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THE ROLE OF THE LIQUIDITY COVERAGE RATIO AND HIGH-QUALITY LIQUID ASSETS PORTFOLIO IN MANAGING BANK LIQUIDITY

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Abstract

In the context of global financial instability, digital transformation and the rapid expansion of real-time payment systems, effective liquidity management has become one of the most important conditions for maintaining the solvency and financial stability of commercial banks. Modern banking activity is increasingly exposed to rapid deposit movements, interest rate volatility, market liquidity shocks and changes in customer behaviour. In such circumstances, banks are required not only to hold sufficient capital, but also to maintain an adequate stock of highly liquid assets that can be converted into cash quickly and without significant loss of value.

The experience of recent banking crises has shown that even banks with relatively sufficient capital may face serious difficulties if their liquidity risk is not properly managed. Liquidity risk is especially relevant in the digital economy, where clients can transfer funds, withdraw deposits and make payments through digital channels within a very short period of time. Therefore, the traditional approach to liquidity management based only on current cash balances is no longer sufficient. Commercial banks need a more comprehensive system based on liquidity stress testing, real-time monitoring, asset-liability management and

regulatory liquidity indicators.

In international banking practice, the Liquidity Coverage Ratio (LCR) is considered one of the key regulatory instruments for assessing the short-term liquidity resilience of banks. According to the Basel III framework, "the LCR requires banks to hold a sufficient amount of unencumbered High-Quality Liquid Assets (HQLA) to meet their net cash outflows over a 30-calendar-day liquidity stress scenario"[1]. This means that a bank should be able to continue fulfilling its payment obligations even under conditions of deposit outflows, market stress and limited access to short-term funding.

High-Quality Liquid Assets are central to the practical implementation of the LCR requirement. HQLA generally include cash, central bank reserves, high-rated government securities and other assets that can be sold or used as collateral in financial markets with minimal loss of value. The quality, marketability and diversification of these assets determine the real strength of a bank's liquidity buffer. Therefore, the HQLA portfolio should not be assessed only by its nominal size, but also by its structure, currency composition, maturity profile and behaviour under stress conditions.

The introduction of the LCR after the global financial crisis of 2007–2009 significantly changed the approach to liquidity regulation. Before the crisis, many banks relied heavily on short-term wholesale funding and assumed that market liquidity would always be available.

[1] Basel Committee on Banking Supervision. *Basel III: The Liquidity Coverage Ratio and liquidity risk monitoring tools*. Basel: Bank for International Settlements, 2013.

Table 1 Key elements of LCR-based liquidity management in international banking practice

Element	Economic content	Impact on bank liquidity
Liquidity Coverage Ratio (LCR)	Measures the ability of a bank to cover 30-day net cash outflows under a stress scenario	Strengthens short-term liquidity resilience
High-Quality Liquid Assets (HQLA)	Includes cash, central bank reserves, government securities and other highly liquid instruments	Creates a liquidity buffer for unexpected outflows
Net cash outflows	Expected cash outflows minus expected inflows during a stress period	Shows the amount of liquidity needed in crisis conditions
Stress scenario	Assumes deposit withdrawals, funding market disruptions and liquidity pressure	Helps assess the bank's ability to survive adverse conditions
Regulatory monitoring	Regular reporting of LCR and liquidity indicators to supervisory authorities	Improves transparency and prudential control
Asset-liability management	Coordination of asset maturities, liability structure and funding sources	Reduces maturity mismatch and liquidity risk
Digital liquidity monitoring	Real-time observation of payment flows and customer behaviour	Allows early identification of liquidity pressures

The table shows that the LCR is not only a regulatory ratio, but also an important management tool. It connects the structure of liquid assets with possible cash outflows and helps banks evaluate whether they have sufficient resources to meet short-term obligations. In this sense, the LCR contributes directly to the solvency of commercial banks, since the inability to meet immediate payment obligations may quickly transform liquidity problems into a broader confidence crisis.

Recent international data confirm the importance of maintaining liquidity buffers above the minimum regulatory requirement. According to the Basel Committee on Banking Supervision, "the Basel III monitoring exercise as of 30 June 2025 included 150 banks, of which 101 were large internationally active Group 1 banks and 49 were Group 2 banks. At the end of June 2025, the weighted average LCR

was 135.0 percent for Group 1 banks and 191.6 percent for Group 2 banks. Moreover, all banks in the sample reported an LCR above the 100 percent minimum requirement, and no aggregate LCR shortfall was observed"[2].

