

Workshop 3 - Understanding Bank Financial Statements III

AFIN8003 Workshop 3

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2025-08-11

1 Simple banking book accounting

1.1 A first look at bank's balance sheet

To begin with, a simple bank has just been established with shareholders' contribution of \$10,000.

Balance Sheet

| | |
|----------------------------|-------------|
| Assets | |
| Cash and Cash Equivalents | \$10,000.00 |
| Total assets | \$10,000.00 |
| Liabilities | |
| Total liabilities | \$0.00 |
| Net assets | \$10,000.00 |
| Shareholders' equity | |
| Shareholders' Equity | \$10,000.00 |
| Total shareholders' equity | \$10,000.00 |

Date: 2025-07-28

1.2 Customer deposit

Now some customers have made some deposits, for example:

- Customer A deposits \$60,000.
- Customer B deposits \$40,000.
- Customer C deposits \$20,000.

Notably, customer deposits are the bank's *liability*. We see an increase in both the bank's total assets and total liabilities, while total shareholders' equity remains unchanged.

Balance Sheet

| | |
|--------------------------------------|--------------|
| Assets | |
| Cash and Cash Equivalents | \$130,000.00 |
| Total assets | \$130,000.00 |
| Liabilities | |
| Deposits and Other Public Borrowings | \$120,000.00 |
| Deposits | \$120,000.00 |

| | |
|----------------------------|--------------|
| Total liabilities | \$120,000.00 |
| Net assets | \$10,000.00 |
| Shareholders' equity | |
| Shareholders' Equity | \$10,000.00 |
| Total shareholders' equity | \$10,000.00 |

Date: 2025-07-28

1.3 Deposit withdraw

Depositors can also withdraw from the bank.

If Customer C has withdrawn all of their deposits (\$20,000), we see a decrease of cash and deposits.

Balance Sheet

| | |
|--------------------------------------|--------------|
| Assets | |
| Cash and Cash Equivalents | \$110,000.00 |
| Total assets | \$110,000.00 |
| Liabilities | |
| Deposits and Other Public Borrowings | \$100,000.00 |
| Deposits | \$100,000.00 |
| Total liabilities | \$100,000.00 |
| Net assets | \$10,000.00 |
| Shareholders' equity | |
| Shareholders' Equity | \$10,000.00 |
| Total shareholders' equity | \$10,000.00 |

Date: 2025-07-28

1.4 Loan disbursement

Of course, the typical business of a bank is to make loans. Let's assume the bank has made an (interest-only) loan of \$80,000 to some borrowers.

Balance Sheet

| | |
|--------------------------------------|--------------|
| Assets | |
| Cash and Cash Equivalents | \$30,000.00 |
| Loans and Advances | \$80,000.00 |
| Total assets | \$110,000.00 |
| Liabilities | |
| Deposits and Other Public Borrowings | \$100,000.00 |
| Deposits | \$100,000.00 |
| Total liabilities | \$100,000.00 |
| Net assets | \$10,000.00 |
| Shareholders' equity | |
| Shareholders' Equity | \$10,000.00 |

| | |
|----------------------------|-------------|
| Total shareholders' equity | \$10,000.00 |
|----------------------------|-------------|

Date: 2025-07-28

1.5 Interest paid on deposits

After some time (e.g., a month), the bank may need to pay interest on customers' deposits, e.g., \$100.

💡 **Income Statement** is included given that we'd like to know the profit and loss (P&L) of the bank over the period.

