BANKIGA DHEXE EE SOOMAALIYA
البنك المركزي الصومالي
CENTRAL BANK OF SOMALIA

Licensing and Supervision Department

REGULATION ON LIQUIDITY RISK MANAGEMENT, 2023

CBS/BS/REG/03
(As Amended 2023)

Contents

1. INTRODUCTION

1.1. Authority

This regulation is made by the Central Bank of Somalia (CBS) pursuant to its authority set forth in Sections 16(1) and 34 of the Financial Institution Law, 2012 ("FIL"), and Sections 38(1) and 52(1) of the Central Bank of Somalia Act 2012, for the purpose of implementing Section 16 (Minimum Holding and Computation of Liquid Assets) of the FIL. This regulation shall replace the current CBS regulation on Liquidity Risk Management 2015.

1.2. Applicability

The requirements of this regulation apply to all financial institutions licensed by the CBS to engage in banking business.

1.3. Scope

(1) This regulation must be applied by each financial institution on a standalone basis, i.e., on a basis that does not consolidate assets and liabilities of its subsidiaries.

(2) The CBS can exempt specific financial institutions (e.g., Foreign Branch) from this regulation on a case-by-case basis.

2. QUANTITATIVE REQUIREMENTS

2.1. LIQUIDITY COVERAGE RATIO (LCR)

2.1.1. Minimum Requirement

(1) Each financial institution must at all times maintain a Liquidity Coverage Ratio equal to or greater than 100% - i.e., LCR ≥ 100%.

(2) The LCR must be reported in the same reporting currency used by the financial institution in its financial statement.

(3) At the calculation date, all foreign currency positions must be converted to the reporting currency based on publicly available foreign exchange rates from official sources of the related currency.

(4) Financial institutions must immediately report to CBS situations in which the LCR has fallen, or is expected to fall, below 100%.

2.1.2. Calculation

$$LCR = \frac{HQLA}{Total\ Net\ Cash\ Outflows}$$

Where:

HQLA is the stock of high-quality liquid assets, as defined in 2.1.3, and

Total Net Cash Outflows as defined in 2.1.4.

2.1.3. High-Quality Liquid Assets (HQLA)

The amount of HQLA, on a given date, is equivalent to:

$$HQLA = \sum_i (1 - Haircut_i) * Asset_i$$

Where:

Haircut is equivalent to a discount in the value of an asset, and

Asset is the value of an asset eligible as HQLA, in accordance with section 2.1.3.1.

2.1.3.1. Assets eligible as HQLA

(1) The following assets are considered as HQLA under this regulation and subject to a 0% haircut:

a. Cash on hand,

b. Unrestricted balances with the CBS, to the extent that they are allowed to be drawn down in times of stress,

c. Marketable securities, including Sukuk and equivalent Shariah-compliant securities, denominated in the local currency, issued, or guaranteed by the Federal Government of Somalia or the CBS,

d. Marketable securities, including Sukuk and equivalent Shariah-compliant securities, issued or guaranteed by sovereigns, central banks, public service entities, the Bank for International Settlements, the International Monetary Fund, the European Central Bank and European Community, the International Islamic Liquidity Management Corporation (IILM) or multilateral development banks, provided that the asset possesses all the following characteristics:

(i) its external credit rating currency is above or equal to AA- or Aa3,

(ii) is traded in large, deep, and active repurchase agreements (Repo) or cash markets, characterised by a low level of concentration, and

(iii) have a proven record as a reliable source of liquidity in the markets (through repo or outright sale) even during stressed market conditions.

(2) An asset to be recognized as HQLA must be unencumbered, i.e., free of any legal, regulatory, contractual, or other restrictions that could prevent the ability to liquidate, sell, transfer, or assign that asset.

(3) An obligation of a financial institution or of any affiliate of a financial institution cannot be accepted as HQLA, even if guaranteed as mentioned in items (c) and (d) of (1).

(4) The value of a marketable security eligible as HQLA should reflect its current market value easily observable in the market or can be determined by a formula that is easy to calculate on the basis of publicly available inputs and that does not depend on strong assumptions.

(5) Once an asset is included as part of the stock of HQLA, its associated cash inflows cannot be counted as cash inflows as determined in 2.1.6.

(6) Where an asset ceases to comply with the HQLA eligibility criteria as set out in this Article, an institution may nevertheless continue to consider it as such for an additional period of 30 days.

2.1.4. Total Net Cash Outflows

For purposes of calculating the LCR, a financial institution's Total Net Cash Outflows is the greater of the following two amounts:

(i) Total Cash Outflows -/minus/less Total Cash Inflows; or

(ii) 25% of Total Cash Outflows.

Where:

Cash Outflows as defined in 2.1.5., and

Cash Inflows as defined in 2.1.6.

2.1.5. Total Cash Outflows

(1) The amount of Total Cash Outflows, on a given date, is equivalent to:

$$Total\ Cash\ Outflows = \sum_i Outflow_i$$

Where:

Outflow is the outstanding balance - or expected outflow for the subsequent 30 calendar days - of a liability or off-balance sheet item on the given date, adjusted by a factor as specified in the Appendix 1.

