



News release

4 August 2016

Financial Policy Committee statement from its policy meeting, 25 July 2016

1. The Bank of England's Financial Policy Committee (FPC) has decided to exclude central bank reserves from the exposure measure in the current UK leverage ratio framework, with immediate effect.
2. In doing so, the FPC's aim is to ensure that the leverage ratio does not act as a barrier to the effective implementation of policy measures that might lead to an increase in central bank reserves. These measures include actions taken to maintain monetary and financial stability since the referendum on the United Kingdom's membership of the European Union: the package of actions being announced today by the Monetary Policy Committee; and the precautionary step announced by the Bank on 30 June to provide additional flexibility in the Bank's provision of liquidity insurance by continuing to offer indexed long-term repo operations on a weekly basis until end-September 2016.
3. The FPC judges that this change to the exposure measure is appropriate because an increase in central bank reserves does not typically expose a firm to additional risks, if matched by liabilities in the same currency: as the ultimate settlement asset, central bank reserves are a unique asset class.
4. The FPC highlighted in its *Financial Stability Report* in July that there was a risk of unintended effects from leverage ratio standards on the ability of the banking system to cushion shocks and draw on central bank liquidity facilities as necessary. As a result, it encouraged the Basel Committee on Banking Supervision to review carefully any possible unintended effects of forthcoming leverage ratio standards.
5. The FPC is making this improvement to the design of the leverage ratio in the United Kingdom now, given the policy measures being put in place. It recognises that, absent offsetting the impact of this change, excluding current central bank reserves from the exposure measure – the denominator of the leverage ratio – mechanically reduces the nominal amount of capital required to meet the leverage ratio standard, other things equal. This is not the FPC's intention. It therefore intends to recalibrate the UK leverage ratio standard to offset this impact. It will consult and decide on the appropriate form of this recalibration as part of its planned review of the leverage ratio framework in 2017, in the light of the finalised international standard. In the intervening period, the Prudential Regulation Authority (PRA) will monitor firms' behaviour.
6. To implement this decision to exclude central bank reserves, the FPC has made the following Recommendation to the PRA: ***The FPC recommends to the PRA that, when applying its rules on the leverage ratio, it considers allowing firms to exclude from the calculation of the total exposure measure those assets constituting claims on central banks where they are matched by***

deposits accepted by the firm that are denominated in the same currency and of identical or longer maturity. Central bank claims for these purposes include reserves held by a firm at the central bank, banknotes and coins constituting legal currency in the jurisdiction of the central bank, and assets representing debt claims on the central bank with a maturity of no longer than three months. The FPC made the Recommendation to the PRA on a comply or explain basis.

7. The FPC has revoked its existing Direction to the PRA on the UK leverage ratio framework, in order to allow the PRA to implement this Recommendation with immediate effect; the FPC's existing powers of Direction do not enable it to vary the exposure measure used to calculate the leverage ratio. Subject to its 2017 review, the FPC intends to take steps to ensure that the change can be put in place on a permanent basis using its powers of Direction, which will require asking HM Treasury for a change in the relevant statutory instrument to allow variation in the exposure measure.
8. The PRA is today making a statement on how it is putting this Recommendation into effect.
9. This announcement does not change the leverage ratio reporting and disclosure requirements that are applicable to UK banks and building societies as set out in the Capital Requirements Regulation (575/2013).
10. The Record of the FPC's meeting is also being published today.

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