



**TOPICS:**

**Banking System**

**SOURCE:**

**International Monetary Fund**

## IMF: Prudential Capital Requirements for Banks - Buffers and the Pillar 2 Capital Assessment

- The note provides a **comprehensive overview** of the evolution, structure and implementation of bank capital regulation under the Basel III framework, with a focus on **capital buffers and Pillar 2** supervisory processes. This **Basel III framework** enhances both the quality and quantity of capital, prioritizing Common Equity Tier 1 (CET1) as the primary loss-absorbing component, while introducing additional safeguards such as leverage ratios and macroprudential buffers.
- A central theme is the role of **capital buffers** as macroprudential tools. The **Capital Conservation Buffer (CCB)** ensures banks maintain a baseline cushion (2.5% of RWAs) and imposes distribution constraints when breached. The **Countercyclical Capital Buffer (CCyB)** is time-varying, designed to build resilience during periods of excessive credit growth and be released during downturns to sustain lending. Additional buffers apply to systemically important institutions (G-SIBs and D-SIBs), reflecting their higher systemic risk. The paper also discusses innovations such as **sectoral buffers** and **positive neutral CCyB approaches**,

which aim to enhance flexibility and responsiveness to evolving financial cycles.

- The note emphasizes that buffers are **complementary to Pillar 2**, not substitutes. While buffers address system-wide risks, **Pillar 2 (Supervisory Review Process)** provides a forward-looking, bank-specific assessment of risks not fully captured under Pillar 1. Through tools such as the Internal Capital Adequacy Assessment Process (ICAAP), stress testing and supervisory judgment, regulators can impose additional capital requirements or qualitative measures tailored to individual institutions.
- **Implementation challenges are particularly relevant** for emerging market and developing economies, where proportionality, institutional capacity and legal frameworks influence adoption. The note highlights the need for flexibility, coordination among authorities, and clear supervisory frameworks to ensure effective deployment of both buffers and Pillar 2 tools.

