

RBI Revises Leverage Ratio Framework for Banks

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Why in News?

Recently, the RBI has revised its capital adequacy framework to align with the global standards established by the Basel Committee on Banking Supervision (BCBS).

- The revised leverage ratio norms are scheduled to take effect on 1 April 2027.
- The RBI declined requests from banks to extend the implementation timeline.
- **Objective** - To strengthen banks' balance sheets and enhance their capacity to absorb financial losses.

Key Features of the Revised Framework		
Feature	Details	
 Implementing authority	Reserve Bank of India	
 Global framework	Basel III	
 Effective date	1 April 2027	
 Domestic Systemically Important Banks (D-SIBs)	Minimum leverage ratio of 4%	
 Other banks	Minimum leverage ratio of 3.5%	
 Compliance requirement	Minimum ratio must be maintained at all times	
 Calculation frequency	At the end of every quarter	
 Alternative calculation	Daily or monthly averages, with RBI approval	

Leverage Ratio

- The leverage ratio quantifies a bank's capital in relation to its total exposure, without adjusting for the risk profile of individual exposures.

Leverage Ratio

$$\text{Leverage Ratio} = \frac{\text{Capital Measure}}{\text{Exposure Measure}} \times 100$$



Revised framework effective **1 April 2027**: minimum leverage ratio
4% for Domestic Systemically Important Banks (D-SIBs) and
3.5% for other banks.

Based on RBI's October 23, 2026 final amendment directions.

- **Capital measure** - It refers to the eligible capital recognized under the relevant Basel III framework.
 - **Exposure measure** - It denotes the bank's total exposure, encompassing both on-balance-sheet and off-balance-sheet items.
- For example, if a bank possesses eligible capital of Rs.4 crore and a total exposure of Rs.100 crore, its leverage ratio would be 4%.
- A higher leverage ratio typically reflects a more robust capital buffer relative to the bank's total exposure.

Leverage Ratio vs Risk-Weighted Capital Adequacy Ratio

Basis	Leverage ratio	Risk-weighted capital ratio
Nature	Non-risk-based	Risk-based
Calculation	Capital ÷ total exposure	Eligible capital ÷ risk-weighted assets
Treatment of assets	Generally, does not differentiate by risk weight	Assigns different risk weights to exposures
Purpose	Limits excessive leverage	Ensures capital is proportionate to assessed risks
Role	Acts as a backstop to risk-based requirements	Main framework for measuring risk-based capital adequacy

Components of Total Exposure

The revised framework encompasses multiple categories of banking exposure.

- **On-balance-sheet assets** - It includes loans, investments, and other recognised assets.
- **Derivatives** - It refers to exposures that arise from financial contracts.
- **Securities financing transactions** - It includes activities such as repurchase agreements (repos) and securities lending.
- **Off-balance-sheet commitments** - It comprises relevant guarantees, credit

commitments, and other contingent exposures.

Treatment of Collateral and Guarantees

- Banks are not permitted to reduce the leverage exposure measure by using physical or financial collateral.
- Guarantees and credit-risk mitigation techniques are not permitted to reduce reported exposure.
- Assets and liabilities may only be netted when explicitly permitted by the framework.

Rationale for the RBI's Tightening of Regulatory Norms

- **Enhancement of financial stability** - Strengthens banks' capacity to absorb unexpected losses.
- **Limitation of excessive borrowing** - Prevents banks from expanding their balance sheets disproportionately relative to their capital.
- **Alignment with Basel III** - Reinforces the prudential framework for banking supervision.
- **Addressing measurement gaps** - Discourages transactions or structures that may understate leverage.
- **Protection of depositors** - Reduces the likelihood that excessive leverage will threaten bank solvency.
- **Systemic risk management** - Imposes a higher minimum leverage ratio on domestic systemically important banks.

Special Powers of the RBI

- The RBI may undertake supervisory action if a bank employs transactions or structures that inadequately capture its sources of leverage.
- The RBI may, at its discretion, temporarily exempt central bank reserves from the exposure measure.
- The RBI may increase the minimum leverage ratio calibration when necessary to support the transmission of monetary policy.
- These provisions provide the RBI with flexibility to address emerging risks and specific monetary policy considerations.

Reference

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