Balance Sheet

| | |
|--------------------------------------|--------------|
| Assets | |
| Cash and Cash Equivalents | \$29,900.00 |
| Loans and Advances | \$80,000.00 |
| Total assets | \$109,900.00 |
| Liabilities | |
| Deposits and Other Public Borrowings | \$100,000.00 |
| Deposits | \$100,000.00 |
| Total liabilities | \$100,000.00 |
| Net assets | \$9,900.00 |
| Shareholders' equity | |
| Shareholders' Equity | \$10,000.00 |
| Retained Earnings | (\$100.00) |
| Total shareholders' equity | \$9,900.00 |

Date: 2025-08-28

Income Statement

| | |
|------------------|------------|
| Income | \$0.00 |
| Expense | \$100.00 |
| Interest Expense | \$100.00 |
| Profit | (\$100.00) |

Date: 2025-08-28

1.6 Loan interest income

i If the bank has only paid interest on deposits over this period, it surely has a net loss or negative profit as shown before.
However, it is more reasonable that the bank also has earned some profits during the same time, especially because it has made some loans.

Suppose that over the 1-month period, the bank has earned some interest income from the loans made earlier, e.g., for a total of \$800.

💡 Overall, the bank has a net profit of \$700. We can observe that the bank's **Retained Earnings** has increased by \$700, too.

Balance Sheet

| | |
|--------------------------------------|--------------|
| Assets | |
| Cash and Cash Equivalents | \$30,700.00 |
| Loans and Advances | \$80,000.00 |
| Total assets | \$110,700.00 |
| Liabilities | |
| Deposits and Other Public Borrowings | \$100,000.00 |
| Deposits | \$100,000.00 |
| Total liabilities | \$100,000.00 |
| Net assets | \$10,700.00 |
| Shareholders' equity | |
| Shareholders' Equity | \$10,000.00 |
| Retained Earnings | \$700.00 |
| Total shareholders' equity | \$10,700.00 |

Date: 2025-08-28

Income Statement

| | |
|------------------|----------|
| Income | \$800.00 |
| Interest Income | \$800.00 |
| Expense | \$100.00 |
| Interest Expense | \$100.00 |
| Profit | \$700.00 |

Date: 2025-08-28

2 Intermediate trading book accounting

2.1 Trading Book

The transactions and non-transactions previous discussed all occur to the bank's **banking book**.

However, a bank also has a **trading book** that holds securities for short-term trading P&L purposes.

i These instruments are named **Fair Value Through Profit and Loss (FVTPL)**.

Accounting for trading book securities is relatively easy. We consider:

1. The purchase
2. The marking-to-market
3. The sale

2.2 FVTPL security purchase

Assume that the bank just purchased a FVTPL security for its trading book at its fair value of \$10,000.

The fair value of the security is recorded on the balance sheet under the *Assets at FVTPL* account.

Balance Sheet

| | |
|--------------------------------------|--------------|
| Assets | |
| Cash and Cash Equivalents | \$30,700.00 |
| Loans and Advances | \$80,000.00 |
| Total assets | \$110,700.00 |
| Liabilities | |
| Deposits and Other Public Borrowings | \$100,000.00 |
| Deposits | \$100,000.00 |
| Total liabilities | \$100,000.00 |
| Net assets | \$10,700.00 |
| Shareholders' equity | |
| Shareholders' Equity | \$10,000.00 |
| Retained Earnings | \$700.00 |
| Total shareholders' equity | \$10,700.00 |

Date: 2025-08-28

Balance Sheet

| | |
|--------------------------------------|--------------|
| Assets | |
| Cash and Cash Equivalents | \$20,700.00 |
| Loans and Advances | \$80,000.00 |
| Assets at FVTPL | \$10,000.00 |
| Total assets | \$110,700.00 |
| Liabilities | |
| Deposits and Other Public Borrowings | \$100,000.00 |
| Deposits | \$100,000.00 |
| Total liabilities | \$100,000.00 |
| Net assets | \$10,700.00 |
| Shareholders' equity | |
| Shareholders' Equity | \$10,000.00 |
| Retained Earnings | \$700.00 |
| Total shareholders' equity | \$10,700.00 |

Date: 2025-08-28

2.3 FVTPL security marking to market

- The *fair value* of FVTPL security is **marked to market** periodically, e.g., daily.
- This ensures consistency in that they are held for trading P&L in the first place.

There are two possible cases:

1. Unrealized trading loss
2. Unrealized trading gain

i These trading gains and losses are *unrealized* because the securities have not yet been sold.

