

DETERMINANTS OF HOME LOAN REPAYMENT PERFORMANCE OF LEASING COMPANY: A CASE STUDY ON IDLC FINANCE LTD.

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ABSTRACT

Real estate sector has great importance to fulfill one of the important human basic needs in the last few decades. The housing sector can work as the savior of the economy by increasing the savings and capital formation, creating huge employment and other economic multiplier benefits, through its backward and forward linkages. In Bangladesh, Housing Finance sector is dominated mainly by self-financing. In recent times, some of the leasing companies are also focusing on Housing Loans, particularly IDLC being the most visible in their activities. This paper mainly focused on the determinants for measuring home loan repayment performance of the IDLC finance Ltd. It has found some variables those are important for measuring performance of the home loan repayment systems in Bangladesh.

Keywords: *Determinants, Performance, Repayment Systems, Home Loan.*

1. INTRODUCTION

One of the renowned names in Bangladesh financial market is Industrial Development Leasing Company (IDLC) Limited. It started operation in the year 1985 as the pioneer leasing company as to facilitate lease- financing and capital investment in industrial sector, with the view of “Become the best performing and most innovative financial solutions provider in the country”. For introducing new multitude of diverse financial products and services in 2007 the company changed its name to IDLC Finance Ltd. Over the last two decades IDLC has contributed relentlessly in the country’s transition into a developing country and has emerged as Bangladesh’s leading multi-product financial institution. The company now offers financial and technological solutions to both institutional and individual clients to cater for their unique requirement.

2. OBJECTIVES OF THE STUDY

The main objective of the study is to measure the home loan repayment performance of the IDLC and the specific objectives are:

- to identify the activities of the Credit Risk Management Division of IDLC;
- to analyze the performance ratio of IDLC home loan;

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- to identify the major problems related to the repayment systems of home loan; and
- to recommend some guidelines to improve the performance of the bank.

3. METHODOLOGY OF THE STUDY

The study mainly focused on quantitative research technique. Data were collected from the primary and secondary sources. The primary data were gathered from the different executives and general clients of the bank through interview technique with the help of semi structured questionnaire.

The secondary information has been collected from the company's annual Report, corporate newsletter, branches manuals, and intranet of the company, different websites and various publications of the institution.

3.1. Sampling Plan

Primary data regarding the home loan repayment performance of the customers of IDLC have been collected from the real estate customer service and collection departments of IDLC. For this study, the stratified sampling method has been followed. The customers have been categorized into two strata based on their repayment performance. The complete list of the regular and overdue customers has been collected whose loan contracts are ongoing and two samples from the two strata have been selected randomly.

3.2. Sample Size

The study is based on a sample of 100 customers; eighty (80) from the regular customers and twenty (20) from the overdue customers.

4. THEORETICAL AND EMPIRICAL DETERMINANTS OF CREDIT RISK

To measure credit risk, lenders gather information about prospective borrowers and the collateral they offer and then assess this information in light of experience gained from extending credit in the past. Historically, lenders have relied heavily on the subjective judgment of underwriters in assessing credit risk. To facilitate the underwriting process, reduce costs, and promote consistency, lenders have brought credit scoring into the process. In some uses, credit scores are based exclusively on credit bureau records and, as such, provide a summary measure of the relative credit risk posed by individuals with differing credit histories. In other uses, credit scores are based on a wider range of information and are used to evaluate the overall credit risk posed by an applicant, providing a summary measure that lenders can use to gauge the acceptability of an application. The data consistently show that credit scores are useful in gauging the relative levels of risk posed by both prospective mortgage borrowers and those with existing mortgages. Although the absolute levels of delinquency and default are low in all score categories, the proportion of problem loans increases as credit scores decrease. That

