**Annex II**



**Net Stable Funding Ratio Guideline**

**November 2024**

**TABLE OF CONTENTS**

[1. INTRODUCTION 5](#_Toc134733739)

[2. DEFINITION AND MINIMUM REQUIREMENTS 6](#_Toc134733740)

[A. Definition of Available Stable Funding 7](#_Toc134733741)

[B. Definition of Required Stable Funding For Assets and Off-Balance Sheet Exposures 10](#_Toc134733742)

[3. APPLICATION ISSUES FOR THE NSFR 16](#_Toc134733743)

[A. Frequency of calculation and reporting 16](#_Toc134733744)

[B. Scope of application 16](#_Toc134733745)

LIST OF ABBREVIATIONS

|  |  |
| --- | --- |
| AFS | Available Stable Funding |
| BCBS | Basel Committee on Banking Supervision |
| HQLA | High Quality Liquid Assets |
| LCR | Liquidity Coverage Ratio |
| NSFR | Net Stable Funding Ratio |
| OBS | Off-Balance Sheet |
| PSE | Public Sector Entity |
| RMBS | Residential Mortgage-Backed Securities |
| RSF | Required Stable Funding |
| CCP | Central Counter Parties |

GLOSSARY

**“Available Stable Funding**” - capital and liabilities not susceptible to fluctuations and are readily available to the Bank at minimal cost and for a longer period of time of at least one (1) year.

**“Required Stable Funding”** is measured based on the broad characteristics of the liquidity risk profile of an institution’s assets and OBS exposures.

**“Secured financing transactions”** are transactions such as repurchase agreements, reverse repurchase agreements, security lending and borrowing, and margin lending transactions, where the value of the transactions depends on the market valuations and the transactions are often subject to margin agreements.

**"Secured funding"** means those liabilities and general obligations that are collateralized by legal rights to specifically designated assets owned by the borrowing institution in the case of bankruptcy, insolvency, liquidation or resolution.

**"Unencumbered"** means free of legal, regulatory, contractual or other restrictions on the ability of the relevant financial institution to liquidate, sell, transfer, or assign the asset. These assets should not be pledged (either explicitly or implicitly) to secure, collateralize or credit-enhance any transaction, nor be designated to cover operational costs (such as rents and salaries).

**"Wholesale funding"** means any liability or general obligation raised from non-natural persons (i.e., legal entities, including sole proprietorships and partnerships).

# **INTRODUCTION**

The net stable funding ratio (NSFR) guideline presents one of the Basel Committee’s key reforms to promote a more resilient banking sector. The NSFR will require banks to maintain a stable funding profile in relation to the composition of their assets and off-balance sheet activities. A sustainable funding structure is intended to reduce the likelihood that disruptions to a bank’s regular sources of funding will erode its liquidity position in a way that would increase the risk of its failure and potentially lead to broader systemic stress. The NSFR limits overreliance on short-term wholesale funding, encourages better assessment of funding risk across all on- and off-balance sheet items, and promotes funding stability.

The Central Bank of Kenya has strengthened its liquidity framework by adopting the NSFR as a minimum standard for funding liquidity. This standard aims at reducing funding risk over a longer time horizon by requiring banks to fund their activities with sufficiently stable sources of funding in order to mitigate the risk of future funding stress. The NSFR is comprised of specific parameters which are internationally "harmonized" with prescribed values. Certain parameters, however, contain elements of national discretion which has been adopted by Kenya to reflect jurisdiction-specific conditions.

# **DEFINITION AND MINIMUM REQUIREMENTS**

* 1. The NSFR is defined as the amount of available stable funding relative to the amount of required stable funding. This ratio should be equal to at least 100 percent on an ongoing basis. “Available stable funding” is defined as the portion of capital and liabilities expected to be reliable over the time horizon considered by the NSFR, which extends to one year. The amount of such stable funding required ("Required stable funding") of a specific institution is a function of the liquidity characteristics and residual maturities of the various assets held by that institution as well as those of its off-balance sheet (OBS) exposures.

|  |  |
| --- | --- |
| **Available amount of stable funding** | **≥ 100 percent** |
| **Required amount of stable funding** |

* 1. The amounts of available and required stable funding specified in the Guideline are calibrated to reflect the presumed degree of stability of liabilities and liquidity of assets. The calibration reflects the stability of liabilities across two dimensions:

1. *Funding tenor* – The NSFR is generally calibrated such that longer-term liabilities are assumed to be more stable than short-term liabilities.
2. *Funding type and counterparty* – The NSFR is calibrated under the assumption that short-term (maturing in less than one year) deposits provided by retail customers and funding provided by small business customers are behaviorally more stable than wholesale funding of the same maturity from other counterparties.
   1. In determining the appropriate amounts of required stable funding for various assets, the following criteria were taken into consideration, recognizing the potential trade-offs between these criteria:
3. *Resilient credit creation* – The NSFR requires stable funding for some proportion of lending to the real economy in order to ensure the continuity of this type of intermediation.
4. *Bank behaviour* – The NSFR is calibrated under the assumption that banks may seek to roll over a significant proportion of maturing loans to preserve customer relationships.
5. *Asset tenor* – The NSFR assumes that some short-dated assets (maturing in less than one year) require a smaller proportion of stable funding because banks would be able to allow some proportion of those assets to mature instead of rolling them over.
6. *Asset quality and liquidity value* – The NSFR assumes that unencumbered, high-quality assets that can be securitized or traded, and thus can be readily used as collateral to secure additional funding or sold in the market, do not need to be wholly financed with stable funding.
   1. Additional stable funding sources are also required to support at least a small portion of the potential calls on liquidity arising from OBS commitments and contingent funding obligations.
   2. NSFR definitions mirror those outlined in the LCR Guideline, unless otherwise specified. For the purposes of calculating the NSFR, HQLA are defined as all HQLA without regard to LCR operational requirements and LCR caps on Level 2 and Level 2B assets that may otherwise limit the ability of some HQLA to be included as eligible HQLA in calculation of the LCR.

## Definition of Available Stable Funding

* 1. The amount of available stable funding (ASF) is measured based on the broad characteristics of the relative stability of a bank’s funding sources, including the contractual maturity of its liabilities and the differences in the propensity of different types of funding providers to withdraw their funding. The amount of ASF is calculated by first assigning the carrying value of a bank’s capital and liabilities to one of five categories as presented below. The amount assigned to each category is then multiplied by an ASF factor, and the total ASF is the sum of the weighted amounts. Carrying value represents the amount at which a liability or equity instrument is recorded before the application of any regulatory deductions, filters or other adjustments.
  2. When determining the maturity of an equity or liability instrument, investors are assumed to redeem a call option at the earliest possible date. For funding with options exercisable at the bank’s discretion, reputational factors should be taken into account that may limit a bank’s ability not to exercise the option.[[1]](#footnote-1)In particular, where the market expects certain liabilities to be redeemed before their legal final maturity date, banks should assume such behaviour for the purpose of the NSFR and include these liabilities in the corresponding ASF category. For long-dated liabilities, only the portion of cash flows falling at or beyond the six-month and one-year time horizons should be treated as having an effective residual maturity of six months or more and one year or more, respectively.

### 

### **Calculation of derivative liability amounts**

* 1. Derivative liabilities are calculated first based on the replacement cost for derivative contracts (obtained by marking to market) where the contract has a negative value. In calculating NSFR derivative liabilities, collateral posted in the form of variation margin in connection with derivative contracts, regardless of the asset type, must be deducted from the negative replacement cost.[[2]](#footnote-2),[[3]](#footnote-3)

### **Liabilities and capital receiving a 100 percent ASF factor**

* 1. Liabilities and capital instruments receiving a 100 percent ASF factor comprise:

1. the total amount of regulatory capital, before the application of capital deductions, excluding the proportion of Tier 2 instruments with residual maturity of less than one year;
2. the total amount of any capital instrument not included in (a) that has an effective residual maturity of one year or more, but excluding any instruments with explicit or embedded options that, if exercised, would reduce the expected maturity to less than one year; and
3. the total amount of secured and unsecured borrowings and liabilities (including term deposits) with effective residual maturities of one year or more (cash flows falling below the one-year horizon but arising from liabilities with a final maturity greater than one year do not qualify for the 100 percent ASF factor).

### **Liabilities in Kenyan Shillings (KES) receiving a 95 percent ASF factor**

* 1. Stable non-maturity (demand) deposits and term deposits with residual maturity of less than one year provided by retail and small business customers in KES.