(2) Where there is a liability or off-balance item that could produce multiple outflows, only the maximum outflow among them should be included in the Total Cash Outflow.

2.1.6. Total Cash Inflows

The amount of Total Cash Inflows, on a given date, is equivalent to:

$$Total\ Cash\ Inflows = \sum_i Inflow_i$$

Where:

Inflow is the expected inflow for the subsequent 30 calendar days of an asset on the given date, adjusted by a factor as specified in the Appendix 2.

2.2. LIQUID ASSETS RATIO (LAR)

2.2.1. Minimum Requirement

(1) Each financial institution must maintain, at every month´s end, a Liquid Assets Ratio equal to or greater than 20% - i.e., LAR ≥ 20%.

(2) Financial institutions must immediately report to CBS situations in which the LAR has fallen, or is expected to fall, below 20%.

2.2.2. Calculation

$$LAR = \frac{LA}{Total\ Assets}$$

Where, at a month´s end:

- LA refers to the stock of liquid assets, as defined in section 2.2.3., and

- Total Assets as reported in the Financial Statement.

2.2.3. Assets eligible as LA

The following assets are considered as LA under this regulation:

a. all those recognized as HQLA, as in section 2.1.3.1, and

b. deposits and investment accounts held in another financial institution which are of a non-operational nature (e.g., not required to facilitate the access and ability to use payment and settlement systems and to facilitate payments of the depository institution at the institution receiving the deposit) and readily available for withdrawn.

3. QUALITATIVE REQUIREMENTS

3.1. Liquidity Risk Management Policy

(1) The Board of directors must approve a written Liquidity Risk Management Policy for the management of the financial institution's liquidity risk that includes a strategy for the day-to-day management of liquidity.

(2) The Board of directors must ensure that management develops, implements, maintains, and monitors as necessary the Liquidity Risk Management Policy

(3) To be considered adequate, the Liquidity Risk Management Policy must address the following measures:

   a. Articulate the liquidity risk tolerance of the financial institution as determined by the board of directors based on the institution's business plan and require that senior management operate within that tolerance when managing the institution's liquidity,

   b. Include a liquidity strategy and a liquidity management plan to monitor, control, and limit liquidity risk overall, and for each currency in which the financial institution is materially active,

c. Set limits on the size of the financial institution's liquidity position over particular time horizons,

d. Provide for methods to ensure proper oversight of the financial institution's liquidity risk management by senior officers, the Risk Management Committee, and the Board of directors,

e. Require that management develop policies and processes to implement the approved strategy and ensure adherence to established controls and limits,

f. Require that a crisis plan be developed and ready for implementation in case of a period of liquidity stress, whether institution-specific or system-wide,

g. Ensure that the financial institution's liquidity risk management process is adequately covered by the institution's internal control system and reviewed by both the internal and external auditors, and

h. Provide for a reporting mechanism to management, the senior officers, and the board of directors on the financial institution's liquidity position, both on a regular basis and in emergencies.

(4) The Liquidity Risk Management Policy should be communicated throughout the financial institution.

(5) At regular times during the year, senior officers and management must review the underlying assumptions of the Liquidity Risk Management Policy to ensure that they remain valid and relevant, recommending changes as deemed necessary.

(6) On a regular basis, the board of directors must review the financial institution's liquidity position and management's adherence to the Liquidity Risk Management Policy.

(7) At least annually, the Board of directors must review the Liquidity Risk Management Policy, its underlying assumptions, and approve revisions to that document as deemed necessary.

3.2. Contingency Funding Plan

(1) A financial institution must have a written Contingency Funding Plan for managing liquidity during a crisis that must include:

a. Methods to cover shortfalls in liquidity across a range of stress environments,

b. Clear triggers, responsibilities and procedures that define when to invoke the Contingency Funding Plan and when to escalate actions under the plan,

c. Timely and consistent internal and external communications (Central Bank, media, analysts, customers, employees), and

d. Regularly testing and updating.

(2) The liquidity contingency plan must be formally approved and reviewed annually by the Board of directors.

3.3. Management Information System

(1) A financial institution must establish and maintain a management information system that provides the Board of director, the senior officers, and the management with adequate and timely information to:

a. Track the financial institution's liquidity positions, including trends, in all currencies in which the bank has material activity,

b. Project the financial institution's liquidity position over different time periods, including daily and longer-term, and under alternative scenarios including stress scenarios,

c. Review risk measures on a timely basis,

d. Compare current liquidity exposures with limits established by the Board of directors.

(2) The management information system must also show the extent of the financial institution's compliance with:

a. Board-approved policies, procedures, and limits, and

b. The CBS's liquidity requirements.

4. REPORTS TO THE CBS

(1) Within 15 days of the end of month, a financial institution must submit to the CBS a report, in the format prescribed by the CBS, showing its calculation of the:

- LCR, at each business day throughout the previous month, and

- LAR, at the end of the previous month.

(2) A financial institution must be able to demonstrate to the CBS, at all times, its compliance with the qualitative requirements prescribed in this regulation.

