

Credit protection is generally an instrument for risk mitigation. Wherever a creditor does not want to bear a claim or financial risk, he has the option of hedging it. The purpose of collateral is to reduce the moment of uncertainty inherent in the lending business as far as possible.

The agreement on the provision of collateral is called the security agreement, the contracting party requiring the loan collateral is called the collateral taker, the party providing the collateral is called the guarantor. The collateral provider does not have to be the borrower, but the collateral taker is always also the lender.

The collateral management is embedded in the UI of the [Customer Impairment Workbench](#).

FlexFinance supports the following aspects regarding collateral:

- Market value**
 Market values can be maintained for collateral. Market values for collateral can be adjusted by automatic haircuts or through individual values manually captured and assigned by a user.
- Validity**
 Collateral can be valid for exactly one or alternatively for several multiple individual assets. FlexFinance supports the definition of validity rules and allocation of collateral to individual deals.
- Allocation**
 The entire amount of collateral can be allocated to one individual deal or portions of collateral can be allocated to multiple financial assets. These assets can belong to exactly one individual customer or many customers of the same economic unit. In order to calculate the individual risk provision, an item of collateral can be allocated using manually captured specific values or by ranking of deals. The rank can be manually or automatically assigned to a deal. Collateral in FX can be allocated with a variable or a fixed FX exchange rate.

The screenshot displays the FlexFinance Customer Impairment Workbench interface. The top navigation bar includes 'Customer Impairment' and 'Edit Customer Recovery Data'. The main content area is divided into several tabs: 'Static Data', 'Documentation', 'Scenarios', 'Irregular Recoveries', 'Regular Recoveries', 'Market Values', 'Collateral Validity', 'Allocation of Collateral', and 'Simulated Data'. The 'Scenarios' tab is active, showing a table with columns for Name, Description, and Probability Weight. Below this, the 'Customer' section displays a table with columns for Customer ID, Customer Name, and Set Of Scenarios. The 'Collaterals' section shows a table with columns for Customer ID and Set Of Scenarios. The 'Allocation of Collateral' tab is also visible, showing a table with columns for Allocation by, Scenario, Market Value, Expected Liquidation Costs, Expected Liquidation Date, and Rank. The interface includes various filters, search bars, and a 'Process Note' section at the bottom.

Figure: Collateral, scenarios and collateral allocation

- Simulation**
 FlexFinance supports the simulation of risk provisioning for different scenarios of collateral allocation, and by doing so, the impact of collateral validity and allocation to specific risk provisions can be analysed before final approval and before consideration in financial accounting.
- Collateral during Expected Credit Loss calculation**
 FlexFinance considers the collateral values allocated during
 - Expected Credit Loss calculation using statistical methods in stage 1 and 2 as well as non-significant deals assigned to stage 3
 - Expected Credit Loss calculation using individual recovery cash flows for stage 3 significant deals
 Collateral adjusts the EAD at individual deal level.

- The different scenarios lead to a probability-weighted Expected Credit Loss for stage 3 impaired significant deals.

Figure: Expected Credit Loss calculation results at individual deal level for specific provisioning