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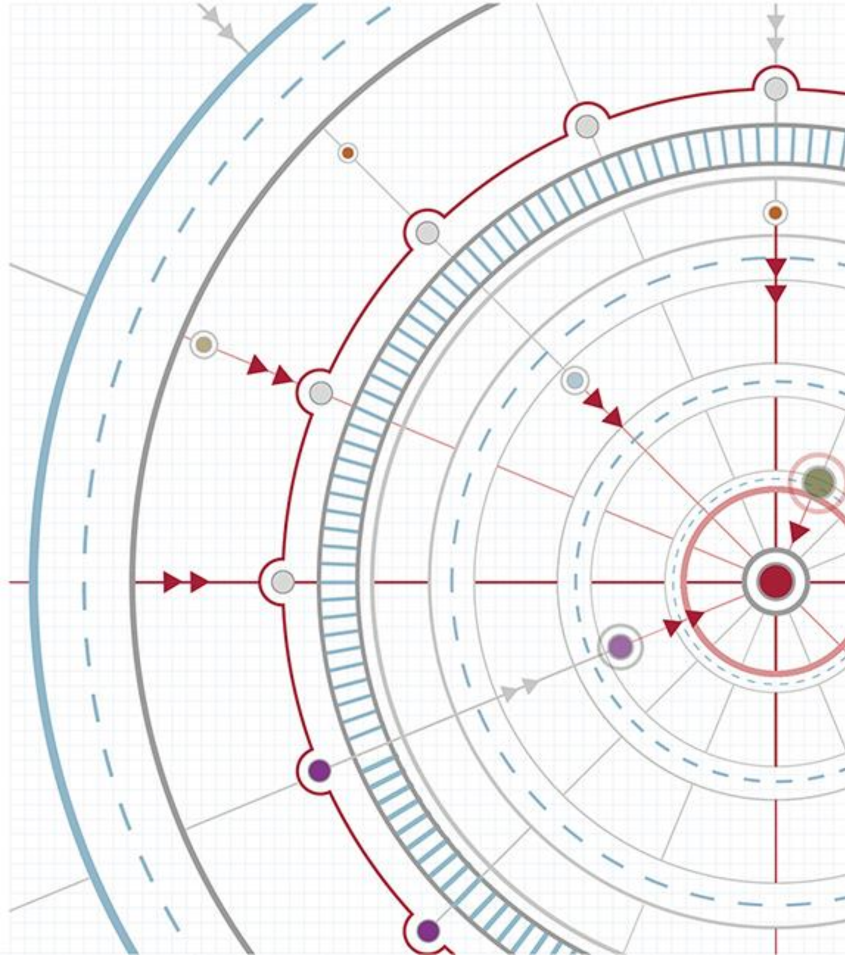

# IFRS 9 *Financial Instruments*: The Expected Loss Model

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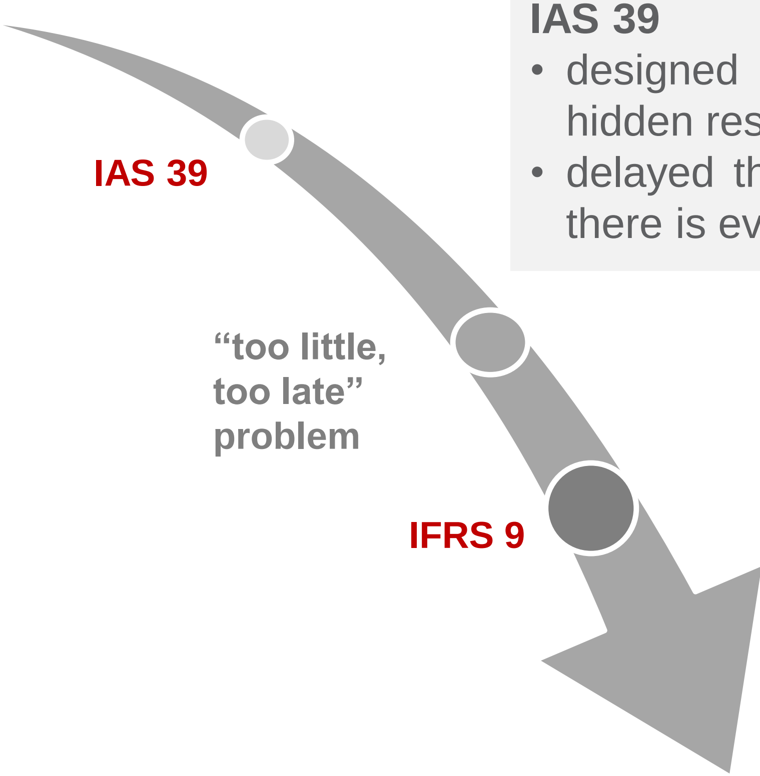
# IAS 39 vs. IFRS 9