The European banking sector also demonstrates strong liquidity positions. According to the European Banking Authority, "in the third quarter of 2025 the LCR of EU/EEA banks stood at 160.7 percent, while the Net Stable Funding Ratio (NSFR) was 126.8 percent. Total assets of EU/EEA banks remained at EUR 29.1 trillion, while the non-performing loan ratio was 1.8 percent"[3]. These indicators show that European banks generally maintain liquidity and stable funding ratios well above the minimum regulatory level.

The data presented in Table 2 indicate that international banks maintain liquidity ratios significantly above the minimum Basel III requirement of 100 percent. This reflects the lessons learned from previous financial crises and confirms the importance of a strong HQLA portfolio. The high level of LCR in both Group 1 and Group 2 banks shows that liquidity regulation has become an essential part of modern banking risk management.

Table 2 Selected international liquidity indicators in banking systems

Banking system / group	Period	Indicator	Value
Basel III monitoring sample	30 June 2025	Number of banks included	150 banks
Group 1 banks	30 June 2025	Number of large internationally active banks	101 banks
Group 2 banks	30 June 2025	Number of other banks	49 banks

[2] Basel Committee on Banking Supervision. *Highlights of the Basel III monitoring exercise as of 30 June 2025*. Basel: Bank for International Settlements, 2026.
[3] European Banking Authority. *Q3 2025 supervisory data confirm solid and stable asset quality, solvency, liquidity and profitability in EU/EEA banks*. Paris: EBA, 2025.

Group 1 banks	30 June 2025	Weighted average LCR	135.0%
Group 2 banks	30 June 2025	Weighted average LCR	191.6%
Group 1 banks	30 June 2025	Weighted average NSFR	123.8%
Group 2 banks	30 June 2025	Weighted average NSFR	134.2%
EU/EEA banks	Q3 2025	Liquidity Coverage Ratio	160.7%
EU/EEA banks	Q3 2025	Net Stable Funding Ratio	126.8%
EU/EEA banks	Q3 2025	Total assets	EUR 29.1 trillion
EU/EEA banks	Q3 2025	Non-performing loan ratio	1.8%

At the same time, the management of the HQLA portfolio requires a balance between liquidity and profitability. Highly liquid assets are usually less profitable than loans and other risk-weighted assets. Therefore, if a bank holds an excessively large amount of low-yield liquid assets, its profitability may decline. On the other hand, if the bank holds insufficient HQLA, it may face liquidity shortages during stress periods. For this reason, international banking practice pays special attention to the optimal structure of the HQLA portfolio, combining safety, liquidity and reasonable return.

Another important aspect of LCR-based liquidity management is the interaction between LCR and NSFR. While LCR focuses on short-term liquidity resilience over a 30-day stress period, NSFR evaluates the stability of funding over a longer horizon. A bank may have a strong LCR but still be vulnerable if its funding structure is unstable. Therefore, LCR and NSFR should be analysed together with capital adequacy, asset quality, deposit stability and interest rate risk.

Digital transformation further increases the importance of liquidity monitoring. In traditional banking, deposit withdrawals and payment flows were relatively

slower and more predictable. In digital banking, however, customers can move large amounts of money almost instantly. This creates the possibility of rapid liquidity pressure, especially during periods of negative market information or declining confidence. As a result, banks need automated systems capable of monitoring payment flows, deposit dynamics and liquidity positions in real time.
In foreign banking practice, liquidity management is increasingly based on the integration of regulatory ratios, internal stress testing and digital data analytics. Banks use scenario analysis to assess the impact of deposit outflows, interest rate shocks, exchange rate movements and market liquidity deterioration on their LCR and HQLA portfolios. Such an approach allows banks to identify vulnerabilities before they become serious financial problems.
For commercial banks, the effective management of LCR and HQLA portfolios provides several important advantages. First, it strengthens the ability of banks to meet short-term obligations. Second, it increases customer and market confidence. Third, it reduces the probability of liquidity crises spreading to the real economy. Fourth, it supports the stability of the payment system, which is especially important under digital transformation.
Thus, the Liquidity Coverage Ratio and High-Quality Liquid Assets portfolio play a crucial role in managing bank liquidity in international banking practice. The experience of Basel III implementation and recent liquidity indicators of international banks show that maintaining a strong and well-diversified HQLA portfolio is essential for ensuring short-term liquidity resilience. In the digital economy, where financial flows are becoming faster and more sensitive to information shocks, banks should strengthen LCR-based monitoring, improve liquidity stress testing and develop real-time liquidity management systems.

References

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