IFRS 9
Rational & Objectives

Rabih Nehme,
Head of Risk
Banking Control Commission of Lebanon, BCCL

Cyclicality: issues

- To what extent is Basel II pro-cyclical?
- Need to find balance between risk-sensitivity & cyclicality
- Banks' business models are inherently cyclical
  - Risk appetite varies with changing economic conditions
- Other sources of cyclicality
  - Accounting rules
  - Provisioning practices

Basel III & Procyclicality

- Range of measures to:
  - address Procyclicality &
  - increase resilience in good times
- Four key objectives:
  1. Dampen cyclicality of the minimum capital requirement
  2. Conserve capital to build buffers at individual banks
  3. Protect banks from periods of excess credit growth
  4. **Promote more forward-looking provisions**

Types of Provisions

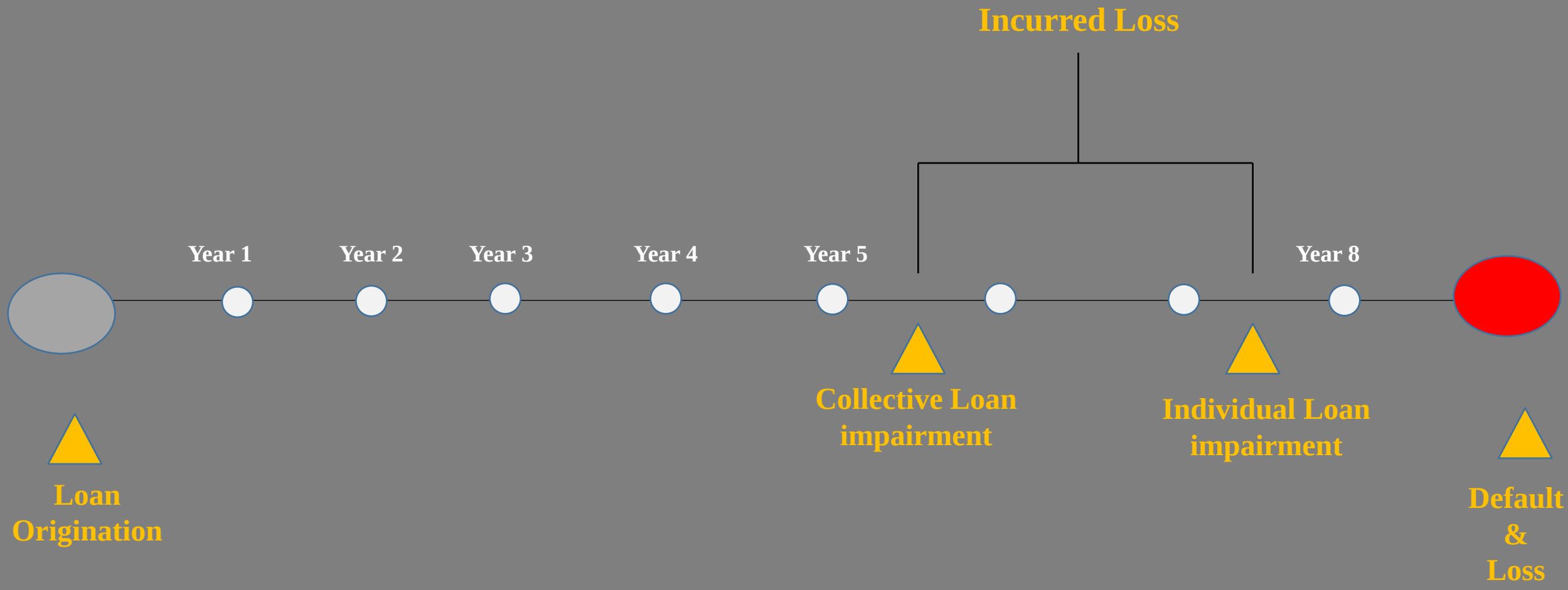
1) Specific Provisions

2) General Provisions

3) Country Risk Provisions

Incurred Loss Model provisioning

- Objective evidence of impairment
- Loans to be collectively reviewed for impairment
- Increase the volatility of banks’ results.