### 

### **Liabilities in Kenyan Shillings (KES) receiving a 90 percent ASF factor**

* 1. Less stable non-maturity deposits and term deposits with residual maturity of less than one year provided by retail and small business customers in KES.

### **Liabilities in foreign currency receiving a 90 percent ASF factor**

* 1. Less stable non-maturity deposits and term deposits with residual maturity of less than one year provided by retail and small business customers in foreign currency.

### **Liabilities in foreign currency receiving a 80 percent ASF factor**

* 1. Less stable non-maturity deposits and term deposits with residual maturity of less than one year provided by retail and small business customers in foreign currency.

### **Liabilities receiving a 50 percent ASF factor**

* 1. Liabilities receiving a 50 percent ASF factor comprise:

1. funding (secured and unsecured) with a residual maturity of less than one year provided by non-financial corporate customers;
2. operational deposits generated by clearing, custody and cash management activities;
3. funding with residual maturity of less than one year from sovereigns, public sector entities (PSEs), and multilateral and national development banks; and
4. other funding (secured and unsecured) not included in the categories above with residual maturity between six months to less than one year, including funding from central banks and financial institutions.

### 

### **Liabilities receiving a 0 percent ASF factor**

* 1. Liabilities receiving a 0 percent ASF factor comprise:

1. all other liabilities and equity categories not included in the above categories, including other funding with residual maturity of less than six months from central banks and financial institutions;
2. other liabilities without a stated maturity. This category may include short positions and open maturity positions. Two exceptions – should be recognized for liabilities without a stated maturity:
   * first, deferred tax liabilities, which should be treated according to the nearest possible date on which such liabilities could be realized; and
   * second, minority interest, which should be treated according to the term of the instrument, usually in perpetuity.

These liabilities would then be assigned either a 100 percent ASF factor if the effective maturity is one year or greater, or 50 percent, if the effective maturity is between six months and less than one year; and

1. NSFR derivative liabilities net of NSFR derivative assets, if NSFR derivative liabilities are greater than NSFR derivative assets.
   1. Table 1 below summarizes the components of each of the ASF categories and the associated maximum ASF factor to be applied in calculating an institution’s total amount of available stable funding under the standard.

**Table 1: Summary of liability categories and associated ASF factors**

| **ASF factor** | **Components of ASF category** |
| --- | --- |
| 100 percent | * Total regulatory capital (excluding Tier 2 instruments with residual maturity of less than one year) * Other capital instruments and liabilities with effective residual maturity of one year or more |
| 95 percent | * Stable non-maturity (demand) deposits and term deposits with residual maturity of less than one year provided by retail and small business customers in KES. |
| 90 percent | * Less stable non-maturity deposits and term deposits with residual maturity of less than one year provided by retail and small business customers in KES. * Less stable non-maturity deposits and term deposits with residual maturity of less than one year provided by retail and small business customers in foreign currency |
| 80 percent | * Less stable non-maturity deposits and term deposits with residual maturity of less than one year provided by retail and small business customers in foreign currency. |
| 50 percent | * Funding with residual maturity of less than one year provided by non-financial corporate customers * Operational deposits * Funding with residual maturity of less than one year from sovereigns, PSEs, and multilateral and national development banks * Other funding with residual maturity between six months and less than one year not included in the above categories, including funding provided by central banks and financial institutions |
| 0 percent | * All other liabilities and equity not included in the above categories, including liabilities without a stated maturity (with a specific treatment for deferred tax liabilities and minority interests) * NSFR derivative liabilities net of NSFR derivative assets if NSFR derivative liabilities are greater than NSFR derivative assets |

