Financial reporting and Risk management

INDIAN BANKING AT THE CROSS ROADS
CHALLENGE OF RISK MANAGEMENT
FROM GLOBALISATION TO FINANCIAL INCLUSION

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BIS workshop held in November 2005

- Accounting standard setters v/s Prudential authorities - different priorities/perspectives.
- Risk perception varies amongst stakeholders
- Conservative accounting standards might influence risk management decisions, contrary to economic logic.
- Financial reporting should provide a good sense of the impact of those risks and uncertainties on measures of valuation, income and cash flows.
- Financial reporting system to be consistent with sound risk measurement and management practices – relevant for making well-informed decisions.
- Financial reporting – beyond numbers, should include estimates of risk profiles.

Regulatory enhancements

- Enterprise risk management, RMF
- Risk appetite
- ICAAP
- Pillar 3 disclosures
- Basel II – advanced approaches
- Basel III – quality of capital
- Risk Based Supervision
- Automated Data Flow – DQ
- XBRL

- New Banking licenses
- IFRS
- Revised Companies Act
- Tax laws

- Globalisation - need for consistent accounting and reporting practices, contagion risk
- Financial inclusion – different business models

- Alignment of business strategy, scalable IT systems, performance management and reporting platforms

FR and RM– the collaboration (1/3)

- IFRS v/s converged IndAS
- Financial reporting is primarily from accounting ledger, whereas risk management data is not
- Chart of accounts level v/s transaction level
- KPI's & KRI's (e.g. CAR, Leverage ratio, liquidity ratio, AD ratio, NPAs, NIMs, operational losses, reputational risk, early alerts, reconciliation breaks)
- Risk measurement, perception of risk, prudential norms (income recognition, impairment and de-recognition norms)
- Global v/s local norms (impacts cost of capital and cost of compliance) (e.g. IFRS, intra group exposures, collateral security, CVA, exposure to CCP, net v/s gross MTM)

FR and RM– the collaboration (2/3)

- Fair valuation v/s Historical cost accounting (MTM, LoCoM) (investments, collateral security) – principal of conservatism, application of risk margins, models validation, accounting v/s economic valuations
- Expected loss (dynamic loan loss provisioning, LGD) v/s Incurred loss
- Off balance sheet exposures
- Unhedged forex exposures
- Unfunded retiral liabilities

FR and RM– the collaboration (3/3)

- Past v/s Forward thinking (trend analysis), MMA, stress testing
- External v/s Internal reporting (slicing/dicing)
- Standardised / template driven disclosures v/s best practices. Additional disclosures in annual reports have increased their size. All of these cannot be verifiable
- Risk Based Supervision – DQ challenges (completeness, accuracy)
- ADF (Data integrity, granularity, zero touch approach), XBRL (consistency, reduced errors, timeliness)

IFRS

ADF

ICAAP

Thank you

Q & A

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