

Client Loan Assessment¹

The Credit Department should deal with the assessment and monitoring of the consumer loans and borrowers. The risk management of consumer lending contains 2 main aspects:

- The assessment and monitoring of every single borrower
- The assessment and monitoring of the portfolio containing all the borrowers

The assessment and monitoring of the market of the borrower

The environment provides the opportunities and threats for the borrower as regards the CSF. Does the borrower belong to a sustainable social group? Does he have a regular income job or other company income?

The assessment and monitoring of the borrower

Important aspects to be assessed are among others the kind of customers being sought the applicant's credit history, income/employment verification, income stability, employment stability, residence stability and debt-to-income ratio.

The assessment should not take much time. One has to check thoroughly the personal and family situation of the borrower:

- Age
- Nationality (Only inhabitants of the country should be entitled to borrow)
- Steady job and regular income (monthly salary)
- Marital status (number of children)
- Steady residence
- Bank account with bank
- No tax or rent payments in arrears
- No other debts outstanding with other banks or financial institutions
- no other people who rely on the applicant financially (parents)
- the applicant should not act as a guarantor for someone else's' debts
- No criminal record

The purpose of the loan should make sense in relation to the applicants' circumstances in terms of added value and earnings capacity to the applying household. And also the money should be used for the purpose told. (for instance if the applicant tells you he/she wants to buy a computer the invoice might be send directly to the bank and paid by the bank instead of first giving the loan to the borrower).

The term of the loan should be in accordance with the depreciation term of the object purchased. (The maximum term of a loan for purchasing a computer/car should be not longer than 3 years.).

The maximum amount as well as the repayment scheme should be in accordance with the financial situation of the borrower.

If necessary, collateral could be demanded either in the form of assets or deposits pledged to the bank (eventually provided by someone else) or a guarantee (from the employer). In this case the existence and the value of the assets or the creditworthiness

¹ Example from Rabobank. See scorecard Smallcap PI

of the guarantor should be assessed as well. This provides opportunities for developing special consumer credit schemes for employees of larger companies.

Usually the credit inspectors are already familiar with this kind of assessment. For assessment purposes one could draw up a document according to the following lay out (see below). This document should enable the credit inspector to determine initially (together with the applicant) whether the application has to be declined or could be taken into consideration for further processing.

A standard for determining the cost of living should be developed for which different methods might be used:

- A fixed amount per year for a normal family situation (2 parents, 2 children) plus adjustments according to a different household situation like more children/ single parent with food obligations to others.
- A specific calculation as percentage of monthly income with regards to the household situation and family situation

	Monthly salary < amount ²	Monthly salary = amount	Monthly salary > amount
Single no family	Fixed amount hh expenses	Fixed amount hh expenses	50% of salary
Family with single income source	Fixed amount hh expenses	Fixed amount hh expenses	50% of salary
Familymembers with income source >1	Fixed amount hh expenses	Fixed amount hh expenses	50% of salary

- A fixed % of the total income of the family based on experience

Borrower Credit Quality

In the initial underwriting process, Lenders and institutions (a.k.a. originators) analyze the credit risks of potential borrowers. Key criteria in evaluating a borrower’s credit quality include:

- payment history: high revolving credit usage
- Delinquency history – A borrower with a delinquency history of 30 days or less is considered to be of prime credit quality.
- Loan-To-Property Value (LTV) – LTV is the measurement of a borrower’s equity contribution to his/her property. A borrower with a LTV of 80% or less is considered to be of prime credit quality.
- Debt-to-Income (DTI) – DTI is the measurement of a borrower’s monthly debt service as a percentage of monthly income. A borrower with a DTI of 36% or less is considered to be of prime credit quality.
- Debt to service (DTS) - DTS is the measurement of a borrower’s yearly debt service as a percentage of savings. A borrower with a DTS of 20% or less is considered to be of prime credit quality.

² minimum wages by law

The assessment is based on assumptions on the following key performance indicators. The weighting factors present the relative importance of the performance indicators. Different counterparty types have different performance indicators with different weighting factors.

Micro-SME parameters:

Cluster	#Questions	Weighted %
Financial Ratios	6	60
Mc1 Net worth		23
Mc2 Normalised Operating profit/total sales		16
Mc3 Net worth/ total assets		15
Mc4 Cash balance/ current assets		19
Mc5 Current assets/ current liabilities		11
Mc6 Change in total sales in amounts		16
Total Financial Ratio		100
Non financial issues	5	40
Mc7 How many years of entrepreneurial experience?		25
Mc8 For how many years has the entrepreneur had a continuing relationship with the bank?		20
Mc9 Does the entrepreneur make use of an advisor?		15
Mc1 Does the entrepreneur make a financial prognosis?		15
0		
Mc1 Did you spot any warning signals with your clients		25
1 business?		
Total Non financial Issues		100
Totaal	11	100

Parameters for starting companies:

Category	#Questions	Weighted %
Non financial questions on the entrepreneurial skills	5	49
St1 What is the motive for the entrepreneur to run his business?		12
St2 How many years of skill-experience does the entrepreneur have in the sector of his business?		17
St3 Is the entrepreneur morally supported by his relatives?		5
St4 Does the entrepreneur actively use the advisory support offered?		10
St5 Is the entrepreneur aware of his shortcomings and are adequate actions taken to overcome these shortcomings?		5
Non financial questions on the entrepreneurial skills	3	21
St6 Are functions and tasks within the organisation clearly assigned?		4
St7 Is there a clear understanding of strategic decisions		6

Category	#Questions	Weighted %
regarding markets, products target client groups? Are these strategic decisions feasible and attainable with the product range?		
St8 Does the entrepreneur have a network of suppliers and buyers?		11
Financial Questions	2	30
St9 Which part of the projected revenues is secured by contracts (book to bill ratio)?		12
St1 Risk bearing capital as % of the balance sheet total		18
Total	10	100

Structuring

Investigate available and additional fund flows or places for savings.

Documentation

Restructuring clause

The borrower is past due more than 90 days after the delinquency date on any credit obligation. (In the case of retail and PSE obligations, for the 90 days figure the supervisor may substitute a figure up to 180 days for different products as it considers appropriate to local conditions).

Termination clause

The borrower is past due more than 180 days and it is determined that is unlikely to pay the debt obligation (principal, interest, or fees) in full and there is no restructuring.