

DIRECTED RISK RESEARCH PROBLEM STATEMENT

Risk Theme	Corporate credit risk	Problem Nr.	PS18003
-------------------	-----------------------	--------------------	---------

Client Name	Frederik van der Walt	Client Org.	Absa		
Designation	Head modelling and analytics: wholesale regulatory models				
E-mail	Frederik.vanderwalt@absa.co.za	Tel (w)	0118466549	Mobile	0825797528

PS Status	Open	Date	18 Jun 2018	Revised PS	n/a
------------------	------	-------------	-------------	-------------------	-----

PROJECT TITLE: The use of Global Credit Data (GCD) data in LGD modelling in South Africa.

PROJECT GOAL

To evaluate the appropriateness/representativeness of pooled credit data, specifically the Global Credit Data (GCD) (formerly known as the Pan-European Credit Data Consortium), in the development of new loss given default (LGD) models for the corporate portfolio and potentially other portfolios.

HIGH LEVEL DESCRIPTION OF PROBLEM

The realised LGD is mostly quantified by, either implicitly or explicitly, discounting the streams of recoveries/costs received/paid after a facility has defaulted. The recovery rate is the net present value of these streams divided by the exposure at default. The loss given default is one minus the recovery rate.

Typically, some model is postulated to predict the realised LGD values. To estimate the postulated model's parameters, sufficient data is required. Often, insufficient credit loss data exists for low default portfolios (especially for corporate and bespoke portfolios).

For this reason, in December 2004, the Pan-European credit data consortium (PECDC) was created by 47 banks across Europe, America, Asia, Australia and South Africa. Subsequently the PECDC was renamed "Global Credit Data" (see <http://www.globalcreditdata.org/>). The data is contributed by each member bank, the GCD then anonymises the data, and redistributes all the data to all member banks. They work on a "give to get" basis. To ensure that the data is anonymised, at least three South African banks are required to form part of the pooled data initiative. Absa, Standard bank, Investec, and FirstRand bank are members of the GCD.

In order for South African banks to use the GCD to facilitate LGD model building in line with Basel Regulation §448, they need to provide evidence to the South African Reserve Bank (SARB) of "*(where) external data is used*" and "*the bank must demonstrate that its estimates are representative of long run experience*".

GCD is available to academic institutions on condition that they research specific aspects of LGD models.

This project aims to perform research on the use of the GCD for LGD modelling by banks in Southern Africa. It will, inter alia, entail comparing the South African data to non-South African data and determining whether the distribution of assets and LGD are similar or comparative between the regions. It needs to address the question of whether the data is representative or not. In LGD terms, representative in terms of, to name a few, recovery legislation, ease of recovery, etc. A positive result would be that GCD data can be used/adapted to facilitate LGD model building by South African banks.

PROJECT OBJECTIVES

The objectives of this project are:

- to define and contrast “appropriateness” and “representativeness” i.e. find industry wide accepted definitions
- to determine the appropriateness/representativeness of the GCD data in the South African context i.e. industry wide accepted methodology on how to test whether data is representative of an internal portfolio
- to make a submission to the GCD member banks and the SARB on our findings.

OUTPUTS REQUIRED

- A paper that assesses the representativeness of international data in South Africa.
- Practical guidance to the industry on how to use the GCD in the South African context.

STRATEGIC VALUE OF DIRECTED RISK RESEARCH

This project will contribute to the whole banking society and ease the use of external data.

REFERENCES

Basel Committee on Banking Supervision (BCBS). 2006. International Convergence of Capital Measurement and Capital Standards. Available online: <https://www.bis.org/publ/bcbs128.pdf>. Date of access: 21 May 2018.