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THE PREMISES AND EVALUATION OF NEW REGULATIONS AIMING AT LIMITING RISK IN THE BANKING SECTOR

Summary

This paper will aim at proving that the introduction of the reforms known as Basel III considerably eliminates the deficits of the Basel regulations from 2004, but will result in lower availability of loans for bank clients and will slow down the economic development.

The article consists of three sections. The first part presents the role and challenges facing banks in times of crisis. In the second part special attention has been paid to the main assumptions of the changes proposed by the Basel Committee on Banking Supervision. The third chapter focuses on analyzing the predicted influence of Basel III on economy and banks operating in Poland and all over the world.

1. Introduction

Prudential standards, shaping for example the required capital level of the banks, should provide access to bank credit for their clients, but also should make banks more resistant to crises.

The aim of this paper is to present the reforms and intended shape of regulations aiming at changing the capital requirements and introducing liquidity norms as an element of the first pillar of capital contract. From various proposals of improving the effectiveness of regulations for the finance sector, special attention should be paid to the concept of solutions for the banking sector presented in 2010 by Basel Committee on Banking Supervision (the so-called Basel III).

The author expects that the proposed reforms of prudential standards in the banking sector, known as Basel III, require further changes, as they contain many unsolved issues necessary for proper operations of the banking sector.

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2. Challenges for banks in times of crisis in finance markets and economy

The banking sector play a special role in economy. Specialist literature distinguishes three main arguments for the existence of banks [Marcinkowska, Gdańsk 2009, p.15]:

- transaction costs – banks provide services of risk sharing and transformation, which borrowers would not afford alone due to transaction costs,
- asymmetry of information – while collecting market information concerning the needs of potential depositors and borrowers, banks have a better possibility of conducting monitoring services,
- depositors and borrowers liquidity preference – banks create liquidity, making transactions of illiquid assets into liquid liabilities.

In this way banks, by gathering deposits of business people and individual customers become public trust institutions. We could state that if the banks did not perform the above functions they would not exist. Apart from the role of the depository, banks lend money to households and entrepreneurs, increasing the money circulation. Another argument for the existence of banks is the fact that many entrepreneurs use credit facilities even though other, alternative (and often cheaper) sources of financing exist, because in this way they can inform other market participants about their credit rating[1].

Specific type of transactions, such as trading financial instruments, is associated with huge risk, as financial instruments are based on the promise to perform a certain service in the future. As D. Korenik claims, the bank is held responsible for obtaining an advantage in risk management to its own benefit and to the benefit of its clients and the whole economy [Korenik, Warszawa 2009, p.171]. Bad management of the bank, not taking into account the risk run, may be one of the causes of financial crises, just as faulty macroeconomic policy or current development of the situation in the market. Turbulences in the operations of banks may also be provoked by improper prudential standards or banking supervision. Therefore it is essential to maintain banks' solvency understood as the ability to cover potential losses and risks with their own funds as well as maintaining required liquidity. In order to perform this task it is necessary to create and implement prudential standards.

Specialist literature provides numerous definitions of a financial crisis referring to the banking sector. One of them states that the crisis is a situation in which a considerable number of financial institutions have assets of lower market value than their liabilities. This leads to the run or movements in their portfolios,

1 Explanation in the theory of signals.

bankruptcy of some of them and government interventions [Masiukiewicz, Warszawa 2011, p.22]. It is worth emphasizing the factors which, in the opinion of the European Social and Economic Committee, were the main causes of the global banking and financial crisis of the end of the first decade of the 21st century [Komunikat, COM (2009) 362, Bruksela 2010, p.1]. These were: loans offered by credit institutions to clients without credit rating; improper systems of remunerations and bonuses for employees of credit institutions serving individual clients; establishing credit securities without due care; purchasing the above securities by banks without due care; insufficient capital reserves, especially in portfolios of commercial banks, creating mechanisms of off-balance sheet financing which did not have sufficient capital coverage; existence of distorted incentives and improper remuneration systems which led to short-sighted decisions and excessive risk; pro-cyclical type of regulations; system deficiencies in risk management concerning the quality of owned securities, adequacy of capital reserves and influence of variables of remuneration systems on accumulation of institutional risk; lack of transparency in financial operations of the banks accounting for the fact that creditors, borrowers, contractors, investors and analysts were unable to meet the expectations of financial markets; insufficient scope of macro-prudential supervision and international coordination.