## Definition of Required Stable Funding For Assets and Off-Balance Sheet Exposures

* 1. The amount of required stable funding is measured based on the broad characteristics of the liquidity risk profile of an institution’s assets and OBS exposures. The amount of required stable funding is calculated by first assigning the carrying value of an institution’s assets to the categories listed. The amount assigned to each category is then multiplied by its associated required stable funding (RSF) factor, and the total RSF is the sum of the weighted amounts added to the amount of OBS activity (or potential liquidity exposure) multiplied by its associated RSF factor.
  2. The RSF factors assigned to various types of assets are intended to approximate the amount of a particular asset that would have to be funded, either because it will be rolled over, or because it could not be monetized through sale or used as collateral in a secured borrowing transaction over the course of one year without significant expense. Under the standard, such amounts are expected to be supported by stable funding.
  3. Assets should be allocated to the appropriate RSF factor based on their residual maturity or liquidity value. When determining the maturity of an instrument, investors should be assumed to exercise any option to extend maturity. For assets with options exercisable at the bank’s discretion, reputational factors should be taken into account that may limit a bank’s ability not to exercise the option. In particular, where the market expects certain assets to be extended in their maturity, banks should assume such behaviour for the purpose of the NSFR and include these assets in the corresponding RSF category. For amortizing loans, the portion that comes due within the one-year horizon – should be treated in the less-than-one-year residual maturity category.
  4. For purposes of determining its RSF, a bank should (i) include financial instruments, foreign currencies and commodities for which a purchase order has been executed, and (ii) exclude financial instruments, foreign currencies and commodities for which a sales order has been executed, even if such transactions have not been reflected in the balance sheet under a settlement-date accounting model, provided that (i) such transactions are not reflected as derivatives or secured financing transactions in the institution’s balance sheet, and (ii) the effects of such transactions will be reflected in the institution’s balance sheet when settled.

### **Encumbered assets**

* 1. Assets on the balance sheet that are encumbered for one year or more receive a 100 percent RSF factor. Assets encumbered for a period of between six months and less than one year that would, if unencumbered, receive an RSF factor lower than or equal to 50 percent -. Assets encumbered for between six months and less than one year that would, if unencumbered, receive an RSF factor higher than 50 percent retain that higher RSF factor. Where assets have less than six months remaining in the encumbrance period, those assets may receive the same RSF factor as an equivalent asset that is unencumbered.

### 

### **Secured financing transactions**

* 1. For secured funding arrangements, use of balance sheet and accounting treatments should generally result in banks excluding, from their assets, securities which they have borrowed in securities financing transactions (such as reverse repos) where they do not have beneficial ownership. In contrast, banks should include securities they have lent in securities financing transactions where they retain beneficial ownership. Where banks have encumbered securities in repos or other securities financing transactions, but have retained beneficial ownership and those assets remain on the bank’s balance sheet, the bank should allocate such securities to the appropriate RSF category.
  2. Securities financing transactions with a single counterparty may be measured net when calculating the NSFR, provided that the netting conditions are met[[4]](#footnote-4).

### **Calculation of derivative asset amounts**

* 1. Derivative assets are calculated first based on the replacement cost for derivative contracts (obtained by marking to market) where the contract has a positive value.
  2. In calculating NSFR derivative assets, collateral received in connection with derivative contracts may not offset the positive replacement cost amount, regardless of whether or not netting is permitted under the bank’s operative accounting or risk-based framework, unless it is received in the form of cash variation margin. Any remaining balance sheet liability associated with (a) variation margin received that does not meet the criteria above or (b) initial margin received may not offset derivative assets and should be assigned a 0 percent ASF factor.

### **Assets assigned a 0 percent RSF factor**

* 1. Assets assigned a 0 percent RSF factor comprise:

1. coins and banknotes immediately available to meet obligations;
2. all central bank reserves (including required reserves and excess reserves); and
3. all claims on central banks with residual maturities of less than six months.

### **Assets assigned a 5 percent RSF factor**

* 1. Assets assigned a 5 percent RSF factor comprise unencumbered Level 1 assets as defined in LCR guideline, excluding assets receiving a 0 percent RSF as specified above, and including:
* marketable securities representing claims on or guaranteed by sovereigns, central banks, PSEs, the International Monetary Fund, the European Central Bank and the European Community, or multilateral development banks that are assigned a 0 percent risk weight under the Basel II/II capital framework for credit risk; and
* certain non-0 percent risk-weighted sovereign or central bank debt securities as specified in the LCR guideline.

### 

### **Assets assigned a 10 percent RSF factor**

* 1. Unencumbered loans to financial institutions with residual maturities of less than six months, where the loan is secured against Level 1 assets as defined in the LCR guideline, and where the bank has the ability to freely rehypothecate the received collateral for the life of the loan.

