

Introduction to Dynamic Risk Management



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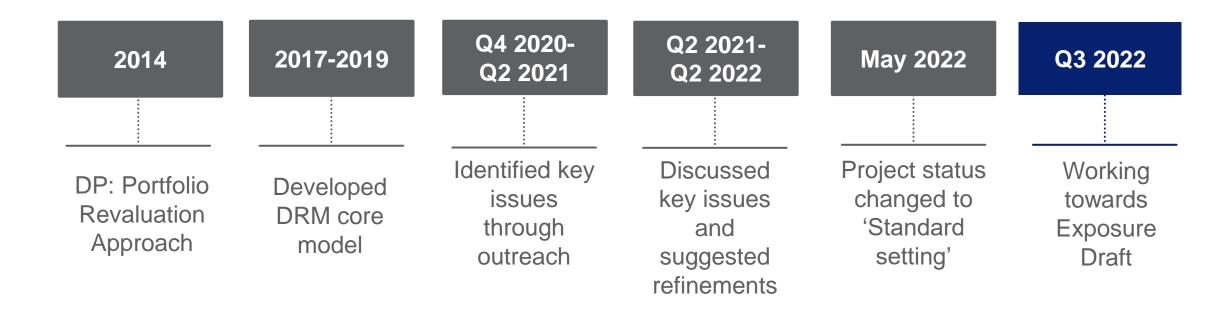


Overview of the DRM project



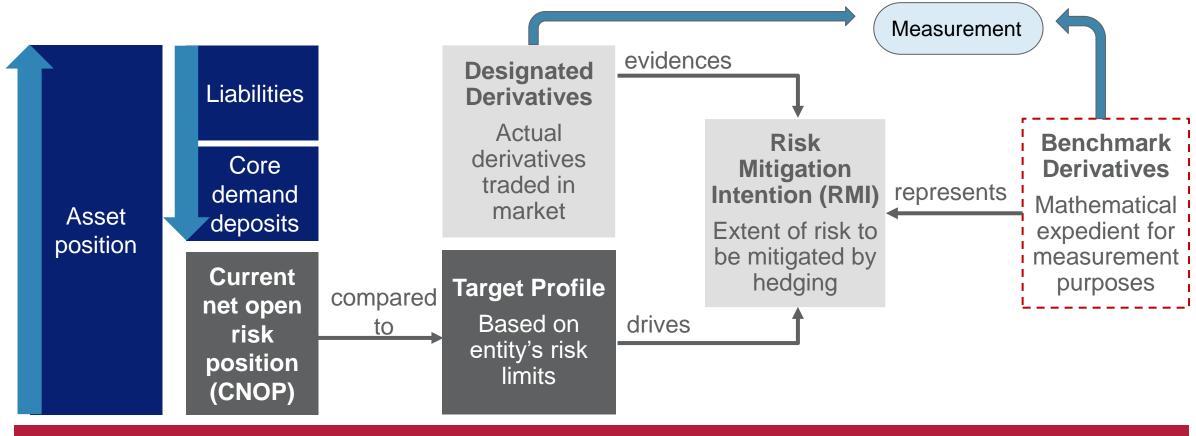
Better reflect:

- How interest rate risk management affects amount, timing and uncertainty of cash flows
- Effect of risk management activities on the financial statements





Elements of the DRM model



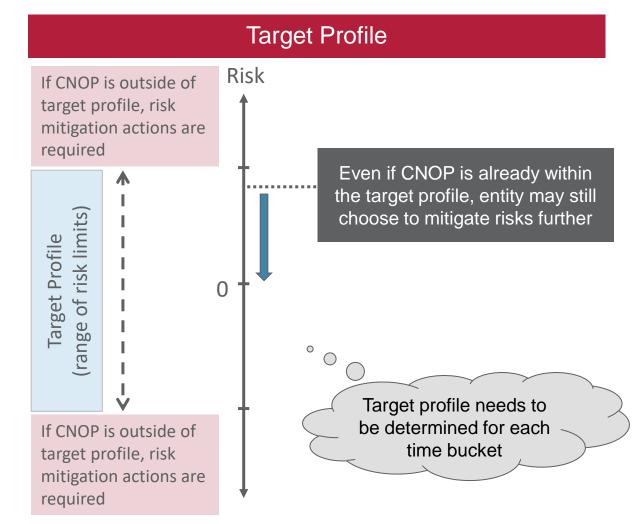
Risk Management Strategy



Risk management strategy and target profile

Risk Management Strategy (RMS)

