

CATEGORIZATION

MAIN ASPECT

IAS 39—categorization:

There are four different categories and generous options for reclassification.

The aim of IFRS 9 is to reduce complexity and to improve the decision-making benefits for the addressee of the annual accounts.

IFRS 9—categorization:

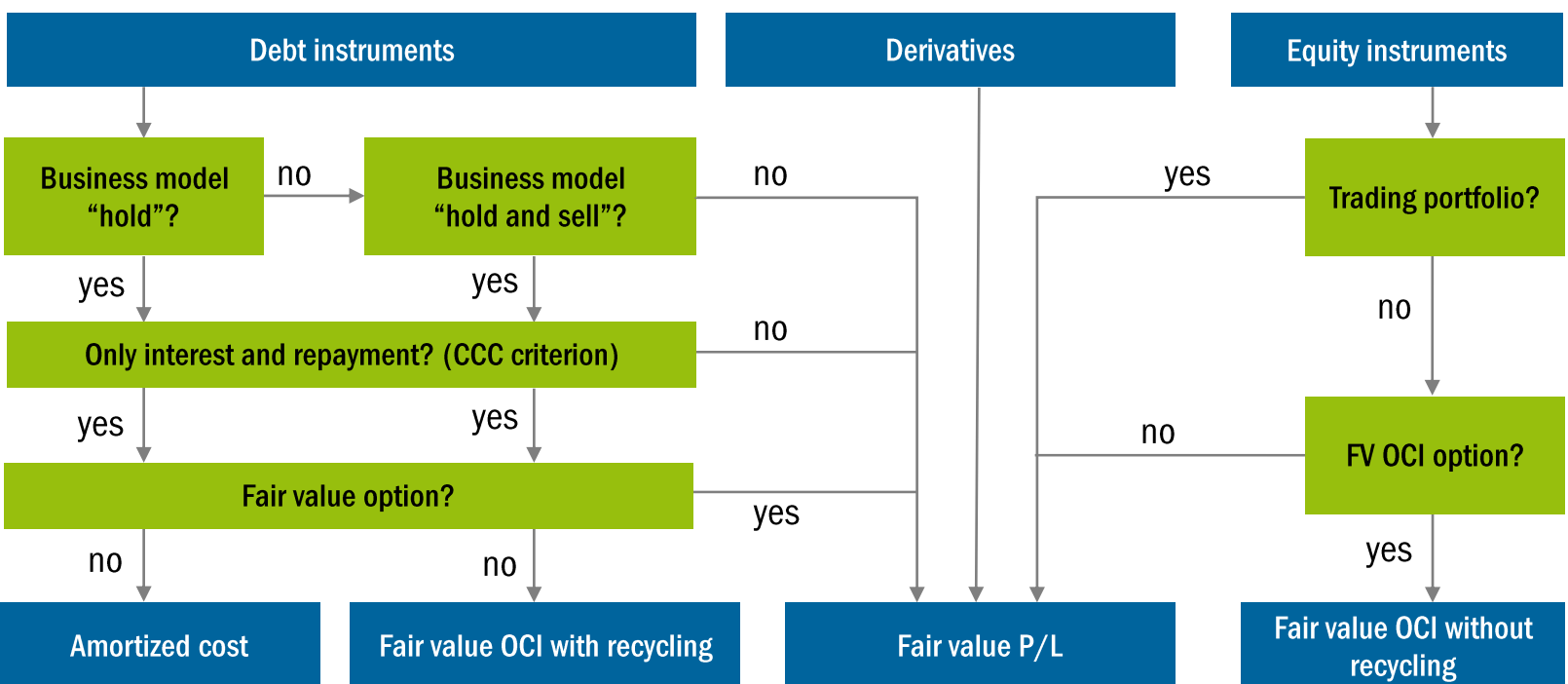
Financial assets are classified according to

- The business model
- The characteristics of the receivable cash flows

There are two basic categories

- Amortized cost
- Fair value (through OCI and P/L)

