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Intro Investment Banker Perspective

Part 1

Public Sector

International Public Sector Accounting Standards (IPSAS)

- **International Public Sector Accounting Standards Board (IPSASB), a specialty board of the International Federations of Accountants (IFAC), New York.**
- **Started in 1977 with 63 members, now comprises 164 members and associates in 125 countries and jurisdictions, representing over 2.5 million accountants.**
- **ICPAK is a member.**



IPSAS

- **For general purpose financial statements of all public sector entities:**
 - **national (central), regional, local governments**
 - **component entities such as departments, agencies, regulator authorities, boards, commissions, etc.**
- **Do not apply to Government Business Enterprises (GBE).**

Importance

- **Global financial crisis highlighted concern IFAC expressed for three decades: ‘to ensure equal access to high-quality financial information, world needs one set of high-quality global accounting standards’.**
- **Action taken post-crisis is to make recommendations to G20 leaders: ‘need for governments to move to IPSAS as a means to improve public sector financial management and financial transparency’.**

Why IPSAS ?

1. True and fair view

Part of accounting in public sector does not give insight into actual situation of assets, finances, revenue (true, fair view).

Difficult for general public, politicians to assess accounting systems.

IPSAS provide assistance with uniform standards.

Why IPSAS ?

2. Internal control and monitoring

Basis for efficient control and monitoring processes in public administration is **valid Information.**

IPSAS helps improve quality of financial information.

This simplifies the internal control and monitoring of public resources.

Why IPSAS ?

3. Compatibility with private sector accounting

As a rule, accounting systems of public and private institutions are incompatible.

System of accounting based on internationally recognised standards reduces these interface problems.

Why IPSAS ?

4. Comparisons and rating

World: plethora of different regulations on accounting in public sector.

Annual accounts of a local authority in Kenya may not be comparable with the local authority in UK, Germany or USA.

Public institutions are reliant on financing through credit and borrowing.

Standardised system considerably simplifies valid assessment of efficiency of public institutions and rating.

IPSAS & IAS

IPSAS based on IAS standards for private companies but adapted to requirements of public sector.

Examples

IPSAS 1	Presentation of Financial Statements	IAS 1
IPSAS 2	Cash Flow Statements	IAS 7
IPSAS 3	Accounting Policies, Changes in Accounting Estimates and Errors	IAS 8
IPSAS 4	The Effects of Changes in Foreign Exchange Rates	IAS 21
IPSAS 5	Borrowing Costs	IAS 23
IPSAS 6	Consolidated and Separate Financial Statements	IAS 27
IPSAS 7	Investments in Associates	IAS 28
IPSAS 8	Interests in Joint Ventures	IAS 31
IPSAS 9	Revenue from Exchange Transactions	IAS 18
IPSAS 10	Financial Reporting in Hyperinflationary Economies	IAS 29
IPSAS 11	Construction Contracts	IAS 11
IPSAS 12	Inventories	IAS 2
IPSAS 13	Leases	IAS 17
IPSAS 14	Events After the Reporting Date	IAS 10

World Implementation

Many countries across all continents have adopted or are in the process of adopting or have plans to adopt.

A number are in the process of implementing Cash Based IPSAS first before moving onto Accrual Based IPSAS.

So, what is the position in Kenya and the EA region ?

Adoption ?

Symbolic adoption: by making general declaration of intent to adopt IPSAS

Operational adoption

- Making legal or contractual commitments**
- Securing financial and human resources**
- Purchasing hardware and software**
- Installing systems and training personnel**
- Putting accounting system into operation**
- Producing financial reports**

GOK Accounting as Institutional Infrastructure

- **Common perception: government accounting as a bureaucratic function**
- **My view: government accounting as an important part of a country's critical institutional infrastructure**
- **Analogies: the foundation of a house, or the sewer lines of a city**
- **Characteristics: invisible until it fails**

Proper Institutional Governance?

- **Autonomy:** Accounting of GOK is necessarily done *by government itself*.
- **Credibility:** But GOK accounting and reporting is not credible if GOK itself decides the rules.
- **Should GOK be required to provide information by a higher political or legal authority ?**
- **Economic leverage:** Generally, sovereign nations could be induced to provide information by prospect of receiving commensurate benefits.

