250%	1250%

Table 4: Short-term ratings and corresponding risk weights for securitisation exposures

S & P assessments	Moody's assessments	GCR assessments	Risk weights
A-1	P-1	A1	15%
A-2	P-2	A2	50%
A-3	P-3	A3	100%
All other ratings	All other ratings	All other ratings	1250%

6.1.2.2 Tables 5 and 6 below depict the mapping for long and short-term securitisation transactions that are assessed as simple, transparent, and comparable (STC) for capital purposes under the external ratings-based approach; also see Tables 7c and 7d in the securitisation regulation 23(6)(o)(ii&iii) of the Regulations.

Table 5: Long-term credit ratings and corresponding risk weights for securitisation exposures

Credit Assessments			Risk weights:			
S&P	Moody's	GCR	Senior tranche		Non-senior (thin) tranche	
			Tranche maturity (M_T)		Tranche maturity (M_T)	
			1 year	5 years	1 year	5 years
AAA	Aaa	AAA	10%	10%	15%	40%
AA+	Aa1	AA+	10%	15%	15%	55%
AA	Aa2	AA	15%	20%	15%	70%
AA-	Aa3	AA-	15%	25%	25%	80%
A+	A1	A+	20%	30%	35%	95%
A	A2	A	30%	40%	60%	135%
A-	A3	A-	35%	40%	95%	170%
BBB+	Baa1	BBB+	45%	55%	150%	225%
BBB	Baa2	BBB	55%	65%	180%	255%
BBB-	Baa3	BBB-	70%	85%	270%	345%
BB+	Ba1	BB+	120%	135%	405%	500%
BB	Ba2	BB	135%	155%	535%	655%
BB-	Ba3	BB-	170%	195%	645%	740%
B+	B1	B+	225%	250%	810%	855%
B	B2	B	280%	305%	945%	945%
B-	B3	B-	340%	380%	1015%	1015%
CCC+/CCC/ CCC-	Caa1/Caa2/ Caa3	CCC+/CCC/ CCC-	415%	455%	1250%	1250%
Below CCC-	Below Caa3	Below CCC-	1250%	1250%	1250%	1250%

Table 6: Short-term credit ratings and corresponding risk weights for securitisation exposures

S & P assessments	Moody's assessments	GCR assessments	Risk weights
A-1	P-1	A1	10%
A-2	P-2	A2	30%
A-3	P-3	A3	60%
All other ratings	All other ratings	All other ratings	1250%

6.1.3. Credit derivative instruments under the STA

6.1.3.1 In the case of a first-to-default structure, the protection provider shall risk weight its exposures in accordance with the weightings set out in Table 11 in regulation 23(9)(d) of the Regulations. Tables 7 and 8 below outline the corresponding long and short-term ratings of GCR and Moody's.

Table 7: Long-term ratings and corresponding risk weights

S & P assessments	Moody's assessments	GCR assessments	Risk weights
AAA to AA-	Aaa to Aa3	AAA to AA-	20%
A+ to A-	A1 to A3	A+ to A-	50%
BBB+ to BBB-	Baa1 to Baa3	BBB+ to BBB-	100%
BB+ to BB-	Ba1 to Ba3	BB+ to BB-	350%
B+ and below or unrated	B1 and below or unrated	B+ and below or unrated	1250% ¹

Table 8: Short-term ratings and corresponding risk weights

S & P assessments	Moody's assessments	GCR assessments	Risk weights
A-1	P-1	A1	20%
A-2	P-2	A2	50%
A-3	P-3	A3	100%
All other ratings	All other ratings	All other ratings	1250% ¹

6.2. Other references to international scale ratings issued by eligible ECAs

6.2.1. In the case of any other relevant reference in the Regulations to international scale ratings issued by eligible ECAs, the same principle as specified above must be applied.

¹ Or such imputed percentage that will effectively result in an amount equivalent to a deduction against capital and reserve funds

7. Proposed directive

- 7.1. Based on the aforesaid and in accordance with the provisions of section 6(6) of the Banks Act, banks are hereby directed:
- 7.1.1. to note the ECAs approved by the PA as eligible institutions in South Africa;
 - 7.1.2. to notify the PA of their nominated ECAs from the list of eligible ECAs within two months from the date of the issue of this [proposed] directive; and
 - 7.1.3. to apply the mapping tables outlined in this proposed directive in the calculation of their minimum required regulatory capital and reserve funds related to credit risk in terms of the Regulations.

8. Invitation for comment

- 8.1. All interested persons are hereby invited to submit their comments on the proposed directive to: SARB-PA@resbank.co.za, and copy RSD-CreditRisk@resbank.co.za for the attention of Mr. B Mtsweni by no later than 17 July 2023.

Fundi Tshazibana

Fundi Tshazibana
Chief Executive Officer

Date: 03/07/23