CLASSIFICATION INTO FOUR CATEGORIES

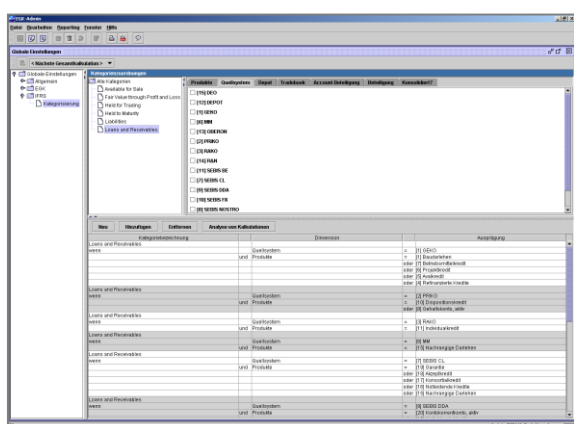


EMBEDDED DERIVATIVES

Embedded derivatives are components of a structured instrument consisting of a non-derivative host contract and a derivative. Contrary to IAS 39, the derivative is not recognized separately from its financial asset host. Instead, under IFRS 9, the overall contract is recognized. In most cases this will lead to a measurement at fair value through profit or loss. In case of a non-financial host contract or financial liability, the accounting of the embedded derivative is still effected in accordance with IAS 39.

OUR SOFTWARE SOLUTION

- Allocation of financial instruments to the defined IFRS categories
- Definition of the categorization rules through a graphical user interface
- Identification of conflicts and discrepancies in the categorization rules
- Audit-proof recording of all settings



Definition of categorization rules

MAIN ASPECT

IAS 39—measurement:

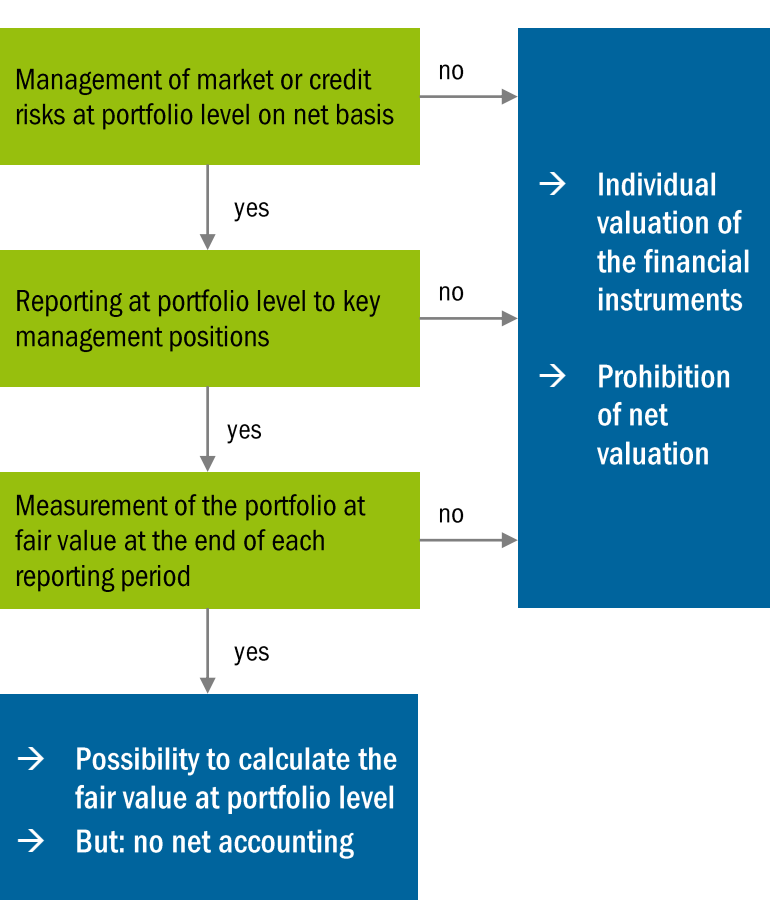
Assets and liabilities are to be valued according to their categorization.

