Package ‘LDPD’

February 19, 2015

Type Package
Title Probability of Default Calibration
Version 1.0.2
Date 2015-01-03
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Description Implementation of most popular approaches to PD (probability of default) calibration: Quasi Moment Matching algorithm (D.Tasche), algorithm proposed by M.van der Burgt, K.Pluto and D.Tasche's most prudent estimation methodology.
License GPL-2
Imports MASS, nleqslv
NeedsCompilation no
Repository CRAN
Date/Publication 2015-01-03 10:26:08

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Description

Implementation of most popular approaches to PD (probability of default) calibration: Quasi Moment Matching approach, M.van der Burgt algorithm, K.Pluto and D.Tasche’s most prudent estimate methodology.

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The package implements three most popular among practitioners approaches to PD calibration:

1. Quasi Moment Matching approach proposed by D.Tasche (see QMMReCalibrate).
2. M. van der Burgt algorithm based on CAP curve smoothing (see VDBCalibratePD).
3. K.Pluto and D.Tasche "most prudent" estimate methodology (see PTOnePeriodPD, PTMultiPeriodPD).

Author(s)

Denis Surzhko <densur@gmail.com>

References


See Also

QMMReCalibrate VDBCalibratePD PTOnePeriodPD PTMultiPeriodPD somers2
Examples

# PD calibration using Multi-period Pluto and Tasche approach
portfolio <- c(10, 20, 30, 40, 10)
defaults <- c(1, 2, 0, 0, 0)
PTMultiPeriodPD(portfolio, defaults, 0.3, cor.St = 0.3, kT = 5, kNS = 1000, conf.interval = 0.5)

# PD Calibration using M. van der Burgt algorithm,
# portfolio distribution is given by rating classes.
portf.rating <- c(20, 50, 60, 70, 10, 5)
VDBCalibratePD(portf.rating, 0.1, 0.15, 0.5, rating.type = 'RATING')

# PD calibration using QMM algorithm,
# portfolio distribution is given by rating classes.
pd <- c(0.2, 0.1, 0.005, 0.001, 0.0001)
portf.rating <- c(100, 200, 200, 200, 100)
qmm <- QMMPRecalibrate(pd, portf.rating, rating.type = 'RATING')
# Plot results of PD calibration.
QMMPPlot(qmm)

### ARestimate

**Accuracy Ratio estimation**

Description

Estimate AR (Accuracy Ratio) and mean portfolio PD (probability of default) based on conditional PDs and portfolio unconditional distribution.

Usage

ARestimate(pd.cond, portf.uncond, rating.type = "RATING")

Arguments

- **pd.cond**: Conditional PD distribution (should be sorted from the worst to the best credit quality).
- **portf.uncond**: Unconditional portfolio distribution (should be sorted from lowest credit quality to higher one).
- **rating.type**: In case ’RATING’, each item in the portf.uncond should contain number of companies in each rating class. In case ’SCORE’, each item in the portf.uncond is an exact score.
Details

Approach to AR estimation is consistent with the algorithm proposed by D. Tasche in the paper: Estimating discriminatory power and PD curves when the number of defaults is small. Working paper, Lloyds Banking Group, 2009.
Mean portfolio PD (also known as Central Tendency of the portfolio) is estimated using unconditional portfolio distribution.

Value

<table>
<thead>
<tr>
<th>Value</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>AR</td>
<td>Estimated accuracy ratio</td>
</tr>
<tr>
<td>CT</td>
<td>Mean PD in the portfolio</td>
</tr>
</tbody>
</table>

Note

The algorithm is using conditional PDs as an input. In case one needs to estimate AR from actual default statistic (BAD/GOOD data), one can use, for example, somers2.

Author(s)

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References


See Also

QMMRecalibrate somers2

Examples

```r
pd.cond <- c(0.1, 0.05, 0.025, 0.01, 0.001)  # PD for given rating class
portf.uncond <- c(10, 20, 30, 50, 10)        # Number of borrowers in each rating class
ARestimate(pd.cond, portf.uncond, rating.type = "RATING")
```
**PTMultiPeriodPD**

**Multi-period Pluto and Tasche Model**

**Description**

Estimates probability of default (PD) according to Multi-period Pluto & Tasche model.

**Usage**

```r
PTMultiPeriodPD(portf.uncond, portf.def, rho, cor.St, kT, kNS = 1000, conf.interval = 0.9)
```

**Arguments**

- `portf.uncond`: Unconditional portfolio distribution (e.g. number of counterparts by rating classes).
- `portf.def`: Number of defaults by rating classes.
- `rho`: Correlation with systematic factor.
- `cor.St`: Correlation matrix of systematic factor realization through the time. In case constant is given - power matrix is used:
  
  \[ \text{Correlation matrix} \ (i, j) = \text{cor.St} \times |s - t|, s = 1..kT, t = 1..kT. \]
- `kT`: Number of periods used in the PD estimation.
- `kNS`: Number of simulations for integral estimation (using Monte-Carlo approach).
- `conf.interval`: Confidence interval for PD estimation.