2.4 Unrealized trading loss - Income Statement

If the market value of the security went down by 5% (\$500.0) the next day, we need to recognize this *unrealized trading loss* in the Income Statement.

| Income Statement | |
|------------------|----------|
| Income | \$800.00 |
| Interest Income | \$800.00 |
| Expense | \$100.00 |
| Interest Expense | \$100.00 |
| Profit | \$700.00 |

Date: 2025-08-28

| Income Statement | |
|-------------------------|------------|
| Income | \$300.00 |
| Interest Income | \$800.00 |
| Trading Income (FVTPL) | (\$500.00) |
| Unrealized Trading Loss | \$500.00 |
| Expense | \$100.00 |
| Interest Expense | \$100.00 |
| Profit | \$200.00 |

Date: 2025-08-29

2.5 Unrealized trading loss - Balance Sheet

If we were to generate the balance sheet now, such net trading loss would reduce the bank's retained earnings.

| Balance Sheet | |
|--------------------------------------|--------------|
| Assets | |
| Cash and Cash Equivalents | \$20,700.00 |
| Loans and Advances | \$80,000.00 |
| Assets at FVTPL | \$10,000.00 |
| Total assets | \$110,700.00 |
| Liabilities | |
| Deposits and Other Public Borrowings | \$100,000.00 |
| Deposits | \$100,000.00 |
| Total liabilities | \$100,000.00 |
| Net assets | \$10,700.00 |
| Shareholders' equity | |
| Shareholders' Equity | \$10,000.00 |
| Retained Earnings | \$700.00 |
| Total shareholders' equity | \$10,700.00 |

Date: 2025-08-28

Balance Sheet

| | |
|--------------------------------------|--------------|
| Assets | |
| Cash and Cash Equivalents | \$20,700.00 |
| Loans and Advances | \$80,000.00 |
| Assets at FVTPL | \$9,500.00 |
| Total assets | \$110,200.00 |
| Liabilities | |
| Deposits and Other Public Borrowings | \$100,000.00 |
| Deposits | \$100,000.00 |
| Total liabilities | \$100,000.00 |
| Net assets | \$10,200.00 |
| Shareholders' equity | |
| Shareholders' Equity | \$10,000.00 |
| Retained Earnings | \$200.00 |
| Total shareholders' equity | \$10,200.00 |

Date: 2025-08-29

! Usually, financial reports are generated at a period's end, such as quarter's end or year's end. What's shown here should be viewed as *what if we close the bank's accounting ledger at this time and generate the reports?*

2.6 Unrealized trading gain - Income Statement

The day after, if the market value of the security went up by 10% (\$950.0), we need to recognize this *unrealized trading gain*.

Income Statement

| | |
|-------------------------|------------|
| Income | \$300.00 |
| Interest Income | \$800.00 |
| Trading Income (FVTPL) | (\$500.00) |
| Unrealized Trading Loss | \$500.00 |
| Expense | \$100.00 |
| Interest Expense | \$100.00 |
| Profit | \$200.00 |

Date: 2025-08-29

Income Statement

| | |
|-------------------------|------------|
| Income | \$1,250.00 |
| Interest Income | \$800.00 |
| Trading Income (FVTPL) | \$450.00 |
| Unrealized Trading Gain | \$950.00 |
| Unrealized Trading Loss | \$500.00 |
| Expense | \$100.00 |
| Interest Expense | \$100.00 |

| | |
|--------|------------|
| Profit | \$1,150.00 |
|--------|------------|

Date: 2025-08-30

2.7 Unrealized trading gain - Balance Sheet

Again, if we were to close the bank's accounting ledger now and check its balance sheet, we will see changes of the bank's retained earnings (increase by \$950.0).