**IAS 39**

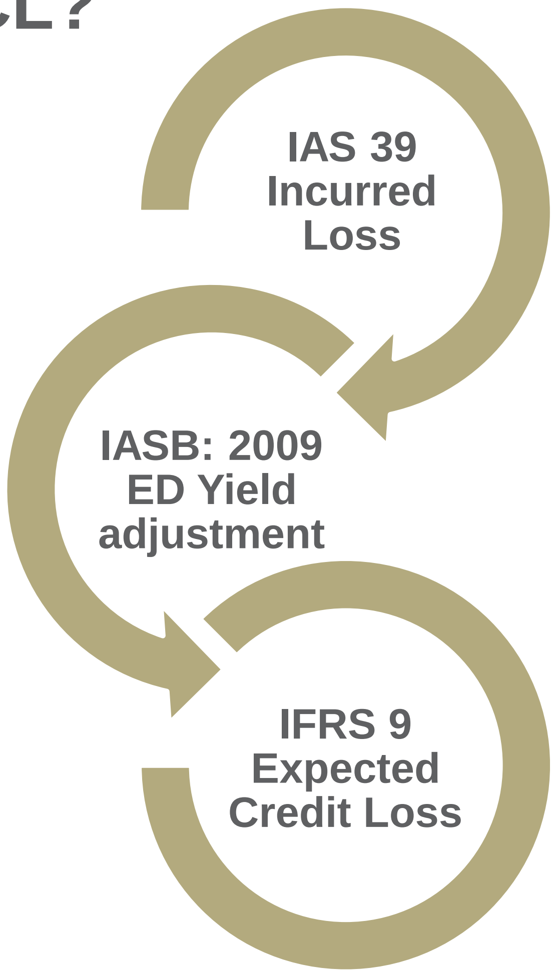
- designed to limit entity’s ability to create hidden reserves
- delayed the recognition of credit losses until there is evidence of a trigger event

**IFRS 9**

- forward-looking impairment model
- Update the amount of expected losses recognised at each reporting date to reflect changes in the credit risk

# IFRS 9: Expected Credit Losses

## How did the IASB land on ECL?




## What does an ECL look like?

Example of Day-1 provision:

- Portfolio of 10m loans repayable over 5 years
- 2% probability of a default occurring in the next 12-months
- Entire loss that would arise on default is 10%
- **ECL** = 20,000 (2%x10%x**10m**)

*Until significant increase in credit risk*

# IFRS 9 *ECL*: Overview



Change in credit risk since initial recognition

| | Stage 1 | Stage 2 | Stage 3 |
|---|---|---|---|
| Expected credit losses | 12-month expected credit losses | Lifetime expected credit losses | Lifetime expected credit losses |
| Interest revenue | Gross basis | Gross basis | Net basis |

# IFRS 9: What information is used to develop ECL?



- Borrower-specific factors:
  - changes in operating results of the borrower, technological advances that affect future operations, changes in collateral supporting the obligation.
- Macroeconomic factors:
  - house price indexes, GDP, household debt ratios.
- The data sources could be:
  - internal data – credit loss experience and ratings; and
  - external data – ratings, statistics or reports.

**Leverage credit risk management**

# Disclosures - objectives



To enable users
to understand the ***effect of credit risk***
on the ***amount***, ***timing*** and ***uncertainty***
of ***future cash flows***

Entities' ***credit risk management practices*** and how they relate to recognition and measurement of ECL

***Quantitative and qualitative information*** to evaluate amounts in the financials arising from ECL

Entities' ***credit risk exposure*** including significant credit risk concentrations

# IFRS 9 *ECL*: Benefits



Forward-looking model that is responsive to changes in credit risk and responds to the calls of the G20 and others

- Broader range of information required to be considered
  - ➢ Ensures more timely recognition of expected credit losses
  - ➢ Elimination of IAS 39 threshold
- ➢ Builds on existing systems to balance costs and benefits
  - ➢ Approximates 2009 ED in more operational manner
- Single model reduces complexity of multiple approaches
- Enhanced disclosures:
  - ➢ Illustrate how an entity has applied the requirements
  - ➢ Show instruments which have significantly increased in credit risk

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