- Basis for the other elements in the DRM model
- Expected to be kept consistent throughout the life of the DRM model and determines:
 - Process to approve and amend RMS
 - Risk management levels and scope
 - Risk metrics used
 - Range of acceptable risk limits (ie the target profile)
 - Risk aggregation method and risk management time horizon
 - Methodologies to estimate expected cash flows or core demand deposits
- Changes to RMS lead to discontinuation of the DRM model





Current net open risk position (CNOP)

Risk managed under DRM model Current net open risk position (organic risk exposures)

Risk from eligible assets

liabilities

eligible future
Risk from transactions
eligible

Risk from

Risk from designated derivatives

Risk outside of DRM model

Risk from other items ineligible for the DRM model

Risk from other derivatives

Total interest rate risk managed by risk managers

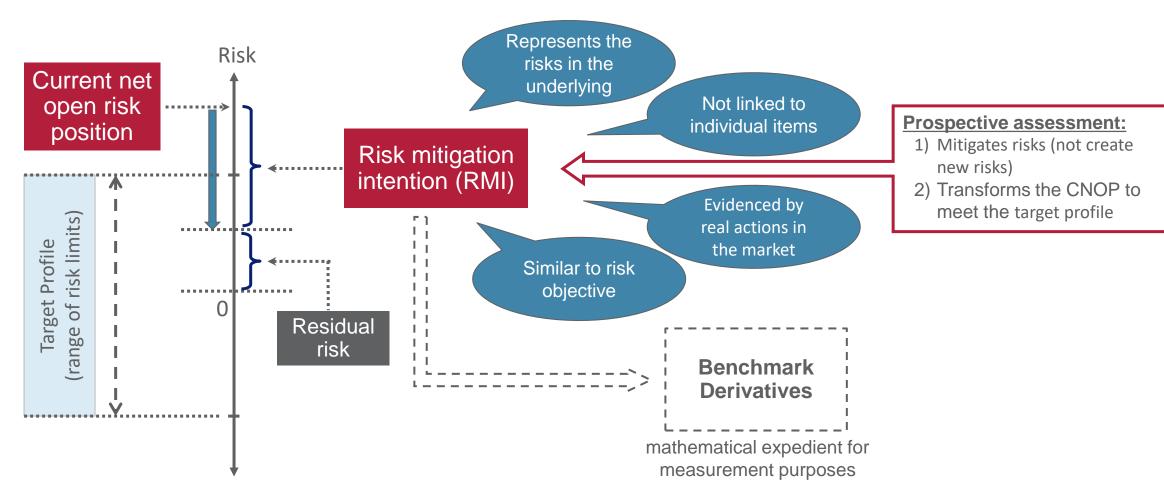
Potential deviation between risk management view and DRM view

