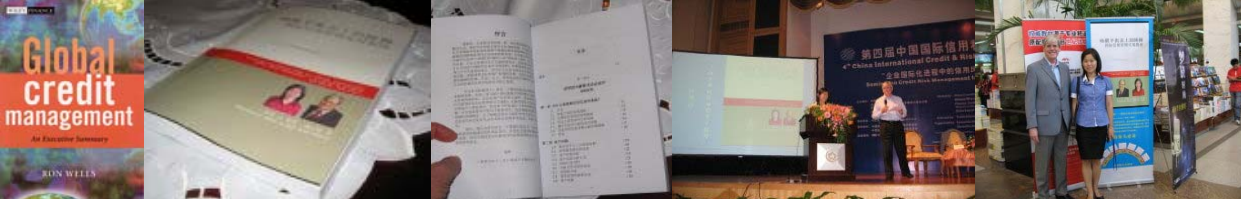


The Role of the Credit Manager in 2008

Ron Wells

FCIB Europe – Nice

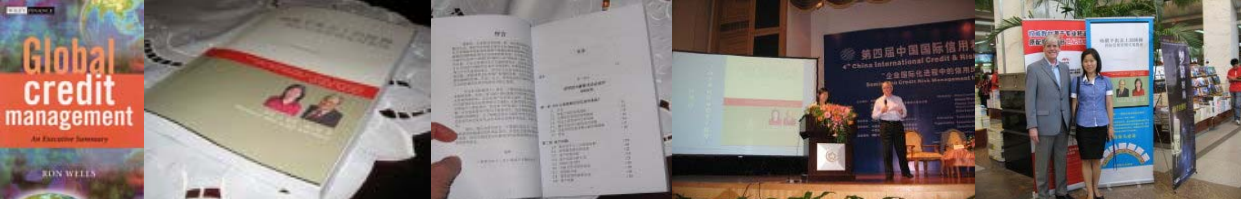
February 2008



Assess and Actively Manage:

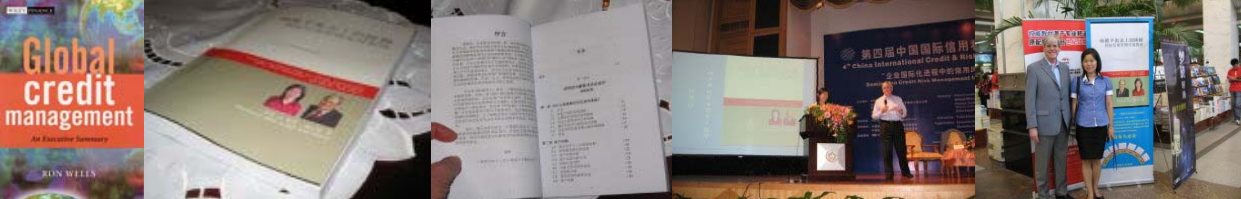
- Counterparty Performance Risk
- Counterparty Credit Risk
- Country Risk
- Bank Risk
- Credit Insurer Risk
- Document/Legal Risk
- Portfolio Risk





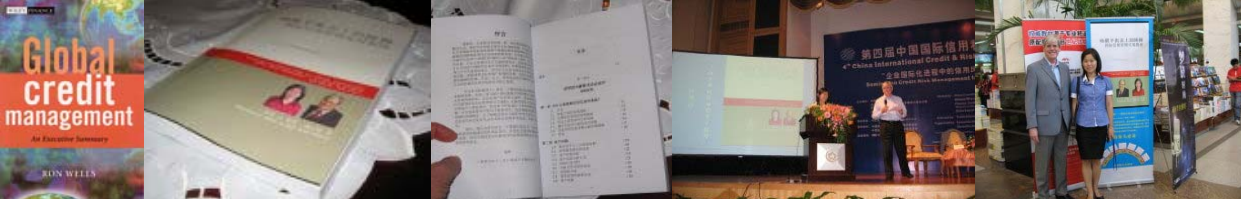
What's New?

- Counterparty versus Customer
- Why Analyse Suppliers as well as Buyers?
 - The need to fix future input costs
 - The need to fix future sales prices
 - Liquid markets for commodities
 - Illiquid markets for non-commodities



What Else is New?

- Performance and Document/Legal Risk
 - In a liquid market with volatile prices, will a supplier meet future fixed price commitments?
 - In an illiquid market, will a supplier meet its future commitments?
 - If a supplier fails to perform, will it be possible to extract compensation?



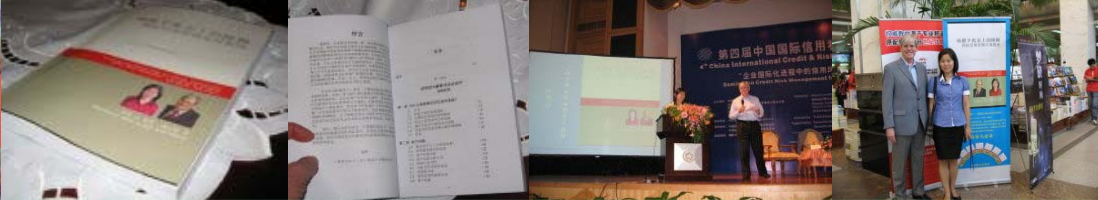
Same Applies to Buyers:

- Performance and Document/Legal Risk
 - In a liquid market with volatile prices, will a buyer meet future fixed price commitments?
 - In an illiquid market, will a buyer meet its future commitments?
 - If a buyer fails to perform, will it be possible to extract compensation?



