What is the Liquidity Coverage Ratio (LCR)?

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About Liquidity Coverage Ratio (LCR):

- It refers to the **proportion of highly liquid assetsheld by financial institutions** to ensure that they maintain an ongoing ability **to meet their short-term obligations** (i.e., **cash outflows for 30 days**).
    - 30 days was selected because, in a financial crisis, a response from governments and central banks would typically take around 30 days.
- It is intended to **make surethat banks** and financial institutions **have a sufficient level ofcapital to ride out** any **short-term disruptions to liquidity**.
- LCR in banking **resulted from the Basel III agreement**, which is a series of measures undertaken **by the Basel Committee on Bank Supervision(BCBS).**
- In India, RBI issued Basel III liquidity guidelines in 2012.
- **RBI implemented LCR in January 2015**, and as per a circular in 2020, banks should maintain sufficient HQLA at all times to meet unexpected withdrawals.
- **Calculation:**

- **LCR = (High Quality Liquid Assets (HQLA)) / (Total net cash outflows over the next 30 calendar days)**
- **Every asset** that can be easily and **instantly converted into cash** at minimum or no cost of value **is a HQLA**.
- These assets **include cash, reserves with central banks**, and central government **bonds**, which can easily be converted into cash.
- **In India, all Statutory Liquidity Ratio (SLR) eligible assets**, which need to be maintained by the banks as per the Banking Regulation Act, 1949, are **permitted to be considered HQLA under LCR requirements if they are in excess.** This helps maintain and optimise both liquidity requirements.

Q1: What is Statutory Liquidity Ratio (SLR)?

Statutory Liquidity Ratio or SLR is a minimum percentage of deposits that a commercial bank has to maintain in the form of liquid cash, gold or other securities. It is basically the reserve requirement that banks are expected to keep before offering credit to customers. These are not reserved with the Reserve Bank of India (RBI), but with banks themselves. The SLR is fixed by the RBI.

Source: Banking Central | RBI’s proposed norms on LCR could be a dampener for some banks

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