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**Implementing Basel III in the EU.  
Covid-19 and the Basel framework: emerging lessons**

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The financial turmoil caused by the Covid-19 pandemic is the first global system-wide stress since the finalisation of the Basel III framework. While the pandemic is still far from over, the Basel Committee has started to evaluate the impact of the Basel III reforms on the global banking system and the economy. What early lessons can be drawn thus far?

First, in contrast to the Great Financial Crisis, when banks were a source and propagator of stress, the banking system has thus far remained resilient and has continued to provide core financial services to help cushion the impact of the pandemic on the broader economy.

Two main factors are behind this positive outcome. First, Basel III greatly enhanced the resilience of the global banking system, with banks entering the pandemic with higher levels of truly loss-absorbing capital and liquidity. Better capitalised banks increased lending to households and businesses more than other banks, highlighting the positive impact of higher capital requirements. Banks would have faced greater stress had the initial set of Basel III reforms not been adopted. Second, the unprecedented scale and scope of public sector measures adopted to mitigate the impact of Covid-19, spanning fiscal, monetary and regulatory measures, have largely shielded banks from losses to date.

Second, while the Basel III framework has largely met its objectives thus far, some features may warrant further evaluation. These include the functioning of capital and liquidity buffers, the degree of countercyclicality provided by prudential standards and the treatment of central bank reserves in the leverage ratio. Insufficient empirical evidence to date, coupled with the stabilising impact of public support measures, means that it is not yet possible to make any conclusive assessments as to whether any targeted revisions to the Basel framework are necessary. The Committee will continue to evaluate these issues over the coming year, alongside an evaluation of the broader impact of the initial Basel III reforms during the past decade.

Third, the resilience of the global banking system cannot be taken for granted. As the pandemic continues to unwind, and as public support measures are unwound, additional bank losses could emerge. Rising public and corporate debt levels could increase the longer-term structural fragilities of banks' balance sheets. Additionally, recent vulnerabilities in non-bank financial intermediation (NBFII) have further highlighted the high degree of

interconnectivity between NBFIs and banks; the risk of spillovers to the latter cannot be excluded.

What are my takeaways from these early lessons? First, the implementation of the initial Basel III reforms has produced clear net benefits to the global economy and society more generally. We have collectively reaped the benefits from Basel III during this pandemic. Let us not forget this lesson.

Second, there is unfinished business in implementing Basel III. The outstanding reforms – encompassing a series of standards aimed at enhancing the robustness and credibility of the riskweighted capital framework – address regulatory fault lines which remain as important today as they were prepandemic. The drafting of this series of standards benefited from an extensive consultation process.

Failure to implement these measures in a full, timely and consistent manner – as repeatedly agreed by G20 Leaders – would result in the remaining structural flaws and fragilities in the global banking system being left unaddressed, at significant cost to the economy and to global financial stability. Covid-19 has highlighted the vital importance of having necessary safeguards in place before the emergence of a shock; this certainly applies to prudential standards and the safety and soundness of the banking system.

Third, in parallel with the Committee’s ongoing “backward-looking” evaluation programme, it is crucial to pursue a forward-looking supervisory approach to identifying, assessing and mitigating emerging risks and structural trends impacting the global banking system. Some of these risks and trends – including the digitalisation of finance, climate-related financial risks, and the evolution and sustainability of banks’ business models – had already been identified before the pandemic. Covid-19 has further underlined the importance of addressing them.