We should also supplement the above list with the role of rating agencies which, evaluating credit risk, had their share in irresponsible creation of toxic assets costing advanced economies hundreds of billions of dollars. Of great significance for the development of the banking system crisis were also the authorities and regulation bodies of particular countries, which accepted the level of capital reserves in their banks. Monetary authorities, especially in the USA, maintained their interest rates on a too low level for too long, which encouraged banks to risk behavior (granting mortgage loans to unreliable customers).

After 2007 once again specialists started worrying about the temptation of abuse created by silent guarantees of capitalizing banks [Ferguson, Kraków 2010, p.360]. It is estimated that the write-off for bad assets since the beginning of the crisis has exceeded 1.3 trillion euro. To cover the losses and improve indicators, banks all over the world gathered 1.1 trillion euro of new capital, vast majority of which came from taxpayers' money [Stypułkowski, Warszawa 2010, p. 93]. The situation of Polish banks looks quite good in comparison. Contrary to G20 advanced economies, where direct public help for financial institutions in 2008-2009 amounted to 3.7% of their 2008 GDP (in Poland this would amount to around 47 billion zlotys), Polish taxpayers did not spend a single zloty on supporting banks. Undoubtedly, the world needs a new bank deal: banking with more capital, less debt, more principles and much stronger supervision [Flejterski, Warszawa 2010, p.151].

Banks are institutions of public trust and in order to perform this role effectively, they must be understandable both to their clients and regulators. New regulations should discourage banks from speculative activities and motivate them to restrict their operations to the services they were established to perform. Greater understanding of the essence of risk by banks and their clients will limit the risk of crisis. The period of 2007-2010 encourages us to think about the direction of prudential standards – many people express an opinion that banks should return to the basics, such as conservative credit policy. The problem is still, however, how to combine the challenges of global economy with the elements that are traditional and limit the possibilities of obtaining additional revenues by the banks. The challenge facing current banking is to find the compromise between expectations of shareholders and bank managers concerning effectiveness with the security of financial means deposited in the banks, clear definition of their operating principles and paying special attention to the ethical dimension of banks' operations. The banking sector in Poland and all over the world will be subject to essential transformations in the nearest future. The direction of these changes will largely depend on trends in global economy, finance and on modifications of prudential standards defined as Basel III.

3. Evolution and principles of new prudential standards

Crises of banks and banking systems are special moments in which changes in regulation areas take place. They show the weaknesses of the existing systems and prudential solutions and force state authorities to introduce new regulations protecting against new crises. New regulations should also minimize their economic effects felt by the society as well as restore public trust in the financial system.

Since 1930s authorities have gradually introduced guidelines regulating the range of banking activities and prudential norms determining the scope of these activities and the degree of risk exposure and risk management. Special attention in these regulations was paid to the issue of bank capital which is the source of financing their activities and the axis of prudential regulations for banks. Fortifying financial institutions with a large number of legal regulations (including prudential norms) results mainly from high bankruptcy costs for these institutions and the danger this poses to stability of global markets.

Economic theories offer two explanations for the activities aiming at regulation of financial institutions, including banks. The first ones are the so-called altruistic theories (public benefits) which define regulations as instruments used by the state to increase effectiveness and honesty of the society. The second one is the agency cost theory, which says that in multi-party relations conflicts and coordination problems grow, therefore introduction of regulations allows one

sector of the society (economy) to grow at the expense of other sectors. The basis of regulations then is imbalance between social and private revenue from assets (risk) which may encourage bank owners and managers to involve in excessive risk [Marcinkowska, Gdańsk 2009, p.72].

