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IFRS 9 – Financial Instruments

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Introduction and objectives

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Overview of IFRS 9

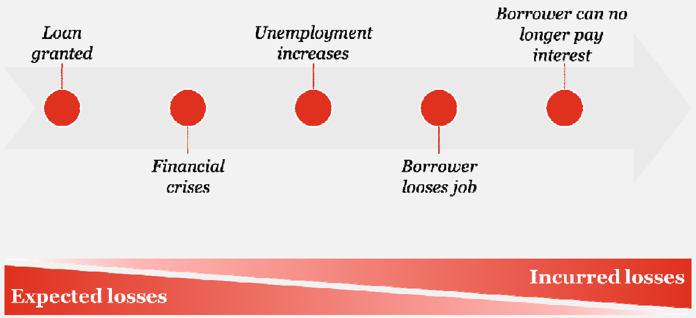
Classification and Measurement

- 3 categories for financial assets dependent on the business model assessment:

  i. Fair value through profit and loss (FVPL)
  ii. Fair value through other comprehensive income (FVOCI)
  iii. Amortized cost

Impairment of financial assets

- Expected credit losses model
- Simplified approach possible for trade receivables



Hedge accounting

- Simplification of hedge accounting and brings it in line with an entity's risk management strategy
- 80-125% effectiveness threshold is removed
- Better treatment for options
- Aggregated exposures and rebalancing
- Hedging of non-financial items
- Discounting for time value of money

Transition and disclosures

- Retrospective application (although some exceptions apply)
- comparatives are not required to be restated (with some minor exceptions for hedge accounting)
- Accounting policy choice to apply IFRS 9 hedge accounting or continue with IAS 39
- Disclosure requirements on first time adoption
- Additional disclosure requirements for IFRS 7

