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THE ROLE OF ECL MECHANISMS IN PROACTIVE CREDIT RISK MANAGEMENT WITHIN IFRS 9

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Abstract:

This thesis analyzes the role of Expected Credit Loss (ECL) mechanisms under IFRS 9 in proactive credit risk management. The results show that the ECL approach is an important tool for early identification of nonperforming loans (NPLs) and strengthening the quality of bank assets.

Keywords: IFRS 9, ECL, credit risks, NPL, proactive management.

In recent years, in the context of global economic instability, macroeconomic shocks, and the expansion of lending volumes, the issue of effective management of credit risks in commercial banks has become particularly relevant. In traditional banking practice, credit risks were assessed mainly based on retrospective indicators, and measures were taken after the occurrence of nonperforming loans (NPL). Such an approach does not allow predicting a decrease in the quality of bank assets.

With the introduction of the international financial reporting standard IFRS 9, a transition has been made from a retrospective approach to a prospective (forward-looking) approach in assessing credit risks. Within the framework of this standard, the model of expected credit losses (ECL) made it possible to predict and proactively manage credit risks. Therefore, it is important to scientifically assess the impact of IFRS 9 and ECL mechanisms on the quality of banking assets and financial stability.



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The importance of the ECL approach in credit risk management is widely covered in international scientific literature. In the studies of J. Bessis, A. Saunders, and M. Cornett, the preliminary assessment of credit risks is interpreted as the main condition for ensuring bank stability. The documents of the Basel Committee on Banking Supervision state that ECL mechanisms serve to reduce credit risks in conjunction with prudential policy.

In the studies of Klein (2022) and Louzis, Vouldis, and Metaxas (2012), it is empirically substantiated that credit risks are often manifested through the lag effect. According to their conclusions, it is not enough to assess credit risks only through the level of problem loans, but mechanisms for predicting risks are necessary.

Although domestic scientists (B.U. Akbarov, J. Bozorov, and others) have analyzed the issues of credit risk management in the banking system of Uzbekistan, the role of ECL mechanisms in proactive management within the framework of IFRS 9 has not been sufficiently comprehensively studied. This circumstance determines the scientific relevance of the research topic.

The study used methods of systematic and comparative analysis, statistical grouping, correlation and regression analysis. Based on the financial indicators of commercial banks of Uzbekistan for 2015-2024, the relationship between ECL reserves, the level of NPL, capital adequacy (CAR), and bank profitability (ROA) was assessed. The research methodology was developed based on the prudential requirements of IFRS 9 and Basel III.

The ECL mechanism, implemented based on IFRS 9, allows for a **forward-looking (forward-looking)** assessment of credit risks, and not a retrospective assessment. While traditional approaches classify loans as problematic only after payment delays occur, the ECL model serves to identify risks in the loan portfolio at the latent stage.



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Table 1 Comparison of approaches to credit risk assessment under IFRS9.¹

Measure	Traditional approach	IFRS 9 (ECL) approach
Evaluation time	Late (ex-post)	Forward-looking
Risk detection	After NPL occurs	At the stage of potential risk
Main indicator	Deferred payment	PD, LGD, EAD, ECL
Control type	Reactive	Proactive
Asset quality	Determined after deterioration	Pre-controlled

As can be seen from the table, the ECL model allows preventing a decrease in the quality of bank assets by identifying credit risks at an early stage.



**Figure 1. Proactive credit risk management scheme based on IFRS 9.²
(GIVEN IN UZBEK)**

¹ Muallif tomonidan xalqaro bank amaliyoti va IFRS 9 standartlari asosida ishlab chiqilgan.

² Prepared by the author



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The mechanism of proactive credit risk management based on IFRS 9 is reflected, which describes the indirect influence of ECL on credit risks not directly, but through PD, LGD, and EAD indicators. This approach allows banks to identify risks and take proactive measures before the NPL level increases.

Empirical analysis has shown that the integration of ECL mechanisms with loan portfolio monitoring and prudential policy is effective in strengthening the quality of bank assets and financial stability. The ECL approach justifies the need to use credit risks not only at the accounting level, but also as a strategic management tool.

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