Subject literature usually gives two basic reasons for the introduction of prudential regulations in banks, namely: the necessity of protecting depositors and provision of security and solidity of the financial system. Regulation of financial entities concerns mostly [Marcinkowska, Gdańsk 2009, p.72]: licensing their activities, restricting free use of bank shares; limiting types of performed activities; limiting risk (dependent on the value of possessed own equity); creating and operating the system of guaranteed deposits; introducing special accounting principles and the obligation to disclose information on the activities and financial results of the banks; possibility of controlling banks by supervisory institutions and exerting pressure on them.

The implementation of regulations brings some direct costs – costs of regulations and costs that obliged entities must incur in order to observe these regulations. We could also mention here social costs connected with the limitations imposed by banks, such as changing interest rates (increase) and deposits (decrease).

We should also observe certain specificity of regulators – banks relations. Regulators take up activities aiming at introducing new restrictions to the financial system (controlling the risk, products, scope of activity), while banks, intent on achievement of their objectives (for example increased value for shareholders, increased profits) are busy looking for ways of avoiding restrictions. Economic entities act faster than public institutions, therefore they usually succeed in avoiding restrictive regulations, which leads to further attempts at tightening the policy by regulators. Therefore the regulation process is continuous.

Although financial markets are increasingly interconnected, the international system of financial regulation is based on the sector approach (for example banking, securities markets, insurance). There are many institutions which have great impact on the sphere of regulations and the shape of financial infrastructure influencing the real economic sphere. We could list here such institutions as: International Monetary Fund, Financial Stability Forum, European Banking Authority[2], supervisory authorities of particular countries [Davies, Green, Warszawa 2010, p.149]. However, special role in the banking sector is played by the so-called concordats (or agreements) determining equity requirements published by the Basel Committee on Banking Supervision (Basel Committee).

2 Since 2011 the powers of the Committee of European Banking Supervisors (CEBS) were taken over by the European Banking Authority (EBA). It will have greater influence on the shape of the market than CEBS. It was assumed that the new system will guarantee uniform use of the Union law and will become a place of coordination for supervisory actions, especially in crisis situations. The resolutions of the agency are to be binding for national supervisors in case of a dispute between them. EBA is also to identify risk for the benefit of stability of European banking sector.

It conducts work on standardization of supervisory regulations and determination of required level of bank's own funds. The Basel concepts – further proposals of the so-called agreements, arrangements or concordats – are discussed by a wide group of regulators, bankers and scientists [Marcinkowska, Gdańsk 2009, p.86].

In 1988 the Basel Committee on Banking Supervision developed a document called Capital Accord (Basel I). The document determined principles of establishing minimum levels of banks' own funds and assuring better conditions for competition between banks operating in the international market. The solutions adopted then concerned mainly credit risk, which had long been the basic type of risk threatening banks' security. Changing environment of the banking sector as well as great changeability of financial markets account for the necessity of taking into account market and operational risk in measuring capital adequacy. Due to a number of wide gaps, the Capital Accord soon became subject of criticism from banking, academic and private sectors.

The answer to this criticism was the document called "International Convergence of Capital Measurement and Capital Standards", known as the New Capital Accord (NCA or Basel II), which was based on more modern methods and tools of risk management. The essence of the New Capital Accord consists in three pillars constituting an integrated package which should be implemented in particular countries: pillar 1 – minimum capital requirements, pillar 2 – supervisory review, pillar 3 – market discipline.

Within the first pillar, banks were obliged to maintain capital adequacy on the level determined in the NCA. The measure of capital adequacy is associated with determining what capital or defined own funds a bank should possess to make its activities secure. NCA kept the requirements concerning the minimum level of banks' solvency ratio at 8%. At the same time it was decided that bank's own funds should be sufficient to cover credit and market risk and, additionally, operational risk.