Incurred Loss
Year 1
Year 2
Year 3
Year 4
Year 5
Year 8
Collective Loan impairment
Individual Loan impairment
Loan Origination
Default & Loss

	2004	2005	2006	2007	2008	2009	2010	2011
Incurred Loss Model	100	120	140	130	100	70	30	-20
Forward Looking Model	80	90	90	90	100	100	100	70
General Provisions	20	30	50	40	-	-	-	-
Stock of Provisions	20	50	100	140	140	110	70	-

Impact on Capital

- if losses not recognized & provisions not allocated accordingly

- it could translate into a series of adverse implications:
  - unrecognized losses
  - inadequate provisions
  - overstated loan values
  - inflated income
  - overstated capital
  - threat of insolvency

Impact on Capital

- **Basel I**: only general provisions are counted towards capital.

- **Basel II**, SA: only general provisions,

- **Basel II**, IA: part of Specific provisions also

compared to the EL amount calculated under the IRB (1-year period)

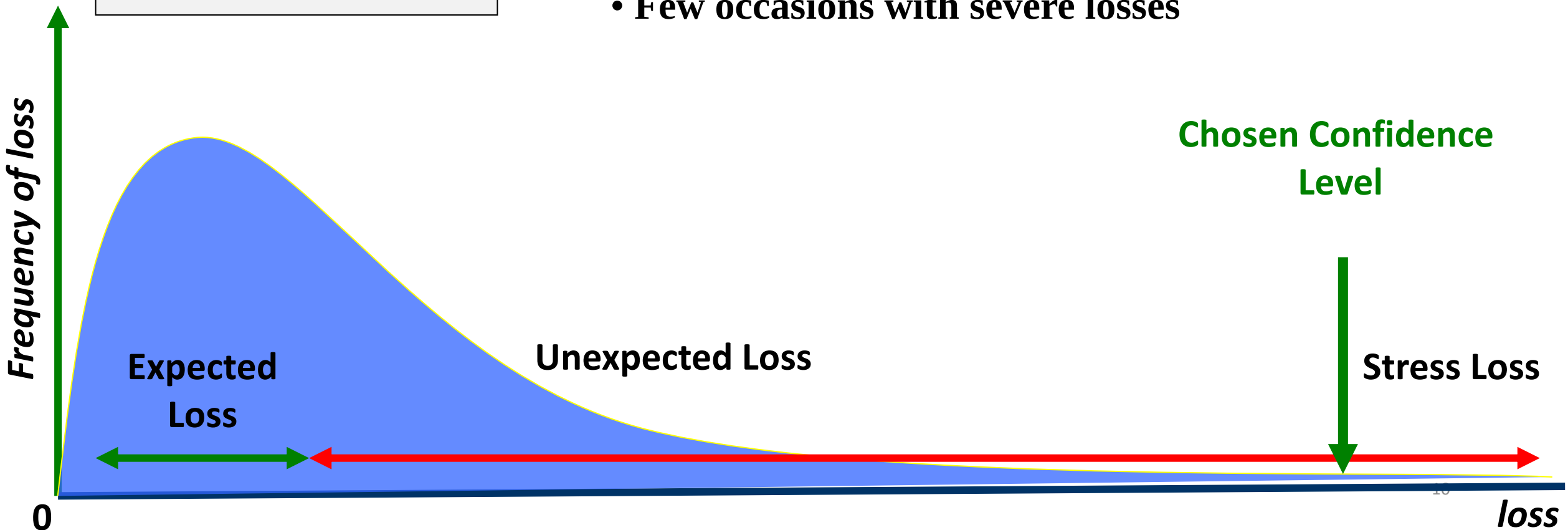
In some developed jurisdictions

all provisions including general provisions, specific provisions as well as country risk provisions, can be counted towards capital.

