Bank Capital Analysis

The Bank Capital Analysis (BCA) presents leverage ratios for U.S. global systemically important banks (G-SIBs), non-U.S. G-SIBs and U.S. large, regional and community banking organizations.[1] By doing so, the BCA provides a horizontal comparison of capital adequacy among banking organizations with different risk profiles.

Adequate capital is critically important for the safety and soundness of banks and overall financial stability. It serves as a buffer against unexpected losses and insolvency, and protects the taxpayer-backed federal safety net for banks. Capital is particularly important for the largest systemically important banking organizations as protection against economy-wide financial instability.

Regulatory capital levels leading up to the 2007-08 financial crisis appeared strong, but proved insufficient. In response, capital rules and measures were revised and new minimum requirements were implemented. While these enhanced capital requirements have increased capital levels and led to a reduction in off-balance sheet exposures, the underlying calculations have become increasingly complex and opaque. In contrast to risk-weighted capital measures, leverage ratio measures – generally defined as equity as a percentage of total assets – are simpler and more transparent, while providing an overall measure of the losses a bank can sustain before becoming insolvent. However, regulatory leverage ratio calculations and requirements vary across jurisdictions and by bank size and complexity.

Asset measurement for G-SIB leverage ratio purposes depends, in part, on the treatment of on- and off-balance sheet items, such as derivatives, securities financing, and commitments. Because these items are often significant in volume and pose enhanced risk, appropriately accounting for them is important for understanding the leverage of G-SIBs. The U.S. supplementary leverage ratio (SLR)/Basel III leverage ratio, which applies to and is reported by G-SIBs, adjusts on- and offbalance sheet exposures for derivatives, securities financing transactions, and commitments. The SLR uses tier 1 capital, which adjusts capital for most intangible assets, as its equity measure. Therefore, as a readily available measurement of financial leverage, the SLR provides a useful comparison of capitalization among G-SIBs. Additionally, it can be compared to the tier 1 leverage ratio for smaller banking organizations, which have negligible exposures to derivatives and securities financing.[2]

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[1] Recognizing that bank financial statements can be challenging to understand even for experts, Thomas Hoenig (former Federal Reserve Bank of Kansas City president and former Vice Chair of the Federal Deposit Insurance Corporation) and Chuck Morris (former Federal Reserve Bank of Kansas City Vice President and Economist) created a semi-annual assessment of capital measures from 2012 to 2017 known as the Global Capital Index (GCI). The Federal Reserve Bank of Kansas City continues this analytical focus with its BCA. We believe this information can assist the public's understanding of capital adequacy as a core component of the bank regulatory framework.

[2] GCI tables produced prior to June 30, 2018 are not directly comparable to BCA tables produced on and after this date. The original GCI included a manually adjusted leverage ratio for U.S. G-SIBs. The numerator used total tangible equity (total equity less goodwill, other intangibles and deferred tax assets). The denominator used total assets less intangibles (goodwill, other intangibles and deferred tax assets) and included the gross amount of derivative contracts.