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# CREDIT EVALUATION MECHANISMS OF COMMERCIAL BANK CUSTOMER

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## Abstract

The article reveals the essence, basic requirements and organizational and methodological aspects of assessing the creditworthiness of commercial bank customers. Proposals have been developed to theoretically and organizationally and methodologically improve the creditworthiness of the bank's customers.

**Keywords:** credit, creditworthiness, financial position, complex analysis, credit risk.

## Introduction

Loans provided by commercial banks to various sectors and industries play an important role in the development of the national economy. Although a number of measures are being taken in the country to improve the investment climate and attract foreign direct investment, in practice, commercial banks are responsible

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for providing businesses with the necessary funds. In recent years, the volume and weight of loans provided by commercial banks of the country has been growing significantly.

The relevant Resolution of the President of the Republic of Uzbekistan contains the following problems related to credit and lending:

- "..., the over-centralization of powers in lending decisions prevents a clear delineation of responsibilities between parent banks and their branches;
- sophisticated mechanisms for reviewing loan applications limit the ability to obtain loans quickly;
- the collection of fees and other charges for the consideration and allocation of loans (microloans) leads to an increase in the real value of the debt;

The inclusion in the contracts of the right to unilaterally change the tariffs for services, interest on loans and attracted deposits, as well as the provision of one service with the provision of additional services violates the rights of consumers of banking services ... "(Resolution, 2018). Although the Resolution of the President of the Republic of Uzbekistan No. PP-3620 sets a number of priorities as a solution to the above problems, the main focus today is to analyze the creditworthiness of the client. Therefore, below we will talk about the organizational and methodological aspects of the analysis and assessment of the creditworthiness of bank customers.

## Literature Review

There are different approaches of economists and specialists in the field of analysis and assessment of creditworthiness, which can be summarized and divided into two groups. While one group of scholars and experts interpret enterprise creditworthiness based on the interests of commercial banks and credit policies, another group of scholars recommends analyzing creditworthiness based on financial condition, efficiency, and business scale. The general idea of both approaches is that the financial condition of the enterprise is an important object in assessing the creditworthiness. However, when analyzing from the point of view of a commercial bank, along with the analysis of the financial situation, special attention is paid to the non-financial indicators of the borrowing business entity.

Economist Mavlanov (2018) studied the creditworthiness of bank customers from both perspectives, classified financial and non-financial indicators from a banking point of view on the basis of certain criteria and proposed to assess

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creditworthiness using a scoring model. He proposed a comprehensive analytical approach based on the indicators of liquidity, balance sheet liquidity, stability and efficiency in improving the creditworthiness analysis based on the financial condition of the enterprise and demonstrated the effectiveness of its use (Mavlanov, 2019).

In her research on the theoretical and organizational aspects of creditworthiness, Turdieva (2019) explained the interpretation of terms used in the analysis of creditworthiness in the example of agricultural enterprises, the role of creditworthiness analysis in complex economic analysis, the classification of customers using non-financial indicators.

Due to the fact that the difference between creditworthiness and solvency is a complex process and is aimed at assessing the situation in the future, the issues of improving the practice of assessing the creditworthiness of customers in commercial banks have also been studied (Mamatov, Kulliev, Pulatova, 2016).

Alimardonov (2017) concluded that in lending to small businesses, the method of assessing their creditworthiness and assessing total cash flows is preferred to the method of financial ratios.

The textbook "Banking", published by a group of scholars, describes the essence of the concept of creditworthiness, its importance in the lending process, methods and procedures for assessing the creditworthiness of individuals and legal entities (Azizov et al., 2016).

In their research, Russian scientists have advanced the concept of business continuity in assessing the creditworthiness of an economic entity, proving that failure to provide creditworthiness can lead to its termination, ie bankruptcy and a serious risk of business continuity (Babicheva, Lyubishin, Kondratev, 2018).

From the above, it can be seen that the analysis and assessment of creditworthiness is one of the important economic relationships. Although many aspects of this process have been revealed by scholars, the theoretical and organizational-methodological aspects of creditworthiness analysis have not been sufficiently studied.

**Research methodology.**

The research is based on scientific research, analyzed through induction and deduction, analysis and synthesis, monographic observation, scientific observation, and the improvement of theoretical and organizational aspects of creditworthiness analysis on the basis of scientific research.

**Analysis and discussion of results.**

Credit analysis is a process aimed at assessing the ability of a client, i.e. a borrower, to repay loans. Creditworthiness refers to the ability of a borrower's customers to use and repay a loan in accordance with clearly defined terms.