5. SANCTIONS

(1) If any of the assumptions behind the calculation of a qualitative requirement by a financial institution are considered inadequate, CBS may determine proper and prompt adjustments.

(2) If the qualitative requirements implemented by a financial institution are deemed by the CBS inadequate or not consistent with its risk profile, corrective measures may be requested by the CBS.

6. EFFECTIVE DATE

The requirements included in that regulation will apply to financial institutions beginning on 1 January 2024.

CENTRAL BANK OF SOMALIA

Regulation on Liquidity Requirements, 2023

Appendix 1

LCR – Outflows

1. Retail Funding

1.1. Definition

(1) For LCR calculation, retail funding is defined as deposits placed by natural persons, micro enterprises, and small enterprises.

(2) Retail funding includes all demand deposits, term deposits and investment accounts - except for those with a residual maturity or withdrawal notice period greater than 30 days and where the depositor has no legal right to withdraw deposits within the next 30 days, or if early withdrawal results in a significant penalty that is materially greater than the loss of profit/interest or capital.

(3) If a depositor is allowed to early withdraw its deposits without applying the contractually agreed penalty, or despite a clause that says the depositor has no legal right to withdraw, those deposits must be considered as subject to outflows for the LCR calculation.

(4) Micro and small enterprises are those eligible in accordance with Attachment 2 of CBS/BS/REG/07/22 Regulation (Bank) Licensing.

1.2. Outflow

The outflow of a retail funding is equivalent to 10% of its nominal amount, including any profit/interest when appropriate.

2. Wholesale Funding

2.1. Definition

For the LCR calculation, wholesale funding, including investment accounts, is defined as those liabilities and general obligations that are raised from non-natural persons (i.e., legal entities), callable within the next 30 days or that has its earliest possible contractual maturity date situated within this horizon, as well as funding with an undetermined maturity. This should include all funding with options that are exercisable at the investors or financial institution´s discretion within the 30-calendar-day horizon.

2.2. Outflow

(1) The outflow of wholesale funding raised from a non-financial customer, not including micro and small enterprises, is equivalent to its nominal amount, including any interest or profit when appropriate, multiplied by 40%.

(2) The outflow of a wholesale funding raised from a financial customer is equivalent to 100% of its nominal amount, including any interest or profit when appropriate.

3. Credit facilities **3.1 Definition** For the LCR calculation, credit facilities are defined as explicit lending commitments, contractual agreements or obligations to extend funds at a future date to retail or wholesale counterparties, regardless of their contractual maturity, and they must have an irrevocable (committed) or conditionally revocable condition.
3.2. Outflow The outflow of a credit facility agreed with: A natural person customer is equivalent to 5% of its undrawn amount. A micro or small enterprise customer is equivalent to 5% of its undrawn amount. A non-financial customer, not including micro and small enterprises, is equivalent to 10% of its undrawn amount. A financial institution is equivalent to 40% of its undrawn amount. Other types of customers not listed above is equivalent to 100% of its undrawn amount.
4. Trade Finance obligations **4.1. Definition** For the LCR calculation, trade finance obligations are defined as contingent funding obligations stemming from trade-related obligations directly underpinned by the movement of goods or the provision of services. **4.2. Outflow** The outflow of a trade finance obligation is equivalent to 5% of its undrawn amount.
5. Other liabilities **5.1. Definition** For the LCR calculation, any other contractual cash outflows within the next 30 calendar days not explicitly referred above must be captured, except for those related to operating costs. **5.2. Outflow** The outflow of any other liability is equivalent to 100% of its expected cash outflows during the next 30 calendar days.

CENTRAL BANK OF SOMALIA
Regulation on Liquidity Requirements, 2023
Appendix 2
LCR – Inflows

1. Loans

1.1. Definition

For the LCR calculation, only inflows related to payments on fully performing loans/financing, and contractually due within a 30-day horizon should be considered.

1.2. Inflow

The inflow of a fully performing loan/financing due within a 30-day horizon is equivalent to its payments (including financial payments and instalments) multiplied by:

a. 100%, if the borrower is a financial institution or a central bank, or

b. 50%, if the borrower is a non-financial customer (including micro and small enterprises), and

c. 50% if the borrower is a natural person.

2. Securities

2.1. Definition

For the LCR calculation, only inflows from securities not considered as HQLA, as laid out in section 2.1.3, and maturing within 30 days can be considered.

2.2. Inflow

The inflow of a non-HQLA security is equivalent to 100% of its payments due during the next 30 calendar days.

3. Deposits

3.1. Definition

For the LCR calculation, only inflows related to the balances in deposits or investment accounts held in another financial institution which are of a non-operational nature (e.g., not required in order to facilitate the access and ability to use payment and settlement systems and to facilitate payments of the depository institution at the institution receiving the deposit) and that may be withdrawn within 30 days can be considered.

3.2. Inflow

(1) The inflow of a non-operational deposit or investment account held in other financial institution is equivalent to 100% of its nominal amount.

(2) For deposits and investment accounts abroad in countries that have a history of introducing capital or foreign exchange controls, the inflow is equivalent to 0% of its nominal amount.

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