### **Assets assigned a 15 percent RSF factor**

* 1. **Assets assigned a 15 percent RSF factor comprise:**

1. unencumbered Level 2A assets as defined in the LCR guideline, including:
   * marketable securities representing claims on or guaranteed by sovereigns, central banks, PSEs or multilateral development banks that are assigned a 20 percent risk weight under the Basel II/III capital framework for credit risk; and
   * corporate debt securities (including commercial paper) and covered bonds with a credit rating equal or equivalent to at least AA–;
2. all other unencumbered loans to financial institutions with residual maturities of less than six months not included in paragraph 2.28

### **Assets assigned a 50 percent RSF factor**

* 1. Assets assigned a 50 percent RSF factor comprise:

1. unencumbered Level 2B assets as defined and subject to the conditions set forth in the LCR Guideline, including:
   * residential mortgage-backed securities (RMBS) with a credit rating of at least AA;
   * corporate debt securities (including commercial paper) with a credit rating of between A+ and BBB–; and
   * exchange-traded common equity shares not issued by financial institutions or their affiliates;
2. any HQLA as defined in the LCR Guideline that are encumbered for a period of between six months and less than one year;
3. all loans to financial institutions and central banks with residual maturity of between six months and less than one year;
4. deposits held at other financial institutions for operational purposes, as outlined in the LCR guideline, that are subject to the 50 percent ASF factor in paragraph 2.14 and
5. all other non-HQLA not included in the above categories that have a residual maturity of less than one year, including loans to non-financial corporate clients, loans to retail customers (ie natural persons) and small business customers, and loans to sovereigns and PSEs.

### 

### **Assets assigned a 65 percent RSF factor**

* 1. Assets assigned a 65 percent RSF factor comprise:

1. unencumbered residential mortgages with a residual maturity of one year or more that would qualify for a 50 percent or lower risk weight under the Basel II/III capital framework; and
2. other unencumbered loans not included in the above categories, excluding loans to financial institutions, with a residual maturity of one year or more that would qualify for a 50 percent or lower risk weight under the Basel II/III capital framework.

### **Assets assigned an 85 percent RSF factor**

* 1. Assets assigned an 85 percent RSF factor comprise:

1. cash, securities or other assets posted as initial margin for derivative contracts. Where securities or other assets posted as initial margin for derivative contracts would otherwise receive a higher RSF factor, they should retain that higher factor.
2. other unencumbered performing loans that do not qualify for the 50 percent or lower risk weight under the Basel II/III capital framework and have residual maturities of one year or more, excluding loans to financial institutions;
3. unencumbered securities with a remaining maturity of one year or more and exchange- traded equities, that are not in default and do not qualify as HQLA according to the LCR guideline; and
4. physical traded commodities, including gold.

### **Assets assigned a 100 percent RSF factor**

* 1. Assets assigned a 100 percent RSF factor comprise:

1. all assets that are encumbered for a period of one year or more;
2. NSFR derivative assets as calculated according to paragraphs 2.24 and 2.25 net of NSFR derivative liabilities as calculated according to paragraph 2.8, if NSFR derivative assets are greater than NSFR derivative liabilities;
3. all other assets not included in the above categories, including non-performing loans, loans to financial institutions with a residual maturity of one year or more, non-exchange-traded equities, fixed assets, items deducted from regulatory capital, retained interest, insurance assets, subsidiary interests and defaulted securities; and
4. 20 percent of derivative liabilities (ie negative replacement cost amounts) as calculated according to paragraph 2.8 (before deducting variation margin posted).
   1. Table 2 summarizes the specific types of assets to be assigned to each asset category and their associated RSF factor.