IFRS 9—measurement:

Financial instruments are also to be valued according to their categorization.

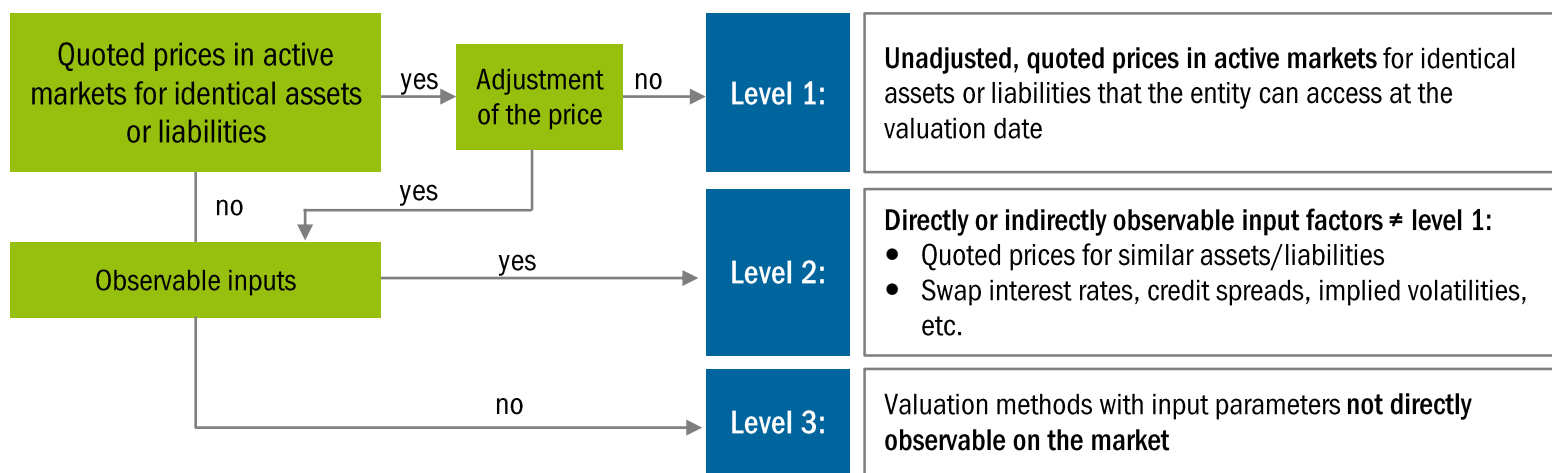
In general, measurement is at (amortized) cost or as "other liability" (through effective interest, if applicable) or at fair value.

MANAGED PORTFOLIOS



MEASUREMENT

FAIR VALUE HIERARCHY UNDER IFRS 13



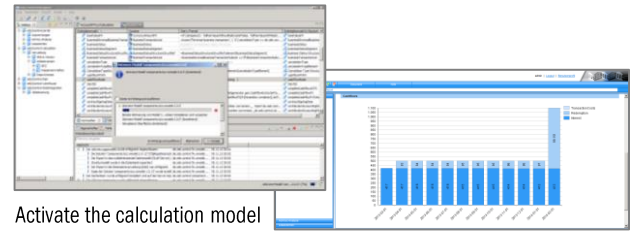
Fair Value = Selling/transfer price for an asset/liability in a regular transaction under current market conditions between economically acting market participants in the principal market

NON-PERFORMANCE RISK IN FAIR VALUE

Liabilities	Own credit spread	<ul style="list-style-type: none">• The price of a liability needs to reflect its solvency• Separately contacted guarantees must not be included in the price• With fair value liabilities, the effect of the own solvency usually has an impact on OCI
Derivatives	CVA	<ul style="list-style-type: none">• The counterparty risk must be included in the fair value• It has a lowering effect on the price• Changes have a direct effect on the P/L statement
	DVA	<ul style="list-style-type: none">• The own credit risk must also be included in the fair value• It has an increasing effect on the price• Changes have a direct effect on the P/L statement
	FVA	<ul style="list-style-type: none">• The funding costs should also be included in the fair value• It has a lowering effect on the price• Changes have a direct effect on the P/L statement

