

**CAPITAL, RISK, AND THE REGULATION OF BANKS: THE
BASEL FRAMEWORK**

Responsible Faculty Instructor:

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Assistant Professor

Credits: 4

Credits Type: Law

Cross-registration: Yes

Pre-requisites: None

COURSE DESCRIPTION (COURSE VISION):

Since their inception in 1988, the Basel Accords have constituted the foundational architecture of international bank capital regulation. Developed by the Basel Committee on Banking Supervision under the auspices of the Bank for International Settlements, they represent the most consequential exercise in international financial standard-setting of the modern era: a series of iterative frameworks, each designed to correct the deficiencies of its predecessor, that now govern the capital, liquidity, and risk management practices of banks in over one hundred jurisdictions. This course offers a rigorous and technically grounded study of the Basel framework from its origins to its present iteration.

The course proceeds systematically through each of the four risk domains that the Accords address: credit risk, market risk, operational risk, and liquidity risk. Students learn to compute regulatory capital requirements under both standardised and internal ratings-based approaches, to evaluate the assumptions and methodological limitations embedded in those calculations, and to assess the adequacy of capital buffers in conditions of financial stress. The course situates these technical skills within a critical analytical framework, engaging the substantial scholarly and policy literature that questions whether capital regulation as currently designed can deliver the financial stability it promises.

The historical and evolutionary dimension of the subject is treated seriously. Basel I, Basel II, Basel III, and the finalised Basel III reforms (commonly designated Basel IV) are examined in sequence, with attention to the political economy of their negotiation, the regulatory failures that drove successive

revisions, and the distributional consequences of global standard-setting for banks operating outside the BCBS member jurisdictions. By the conclusion of the course, students will possess both the quantitative competence to work with Basel capital models and the critical perspective necessary to evaluate the framework's adequacy against the demands of contemporary financial regulation.

TEACHING METHODOLOGY:

The course is taught through a combination of lectures and tutorials. Lectures provide conceptual and technical foundations, introducing the regulatory framework, the risk measurement methodologies, and the critical literature that surrounds them. Tutorials apply these foundations to worked examples and practical calculations, requiring students to compute capital requirements under different approaches, compare their outputs, and assess their implications for bank behaviour and regulatory design.

Case study is integral to the course's method. The 2007–2009 global financial crisis receives dedicated treatment as a module in its own right: students examine the causal chain from subprime mortgage lending and securitisation through the CDO market, excessive leverage, shadow banking, and deregulation to the systemic collapse, and then assess precisely which features of the pre-crisis Basel II framework failed and why. The collapse of Silicon Valley Bank in 2023, the state-facilitated resolution of Credit Suisse, and other more recent episodes of institutional stress are also used as analytical touchstones. This approach grounds abstract regulatory architecture in concrete institutional experience and enables students to evaluate whether successive revisions have substantively addressed the vulnerabilities they were designed to correct.

Students are expected to engage critically with the assigned readings, to challenge the assumptions underlying risk measurement models, and to develop independent views on the fundamental questions of the field: whether capital regulation is the appropriate primary instrument of financial stability policy, whether internal models can be trusted, and whether the Basel framework is structurally adequate to the risks posed by modern banking. The course thereby seeks to produce graduates capable of both practising within the regulatory framework and contributing to its reform.

INTENDED LEARNING OUTCOMES:

Upon successful completion of this course, students will be able to:

1. critically discuss the role and management of capital in financial institutions, and explain the theoretical justifications for and critiques of

- minimum capital requirements as an instrument of financial stability policy;
2. demonstrate a systematic understanding of the institutional and historical development of the Basel Accords, from the founding of the Basel Committee on Banking Supervision in 1974, through Basel I (1988), Basel II (2004), Basel III (2010), and the finalised Basel III reforms (2017), situating each iteration within the regulatory failures, political negotiations, and evolving understanding of banking risk that produced it;
 3. compute regulatory capital requirements for credit, market, operational, and liquidity risk under the standardised and internal ratings-based approaches prescribed by the Basel framework, and critically evaluate the assumptions and limitations embedded in those calculations;
 4. critically interpret and review assessments of credit, market, operational, and liquidity risk, identifying the methodological choices that drive outputs and the conditions under which model-based approaches may underestimate actual exposures;
 5. analyse the 2007–2009 global financial crisis as a case study in the failure of the pre-crisis regulatory framework, identifying the specific mechanisms — subprime securitisation, excessive leverage, shadow banking, and credit rating agency failure — that the Basel II framework was unable to constrain, and evaluate the adequacy of the Basel III reforms as a response to those failures;
 6. critically evaluate the limitations of the Basel capital framework, including its procyclical effects, its reliance on credit rating agencies and internal models, its treatment of systemic risk, and its distributional consequences for banks in developing and emerging economies;
 7. assess the challenges of national implementation of the Basel Accords, including the divergence between advanced and emerging market jurisdictions, regulatory arbitrage, the risks of competitive inequality arising from inconsistent enforcement, and the distributional consequences of global standard-setting for jurisdictions outside the BCBS membership;
 8. apply the analytical tools developed in the course to professional contexts in risk management, regulatory compliance, financial supervision, and policy design involving bank capital adequacy; and
 9. conduct independent research on questions of bank capital regulation, deploying both quantitative and critical methodological approaches, and present findings with analytical precision and scholarly rigour.