Classification and measurement

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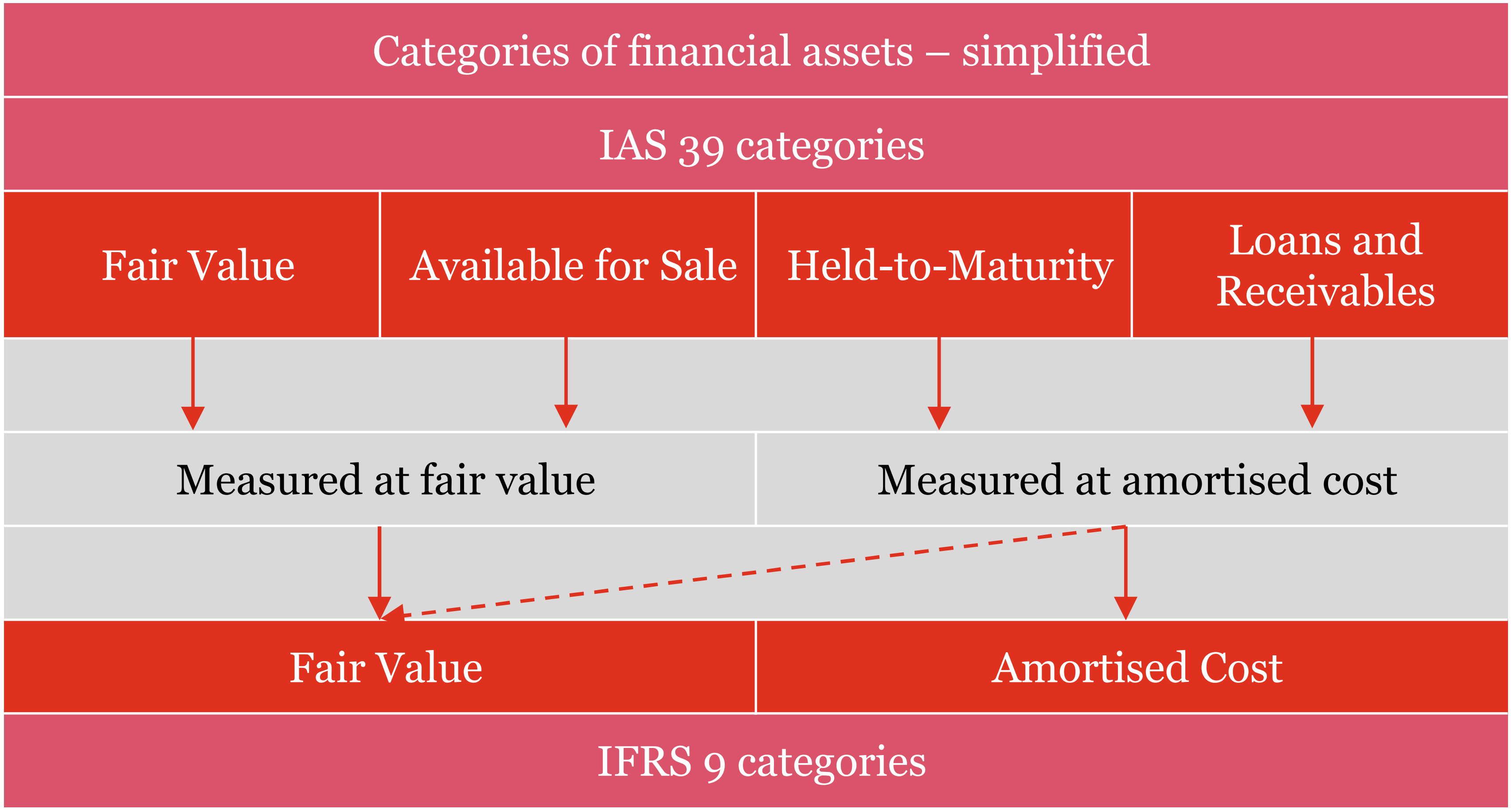
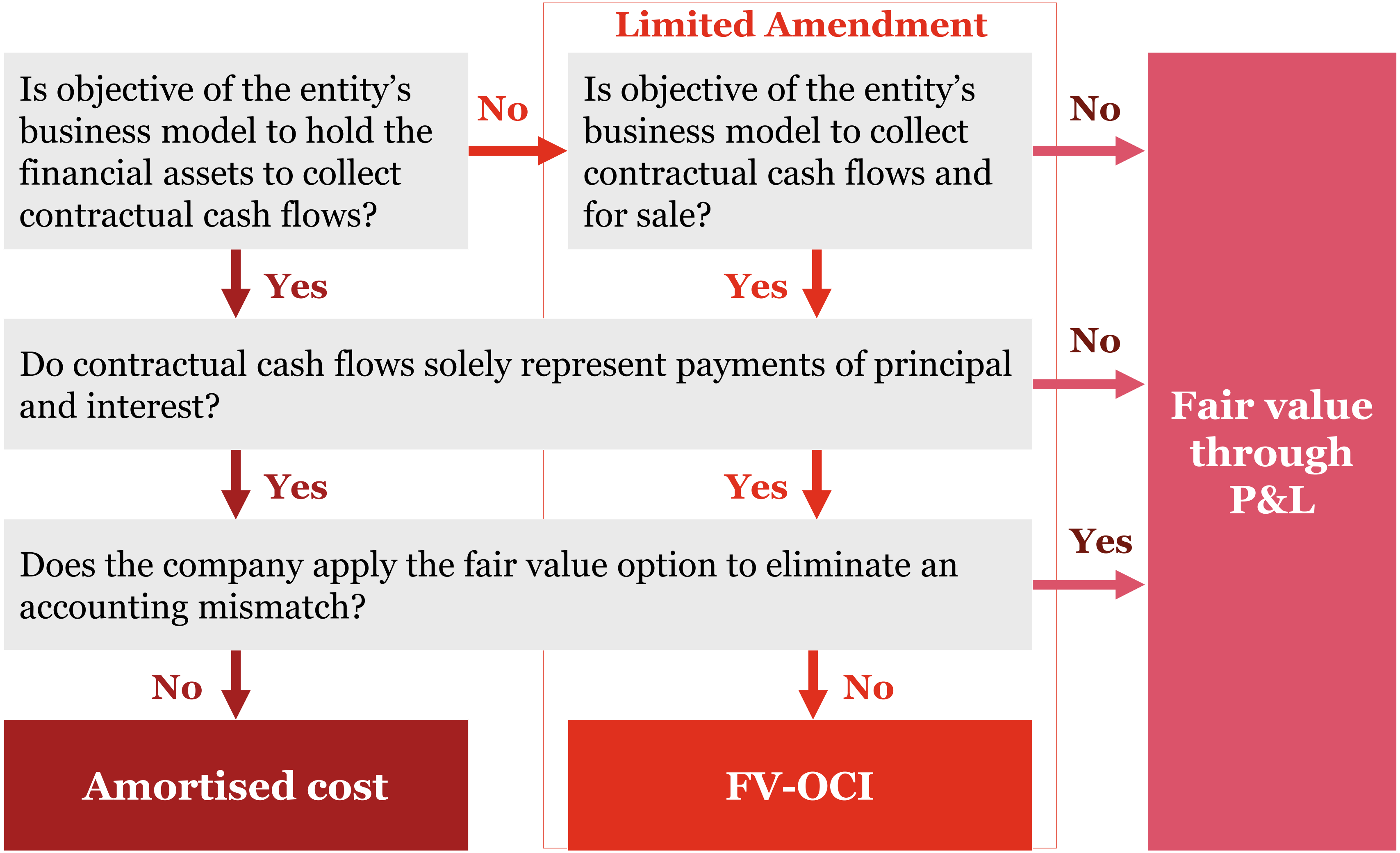
IFRS 9 – Financial assets