OUR SOFTWARE SOLUTION

- Supports all IFRS-relevant measurement methods (amortization at a constant effective interest rate, connection to an external price feed, mark-to-model valuation)
- Covers a broad product range in the customer business as well as in proprietary trading



Activate the calculation model Interest risk calculation

CONSEQUENCES

CHALLENGES

- Analysis of business models and portfolios as to the necessity of using the fair value approach and of the discretion available for AC measurement
- The classification is usually carried out at portfolio level - this mostly being the financial & risk management level of credit institutions. The aggregation of portfolios is possible, as long as this is compliant with the financial and risk management.
- Analysis of contractual CF characteristics

APPROACH

- Flexible simulation and pricing of the product portfolio to be calculated
- Identification of conflicts and discrepancies in the categorization rules

CHALLENGES

- Analysis of existing loan contracts for the determination of fair value using the DCF method or a suitable model
- In the FV measurement, the solvency of the parties involved in the contract of a financial instrument has to be taken into account

APPROACH

Re-usable standard valuation algorithms (functional modules) of zeb or specific ones of the client

CHALLENGES

- The closer relation to risk management / treasury leads to improved realization capacities in hedge accounting, i.e. a stronger link to economic management possible
- Examination of the applicability of methods and parameters from risk controlling

APPROACH

Early analysis and simulation to assess the possible impact (positive / negative) of hedge accounting when changing to IFRS 9 general hedge accounting

CHALLENGES

- Early conception and implementation of the EL/ELL-based impairment model, perform impairment simulations for managing future P&L volatility & creation of transparency about the first-time adoption effect
- Review and follow-up checks of periodic changes of the credit quality for purposes of (re-)allocation via the three-stage logic

APPROACH

- Institution-specific definition of stage-transfer criteria depending on borrower groups, volumes, days in arrears, etc.
- Development of appropriate calculation models for EL/ELL and analysis of quantitative impacts

HEDGE ACCOUNTING

CORE ASPECT

IAS 39—Hedge accounting:

Focus on balance sheet, only limited coverage of economic risk hedging under IAS 39 provisions

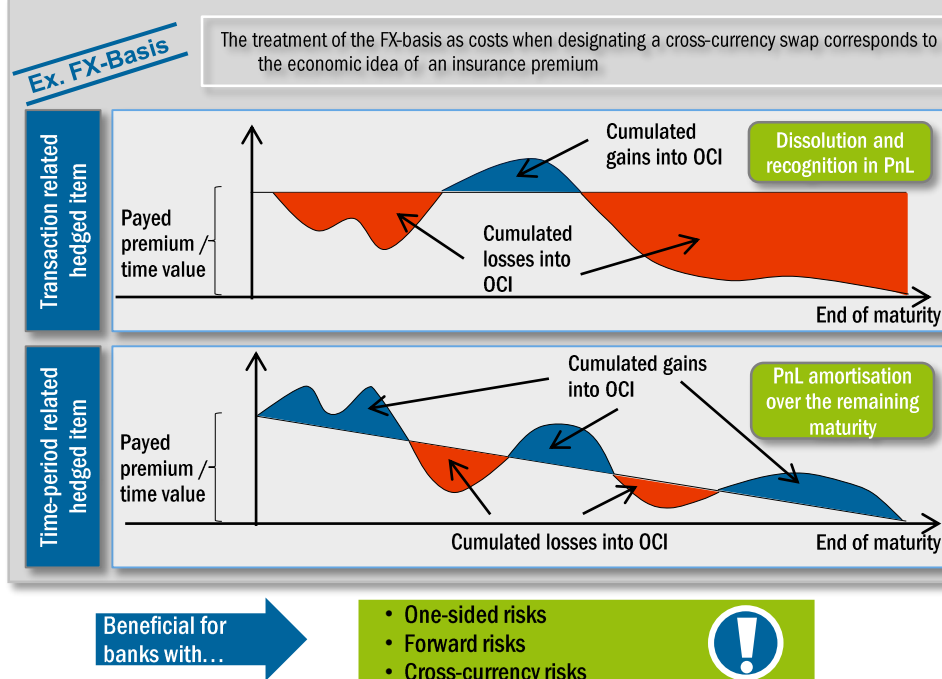
IFRS 9—Hedge accounting:

Economic focus, aimed at an integrated view on risk management up to financial reporting hedge accounting

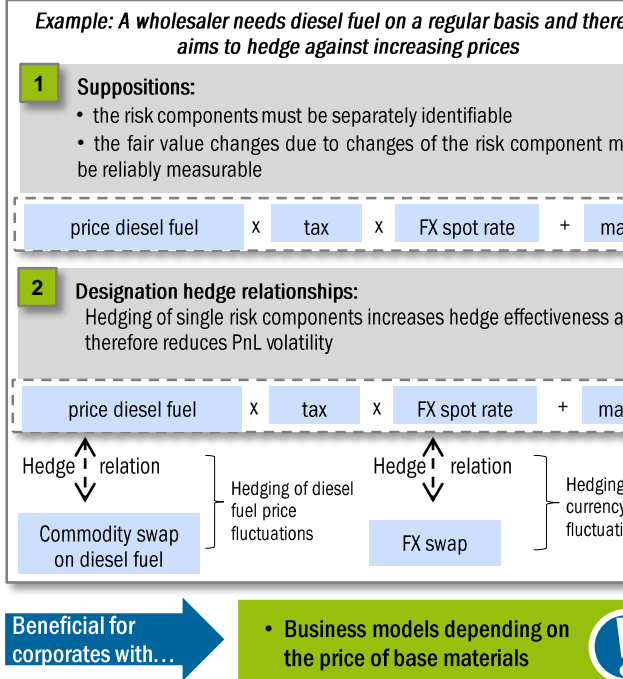
On effective date of first application of IFRS 9, an entity may choose to apply IAS 39 hedge accounting instead

Application of IAS 39 interest rate risk portfolio FVHA still allowed

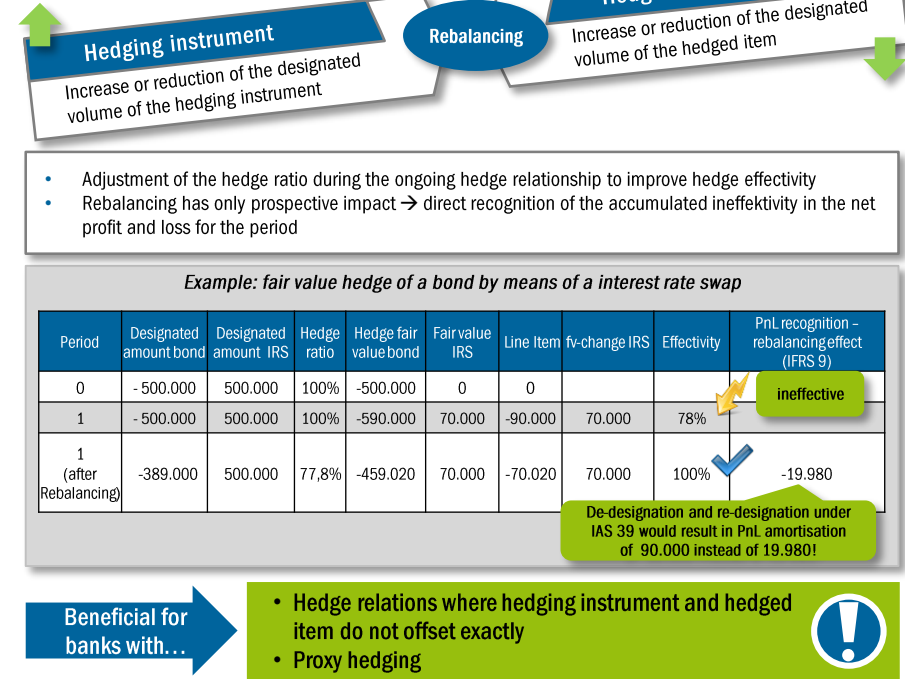
SEPARATION OF TIME VALUE OF OPTIONS, SPOT LEG OF FORWARDS AND FX-BASIS OF CROSS-CURRENCY SWAPS