In the European Union, the issues of banking activities and banking supervision are regulated by directives 2006/48/EC, 2006/49/EC and 2007/64/EC amended by directive 2009/111/EC as regards banks affiliated to central institutions, certain own funds items, large exposures, supervisory arrangements and crisis management.

Currently the European Union is preparing to implement new banking regulations. In July 2011 the European Commission is to present the draft of a directive introducing recommendations made by the Basel Committee on Banking Supervision in the European Union. The Committee presented a wide range of new requirements for banks. Compared with the currently valid regulations, Basel III introduces a number of innovations and goes in two directions. One is change of capital requirements, the other – introduction

of liquidity norms as an element of the first pillar of capital accord. The above proposals cover:

- raising the quality, consistency and transparency of banks' capital base,
- taking into account a wider spectrum of risk the bank is exposed to (for example commercial portfolio, off-balance items),
- supplementing adequacy ratio with leverage ratio, which is to enable the limitation of the consequences of the process consisting in quick fall of bank assets prices, which is harmful to banks and the whole economy,
- reducing pro-cyclicality and promoting anti-cyclical capital surplus – the dependence of credit reliability of financial institutions and companies outside this sector on the economic cycle causes, due to introduction of methods of calculating capital requirements proposed by NCA, that in times of economic prosperity banks are less burdened with capital requirements, while in times of recession, requirements are higher. Banks are obliged then to maintain higher level of capital and, due to deteriorating client ratings, must slow down credit activity or sell assets. The growing cost of maintaining capital increases the cost of credit, reducing its availability and aggravating bad economic situation.

These changes will be gradually introduced until 2019. Also banks' assets will be subject to tighter control, which is to eliminate creation of investment transactions outside balance sheets. Before the crisis, banks kept some of their assets in various investment funds and in this way they could keep less capital. All these regulations aim at better protection of banks against losses incurred in times of crisis.

New capital requirements modify not only the quality but also the quantity of required capital. Basel III states that while preserving the old general level of obligatory own funds at 8% of risk-weighted assets, by 2015 banks will be obliged to increase the size of required equity (*Common Equity Tier 1 – CET 1*[3]) to the level of at least 4.5% of their assets, which is 2.5% more than the present level. In the same period banks should also increase required capital funds (*Tier 1 Capital*[4]*)* from 4% to 6% in 2015, the remaining 2% may be covered by additional own funds (*Tier 2 Capital*) so as to preserve the required 8% ratio all the time. Financial institutions will have to take into account capital requirements increasing because of deteriorating credit rating of a contracting party. These requirements will also be increased in case of the so-called bad direction of risk, when the probability of insolvency is positively correlated with the size of the investment [Sikorzewski, Warszawa 2011, p. 15].

3 Mostly own shares, undistributed profits and on some conditions, minority shares in the equity of related companies.

4 Tier 1 capital will include some hybrid instruments.

Basel III introduces additional security mechanisms, such as: safety and anti-cyclical buffers. The safety buffer will be gradually introduced from the level of 0.625 of risk-weighted assets in 2016 to the level of 2.5% in 2019. Another important assumption is the fact that this buffer may only be covered by CET 1 funds. In case banks fail to meet this requirement, they will be subject to certain restrictions, such as lower bonuses for their boards. It should be emphasized that this buffer is not identical with own funds within Tier 2 Capital. Banks will have to maintain the capital security buffer in the amount of 2.5% of their assets and the capital ranging from 0 to 2.5% of their assets depending on the economic situation and the decision of a national supervisory authority. It will be built in economic boom periods and reduced in times of economic slow-down.

New regulations also stipulate the introduction of prudential measures concerning financial leverage and liquidity norms. The introduction of financial leverage ratio aims at avoiding excessive use of this leverage in times of economic boom, which could lead to considerable deleverage and breakdown of credit activity in crisis times. The Basel Committee is treating it as a minimum capital requirements ratio in comparison to measures based on risk0weighted assets. This ratio will compare own capital (*Tier 1*) with un-weighted value of all net exposures, including some off-balance elements [Sikorzewski, Warszawa 2011, p. 16]. Initially, to test it, it is planned to introduce this ratio at the level of 3% in 2013-2017, and then to make it obligatory.