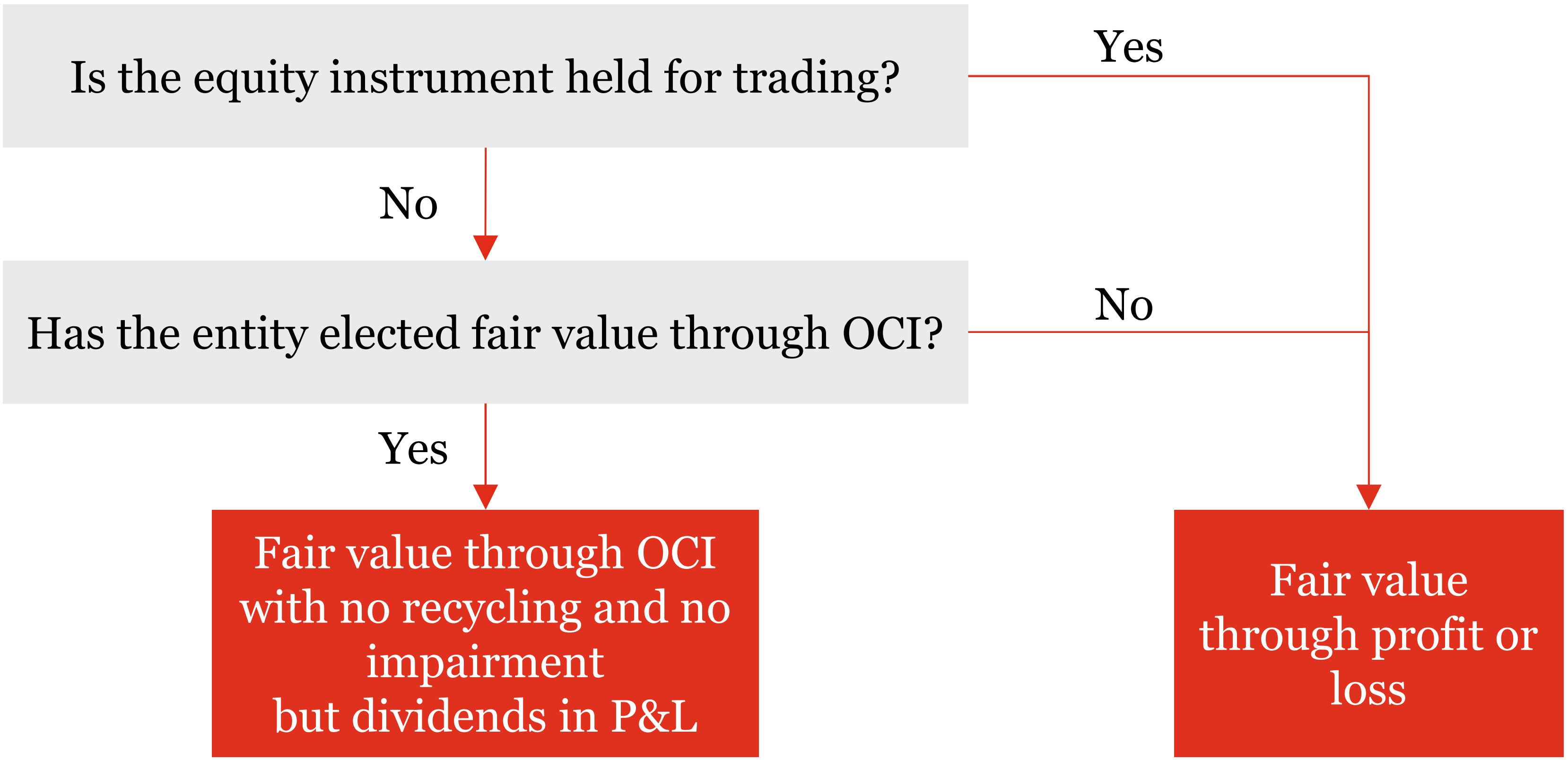
IAS 39 vs. IFRS 9 categories



Classification model for debt instruments



Classification model for equity instruments



Impairment of financial assets

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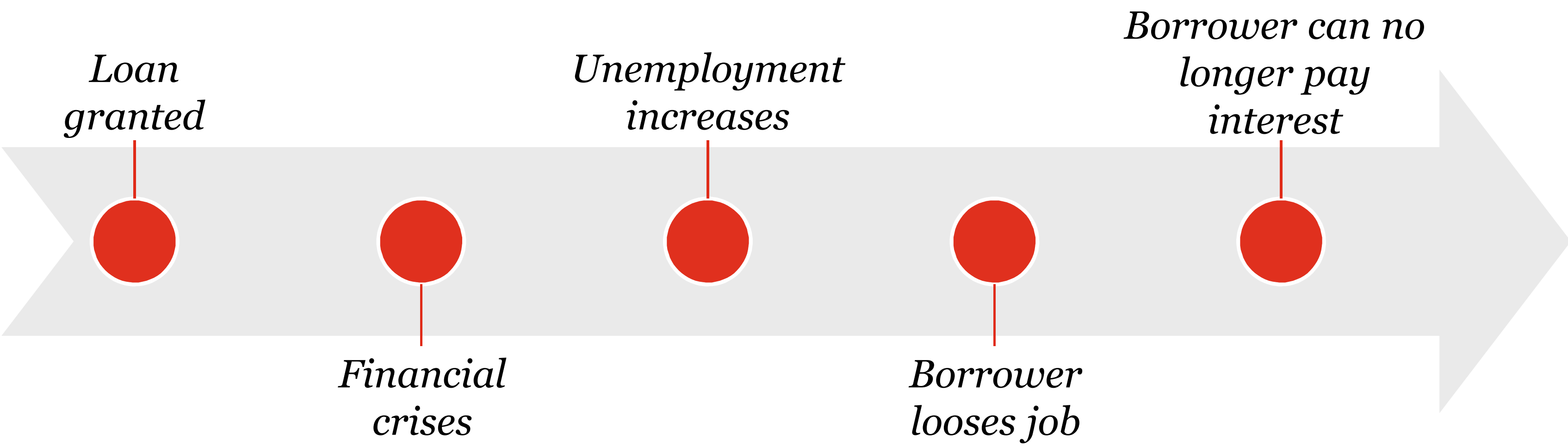
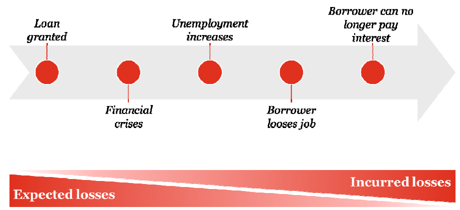
Impairment of financial assets

Expected vs. Incurred losses



Impairment of financial assets

Simplified approach for trade receivables



Always recognise lifetime expected credit losses

- Company M has a portfolio of trade receivables of CHF 30 m in 2017
- To determine the expected credit losses, Company M uses a provision matrix based on historical observed default rates