**Details**

Estimates probabilities of default according to multi-period Pluto and Tasche model (additionally captures the inter-temporal correlation effects).

**Value**

Conditional PDs according to Multi-period Pluto and Tasche model

**Note**

Portfolio and default data should be sorted by rating classes from lowest credit quality to higher one.

**Author(s)**

Denis Surzhko <densur@gmail.com>

**References**

See Also

PTOnePeriodPD

Examples

portfolio <- c(10, 20, 30, 40, 10)
defaults <- c(1, 2, 0, 0, 0)
PTMultiPeriodPD(portfolio, defaults, conf.interval = 0.9)

Description

Estimates probability of default according to One-period Pluto and Tasche model.

Usage

PTOnePeriodPD(portf.uncond, portf.def, conf.interval = 0.9)

Arguments

portf.uncond  Unconditional portfolio distribution (e.g. number of counterparts by rating classes).
portf.def     Number of defaults by rating classes.
conf.interval Confidence interval for PD estimation.

Details

Implementation of simple one-period Pluto and Tasche probability of default (PD) calibration model.

Value

Conditional PDs according to one-period Pluto and Tasche model

Note

Portfolio and default data should be sorted by rating classes from lowest credit quality to higher one.

Author(s)

Denis Surzhko <densur@gmail.com>

References

Description

Plot detailed results of probability of default calibration using Quasi Moment Matching algorithm.

Usage

qmmplot(x)

Arguments

x Output of QMMRecalibrate function.

Details

Plot contains conditional PD (probability of default) values:

- before re-calibration (sample Central Tendency and AR (accuracy ratio));
- after re-calibration (target Central Tendency and AR);
- upper confidence interval PDs (target Central Tendency and target AR minus one standard deviation of sample AR);
- lower confidence interval PDs (target Central Tendency and target AR plus one standard deviation of sample AR).

Value

Plot of conditional PDs.

Note

In case rating.type is 'RATING', PD plot is produced against unconditional cumulative portfolio distribution.
In case rating.type is 'SCORE', PD plot is produced against scores.

Author(s)

Denis Surzhko <densur@gmail.com>
References


See Also

QMMRecalibrate

Examples

```r
pd <- c(0.2, 0.1, 0.005, 0.001, 0.001)
portfolio <- c(100, 200, 200, 200, 100)
qmm <- QMMRecalibrate(0.05, pd, portfolio, rating.type = 'RATING')
QMMPlot(qmm)
```

---

**QMMRecalibrate**

*Probability of Default Calibration using Quasi Moment Matching Algorithm*

**Description**

Calibrates conditional probabilities of default (PD) according to Quasi Moment Matching (QMM) algorithm.
Calibration is based on target accuracy ratio (AR) and mean portfolio PD (Central Tendency). For the information purposes, also AR standard deviation is estimated using bootstrap approach.

**Usage**

```r
QMMRecalibrate(pd.uncond.new, pd.cond.old, portf.uncond, portf.condND = NULL, AR.target = NULL, rating.type = "RATING")
```

**Arguments**

<table>
<thead>
<tr>
<th>Name</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>pd.uncond.new</td>
<td>Target Mean PD (Central Tendency) for the portfolio.</td>
</tr>
<tr>
<td>pd.cond.old</td>
<td>Conditional PD distribution.</td>
</tr>
<tr>
<td>portf.uncond</td>
<td>Unconditional portfolio distribution.</td>
</tr>
<tr>
<td>portf.condND</td>
<td>Conditional on non-default portfolio distribution. If portf.condND is NULL, portf.uncond will be used as a proxy.</td>
</tr>
<tr>
<td>AR.target</td>
<td>Target accuracy ratio(AR), in case is NULL - implied by pd.cond.old AR is used (ARestimate is called for AR estimation purposes).</td>
</tr>
<tr>
<td>rating.type</td>
<td>In case ‘RATING’, each item in the portf.uncond contains number of counterpart in a given rating class. In case ‘SCORE’, each item in the portf.uncond is treated as an exact score of counterparty.</td>
</tr>
</tbody>
</table>
Details

PD curve is fitted using robust logit function proposed by D. Tasche. For the information purposes output of the function also contains PD fitted using target CT and AR plus/minus one standard deviation.