From the definition of the concepts of creditworthiness and credit analysis, we can see how important it is for commercial banks to conduct a qualitative and objective creditworthiness analysis. Also, by realistically assessing the borrower's creditworthiness, commercial banks can get rid of problem loans quickly and easily.

Today, scientific research is being conducted to improve the analysis of creditworthiness in the practice of commercial banks of the country. These studies also highlight the current procedure for assessing the creditworthiness of commercial banks and its shortcomings. In particular, Mavlanov (2019) recognizes the coefficient method as the most widely used method in practice. He also noted the following shortcomings in the criteria for assessing creditworthiness:

- shortcomings in the method of calculating coefficients;
- inability to fully assess the financial condition of the business entity on the basis of these ratios;
- insufficient attention to non-financial indicators;
- failure to take into account foreign experience (Mavlanov, 2019).

In addition, Mavlanov (2019) developed a seven-step analysis methodology, proposing a step-by-step method that allows to achieve clear results in the analysis of creditworthiness of business entities in order to overcome these shortcomings.

In our opinion, the step-by-step method proposed by Mavlanov (2019) gives a high efficiency in the analysis of creditworthiness in terms of the interests of commercial banks. At the same time, the introduction of procedures for dynamic, factorial and prospective analysis of creditworthiness, without forgetting the interests of the business entity, complicates the process. Indeed, commercial banks rarely use factor and perspective analysis in their creditworthiness analysis, and the implementation of these analyzes poses some difficulties in terms of organizational and information provision.

Based on the above, the analysis of the creditworthiness of a client with the status of a legal entity analyzes information on past business success, current market situation, human resources, industry and industry, financial statements, feasibility study of the project and the borrower's credit history includes.

Table 1 Principles used in the analysis and assessment of creditworthiness and their content

| № | Principles | Content and application |
|---|---|---|
| 1. | **Openness** | Transparency of the types of loans offered by the Bank to customers and the necessary information on obtaining them. Transparency and clarity of credit policy. Every client should have information about the types of loans, the procedure for obtaining them, the method of assessing creditworthiness. |
| 2. | **Speed** | The process of assessing the creditworthiness of the bank's customers should be carried out as quickly as possible at an economically significant level. This saves borrowers time and other related resources. |
| 3. | **Reliability** | Ensuring the reliability of the information provided in the assessment of creditworthiness by comparing it with different sources. It is necessary to use blockchain technology effectively. |
| 4. | **Savings** | Determining the creditworthiness of customers by the bank should be cost-effective for both the bank and the customer. This is done by reducing the working hours of bank employees in the process of allocating loans and minimizing the costs associated with obtaining loans from customers. |
| 5. | **Objectivity** | Ensuring fairness by minimizing the human factor in creditworthiness assessment and credit allocation decisions. |

Different approaches and specific methodologies are presented in the research and analysis of the creditworthiness of business entities and in the works of scientists in the field. One group of scholars approached the issue from the point of view of the interests of lenders, while another group expressed their views from the point of view of the business entity.

In our view, creditworthiness analysis is a separate object of economic analysis and has its own goals and objectives. Therefore, we consider it necessary to consider the creditworthiness analysis not as an integral part of financial analysis or part of a complex economic analysis, but as a separate process, a holistic system and on this basis to improve the organizational and methodological framework of the analysis.

In conducting a creditworthiness analysis, it is first necessary to identify the principles that play an important role in it. Indeed, the results of the analysis conducted in accordance with certain principles will be reliable and effective. We

ISSN: 2776-0960 Volume 2, Issue 6 June, 2021

believe that the following principles are important in the analysis and assessment of creditworthiness based on the requirements of the digital economy (Table 2).
We believe that the decisions taken on the allocation of loans in accordance with these principles will serve to further improve the quality of banking services, create opportunities for greater customer engagement and reduce the risk of loan repayment.
A number of information sources and indicators are widely used in creditworthiness analysis. This information is grouped in terms of quantity and quality. In some literature, these indicators are described as financial and non-financial information.
In assessing creditworthiness based on the analysis of financial indicators, the focus is on the financial statements of the business entity. In this regard, many literatures refer to financial indicators, in particular, financial ratios, the procedure for determining them and ways to evaluate on this basis. Particular attention should be paid to verifying the reliability of the indicators used in the analysis of financial indicators and the financial information required for their calculation.
If we analyze the work carried out by commercial banks on the development of the economy of Uzbekistan, as of January 1,2021, gross domestic product of Uzbekistan amounted to 580.2 trillion soums and increased by 11.8% compared to January 1, 2020. In 2020, the gross domestic product reached 511.8 trillion soums and increased by 25.8% compared to 2019. In 2014-2020, the country's GDP and the volume of loans from commercial banks had a growing trend. The volume of loans to the real sector of the economy increased by 26.3% compared to previous years and as of January 1, 2020 amounted to 211.5 trillion soums. The growth rate of loans to GDP amounted to 41.3%. From this we can conclude that in our country, in fact, creative work is widespread, the demand for money is growing, and this indicates an increase in the level of credit. However, the fact that the relative level of loans to GDP increased by only 0.1% compared to previous years shows that the loans allocated to the real sector in this country are insufficient (Figure1).
Over the past 10 years, the volume of loans in Uzbekistan has increased 35 times, and bank assets – more that 23 times. In particular, during 2017-2019, the growth rates of assets and loans of commercial banks were high, especially in October 2017, this figure increased significantly. The main reason for this is the adoption in recent years of a number of regulations related to the banking system. In