	Lifetime expected credit loss rate	Gross carrying amount in CHF	Lifetime expected credit loss allowance in CHF
Not past due	0.3%	15,000,000	45,000
1-30 days past due	1.6%	7,500,000	120,000
31-60 days past due	3.6%	4,000,000	144,000
Over 60 days past due	6.6%	3,500,000	231,000
		30,000,000	**540,000**

Hedge accounting

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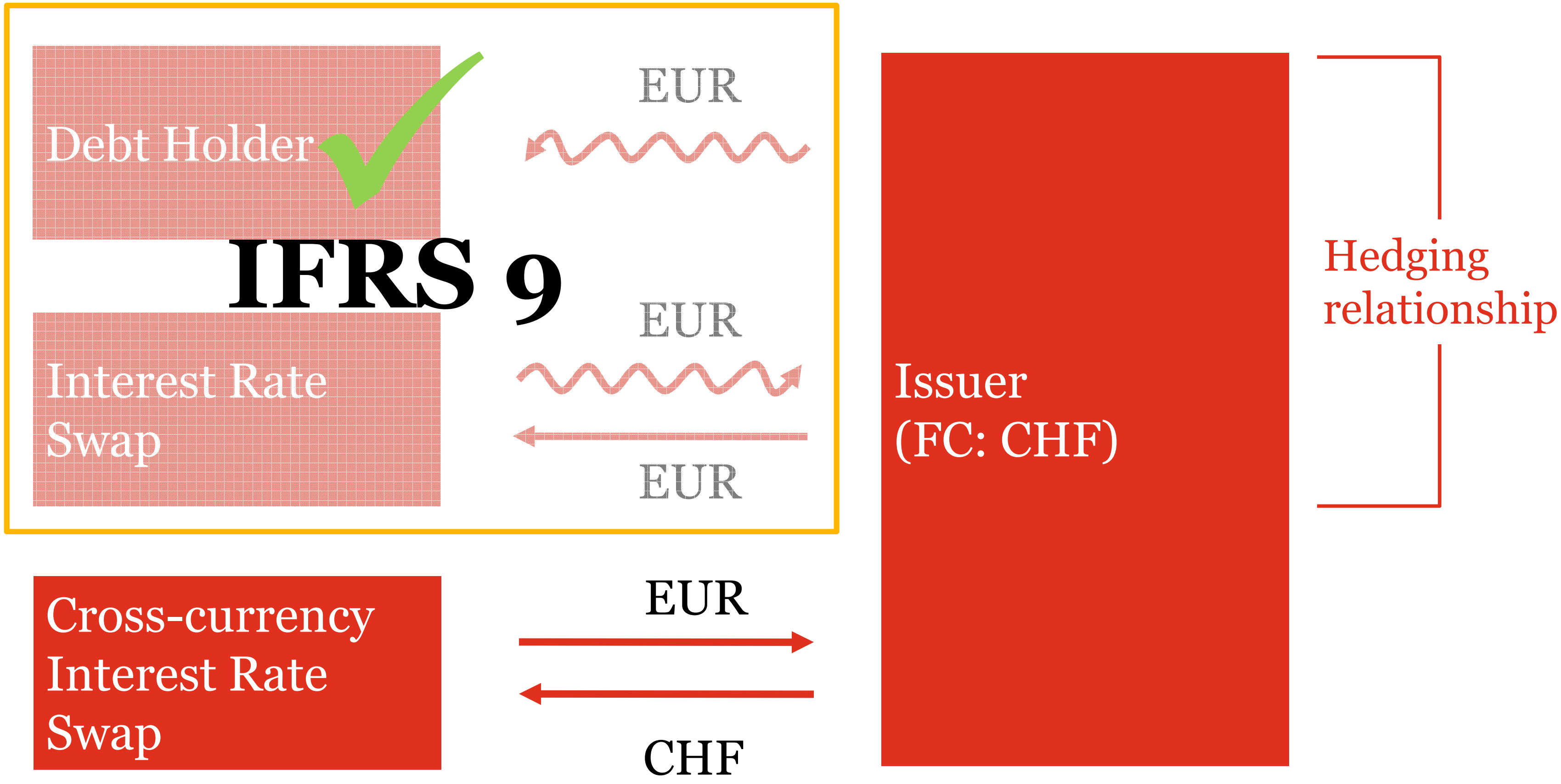
Reminder - How hedge accounting works