Also new requirements concerning financial institutions short- and long-term liquidity are being proposed. The latest crisis has clearly demonstrated that the bank affected by liquidity crisis may become insolvent very quickly. If customers withdraw their money, it is forced to sell its assets. If these assets are not very liquid, it sells them at lower and lower prices. At some point the value of its assets is exceeded by the value of its liabilities. Such mechanism threatens mostly the institutions which borrow money for a short time to purchase assets with long-term maturity. The Basel Committee is proposing introduction of two requirements. The first one – liquidity cover ratio (LCR) states that every bank should keep sufficient amount of liquid assets[5], to secure financing for the period of 30 days of a potential liquidity crisis. A thirty-day outflow of net monetary means reflects the situations of serious financial shock, mass outflow of deposits and lowering credit rating by three classes. In order to secure stable financing in a longer period of time it is also proposed to control the assets and liabilities liquidity features by net funding stability ratio (NFSR) NFSR forces banks to finance their long-term assets, such as mortgage loans, with liabilities due after one year. According to the accepted

5 Instruments of low correlation with risky assets, traded in active and stable markets in presence of market animators and characterized by low concentration of buyers and sellers.

solution, available sources of stable financing[6] are supposed to cover at least the required means of stable financing[7].

4. The areas of applying new prudential regulations and assessment of potential financial implications for banks and their clients

Currently work on improving prudential regulations is conducted all over the world, which is the consequence of gaps and mistakes diagnosed during the financial crisis. Also work on the new Basel III is approaching its end at the Basel Committee on Banking Supervision, which is the main institution dealing with banking regulations globally. It is vital that new regulations are implemented in a coordinated and coherent way, which will allow us to avoid disturbances in financial markets, competition or regulatory arbitration. The aim of the reform is to improve the ability of the banking sector to deal with the shocks resulting from financial and economic difficulties, irrespective of their source, and by doing this, to lower the risk of negative influence of the banking sector on real economy. [Basel III: A global regulatory framework for more resilient banks and banking systems, Basel 2011, p.9].

The agreements issued by the Basel Committee are not legally binding; their aim is to create common supervision standards promoting attempts at developing a common approach and facilitating harmonization of conditions of competition for banks conducting international operations. In the USA the latest reforms are included in the so-called Dodd-Frank Act. In case of the EU legislation, the implementation of the Committee guidelines will be transposed by the so-called CRD IV Directive, developed by the European Commission. It is a legal tool implementing new regulations in the European Union. The directive is mostly compliant with the Basel regulations, however it reflects the EU specificity [Didenkow, Warszawa 2011, p. 24]. Particular countries will be introducing different regulations (they have the freedom of choice and the freedom of implementation), moreover, financial systems in various regions of the world possess specific features which may matter in assessment of the effects of proposed changes. So far some research has been conducted, aiming at assessing the influence of Basel III on banks and economy.

As J. Zombirt claims, the impact of new regulations on banks may be considered in three areas [Zombirt, Warszawa 2011, p. 20]:

6 Own funds - Tier 1 and Tier 2, long-term liabilities and appropriately weighted liabilities to stable individual depositors and enterprises

7 Properly weighted maturity of loans provided for individual clients and enterprises, as well as bank investments in financial instruments.

- specific influence on the balance on the level of a banking enterprise, which cannot be attributed to any business lines, for example deductions for regulatory capital – in various ways they will concern balance sheets of particular banks, depending on possessed assets, but they will not particularly influence their activities,
- general influence on all banks and business lines – for example new capital requirements and leverage ratios will proportionally influence the whole activity of banks. The impact of these regulations will be mostly visible in business activity bringing relatively low income, but this will negatively influence the whole business activity (assuming that increased costs will not be transferred on customers),
- influence on specific types of activity – we could mention here new regulations concerning risk-weighted assets, liquidity and long-term financing – these are to affect reduction of problems revealed by the crisis.