**Table 2. Summary of asset categories and associated RSF factors**

| **RSF factor** | **Components of RSF category** |
| --- | --- |
| 0 percent | * Coins and banknotes * All central bank reserves * All claims on central banks with residual maturities of less than six months |
| 5 percent | * Unencumbered Level 1 assets, excluding coins, banknotes and central bank reserves |
| 10 percent | * Unencumbered loans to financial institutions with residual maturities of less than six months, where the loan is secured against Level 1 assets as defined in LCR Guideline, and where the bank has the ability to freely rehypothecate the received collateral for the life of the loan |
| 15 percent | * All other unencumbered loans to financial institutions with residual maturities of less than six months not included in the above categories * Unencumbered Level 2A assets |
| 50 percent | * Unencumbered Level 2B assets * HQLA encumbered for a period of six months or more and less than one year * Loans to financial institutions and central banks with residual maturities between six months and less than one year * Deposits held at other financial institutions for operational purposes * All other assets not included in the above categories with residual maturity of less than one year, including loans to non-financial corporate clients, loans to retail and small business customers, and loans to sovereigns and PSEs |
| 65 percent | * Unencumbered residential mortgages with a residual maturity of one year or more and with a risk weight of less than or equal to 50 percent under the Basel II/II Capital Framework. * Other unencumbered loans not included in the above categories, excluding loans to financial institutions, with a residual maturity of one year or more and with a risk weight of less than or equal to 50 percent under the Basel II/II Capital Framework. |
| 85 percent | * Cash, securities or other assets posted as initial margin for derivative contracts and cash or other assets provided to contribute to the default fund of a CCP * Other unencumbered performing loans with risk weights greater than 50 percent under the Basel II/II Capital Framework and residual maturities of one year or more, excluding loans to financial institutions * Unencumbered securities that are not in default and do not qualify as HQLA with a remaining maturity of one year or more and exchange-traded equities * Physical traded commodities, including gold |
| 100 percent | * All assets that are encumbered for a period of one year or more * NSFR derivative assets net of NSFR derivative liabilities if NSFR derivative assets are greater than NSFR derivative liabilities * 20 percent of derivative liabilities as calculated according to 2.8 * All other assets not included in the above categories, including non-performing loans, loans to financial institutions with a residual maturity of one year or more, non-exchange-traded equities, fixed assets, items deducted from regulatory capital, retained interest, insurance assets, subsidiary interests and defaulted securities |

### 

### **Off-balance sheet exposures**

* 1. Many potential OBS liquidity exposures require little direct or immediate funding but can lead to significant liquidity drains over a longer time horizon. The NSFR assigns an RSF factor to various OBS activities in order to ensure that institutions hold stable funding for the portion of OBS exposures that may be expected to require funding within a one-year horizon.
  2. Consistent with the LCR, the NSFR identifies OBS exposure categories based broadly on whether the commitment is a credit or liquidity facility or some other contingent funding obligation. Table 3 identifies the specific types of OBS exposures to be assigned to each OBS category and their associated RSF factor.

**Table 3. Summary of off-balance sheet categories and associated RSF factors**

|  |  |
| --- | --- |
| **RSF factor** | **RSF category** |
| 5 percent of currently undrawn portion | * Irrevocable and conditionally revocable credit and liquidity facilities to any client |
| 5 percent of currently undrawn portion | * Trade finance-related obligations (including guarantees and letters of credit) |
| 10 percent of currently undrawn portion | Other contingent funding obligations, including products and instruments such as:   * Unconditionally revocable credit and liquidity facilities * Guarantees and letters of credit unrelated to trade finance obligations * Other Non-contractual obligations 10 percent |

# **APPLICATION ISSUES FOR THE NSFR**

## Frequency of calculation and reporting

1. Banks are expected to meet the NSFR requirement on an ongoing basis. The NSFR should be reported semi-annually.

## Scope of application

1. The application of the requirements in this document follows the existing scope of application of the Capital Framework. The NSFR Guideline should be applied to banks on a consolidated basis.
2. A bank should actively monitor and control liquidity risk exposures and funding needs at the level of individual legal entities, foreign branches and subsidiaries, and the group as a whole, taking into account legal, regulatory, and operational limitations to the transferability of liquidity.

## Transitional arrangements

## CBK to advise the banking sector on the transitional arrangements.

1. This could reflect a case where a bank may imply that it would be subject to funding risk if it did not exercise an option on its own funding [↑](#footnote-ref-1)
2. NSFR derivative liabilities = (derivative liabilities) – (total collateral posted as variation margin on derivative liabilities). [↑](#footnote-ref-2)
3. To the extent that the bank’s accounting framework reflects on-balance sheet, in connection with a derivative contract, an asset associated with collateral posted as variation margin that is deducted from the replacement cost amount for purposes of the NSFR, that asset should not be included in the calculation of a bank’s required stable funding (RSF) to avoid any double-counting. [↑](#footnote-ref-3)
4. See BCBS: p.33i of “Basel III leverage ratio framework and disclosure requirements”, January 2014 [↑](#footnote-ref-4)