relationship puts the focus of business concern on the prospective and existing borrowers with low scores because even small increases in the rate of default may mean the difference between profit and loss. Analysis of the distribution of borrowers across credit history score ranges suggests that most households have relatively high scores, regardless of the income or home value characteristics of the areas in which they reside. However, relatively more of those who reside in lower-income locations or in locations with lower home values have lower scores. For many institutions in the mortgage market, evaluating and managing the risks of lending to nontraditional borrowers and the risks of allowing greater flexibility in underwriting are relatively new experiences. Carefully evaluating the experiences to date provides important insights. Problems to date appear to have been concentrated among loans in which underwriting flexibilities have been layered and loans in which third-party down-payment assistance has been allowed. Market participants generally agree that, to be viable, affordable home lending programs must be accompanied by effective risk mitigation activities, including homebuyer education programs and enhanced loan servicing. Affordable lending programs are evolving and, as experience is gained, lenders are likely to find ways to expand home buying opportunities without accepting undue risks.

5. ANALYSIS AND DISCUSSION

Following is the descriptive analysis of the independent variables for both the regular and overdue customer categories. The descriptive analysis has actually provided a summarized picture of the data of the independent variables.

Table-1.1: Descriptive Statistics of Regular Customers

Independent Variables	Sample Size	Minimum	Maximum	Mean	Std. Dev.
Loan Term	80	3	15	8.69	3.30
Income Level	80	15000	400000	85381	77047.09
Debt Burden Ratio	80	0.06	0.81	0.3500	0.1416
Installment to Income	80	0.02	0.81	0.2966	0.1432
Fixed Obligation to Income	80	0.24	0.99	0.7078	0.1574
Loan to Value	80	0.04	0.71	0.3891	0.1512

Source: Authors' own creation based on sample data

Table-1.2: Descriptive Statistics of Overdue Customers

Independent Variables	Sample Size	Minimum	Maximum	Mean	Std. Dev.
Loan Term	20	3	15	7.92	3.56
Income Level	20	28000	200000	73937	42844.26
Debt Burden Ratio	20	0.38	0.85	0.5610	0.1076

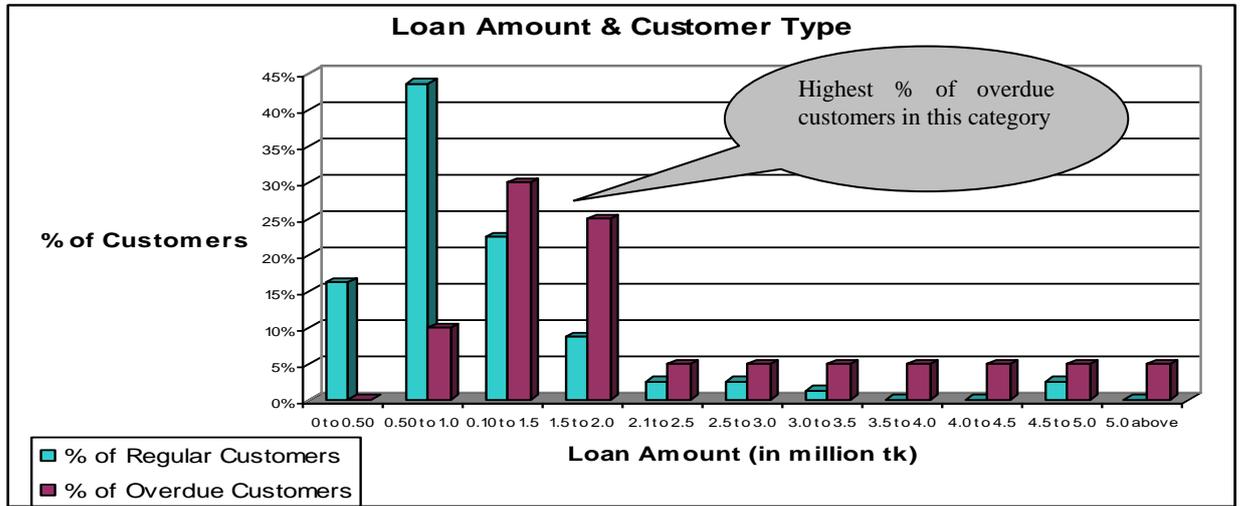
Installment to Income	20	0.04	0.85	0.4985	0.1722
Fixed Obligation to Income	20	0.59	0.98	0.8730	0.1113

Source: Authors' own creation based on sample data

5.1 Frequency Analysis

The frequency analysis has focused on the percentage of regular and overdue customers in different category.