Some Key Interested Parties

- **Ministry of Finance**
- **Kenya National Audit Office**
- **ICPAK and Members**
- **Parliament**
- **Central Bank of Kenya**
- **Kenya Bankers Association**
- **Capital Markets Authority**
- **Nairobi Stock Exchange**
- **Investment Banks**
- **IMF**
- **World Bank**

Part 2

Financial Stability

Report

Vital services

Preserving financial stability involves maintaining the supply of three vital services to the wider economy:

- 1. providing the main mechanism for paying for goods, services and financial assets;**
- 2. intermediating between savers and borrowers through bank credit, and debt and equity instruments; and**
- 3. recognizing and dispersing risk.**

Provision of Financial Services

- **Selected payment systems**
- **Household, corporate deposit growth**
- **Spreads-quoted household deposit rates**
- **Spreads on lending to households**
- **Changes-availability of household credit**
- **Mortgage product availability**
- **Comparison of historical household lending spreads**
- **Corporate lending costs by firm size**
- **Issuance of corporate bonds**
- **Issuance of corporate equity**

Risks from the Regional Financial System

Kenyan banks and other financial sector actors are increasingly becoming materially exposed to risks from the regional financial system, given their increasing sophistication and focus.

A Cross-border Capital flows:

- **Political environment**
- **Macroeconomic indicators**
- **Government fiscal balances**
- **Country ratings**
- **Bill, bond yields**
- **Equity indices**
- **Safe assets (inc gold, silver),**
- **Portfolio funds into Africa**
- **Corporate bond spreads, ratings**

B Sources of risk from the regional financial system:

- **market risk from a sudden reversal in bond yields and a reappraisal of asset valuations;**
- **sovereign risk concerns in the region, which could result in flight to quality;**
- **funding liquidity risk**

Credit risks to banking system

Driven ultimately by losses on loans to households, companies and sovereigns (GOK, public sector, parastatals) which account for majority of lending:

- 1. Claims on Kenyan owned banks and non-banks**
- 2. Gross debt to GDP ratio**
- 3. Banks' return on assets & loan loss reserve**
- 4. Usage of Central Bank liquidity facilities**
- 5. Corporate and household write-off rates**

6. Systemic risk survey:

- **Economic downturn**
- **Funding problems**
- **Liquidity problems**
- **Regulation impact**
- **Property price falls**
- **Sovereign risk/public debt**
- **Financial market disruption /dislocation**
- **Household defaults**
- **Corporate defaults**
- **Financial institution failure/distress**

- 7. Corporate liquidations**
- 8. Household liquidations**
- 9. Cross-border borrowings**
- 10. Corporate capital gearing & distribution**
- 11. Household capital and income gearing**
- 12. Property price to rent indices**
- 13. Unsecured debt repayment gearing**

Resilience of financial system

- **Stress Tests**
- **Banks' pre-tax profits trend**
- **Banks' sources of revenue, impairments**
- **Banks' total assets trend**
- **Banks' large exposures (> 10% to capital)**
- **Banks' core capital trend**

Resilience of financial system

- **Historical household saving ratio, deposits and loans trend**
- **Reduction in banks' pre-tax profits from a hypothetical shock**
- **Banking system refinancing requirements**

- **Impairment charges, write-offs and changes in GDP**
- **Banks' current impairment allowances compared to potential expected losses in illustrative scenarios**
- **Banks' aggregate balance sheet trend**
- **Banks' price to book ratios trend**
- **Banks' pre-tax return on equity trend**
- **Insurers financial performance**

- **Capital markets licensees financial performance**
- **Microfinanciers financial performance**
- **Forex bureaus financial performance**
- **Co-operatives financial performance**
- **Others financial performance**

Preserving financial stability

- **Comparison of current and new capital requirements for various groups of financial institutions**
- **Phase-in arrangements for changes to regulatory capital requirements**
- **Total capital ratios in the region and internationally**
- **Risk based key ratios**

Contingent capital

Should systemically important financial institutions (SIFIs) be subject to higher loss-absorbency standards in the future ?

Should we require SIFIs to issue additional common equity or 'contingent capital' in the future ?

Contingent capital

**‘precautionary’ contingent capital,
designed to absorb losses in
relatively early stages of financial
distress;**

**‘non-viability’ contingent capital,
designed to absorb losses when
institution is on verge of failure.**

**Knowledge is power.
Information is power.
Information is liberating.
Liberation is democracy.
Enhanced democracy can
lead to more confidence.**



simply, we are the standard

Thank you

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