CREDIT APPROVAL MECHANISM FOR BANKWIDE CORPORATE BORROWERS OF A LOCAL UNIVERSAL BANK IN THE PHILIPPINES
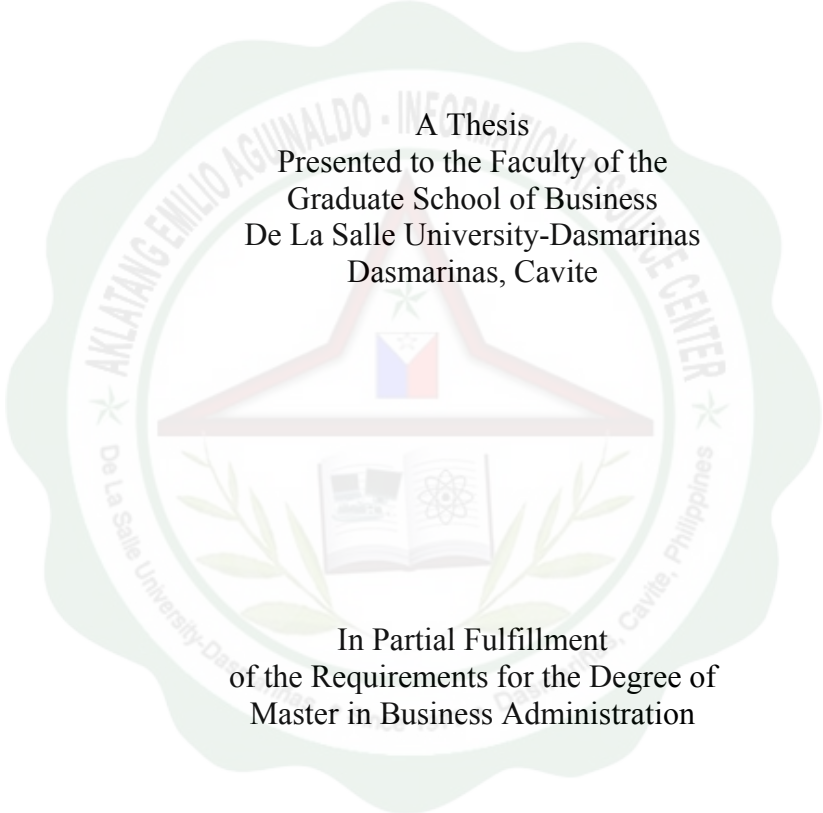
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ABSTRACT

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Various studies have looked into the different models of the credit evaluation process of banks to ascertain the importance of each credit factor in the approval of loans. The usual model employed in credit analysis is the five Cs of credit with a combination of quantitative analysis which includes credit scoring or credit risk rating. There is a growing view that the client's relationship with the bank may play a vital role in the credit evaluation process of banks. Studies in the Philippines have rarely investigated bank relationship as a determinant of loan approval.

This study was an attempt to shed some light on the possible influence of the five Cs of credit as well as bank relationship factors in the credit approval process. The research tested the model by employing statistical tools to determine the importance of each credit mechanism, including relationship, in the approval results and in the amount of loan granted.

These were tested to 735 corporate borrowers of this local Universal Bank by employing statistical tools such as Pearson's Chi-square, ANOVA, ordinary least square regression and logistic regression.

Generally, the findings support previous studies that five Cs as well as relationship variables both play important roles in determining credit approval and the loan amount granted by banks. There appeared in the model that the independent variables, five Cs of credit and bank relationship are significant in predicting the amount of loan. Cash flow and other business (capacity variable), total assets, networth and leverage (capital variable), unsecured (collateral variable), working capital and capital expenditures under loan purpose (condition variable), credit risk rating (character variable), and the relationship variable indicators (length and activity), were all highly significant at one percent, except for leverage (capital variable) which was marginally significant at 10 percent. Furthermore, 61 percent of the variation in the amount of loan approved can be explained by the underlying variation in the five Cs of credit and bank relationship. The F-stat result also indicates that the predictors used as a group explained statistically significant share of variation in the amount of loan approved.

The result also showed the effect of five Cs of credit and bank relationship in association with the approval or disapproval of loan. Using logistic regression in predicting the likelihood of loan approval which gives the odds ratio of 1 if approved, otherwise, 0 if disapproved, there appeared that working capital under loan purpose (condition variable), liquidity under financial condition (condition variable) and credit risk rating (character variable) were significant at five percent. On the other hand, unsecured (collateral variable) and capital expenditures under loan purpose (condition variable) appeared to be marginally significant at 10

percent.   The capital expenditure under loan purpose (condition variable) with a coefficient of 2.482 appears to be the most influential in the approval of loan followed by another condition variable, working capital, with a coefficient of 2.217. Relationship variables, activity and length appeared to be positively related, while the number of depository and lender banks were negatively related but not significant at 10 percent level.

The classification table shows that 91.1 percent of the sample observations is correctly classified. About 98.2 percent or 442 sample observations are predicted as approved accounts, while 18.2 percent or 8 accounts are correctly classified and predicted as disapproved.

Based on the results, it could be suggested that both regressions could be used in predicting the amount of loan and in determining the credit approval results. The results could also be used for future studies on bank relationships particularly on the effect on the interest rate and term of loan which were not covered by this study.

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