Underlying positions

Derivatives

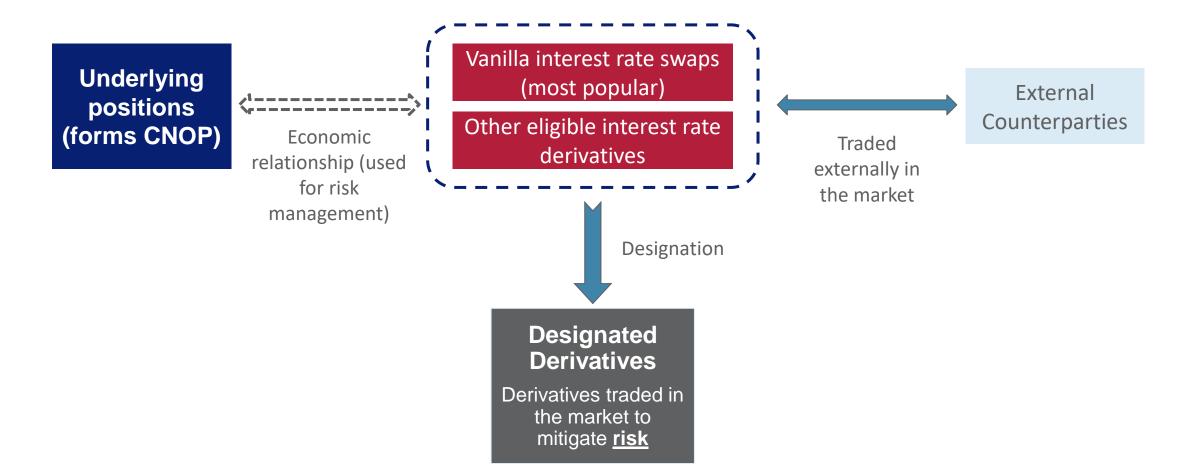


Illustration of RMI bringing CNOP within target profile



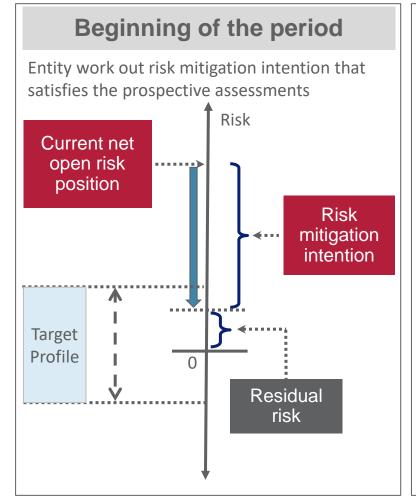


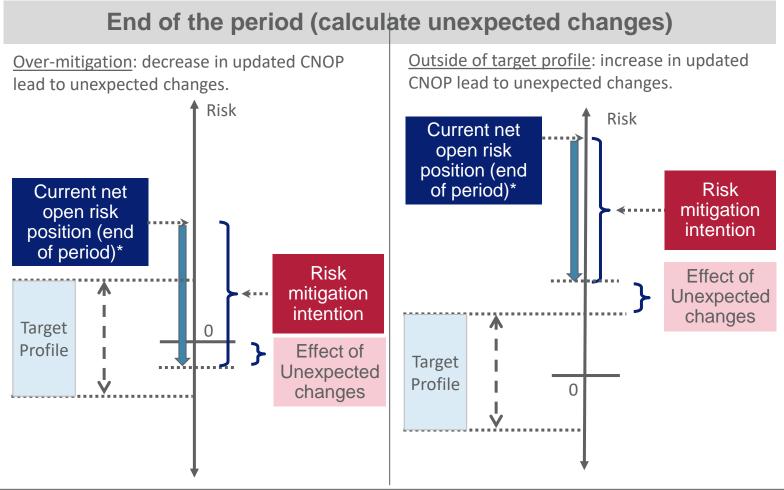
Designated Derivatives





Retrospective assessment



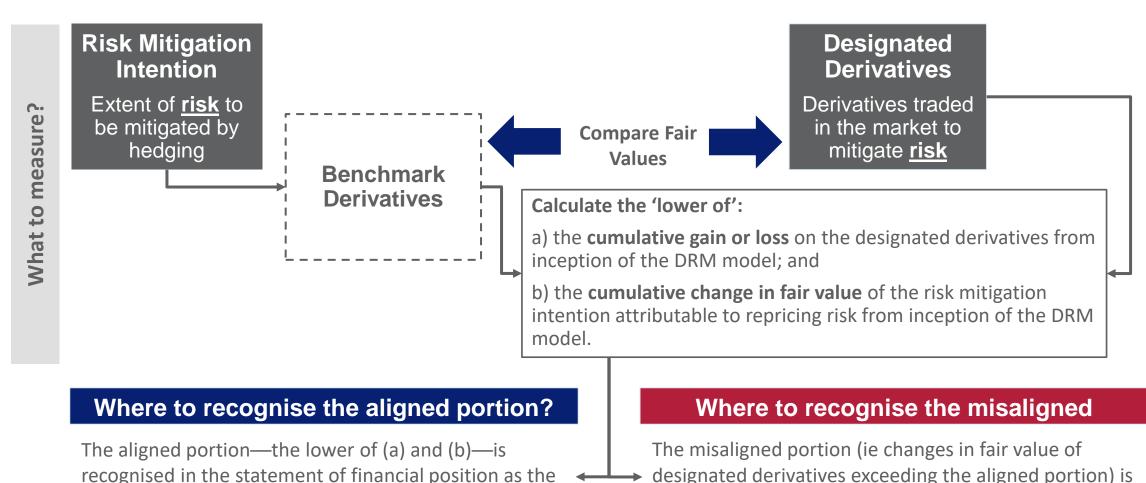


^{*} This is the current net open risk position at the end of the period, excluding new business generated and funding raised.



DRM adjustment

Mechanics of the DRM Model—Measurement



recognised in profit or loss



DRM model cycle

Prospective

Accountant

Work out risk mitigation intention (Step 2)

Risk Manager

Decide risk balancing prospectively (Step 1)

Accountant

Construct benchmark derivatives (Step 3)

Retrospective

Accountant

Work out DRM accounting adjustments (Step 6)

Accountant

Assess unexpected changes (Step 4)

Accountant

Determine the effect of unexpected changes (Step 5)



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