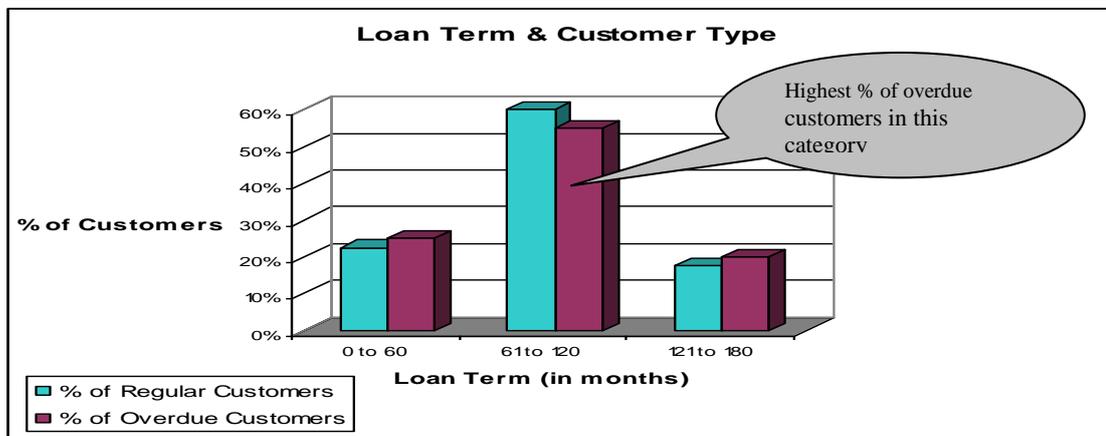
Chart -1.1: Loan allotment based on customer category



Source: Authors' own creation based on sample data

From the chart -1.1, it is evident that the highest percentage (30%) of the overdue customers have the loan amount between BDT 1.0 million to BDT 1.5 million and the lowest (0%) have the loan amount between BDT 0 to BDT 0.50 million. In case of regular customers, the highest percentage (44%) has the loan amount between BDT 0.50 to BDT 1.0 million.

Chart-1.2: Loan term based on customer category

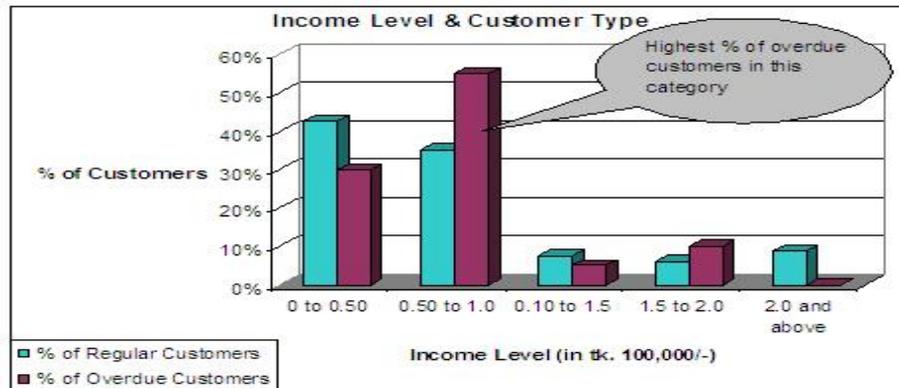


Source: Authors' own creation based on sample data

From the chart -1.2, it is evident that the highest percentage (55%) of the overdue customers has the loan term between 61 months to 120 months and the lowest (25%) have the loan term between 121 months to 180 months. In case of regular customers, the highest percentage (60%) has the loan term between 61 months to 120 months.

