

IRS valuations

Methodology

Overview

CRISIL's Fixed Income and Fund Services group under Research provides mutual fund rankings, valuations, indices, etc. thereby furthering CRISIL's objective to make markets function better. IRS valuations are provided to mutual funds following valuation guidelines provided by AMFI.

Background

Interest rate swap is a type of Derivative contract in which one stream of future interest payment is exchanged for another on a notional principal amount (Fixed for floating exchange).

In a swap contract the principal does not change hands. One cash flow is generally fixed whereas the other is variable (based on benchmark interest rate).

Valuation methodology

- Current practice for valuation assumes floating leg will always be valued at par.
- Since floating leg is assumed to be at par, only valuation of fixed leg is provided as per terms and conditions provided by client.
 - For valuation of Fixed leg, cash flows are plotted till maturity and Interest payment dates are adjusted for Interest Payment dates falling on weekends.
 - For discounting of IRS, we use Overnight MIBOR rate and we source the remaining curve from CCIL/ third party vendors where VWAY of trades is taken for valuation for which quantity is greater than 25 crore.
 - Last Traded Yield will be considered during exceptional days to account for intraday volatility. **

***Exceptional days will be tracked internally by team in case the difference between LTY & VWAY of CCIL trades is greater than 25 bps we will initiate polling whether to consider LTY for that day. Exceptional days may include monetary policy/credit policy, quarter end days, union budget, specific events which may have material impact on yields and others.*

- Yields of individual IRS are arrived at using interpolation technique to match with residual tenor of the IRS.
- The fixed cash-flows are discounted at the yield to arrive at the final price.

Governance mechanism

CRISIL has an internal committee comprising of President, Senior Director/s, Director/s and Associate Director/s which has following role as provided below.

- **Criteria Committee:** Valuation policy and any changes to such policies are discussed with the committee and are incorporated post approval by the committee.
- **Valuation Committee:** Matters pertaining to exceptions, are discussed with valuation committee and acted upon based on its feedback. Exceptions may include any methodology changes, regulatory changes, market events impacting yields ,etc.

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