Gain or Loss in P/L

	2017	*2018*	*Total*
Net profit / (loss) without hedge accounting			
Hedged item		500	500
Hedging instrument	(500)		(500)
Net profit / (loss)	(500)	500	0
Net profit / (loss) with a fair value hedge			
Hedged item	500	0	500
Hedging instrument	(500)		(500)
Net profit / (loss)	(0)	0	0
Net profit / (loss) with a cash flow hedge			
Hedged item	0	500	500
Hedging instrument	(0)	(500)	(500)
Net profit / (loss)	(0)	0	0

Hedge accounting - Main new features

Aggregated exposure



Hedge accounting - Main new features

Options as hedging instruments

Current market price of underlying = 12

Strike price = 10

Intrinsic value = 2

Time value = 4

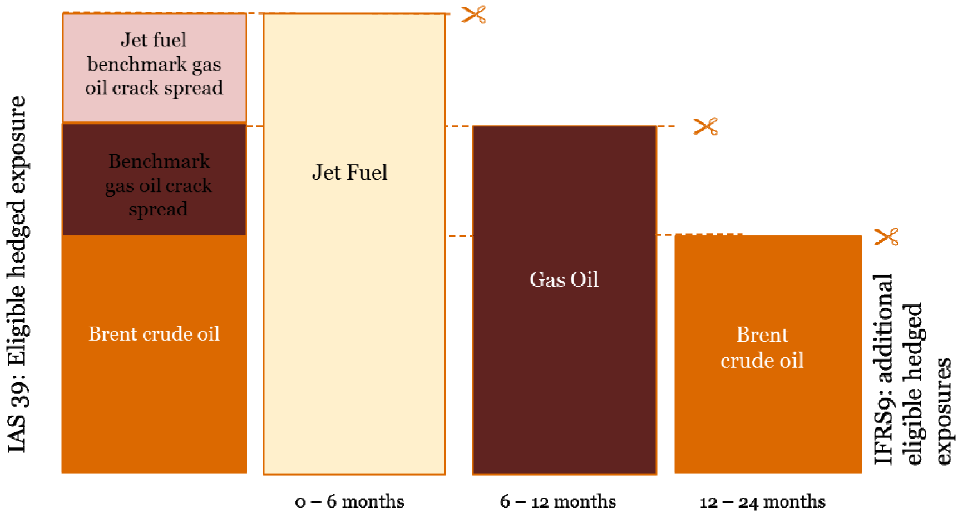
Premium paid = 6

Transaction related: The initial time value paid has the character of the costs of that transaction.

Time-period related: The initial time value has the character of a cost for obtaining protection against a risk over a particular period of time.