5.2. Income Level

Chart-1.3: Income level based on customer category

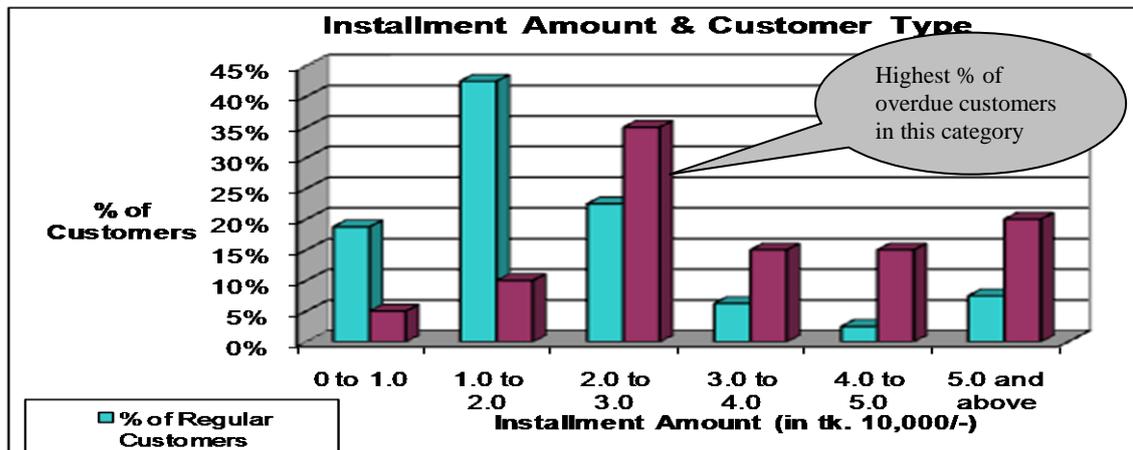


Source: Authors' own creation based on sample data

From the chart -1.3, it is evident that the highest percentage (55%) of the overdue customers has the income between BDT 50,000/- to BDT 100,000/- and the lowest (5%) have the income of BDT 200,000/- and above. In case of regular customers, the highest percentage (43%) has the income up to BDT 50,000/-.

5.3 Installment Amount

Chart-1.4: Installment amount based on customer category



Source: Authors' own creation based on sample data

From the chart -1.4, it is evident that the highest percentage (35%) of the overdue customers has the installment between BDT 20,000/- to BDT 30,000/- and the lowest

(5%) have the installment of BDT 10,000/- and below. In case of regular customers, the highest percentage (43%) has the installment between BDT 10,000/- to BDT 20,000/-