Balance Sheet

| | |
|--------------------------------------|--------------|
| Assets | |
| Cash and Cash Equivalents | \$20,700.00 |
| Loans and Advances | \$80,000.00 |
| Assets at FVTPL | \$9,500.00 |
| Total assets | \$110,200.00 |
| Liabilities | |
| Deposits and Other Public Borrowings | \$100,000.00 |
| Deposits | \$100,000.00 |
| Total liabilities | \$100,000.00 |
| Net assets | \$10,200.00 |
| Shareholders' equity | |
| Shareholders' Equity | \$10,000.00 |
| Retained Earnings | \$200.00 |
| Total shareholders' equity | \$10,200.00 |

Date: 2025-08-29

Balance Sheet

| | |
|--------------------------------------|--------------|
| Assets | |
| Cash and Cash Equivalents | \$20,700.00 |
| Loans and Advances | \$80,000.00 |
| Assets at FVTPL | \$10,450.00 |
| Total assets | \$111,150.00 |
| Liabilities | |
| Deposits and Other Public Borrowings | \$100,000.00 |
| Deposits | \$100,000.00 |
| Total liabilities | \$100,000.00 |
| Net assets | \$11,150.00 |
| Shareholders' equity | |
| Shareholders' Equity | \$10,000.00 |
| Retained Earnings | \$1,150.00 |
| Total shareholders' equity | \$11,150.00 |

Date: 2025-08-30

2.8 FVTPL security sale

The next day, if the bank sold the security at the prevailing market price (assumed 2% up), we recognize *realized trading gain*.

Tracking the P&L of this particular FVTPL security,

1. On day 1, we had a loss of \$500.0 ($\$10000 \times 95\% = \9500.0).
2. On day 2, we had a gain of \$950.0 ($\$9500.0 \times 110\% = \10450.0).
3. On day 3, we had a gain of \$209.0 ($\$10450.0 \times 102\% = \10659.0).

The total P&L from this security is therefore a net gain of \$659.0, which shows up in the Income Statement.

i Because of the sale, the *unrealized trading gain/loss* associated with this security must be **reclassified** to *realized gain/loss*.

2.9 FVTPL security sale - Income Statement

Income Statement

| | |
|-------------------------|------------|
| Income | \$1,250.00 |
| Interest Income | \$800.00 |
| Trading Income (FVTPL) | \$450.00 |
| Unrealized Trading Gain | \$950.00 |
| Unrealized Trading Loss | \$500.00 |
| Expense | \$100.00 |
| Interest Expense | \$100.00 |
| Profit | \$1,150.00 |

Date: 2025-08-30

Income Statement

| | |
|------------------------|------------|
| Income | \$1,459.00 |
| Interest Income | \$800.00 |
| Trading Income (FVTPL) | \$659.00 |
| Realized Trading Gain | \$1,159.00 |
| Realized Trading Loss | \$500.00 |
| Expense | \$100.00 |
| Interest Expense | \$100.00 |
| Profit | \$1,359.00 |

Date: 2025-08-31

- Trading gain: $\$209.0 + \$950.0 = \$1159.0$
- Trading loss: \$500.0
- Net gain: \$659.0
- Gain/loss *reclassified* from unrealized to realized

2.10 FVTPL security sale - Balance Sheet

Now, if we were to close the bank's accounting ledger and produce its balance sheet, we will have:

Balance Sheet

| | |
|--------------------------------------|--------------|
| Assets | |
| Cash and Cash Equivalents | \$20,700.00 |
| Loans and Advances | \$80,000.00 |
| Assets at FVTPL | \$10,450.00 |
| Total assets | \$111,150.00 |
| Liabilities | |
| Deposits and Other Public Borrowings | \$100,000.00 |
| Deposits | \$100,000.00 |
| Total liabilities | \$100,000.00 |
| Net assets | \$11,150.00 |
| Shareholders' equity | |
| Shareholders' Equity | \$10,000.00 |
| Retained Earnings | \$1,150.00 |
| Total shareholders' equity | \$11,150.00 |

