

The loss given default quantifies the loss that is expected to occur when an asset goes into default; once the foreclosure process is finished, possible recoveries are paid and collateral liquidated. It is denoted in percentage for the remaining outstanding amount.

There are different options available, each reflected in a separate component, for determining the LGD that is to be considered for a segment during ECL calculation. For different segments, various components can be applied:

- Variant A calculates the LGD on the basis of historical default and recovery data.
- Variant B individually calculates the LGD for collateralised deals, using the current outstanding amount of the deal as well as the current market value of the corresponding collateral.
- Variant C expects the delivery of an LGD from an external source.

Variant A – Component 'LGD Vintage'

This component uses the workout/recovery method with consideration of macroeconomic parameters to estimate the LGD. It calculates a through-the-cycle value which is used to derive the LGD (PIT) using the appropriate macroeconomic parameters. The calculation of this component requires historical recovery data as input, including date of default, the outstanding principal on the default date and recovery amounts on a monthly basis.

Variant B – Component 'LGD Collateral Value'

This component calculates an LGD on individual deal level. The value is determined as the proportion of the outstanding amount, adjusted by the market value of the related collateral, to the outstanding amount. The market value of the collateral itself can also be adjusted, namely by multiplying it with a constant between 0 and 1 (the collateral loss ratio). The collateral loss ratio can be based, for example, on the current overall economic situation.

Variant C – Component 'LGD Mapping'

Depending on the geographical region and legal authorities, there are several sources for LGDs, e.g.

- EBA stress test table
- S&P publication by rating
- LGD in F-IRB in the Basel accord