HOUSE OF REPRESENTATIVES STANDING COMMITTEE ON ECONOMICS

REVIEW OF THE FOUR MAJOR BANKS (FIFTH HEARINGS)

Commonwealth Bank of Australia

CBA04QON: Page 20

Mr CRAIG KELLY: Let's take this example: there's a million-dollar loan to a particular company or business. You're holding $1.5 million in security. Can you give me some numbers on what that additional cost would be? What does it look like from your perspective? You have to hold additional capital. How much would it be for that million-dollar loan?

Mr Comyn: [This] is where it may get complicated... I will happily, on notice, give you a couple of examples.

Answer: We comply with Australian Prudential Regulation Authority (APRA) capital adequacy rules. Under APRA rules[1], the capital requirements for loans in default are substantially higher than an equivalent performing loan.

Using the example of a $1 million defaulted SME Retail loan that is well secured, the regulatory capital requirement for this loan ($286,200 from table 1) is in excess of 500% higher than the portfolio average for CBA SME Retail loans ($55,512 from table 2).

Table 1. Illustrative regulatory capital requirements for $1 million defaulted non-specialised loan by security position, assuming no provisions are raised.

Security Position	Regulatory Loss Given Default[2]	Risk Weight	Regulatory Capital Requirement
Well Secured	20%	265%	$286,200
Partially Secured	40%	530%	$572,400
Unsecured	60%	795%	$858,600

[1] APRA's Internal Ratings Based (IRB) approach to credit risk described in Australia Prudential Standard (APS) 113. Vast majority (95%+) of CBA credit risk requirements are calculated under APS 113.

[2] Under the IRB approach, Loss Given Default (LGD) is a bank's internal estimate based on historical experience of the actual loss the bank would incur after any security is sold or otherwise realised. LGD values in the table are for illustrative purposes.

Table 2. CBA portfolio average regulatory capital requirement as at December 2018 on an $1m loan

CBA Portfolio	Portfolio Average Risk Weight[3]	Average Regulatory Capital Requirement
Mortgages	25.1%	$27,108
SME Retail	51.4%	$55,512
SME Corporate	55.2%	$59,616

[3] Risk weight is a reflection of risk measured under APRA's regulatory capital framework. Risk weights are a factor in determining how much capital must be held by a bank.
For example, assets where the risk of loss from non-repayment is low, such as Australian Government securities, receive a low risk weight, while assets with high exposure to loss, such as loans already in arrears, receive high risk weights.