A significant change is the introduction of higher risk weights for financial institutions.

Table 1. Value of planned shortfall of capital and short- and long-term liquidity of European and US banks as a result of introducing new prudential regulations (in trillion euro)

Type of shortfall	Europe	USA	Total
Shortfall of capital	1.1	0.6	1.7
Shortfall of short-term liquidity	1.3	0.6	1.9
Shortfall of long-term liquidity	2.3	2.2	4.5

Source: own elaboration on the basis of: J. Zombirt, Czy to wystarczy, „Bank" 2011, No 2 (calculations on the basis of balance sheet data of selected banks for the 2nd quarter of 2010).

Drawing conclusions from the latest crisis, the Basel Committee stated that the risk of such exposures correlations is much greater that it had been assumed. Table 1 presents the value of planned shortfall of capital and liquidity of European and US banks due to new prudential regulations. As J. Zombirt states (assessing the analyzed shortfalls on the basis of balance sheet data for the 2nd quarter of 2010), the total shortfall of capital will reach 1.7 trillion euro, shortfall of short-term liquidity – 1.9 trillion euro, and shortfall of long-term liquidity – nearly 4.5 trillion euro. According to calculations made by other institutions (for example Ernst & Young) obtaining additional capital by European banks will cause decrease of the ROE ratio in this sector in 2012 by 5% [Zombirt, Warszawa 2011, p. 20].

Analyzing the impact of the Basel III on capital requirements we should mention Quantitative Impact Studies (QIS) conducted by the Basel Committee on Banking Supervision. The aim of the research was to assess the influence of proposed solutions on capital requirements globally. The survey was conducted in 2010 in 263 banks from 23 countries.

Table 2. Solvency ratio at different counters reflecting target regulations of Basel III (banks surveyed by QIS in 2010)

Group of banks	Number of banks in a group	Counter of solvency ratio			
		Equity capital (CET 1)		Primary funds (Tier 1)	
		Level of solvency ratio at a given counter (in percentage)			
		Gross	Net	Basel II	Basel III
Group 1	74	11.1	5.7	10.5	6.3
Group2	133	10.7	7.8	9.8	8.1

Source: own elaboration on the basis of: M. Olszak, Kosztowna Bazylea III, „Bank” 2011, No 4.

Table 2 presents the levels of solvency ratio calculated according to the old method (Basel II) and the new one determined in guidelines accepted by the Basel Committee in 2010. CET 1 is a new ratio, which has not been determined by banks all over the world before (Common equity tier capital ratio: equity capital divided by risk-weighted assets). Gross CET 1 does not reflect deductions from equity capital determined in Basel III, while net CET 1 takes them into account. Tier 1 is an equivalent of the solvency ratios currently provided by banks (relation of primary funds to risk-weighted assets).

The most severe consequences of new prudential regulations will be felt by big international banks. They will witness clearly the biggest decreases of all ratios, contrary to smaller banks, whose ratios will experience lower falls. In case of CET 1 big banks will have net ratios nearly lowered by half in comparison to current ones (fall from 11.1% to 5.7%). CET 1 ratios of smaller banks will not decrease so dramatically, as they will fall from 10.7% to 7.8%. A similar trend can be observed in case of Tier 1 solvency ratios [Olszak, Warszawa 2011, p. 27]. Taking into account the 2009 structure and capitalization of banks and the target need to establish the CET 1 ratio at the level of 7%, in case of analyzed banks this would mean the shortfall of 577 billion euro for the group of big banks, which is 2.5 times the size of their 2009 profits. For smaller banks these figures are respectively 25 billion euro and 1.25 times their annual profits. The study confirms that banks must obtain additional capital by 2019.