Modelling Credit Losses

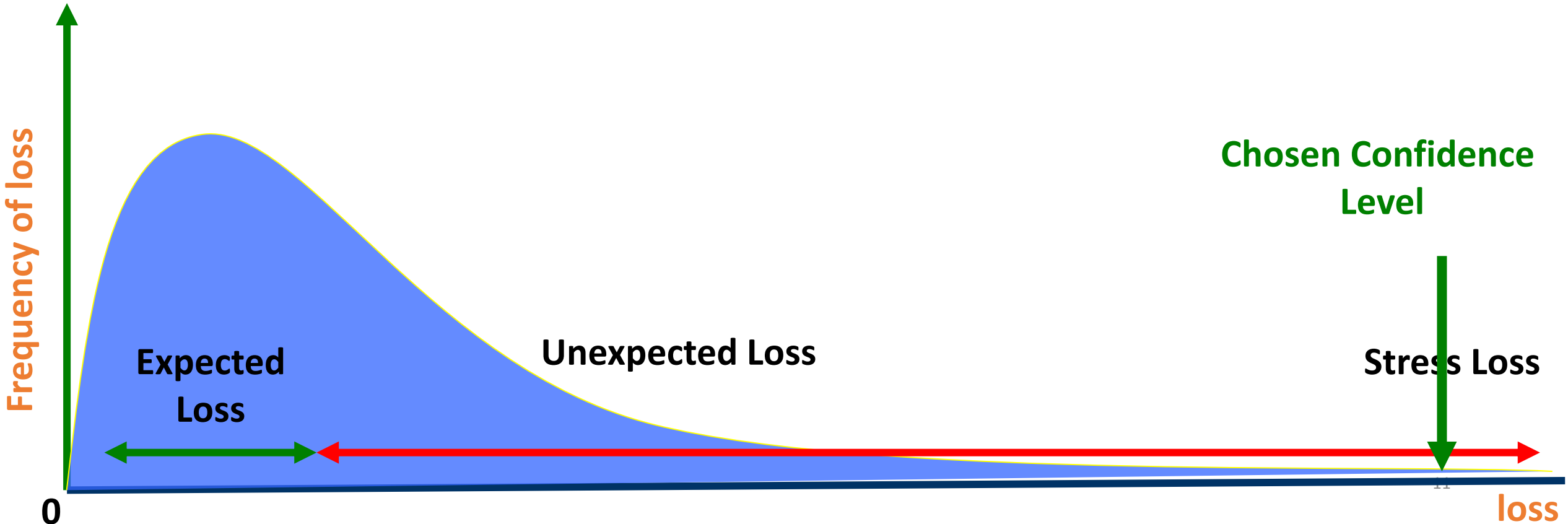
Retail Loan Portfolio

- Large number of small losses
- Few occasions with severe losses

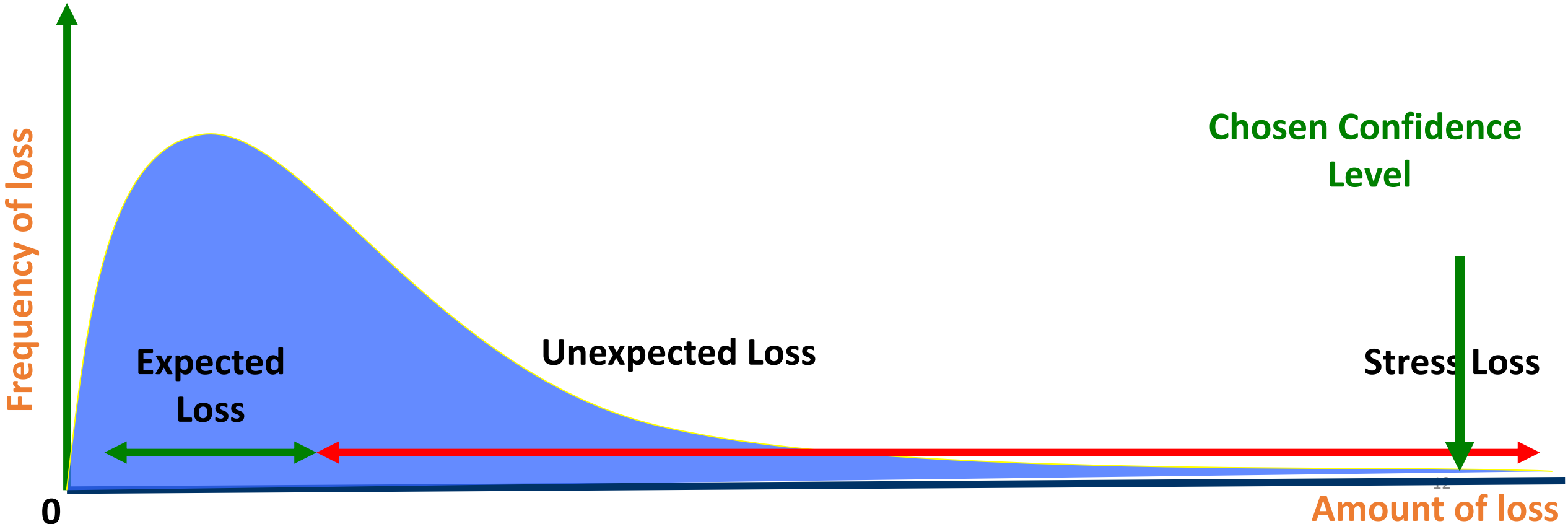


Expected Losses :

- The amount a bank can expect to lose on average, based upon its historical loss data.