Value

<table>
<thead>
<tr>
<th>Value</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>CT.ac</td>
<td>Mean PD after calibration, e.g. target CT.</td>
</tr>
<tr>
<td>AR.ac</td>
<td>AR after calibration, e.g. target AR.</td>
</tr>
<tr>
<td>CT.bc</td>
<td>Mean PD before calibration, as implied by conditional PDs and portfolio unconditional distribution.</td>
</tr>
<tr>
<td>AR.bc</td>
<td>AR before calibration estimated from conditional PDs.</td>
</tr>
<tr>
<td>AR.sdev</td>
<td>AR standard deviation (based on sample data).</td>
</tr>
<tr>
<td>condPD.ac</td>
<td>Conditional PDs after QMM calibration.</td>
</tr>
<tr>
<td>condPD.bc</td>
<td>Conditional PDs before calibration.</td>
</tr>
<tr>
<td>condPD.ac.upper</td>
<td>Conditional PDs given AR as initial AR plus one standard deviation and target CT.</td>
</tr>
<tr>
<td>condPD.ac.lower</td>
<td>Conditional PDs given AR as initial AR minus one standard deviation and target CT.</td>
</tr>
<tr>
<td>portf.cumdist</td>
<td>Cumulative portfolio distribution needed to estimate logit PDs (conditional on non-default portfolio distribution if such data is given).</td>
</tr>
<tr>
<td>portf.uncond</td>
<td>Unconditional portfolio distribution from the worst to the best credit quality.</td>
</tr>
<tr>
<td>rating.type</td>
<td>In case ‘RATING’, each item in the portf.uncond contains number of counterpart parts in a given rating class. In case ‘SCORE’, each item in the portf.uncond is treated as an exact score of counterparty.</td>
</tr>
</tbody>
</table>

Note

Portfolio and default data should be sorted by rating classes from lowest credit quality to higher one.

Author(s)

Denis Surzhko <densur@gmail.com>

References

See Also

QMMPlot

Examples

```r
pd <- c(0.2, 0.1, 0.005, 0.001, 0.001)
portfolio <- c(100, 200, 200, 200, 100)
qmm <- QMMRecalibrate(0.05, pd, portfolio, rating.type = 'RATING')
QMMPlot(qmm)
```

VDBCalibratePD  

Probability of Default Calibration using M. Van Der Burgt Algorithm

Description

Calibrates conditional probabilities of default (PD) according to algorithm proposed by M. van der Burgt. Decomposition of PDs by rating classes is based on smoothed Cumulative Accuracy Profile (CAP) curve and target mean portfolio PD (Central Tendency - CT).

Usage

VDBCalibratePD(portf.uncond, pd.uncond.old, pd.uncond.new, AR, rating.type)

Arguments

<table>
<thead>
<tr>
<th>Argument</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>portf.uncond</td>
<td>Unconditional portfolio distribution.</td>
</tr>
<tr>
<td>pd.uncond.old</td>
<td>Unconditional PD of the sample on which AR had been estimated (in case is zero, approximation AR = 2*AUC - 1 is used for parameters estimation).</td>
</tr>
<tr>
<td>pd.uncond.new</td>
<td>Target Mean PD (Central Tendency) for the portfolio.</td>
</tr>
<tr>
<td>AR</td>
<td>Accuracy ration (AR) of the ranking model.</td>
</tr>
<tr>
<td>rating.type</td>
<td>In case 'RATING', each item in the portf.uncond contains number of counterpart in a given rating class. In case 'SCORE', each item in the portf.uncond is treated as an exact score of counterparty.</td>
</tr>
</tbody>
</table>

Details

One parameter approximation of CAP curve is used. Parameter is fitted in the way that the AUC (Cumulative Accuracy Profile) implied by the provided AR should be equal to the area under the approximation curve.
Value

- `pd.cond`  Conditional PDs after calibration.
- `portf.cumdist`  Cumulative portfolio distribution needed to estimate logit PDs (conditional on non-default if such data is given).
- `portf.uncond`  Unconditional portfolio distribution from the worst to the best credit quality.
- `rating.type`  In case 'RATING', each item in the portf.uncond contains number of counterparties in a given rating class. In case 'SCORE', each item in the portf.uncond is treated as an exact score of counterparty.

Note

Portfolio and default data should be sorted by rating classes from lowest credit quality to higher one.

Author(s)

Denis Surzhko <densur@gmail.com>

References


See Also

`ARESTimate`

Examples

```r
portf.rating <- c(20, 50, 60, 70, 10, 5)
portf.scores <- seq_len(1000)
VDBCalibratePD(portf.scores, 0.1, 0.15, 0.5, rating.type = 'SCORE')
VDBCalibratePD(portf.rating, 0.1, 0.15, 0.5, rating.type = 'RATING')
```
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