

ALM, FAIR VALUATION AND BALANCE SHEET OPTIMISATION

12-hour course

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Course Outline

This course provides a practitioner's insight into how a bank and an insurance company handle their Assets and Liabilities Management (ALM) and how they seek to manage their balance sheet and P/L (profit and loss account) in the face the new regulatory environment, and in particular the Basle 3 and Solvency II solvency, liquidity and leverage requirements.

The course covers the fundamentals of ALM of a bank and an insurance company, managing the risks arising from assets and liabilities mismatches. It reviews in particular the management of interest rate and liquidity risks, as well as transfer pricing issues and commercial margins monitoring. The course also dissects how hedges are used in bank's hedge accounting format, to mitigate the P/L volatility and protect NAV.

It also examines in a practical way how new / advancing accounting rules impact a bank's balance sheet and P/L, in particular the valuation of financial instruments, including derivatives. It analyses the key issues for banks deriving from the shift to IFRS rules (from IAS39 to IFRS 9), the assessment of fair values and the need for fair value adjustments, including Credit Value Adjustment (CVA), Debit Value Adjustment (DVA), and Funding Value Adjustment (FVA) for derivatives.

For each part of the course, some practical exercises are used in class to allow Participants to translate their understanding into practical skills usable in their professional environment.

The course includes a session where Participants use a bank-designed model to assess the impact on the balance sheet and the P/L account of the range of different Basel 3 requirements: solvency requirements, liquidity ratios (Liquidity Coverage Ratio and Net Stable Funding Ratio) and leverage ratio. For this purpose, Participants work in teams, using a stylized balance sheet of a bank, with the objective, through three successive rounds of optimization, to maximize the profit profile while respecting at all times the relevant regulatory requirements. It allows Participants to apprehend the interplay of the different regulatory constraints in a real business context and understand how a bank's management make decisions on business activities growth.

At the end of the course, Participants will be able to:

- understand ALM drivers and tools and use them in a professional context
- apprehend the key facets of interest rate and liquidity risks in a bank and insurance company, and how they manage them
- assess the major impacts that fair value requirements have on a bank and how these effects can be managed
- integrate the key Basel 3 requirements, and the interplay between them, into a business analysis that seeks to optimize the P/L implications.

Course structure

- I. **Introduction**
- II. **Asset and Liabilities Management**
 - a. Management of interest rate risk
 - b. Management of liquidity risk
 - c. Transfer pricing system
 - d. Commercial margins
 - e. Hedge accounting
- III. **Financial Instruments Valuation**
 - a. From IAS 39 to IFRS 9 – key business and financial implications
 - b. Fair value credit and funding charges
 - i. Credit Value Adjustment (CVA)
 - ii. Debt Value Adjustment (DVA)
 - iii. Funding Value Adjustment (FVA)
- IV. **Balance Sheet and Profit and Loss Optimisation**
 - a. Basel 3 Optimisation Exercise
 - b. Key lessons drawn