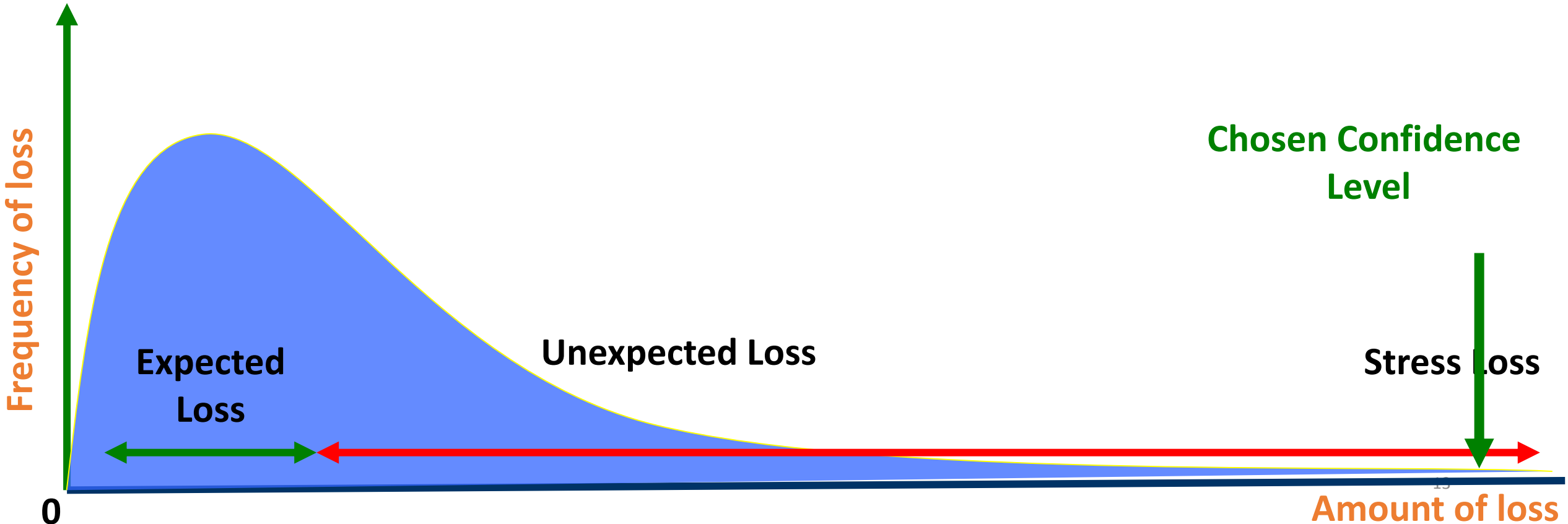


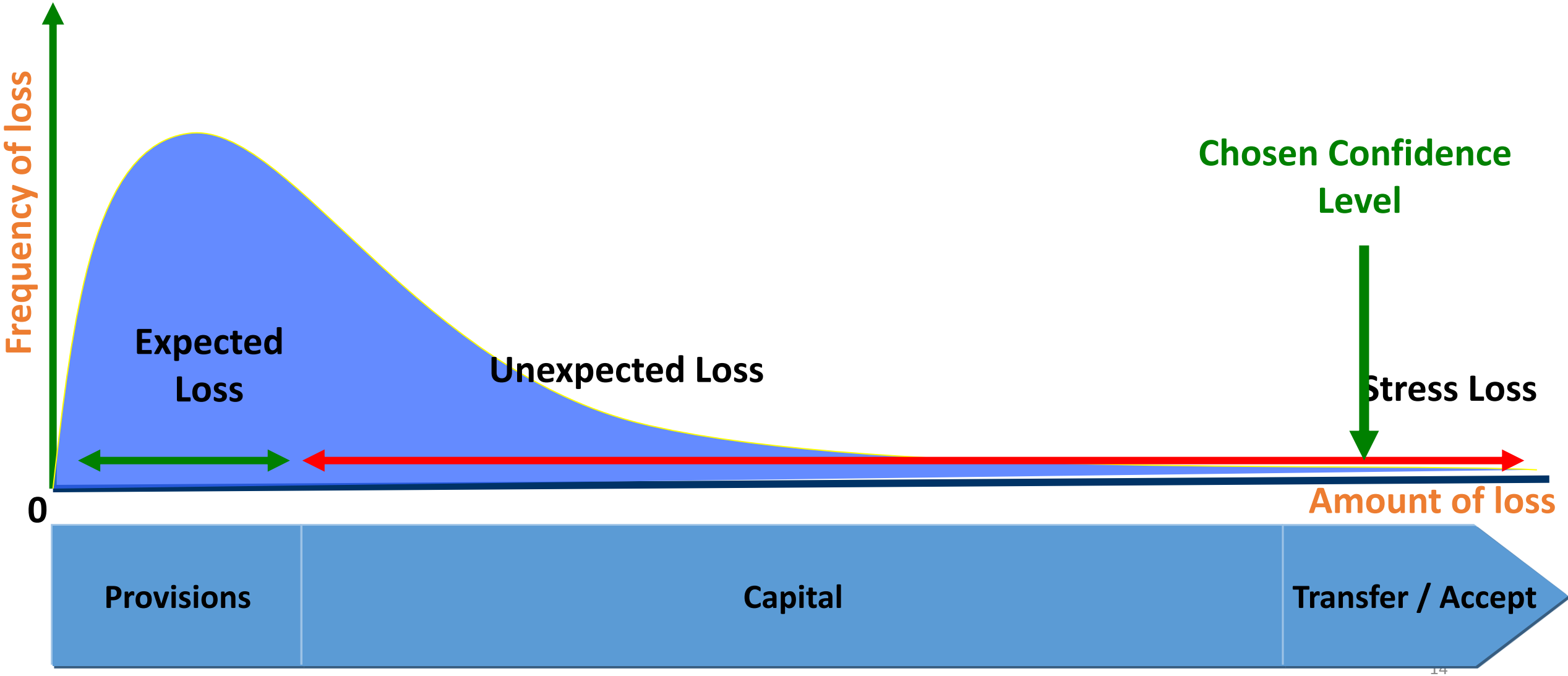
Unexpected Losses :
the actual loss that exceeds the expected loss the bank has anticipated over a period



Stress Losses :

- Those exceeding the chosen level of confidence
- Occur very rarely, but their impact is considerable




Frequency of loss
Expected Loss
Unexpected Loss
Chosen Confidence Level
Stress Loss
0
Amount of loss
Provisions
Capital
Transfer / Accept

Thank You