Date: 2025-08-30

Balance Sheet

| | |
|--------------------------------------|--------------|
| Assets | |
| Cash and Cash Equivalents | \$31,359.00 |
| Loans and Advances | \$80,000.00 |
| Total assets | \$111,359.00 |
| Liabilities | |
| Deposits and Other Public Borrowings | \$100,000.00 |
| Deposits | \$100,000.00 |
| Total liabilities | \$100,000.00 |
| Net assets | \$11,359.00 |
| Shareholders' equity | |
| Shareholders' Equity | \$10,000.00 |
| Retained Earnings | \$1,359.00 |
| Total shareholders' equity | \$11,359.00 |

Date: 2025-08-31

2.11 FVTPL security sale - Balance Sheet

Compared to the balance sheet before the bank purchased this FVTPL security, the retained earnings increased by exactly \$659.0.

Balance Sheet

| | |
|---------------------------|--------------|
| Assets | |
| Cash and Cash Equivalents | \$30,700.00 |
| Loans and Advances | \$80,000.00 |
| Total assets | \$110,700.00 |
| Liabilities | |

| | |
|--------------------------------------|--------------|
| Deposits and Other Public Borrowings | \$100,000.00 |
| Deposits | \$100,000.00 |
| Total liabilities | \$100,000.00 |

Net assets \$10,700.00

| | |
|----------------------------|-------------|
| Shareholders' equity | |
| Shareholders' Equity | \$10,000.00 |
| Retained Earnings | \$700.00 |
| Total shareholders' equity | \$10,700.00 |

Date: 2025-08-28

Balance Sheet

| | |
|---------------------------|--------------|
| Assets | |
| Cash and Cash Equivalents | \$31,359.00 |
| Loans and Advances | \$80,000.00 |
| Total assets | \$111,359.00 |

| | |
|--------------------------------------|--------------|
| Liabilities | |
| Deposits and Other Public Borrowings | \$100,000.00 |
| Deposits | \$100,000.00 |
| Total liabilities | \$100,000.00 |

Net assets \$11,359.00

| | |
|----------------------------|-------------|
| Shareholders' equity | |
| Shareholders' Equity | \$10,000.00 |
| Retained Earnings | \$1,359.00 |
| Total shareholders' equity | \$11,359.00 |

Date: 2025-08-31

3 Intermediate banking book accounting

3.1 Banking book

Apart from loans, a bank's banking book contains other assets that are held mostly for interest income. However, depending on whether the bank intends to hold them until maturity, these non-loan banking book assets can be either of:

1. **Fair Value Through Other Comprehensive Income (FVOCI),**
2. **At Amortized Cost** or Held to Maturity (HTM).¹

For example, Treasury bonds, corporate bonds, MBS, etc., are usually FVOCI or HTM banking book assets.

¹Now called "at amortized cost" under IFRS 9 / AASB 9.

| | Note | Group | | Bank | |
|--|------|------------------|------------------|------------------|------------------|
| | | 30 Jun 23 | 30 Jun 22 | 30 Jun 23 | 30 Jun 22 |
| | | \$M | \$M | \$M | \$M |
| Assets | | | | | |
| Cash and liquid assets | 5.1 | 116,619 | 161,154 | 108,367 | 150,974 |
| Receivables from financial institutions | 5.2 | 6,079 | 6,845 | 5,422 | 6,071 |
| Assets at fair value through Income Statement | 5.3 | 67,627 | 25,315 | 67,641 | 25,249 |
| Derivative assets | 5.4 | 23,945 | 35,736 | 25,585 | 37,774 |
| Investment securities: | | | | | |
| At amortised cost | 5.5 | 2,032 | 3,217 | 2,032 | 3,217 |
| At fair value through Other Comprehensive Income | 5.5 | 84,072 | 79,086 | 77,232 | 72,191 |
| Assets held for sale | 11.3 | 5 | 1,322 | 5 | 28 |
| Loans and other receivables | 3.1 | 926,082 | 878,854 | 816,140 | 773,042 |
| Shares in and loans to controlled entities | 11.2 | – | – | 54,636 | 56,719 |
| Property, plant and equipment | 6.1 | 4,950 | 4,887 | 3,549 | 3,627 |
| Investments in associates and joint ventures | 11.1 | 2,848 | 2,801 | 1,430 | 1,407 |
| Intangible assets | 6.2 | 7,393 | 6,899 | 4,340 | 3,883 |
| Deferred tax assets | 2.5 | 3,811 | 3,173 | 3,640 | 3,069 |
| Other assets | 6.3 | 7,382 | 5,971 | 6,799 | 5,387 |
| Total assets | | 1,252,845 | 1,215,260 | 1,176,818 | 1,142,638 |