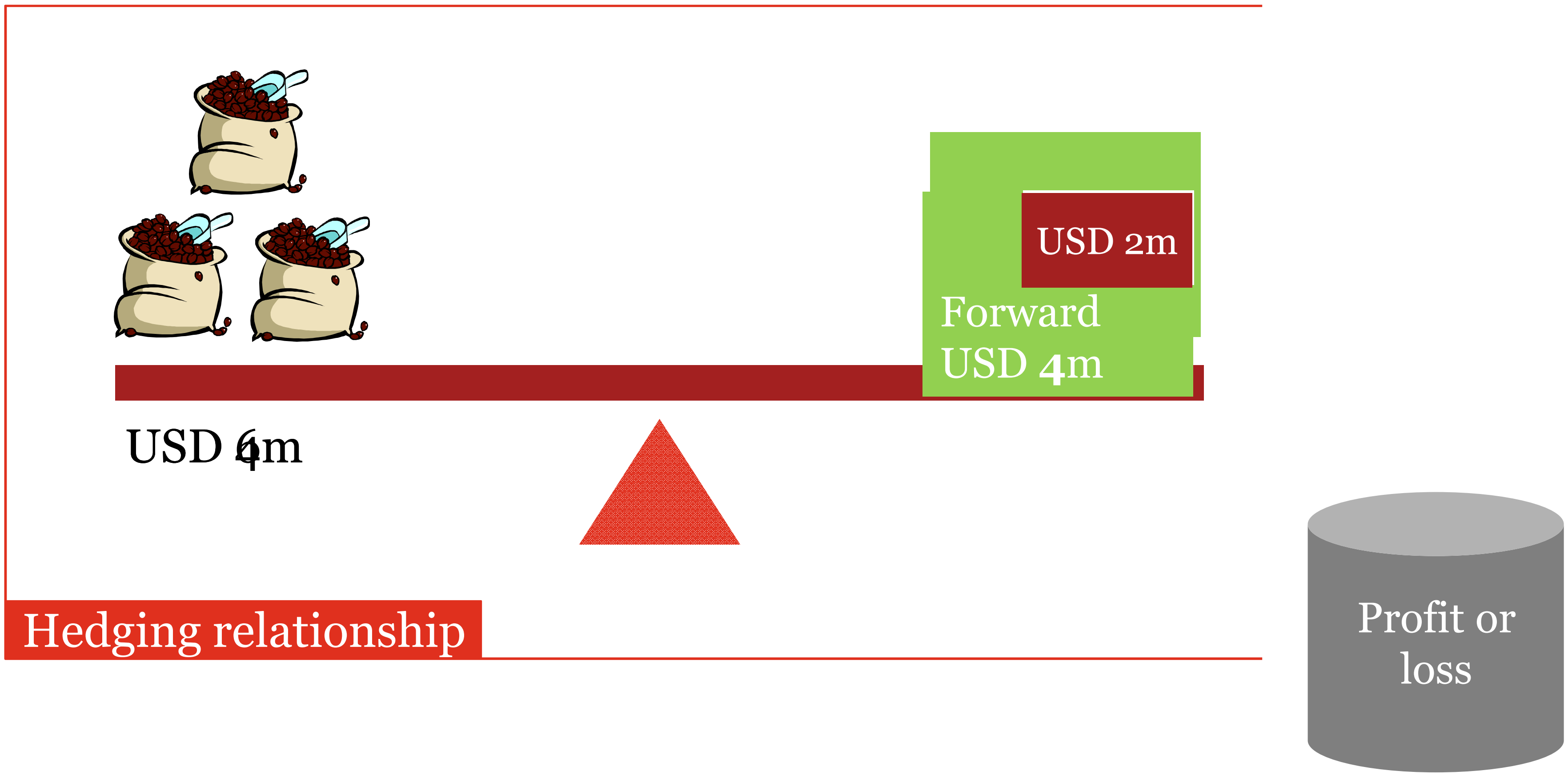
Hedge accounting - Main new features

Non-financial risk components



Main new features

Rebalancing – example



Disclosures

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Disclosure requirements - overview

Main effects on disclosures…

- Basis of preparation – New and amended standards adopted by the company (i.e. IFRS 9)
- Change in Accounting policies – Summary of all changes from IFRS 9
- Classification and measurement of financial instruments (FVOCI, FVTPL, Amortized Cost) – Effects from re-classifications. Additional detailed requirements and first time application
- Derivatives and hedging activies – Risk management strategy, timing and effect from hedge accounting in financial statements
- Credit risk and impairment of financial assets – IFRS 9 Credit loss model

Some other topics

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Lessee accounting – impact IFRS 16 (1/4)

IAS 17: Classification based on risk and rewards

	Finance lease		Operating lease
Balance sheet	Asset Lease liability		
Income statement	Depreciation expense Interest expense		Lease expense

Lessee accounting – impact IFRS 16 (2/4)