5.4 Debt Burden Ratio

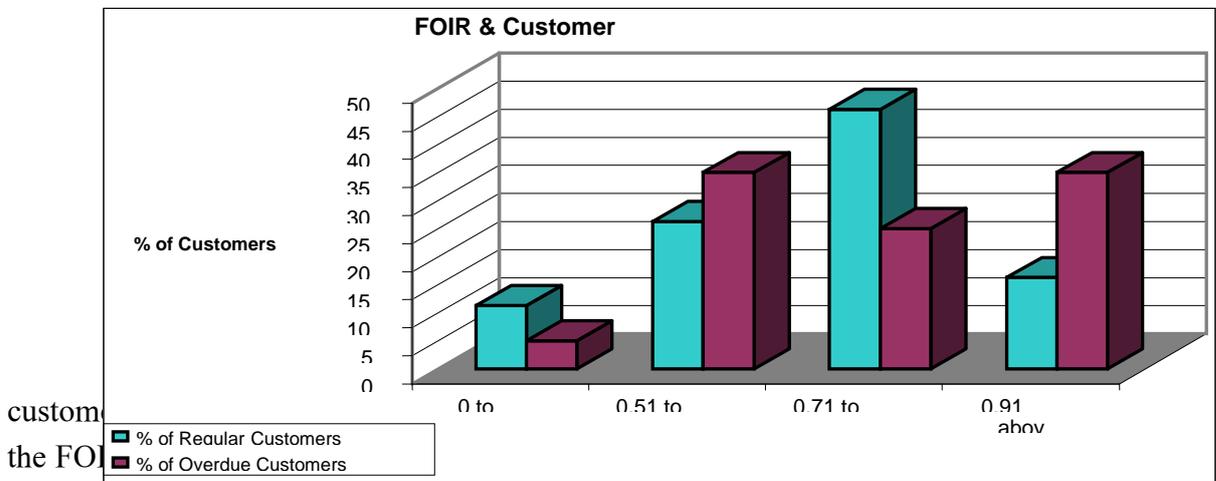
From the collected data, it is evident that the highest percentage (70%) of the overdue customers has the DBR of 0.51 and above. In case of regular customers, the highest percentage (31%) has the DBR between 0.31 and 0.40.

5.2.6 Installment to Income Ratio.

From the collected data, it is evident that the highest percentage (55%) of the overdue customers has the IIR of 0.51 and above and the lowest (0%) has the IIR between 0.11 and 0.20. In case of regular customers, the highest percentage (29%) has the IIR between 0.31 and 0.40.

5.2.7 Fixed Obligation to Income Ratio

Chart-1.5: Fixed Obligation to Income Ratio

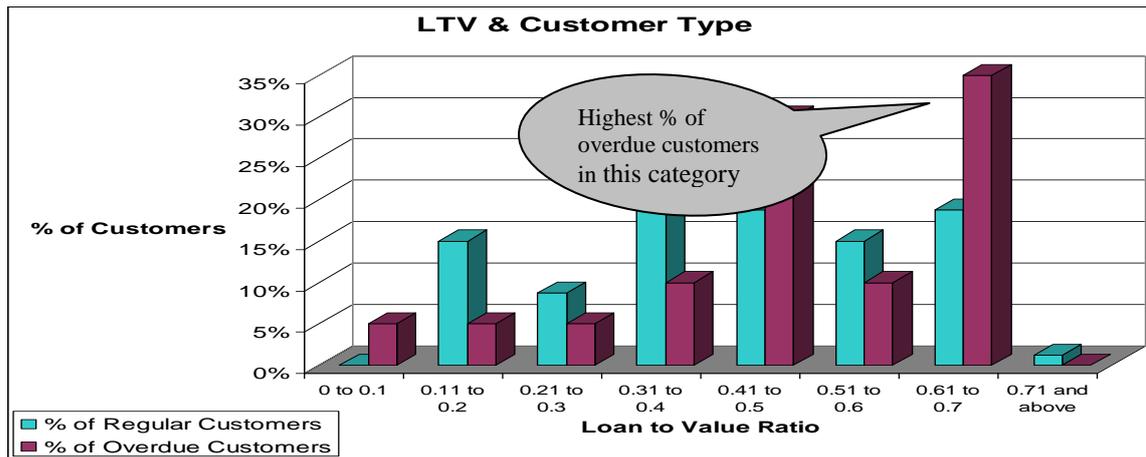


customers has the FOIR between 0.71 and 0.90.

5.2.8 Loan to Value Ratio

From the chart -1.6, it is evident that the highest percentage (35%) of the overdue customers has the LTV between 0.61 and 0.70 and the lowest (0%) has the LTV between 0 and 0.10. In case of regular customers, the highest percentage has the LTV between 0.31 and 0.40.