DESIGNATION OF RISK COMPONENTS OF NON-FINANCIALS

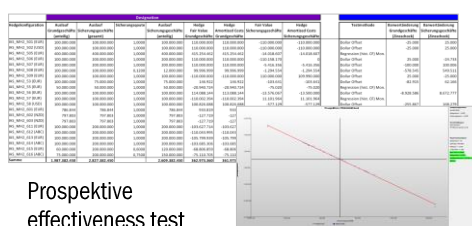


REBALANCING AND OMISSION OF THE RETROSPECTIVE TEST



OUR SOFTWARE SOLUTION

- Implementation of all variants under IFRS 9 general hedge accounting
- Integrated simulation and decision-making model for ALM and hedge accounting
- Process support and extensive reporting functions



Prospective effectiveness test by means of regression analysis

IMPAIRMENT

CORE ASPECT

IAS 39 — Incurred loss model

Loss provisioning at the point where the loss has actually been incurred

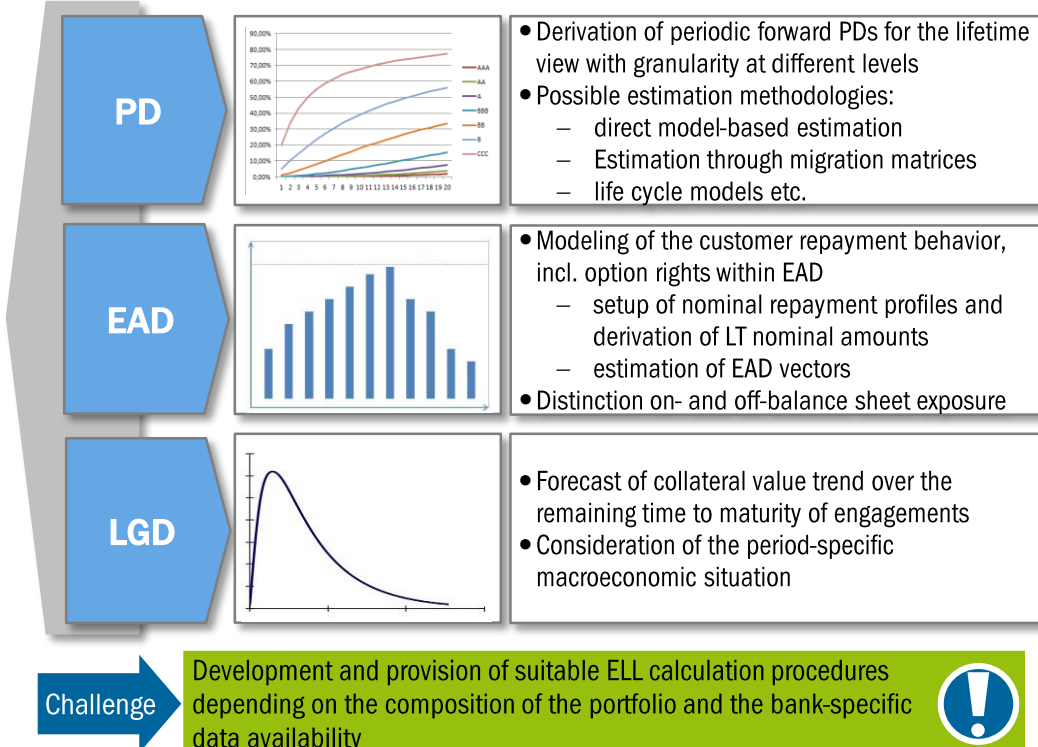
Criticism: Losses often recognized too late and to an insufficient extent