Figure 1: Excerpt of CBA's 2023 balance sheet - assets

3.2 FVOCI security

FVOCI assets in the banking book are typically debt securities that:

- Earn interest income for the bank.
- Can be sold before maturity but are *not actively traded* like FVTPL securities.
- Experience fair value changes that are recorded in **Accumulated Other Comprehensive Income (AOCI)** instead of directly impacting net income.
- Upon sale, unrealized gains/losses from AOCI are transferred to Net Income.

3.3 FVOCI security purchase

Assume that the bank now purchased a Treasury bond at a fair value of \$30,000. The bank may sell the bond before it matures, and hence classify it as a FVOCI asset on the banking book.

Balance Sheet

| | |
|--------------------------------------|---------------------|
| Assets | |
| Cash and Cash Equivalents | \$31,359.00 |
| Loans and Advances | \$80,000.00 |
| Total assets | \$111,359.00 |
| Liabilities | |
| Deposits and Other Public Borrowings | \$100,000.00 |
| Deposits | \$100,000.00 |
| Total liabilities | \$100,000.00 |
| Net assets | \$11,359.00 |
| Shareholders' equity | |
| Shareholders' Equity | \$10,000.00 |
| Retained Earnings | \$1,359.00 |
| Total shareholders' equity | \$11,359.00 |

Date: 2025-08-31

Balance Sheet

| | |
|--------------------------------------|--------------|
| Assets | |
| Cash and Cash Equivalents | \$1,359.00 |
| Loans and Advances | \$80,000.00 |
| Investment Securities | \$30,000.00 |
| Investment Securities at FVOCI | \$30,000.00 |
| Total assets | \$111,359.00 |
| Liabilities | |
| Deposits and Other Public Borrowings | \$100,000.00 |
| Deposits | \$100,000.00 |
| Total liabilities | \$100,000.00 |
| Net assets | \$11,359.00 |
| Shareholders' equity | |
| Shareholders' Equity | \$10,000.00 |
| Retained Earnings | \$1,359.00 |
| Total shareholders' equity | \$11,359.00 |

Date: 2025-08-31

i The fair value of the security is recorded on the balance sheet under the *Investment Securities at FVOCI* account.

3.4 FVOCI security marking to market

- The *fair value* of FVOCI security is **marked to market** periodically, e.g., daily.
- This is because such securities do have market values (e.g., Treasury securities).

There are two possible cases:

1. Unrealized loss
2. Unrealized gain

i These gains and losses are *unrealized* because the securities have not yet been sold.

! These gains and losses are not through *trading*.

3.5 Unrealized gain

Suppose the next day the market value of the FVOCI security went up by 5% ($\$600 = \$30,000 \times 5\%$).

It is important to note that FVOCI security's fair value changes affect AOCI, an equity account.

It does not affect Income Statement P&L until it's eventually sold.