Quantifying Performance Risk:

- Also called Marked-to-Market (m2m) Risk; Value at Risk (VaR) calculations are used by Banks. VaR purports to quantify Potential Future Exposure (**PFE**)
- Credit Value at Risk (CVaR) adds consideration of the 'likelihood of failure' (**PD**) and the 'loss given failure' (**LGD**)

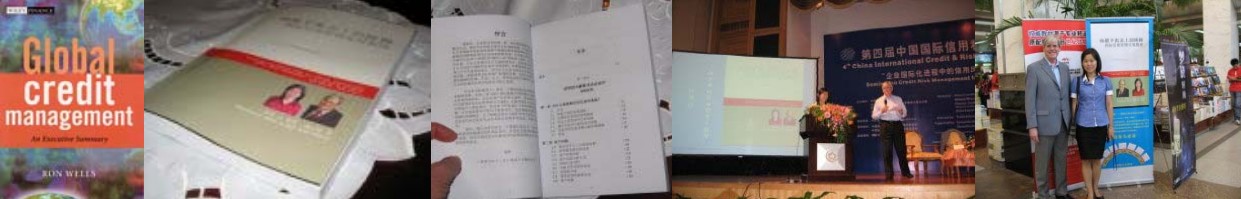


VaR Is it meaningful?

- Probability Theory
- Black-Scholes (Merton 1973 paper)
- Monte Carlo Simulation Method
- Assumptions
- Data Requirements

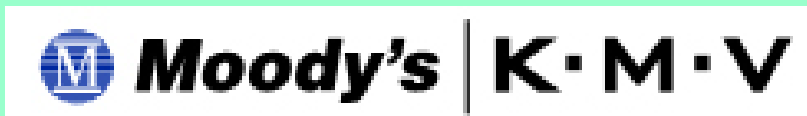


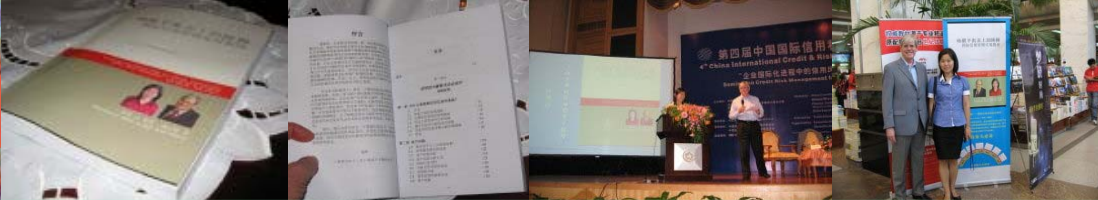
1997 - Robert C. Merton,
Myron S. Scholes



PD and LGDLimitations

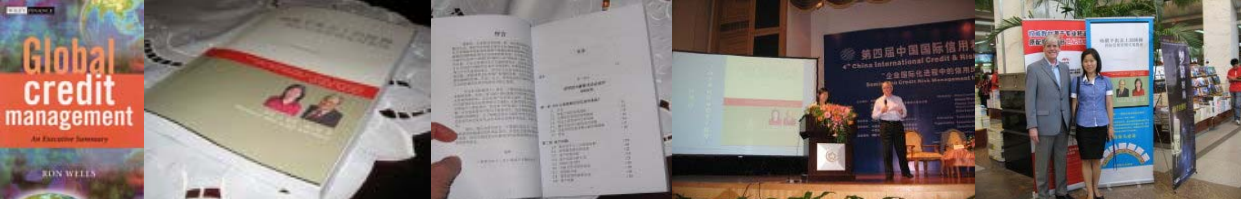
- Assumptions
- Data Requirements





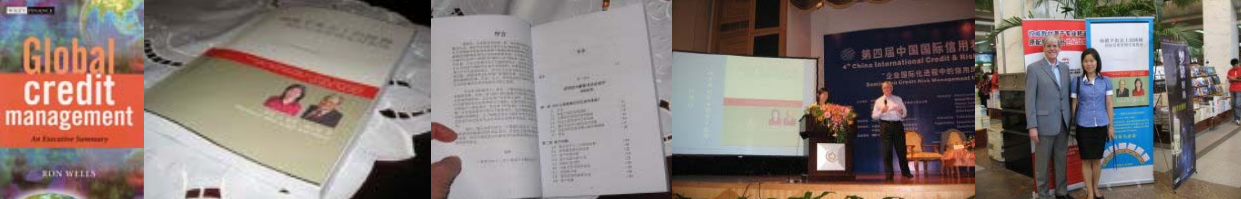
Performance Risk Review:

- Also called Marked-to-Market (m2m) Risk; Value at Risk (VaR) calculations are used by Banks. VaR purports to quantify Potential Future Exposure (**PFE**)
- Credit Value at Risk (CVaR) adds consideration of the 'likelihood of failure' (**PD**) and the 'loss given failure' (**LGD**)



Performance Risk Assessment

If **CVaR** is not practical and/or not meaningful, is there another way?



Possible Alternatives; to be developed:

- **Scenario Planning** as a basis to estimate the Potential Future Exposure
- A **Recovery Rate Model** to estimate the Loss Given Default
- A **Performance Risk ScoreCard** to produce a Probability of Performance Default