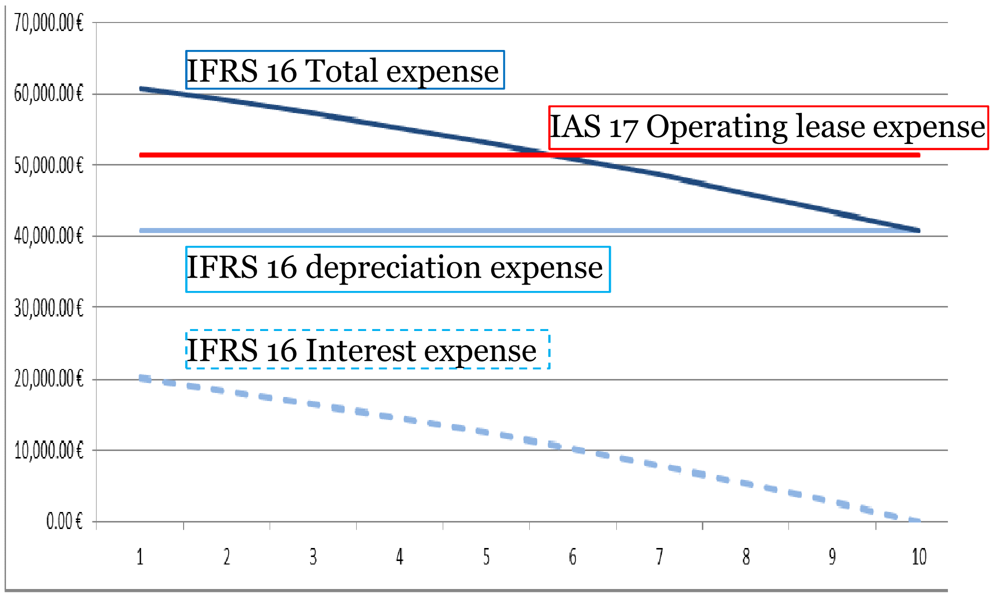
IFRS 16: All leases on the balance sheet

All leases

- Right-of-use asset
- Lease liability

- Depreciation expense
- Interest expense

Pattern of expense recognition in profit or loss



Lease Accounting – IFRS 16 (3/4)

- Balance sheets will grow, gearing ratios will increase, and capital ratios will decrease.
- Rent expenses replaced with depreciation and interest expense.
- Acceleration of lease expense relative to the recognition pattern for operating leases today.
- These changes may affect loan covenants, credit ratings and borrowing costs, and could result in other behavioural changes.
- The cost to implement and continue to comply with the new leases standard could be significant for most lessees. Particularly if they do not already have an in-house lease information system.
- Lessor accounting remains largely unchanged from IAS 17.
- Effective as of January 1, 2019.

Impact of lease capitalization – IFRS 16 (4/4)

Industries with heavy use of rentals will be impacted…

Industry	*Median increase debt (*)*	*Median increase EBITDA*	*Median change leverage (**)*		*Median decrease in solvency (***)*	
			Before standard	*After standard*	*Before standard*	*After standard*
All companies	**22%**	**13%**	**2,03**	**2,14**	**35%**	**32%**
Retailers	98%	41%	1,17	2,47	41%	28%
Airlines	47%	33%	3,26	3,63	25%	19%
Professional services	42%	15%	0,53	0,96	40%	37%
Health care	36%	24%	2,11	2,92	22%	19%
Wholesale	28%	17%	2,04	2,31	31%	29%
Transport & Infrastructure	24%	20%	2,21	2,52	36%	30%
Entertainment	23%	15%	1,78	1,30	30%	25%
Telecommunications	21%	8%	1,65	2,00	23%	21%

Source: PwC Global Lease Capitalization study of 3,199 listed IFRS reporters.

(*) Interest-bearing debt
(**) Net debt / EBITDA
(***) Equity less Intangibles / Total Assets

IFRIC clarification on notional pooling

Offset not available if cash movements expected before next settlement date

To have offset – IAS 32 requires:

- Legal right of offset
- Practice and intent of net settlement

Clarification Interpretations Committee:

"To the extent to which the group did not expect to settle its subsidiaries' period-end account balances on a net basis, it would not be appropriate for the group to assert that it had the intention to settle the entire period-end balances on a net basis at the reporting date."

Will make it very difficult to prove intent, unless the period-end balance is the balance which will be net-settled.

Questions and discussion

With you today

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Thank you!

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