READING LIST (upto 10 select readings):

1. J Wernz, *Bank Management and Control: Strategy, Pricing, Capital and Risk Management* (2nd edn, Springer 2020)
2. E Avgouleas and C A E Goodhart, 'Critical Reflections on Bank Bail-ins' (2015) 1(1) *Journal of Financial Regulation* 3
3. A Admati and M Hellwig, *The Bankers' New Clothes: What's Wrong with Banking and What to Do about It* (2nd edn, Princeton UP 2024)
4. D K Tarullo, *Banking on Basel: The Future of International Financial Regulation* (Peterson Institute for International Economics 2008)
5. C A E Goodhart, *The Basel Committee on Banking Supervision: A History of the Early Years 1974–1997* (CUP 2011)
6. J C Hull, *Risk Management and Financial Institutions* (6th edn, John Wiley & Sons 2023)
7. A J McNeil, R Frey and P Embrechts, *Quantitative Risk Management: Concepts, Techniques and Tools* (rev edn, Princeton UP 2015)
8. R B Myerson, 'Rethinking the Principles of Bank Regulation: A Review of Admati and Hellwig's *The Bankers' New Clothes*' (2014) 52(1) *Journal of Economic Literature* 197
9. M K Brunnermeier, 'Deciphering the Liquidity and Credit Crunch 2007–2008' (2009) 23(1) *Journal of Economic Perspectives* 77
10. J Danilsson and others, 'An Academic Response to Basel II' (LSE Financial Markets Group, Special Paper No 130, 2001)

WEEKLY READING PLAN (WEEKLY OUTLINE):

MODULES	WEEK(S)
<p style="text-align: center;">MODULE 1: THE BIS, THE BASEL COMMITTEE, AND THE BASEL PROCESS</p> <p>This module introduces the institutional architecture within which the Basel Accords are produced, examining the origins of the Bank for International Settlements, the founding of the Basel Committee in 1974, and the mechanics by which non-binding international standards are translated into binding national law.</p>	Week 1
<p style="text-align: center;">MODULE 2: BANK CAPITAL: FOUNDATIONS, TIERS, AND THE RATIONALE FOR REGULATION</p> <p>This module establishes the technical and conceptual foundations of the course, examining regulatory capital composition, the Tier 1 and Tier 2 hierarchy, risk-weighted</p>	Weeks 2–3

assets, and the competing theoretical accounts of what minimum capital requirements can and cannot achieve.	
<p style="text-align: center;">MODULE 3: BASEL I AND BASEL II: EVOLUTION, ARCHITECTURE, AND SHORTCOMINGS</p> <p>This module traces the development of the Basel framework from the 1988 Capital Accord through the 2004 three-pillar architecture of Basel II, examining the shortcomings of Basel I that drove revision and the critical literature on Basel II's reliance on internal models, credit rating agencies, and procyclical capital requirements.</p>	Weeks 4–5
<p style="text-align: center;">MODULE 4: CREDIT RISK, MARKET RISK, AND OPERATIONAL RISK</p> <p>This module examines the measurement and capitalisation of the three primary risk categories across the Basel framework: the standardised and internal ratings-based approaches to credit risk, the evolution from value-at-risk to expected shortfall under the Fundamental Review of the Trading Book, and the progression from advanced measurement approaches to the standardised measurement approach for operational risk.</p>	Weeks 6–8
<p style="text-align: center;">MODULE 5: THE GLOBAL FINANCIAL CRISIS (2007–2009) AS REGULATORY FAILURE</p> <p>This module examines the 2007–2009 global financial crisis as a case study in the failure of the pre-crisis regulatory framework, tracing the collapse from subprime securitisation and excessive leverage through systemic breakdown to identify the specific inadequacies of Basel II that drove the post-crisis reform agenda.</p>	Week 9
<p style="text-align: center;">MODULE 6: BASEL III: CAPITAL QUALITY, LIQUIDITY, AND THE LEVERAGE RATIO</p> <p>This module examines the Basel III framework as a direct regulatory response to the global financial crisis, covering enhanced capital quality requirements, the conservation and countercyclical buffers, the Liquidity Coverage Ratio and Net Stable Funding Ratio, and the non-risk-based leverage ratio introduced as a backstop to risk-weighted requirements.</p>	Weeks 10–11

<p style="text-align: center;">MODULE 7: STRESS TESTING, MACRO-PRUDENTIAL SUPERVISION, AND RESOLUTION</p> <p>This module examines the supervisory tools that sit alongside capital requirements in the post-crisis regulatory architecture: the design and conduct of regulatory stress tests, the macro-prudential instruments of the countercyclical and systemic risk buffers, and the resolution framework including total loss-absorbing capacity and bail-in under the FSB’s TLAC standard and the EU’s MREL regime.</p>	Weeks 12–13
<p style="text-align: center;">MODULE 8: THE FINALISED BASEL III REFORMS (BASEL IV)</p> <p>This module examines the December 2017 finalised Basel III reforms — commonly designated Basel IV — addressing the output floors constraining internal model outputs, the revised standardised approaches for credit and operational risk, and the variation in national implementation across the EU’s Capital Requirements Regulation and the US framework.</p>	Week 14
<p style="text-align: center;">MODULE 9: CRITICAL PERSPECTIVES AND COMPARATIVE IMPLEMENTATION</p> <p>This module engages the critical literature on the Basel framework as a whole — procyclicality, model homogeneity, regulatory capture, and the argument that capital levels remain structurally insufficient — and examines comparative implementation across advanced and emerging market jurisdictions, including the distributional consequences of global standard-setting for countries outside the BCBS membership.</p>	Weeks 15–16
REVISION	Week 17