It is worth analyzing the impact of new prudential regulations on retail and corporate banking globally. New capital requirements will be felt

particularly by retail banks, which in recent years, have had visibly lower capital ratios than corporate banks. Due to the fact that retail banks use mainly customers' deposits as a source of financing, the influence of new regulations on specific requirements concerning new products will be less visible. The Basel Committee accepted deposits as a source of long-term financing, even with reference to mortgage loans. On this example we can observe strong influence of bankers on regulators, because as late as in July 2010 mortgage loans had to be 100% financed from long-term sources of financing, while currently this coverage must be at least 65%. Corporate banking will suffer most from new requirements concerning new prudential norms. It is expected that long-term corporate loans and long-term financing of assets will be more expensive by 10 base points than now. The cost of credit lines for enterprises and financial institutions will also grow. The costs of other bank products with high risk weight (credit without security, structured financing) will grow significantly, by 60 base points. Planned increase of risk weights for financing commerce will reach 20-30% for financial institutions (for example increased risk weights for letters of credit opened in one bank ordered by another bank).

Researchers from the Basel Committee on Banking Supervision claim that financial and macroeconomic effects of new regulations will be quite limited. In their opinion, banks' financing costs resulting from higher capital requirements, will grow by merely 0.2%. Economic growth will be lower by only 0.03-0.05%. Quite similar calculations were presented by OECD experts. In their view, full implementation of Basel III regulations will increase the costs of credit by 0.15-0.5%, while subsequent economic growth will be lower by 0.15%. [Assessing the macroeconomic impact of the transition to stronger capital and liquidity requirements, Basel 2010]. Quite different calculations were presented by the Institute of International Finance (IIF) from Washington. Experts of this institution claim that the credit costs after full implementation of new regulations may increase by 1.3%, which is three times higher than the OECD calculation. The income loss may also be much greater and reach even 3.8% within four years, which is around 1% each year [www.iif.com].

The introduction of higher solvency ratio will force considerable increases in banks' own funds (especially CET1), which is much more expensive than Tier 1 or 2 own funds. This will cause significant growth of the costs of obtaining capital. This cost will probably be transferred to borrowers, which may worsen their financial situation or limit credit availability in economy. Such situation may negatively influence the GDP dynamic and create turbulences in the labor market. If banks do not obtain appropriate additional own funds, they will have to limit their risk-weighted assets. Experts expect the following behavior of banks caused by new prudential regulations:

- optimization of sources of finance and improvement in balance sheet management,
- verification of business strategies (verifying customer base, geographic scope, strategy of transforming risk and cost reduction, review of business portfolio, including reduction or abandoning some business areas, verification of possibilities of financing them).

As far as banks in Poland are concerned, the implementation of new Basel III regulations may cause difficulties in obtaining means to cover long-term liabilities. The capital market in Poland is quite narrow and there are no regulations concerning the issue of mortgage bonds, an instrument which is used by foreign banks together with capital market bonds. Commercial banks operating in Poland should not have any problems complying with new capital norms. Cooperative banks may face more serious problems, as their shareholders are less willing to capitalize them again. Another challenge will be to gather larger finance due after one year to finance long-term loans. This problem is vital in Poland, where citizens do not show much interest in long-term saving. Therefore it is often emphasized that the introduction of CRD IV Directive in Poland will have to take into account specific features of Polish financial market.

5. Conclusions

New supervisory regulations are introduced in times of great instability of financial markets in the world. This situation makes it difficult to assess the real effects of reform implementation, but, as M. Marcinkowska claims, this situation constitutes a test of effectiveness of new solutions for banks, supervisors and financial markets [Marcinkowska, 2009, p. 524].

The results of the research presented in the article confirm that Basel III may limit credit availability due to increased requirements concerning capital adequacy and liquidity of banks. The consequence of such a solution will be slower economic growth in many countries all over the world. It should be pointed out that stability and safety of banks should be guaranteed not only by appropriate legal regulations but also by common sense, ethical conduct and responsibility of bank owners and managers.

In order to minimize costs, the process of verifying and shaping prudential norms and determining the consequences of their implementation remains the subject of debate among scientists, bankers and supervisory institutions all over the world.

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