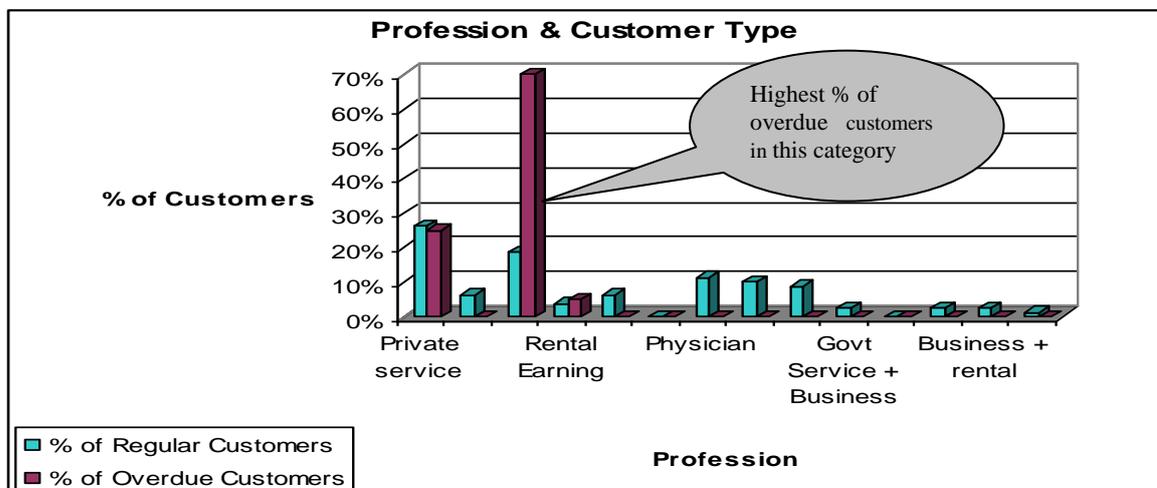
Chart-1.6: Loan to Value Ratio



Source: Authors' own creation based on sample data

5.2.9 Profession

Chart-1.7: Profession of the customer type



Source: Authors' own creation based on sample data

From the chart -1.7, it is evident that, about 70% of the overdue customers are business persons and highest percentages of the regular customers are involved in private service.

6. RECOMMENDATIONS:

From the study research find the following recommendation for credit evaluation and collection process of IDLC Finance Ltd. we can recommend following points-

- The loan amount should be in general kept under BDT 1.00 mln for home loans. In case of larger amount thorough credit evolution and security pricing and mortgage has to be followed,
- The loan term should be within 12 years.

- The loan should be processed in such a way that the installment amount is within BDT 20,000.
- Debt burden ratio should be kept under 0.40:1 to be in safe side.
- Safe loan to value ratio is 40:1.
- The best payment performances are of service holders and worst are business persons. So in time of lending to business personals IDLC should take special care to asses there business activities and financial position.

7. CONCLUSION

The study has been prepared on the topic of “Determinants of Home Loan Repayment Performance of Leasing Company: A Study on IDLC Ltd.”. Some of the identified variables are quantifiable and some others are descriptive. The variables used in the model are loan term, income level, loan to value ratio, debt burden ratio, installment to income ratio and fixed obligation to income ratio. It has been found that, loan to value ratio, debt burden ratio, installment to income ratio and fixed obligation to income ratio negatively affect the loan repayment performance i.e. when the value of these variables increase, repayment performance seems to worsen and customers have the chance to default. On the other hand, loan term and income level positively affect the home loan repayment performance. i.e. when the value of these variables increase, repayment performance seems to get better.

So, the research concludes that, IDLC credit team should carefully evaluate the above-mentioned variables in reaching the decision of financing a customer. It is to be noted that, along with the quantifiable variables, the credit team should also focus on the subjective variables such as the profession of a customer, his credit attitude information of which can be found out and verified by collecting data from his neighborhood, business associates, financiers and last but not the least, the security against which the financing is being made. Security documentation should be complete to avoid the ultimate risk of default.

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