Balance Sheet

| | |
|---------------------------|------------|
| Assets | |
| Cash and Cash Equivalents | \$1,359.00 |

| | |
|--------------------------------------|--------------|
| Loans and Advances | \$80,000.00 |
| Investment Securities | \$30,000.00 |
| Investment Securities at FVOCI | \$30,000.00 |
| Total assets | \$111,359.00 |
| Liabilities | |
| Deposits and Other Public Borrowings | \$100,000.00 |
| Deposits | \$100,000.00 |
| Total liabilities | \$100,000.00 |
| Net assets | \$11,359.00 |
| Shareholders' equity | |
| Shareholders' Equity | \$10,000.00 |
| Retained Earnings | \$1,359.00 |
| Total shareholders' equity | \$11,359.00 |

Date: 2025-08-31

Balance Sheet

| | |
|--------------------------------------|--------------|
| Assets | |
| Cash and Cash Equivalents | \$1,359.00 |
| Loans and Advances | \$80,000.00 |
| Investment Securities | \$30,600.00 |
| Investment Securities at FVOCI | \$30,600.00 |
| Total assets | \$111,959.00 |
| Liabilities | |
| Deposits and Other Public Borrowings | \$100,000.00 |
| Deposits | \$100,000.00 |
| Total liabilities | \$100,000.00 |
| Net assets | \$11,959.00 |
| Shareholders' equity | |
| Shareholders' Equity | \$10,000.00 |
| Accumulated OCI | \$600.00 |
| Unrealized OCI Gain | \$600.00 |
| Retained Earnings | \$1,359.00 |
| Total shareholders' equity | \$11,959.00 |

Date: 2025-09-01

3.6 Unrealized loss

If the market value of the security went down by 2% ($\$612 = \$30,600 \times 2\%$) the next day, we recognize this *unrealized OCI loss* of AOCI.

Balance Sheet

| | |
|--------------------------------|-------------|
| Assets | |
| Cash and Cash Equivalents | \$1,359.00 |
| Loans and Advances | \$80,000.00 |
| Investment Securities | \$30,600.00 |
| Investment Securities at FVOCI | \$30,600.00 |

| | |
|--------------------------------------|--------------|
| Total assets | \$111,959.00 |
| Liabilities | |
| Deposits and Other Public Borrowings | \$100,000.00 |
| Deposits | \$100,000.00 |
| Total liabilities | \$100,000.00 |
| Net assets | \$11,959.00 |
| Shareholders' equity | |
| Shareholders' Equity | \$10,000.00 |
| Accumulated OCI | \$600.00 |
| Unrealized OCI Gain | \$600.00 |
| Retained Earnings | \$1,359.00 |
| Total shareholders' equity | \$11,959.00 |

Date: 2025-09-01

Balance Sheet

| | |
|--------------------------------------|--------------|
| Assets | |
| Cash and Cash Equivalents | \$1,359.00 |
| Loans and Advances | \$80,000.00 |
| Investment Securities | \$29,988.00 |
| Investment Securities at FVOCI | \$29,988.00 |
| Total assets | \$111,347.00 |
| Liabilities | |
| Deposits and Other Public Borrowings | \$100,000.00 |
| Deposits | \$100,000.00 |
| Total liabilities | \$100,000.00 |
| Net assets | \$11,347.00 |
| Shareholders' equity | |
| Shareholders' Equity | \$10,000.00 |
| Accumulated OCI | (\$12.00) |
| Unrealized OCI Gain | \$600.00 |
| Unrealized OCI Loss | \$612.00 |
| Retained Earnings | \$1,359.00 |
| Total shareholders' equity | \$11,347.00 |

Date: 2025-09-02

3.7 FVOCI, AOCI, and capital ratios

Because FVOCI's (even unrealized) gain/loss changes AOCI, and AOCI is part of a bank's CET1 capital, FVOCI's fair value movement can cause volatility in the bank's regulatory capital ratios.

- i** CET1 is the primary or core capital of a DI.
- **Common shares**
 - Share premium resulting from the issue of CET1 instruments
 - **Retained earnings**
 - **Accumulated and other comprehensive income (AOCI)**
 - Other disclosed reserves
 - Certain minority interests
 - Regulatory adjustment applied in the calculation of CET1 Capital.

Today, banks with total assets below \$250 billion are permitted to exclude AOCI when reporting applicable regulatory ratios.

3.8 FVOCI security sale

The next day, if the bank sold the FVOCI security at the prevailing market price (assumed 2% down), we recognize *realized OCI loss*.