IFRS 9 — Expected loss model

Loss provisioning at initial recognition and subsequent adjustment depending on credit quality changes of a financial asset

Idea: providing timely information on credit default risk and prevention of pro-cyclical lending

POSSIBLE APPROACHES FOR MODELING 1YR AND LIFETIME EL



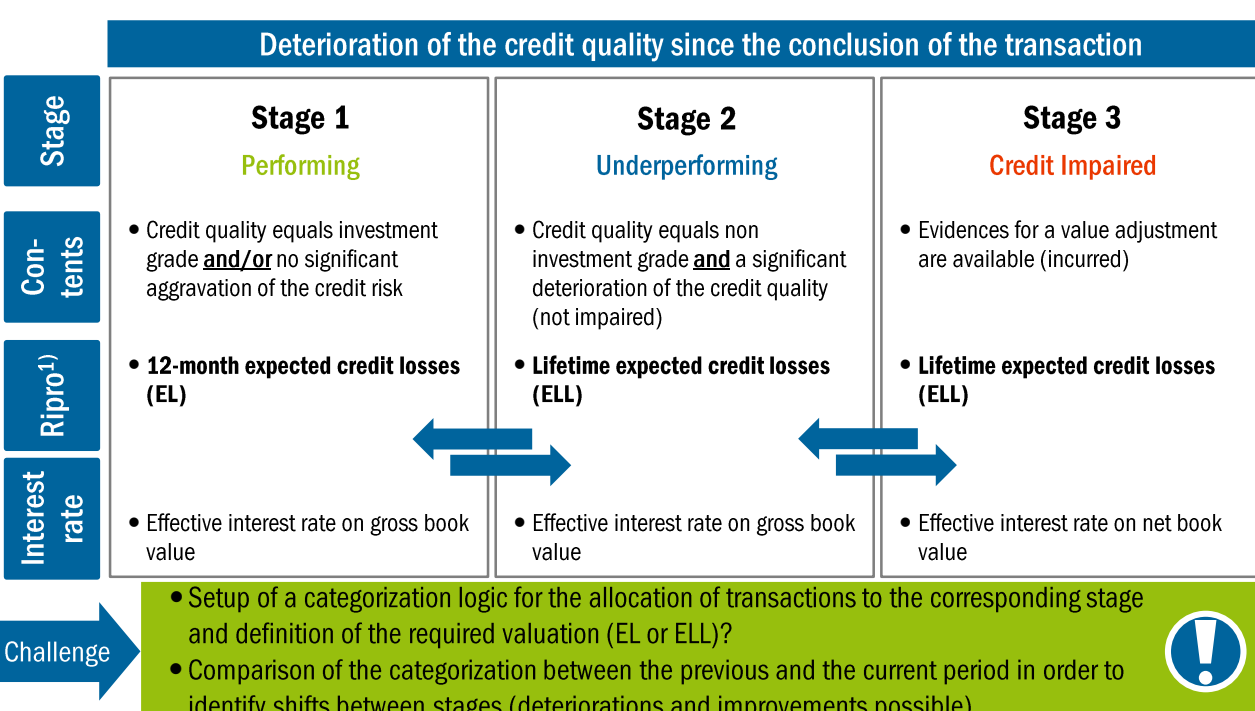
OUR SOFTWARE SOLUTION

- Customized configuration of the stage allocation process
- Calculation of EL/ELL on single contract level based on CFs and parameters
- Comprehensive options for reporting and simulations over the course of time



Overview of impairment

3-STAGE IMPAIRMENT MODEL AND CATEGORIZATION REQUIREMENTS



1) Risk provision

IFRS 9: INCURRED VS. EXPECTED LOSS MODEL