Tracking the AOCI gain/loss of this particular FVOCI security,

1. On day 1, we had a gain of \$600.
2. On day 2, we had a loss of \$612.
3. On day 3, we had a loss of \$599.76.

The total net loss of this security is therefore \$611.76.

3.9 FVOCI security sale - Income Statement

Now that the FVOCI security is sold, its gain/loss is moved from AOCI to Income Statement as *Investment Income (FVOCI)*.

Income Statement

| | |
|------------------------|------------|
| Income | \$1,459.00 |
| Interest Income | \$800.00 |
| Trading Income (FVTPL) | \$659.00 |
| Realized Trading Gain | \$1,159.00 |
| Realized Trading Loss | \$500.00 |
| Expense | \$100.00 |
| Interest Expense | \$100.00 |
| Profit | \$1,359.00 |

Date: 2025-09-02

Income Statement

| | |
|---------------------------|------------|
| Income | \$847.24 |
| Interest Income | \$800.00 |
| Trading Income (FVTPL) | \$659.00 |
| Realized Trading Gain | \$1,159.00 |
| Realized Trading Loss | \$500.00 |
| Investment Income (FVOCI) | (\$611.76) |
| Realized OCI Gain | \$600.00 |
| Realized OCI Loss | \$1,211.76 |
| Expense | \$100.00 |

| | |
|------------------|----------|
| Interest Expense | \$100.00 |
| Profit | \$747.24 |

Date: 2025-09-03

3.10 FVOCI security sale - Balance Sheet

When P&L accounts of income statement are closed, the net gain/loss of Investment Income (FVOCI) changes the bank's retained earnings.

Balance Sheet

| | |
|--------------------------------------|--------------|
| Assets | |
| Cash and Cash Equivalents | \$1,359.00 |
| Loans and Advances | \$80,000.00 |
| Investment Securities | \$29,988.00 |
| Investment Securities at FVOCI | \$29,988.00 |
| Total assets | \$111,347.00 |
| Liabilities | |
| Deposits and Other Public Borrowings | \$100,000.00 |
| Deposits | \$100,000.00 |
| Total liabilities | \$100,000.00 |
| Net assets | \$11,347.00 |
| Shareholders' equity | |
| Shareholders' Equity | \$10,000.00 |
| Accumulated OCI | (\$12.00) |
| Unrealized OCI Gain | \$600.00 |
| Unrealized OCI Loss | \$612.00 |
| Retained Earnings | \$1,359.00 |
| Total shareholders' equity | \$11,347.00 |

Date: 2025-09-02

Balance Sheet

| | |
|--------------------------------------|--------------|
| Assets | |
| Cash and Cash Equivalents | \$30,747.24 |
| Loans and Advances | \$80,000.00 |
| Total assets | \$110,747.24 |
| Liabilities | |
| Deposits and Other Public Borrowings | \$100,000.00 |
| Deposits | \$100,000.00 |
| Total liabilities | \$100,000.00 |
| Net assets | \$10,747.24 |
| Shareholders' equity | |
| Shareholders' Equity | \$10,000.00 |
| Retained Earnings | \$747.24 |
| Total shareholders' equity | \$10,747.24 |

3.11 Investment securities at amortized cost

- Measurement
 - Initially recorded at fair value plus transaction costs.
 - Subsequently measured at **amortised cost** using the **effective interest method**.
 - Carrying amount = purchase price \pm cumulative amortisation of premium/discount – impairment allowance.
- Income Recognition
 - **Interest income** recognised in profit or loss using the effective interest rate (EIR).
 - Amortisation of premiums or discounts included in interest income.
- Gains and Losses
 - No recognition of unrealised fair value changes in P&L or OCI.
 - Realised gains/losses recognised in P&L only upon sale or derecognition.
- Impairment
 - Subject to **expected credit loss (ECL)** model under IFRS 9/AASB 9.
 - ECL recognised in P&L and reduces the carrying amount.