particular, the Resolution of the President of the Reublic of Uzbekistan dated September 2, 2017 "On priority measures to liberalize the exchange rate" PP-3272, dated September 12, 2017 "On measures to further develop and increase the stability of the banking system of the Republic" – Decisions №. 3270 allowed to increase the financial performance of banks.

On April 10, 2020, according to the international rating agency Fitch Ratings, the country's sovereign credit rating was maintained at "VV-" ("Stable" forecast).

According to Fitch Ratings, the main factors in maintaining Uzbekistan's rating in the context of the global crisis caused by the COVID-19 pandemic are the availability of strong external and fiscal reserves, diversified export base and access to external financial resources.

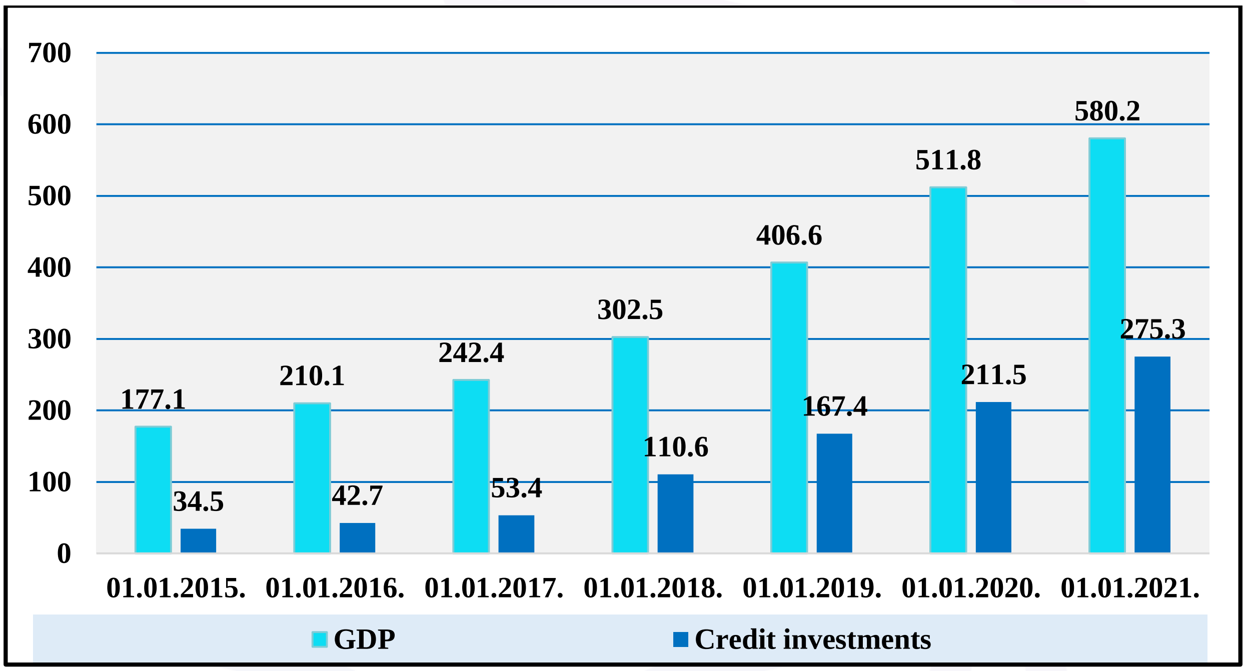


Figure 1. Amount and share of credit investments of GDP and commercial banks in the country.

Given the existence of different approaches to the classification of financial indicators used in the analysis of creditworthiness, we consider it appropriate to group them as follows, examining the views recognized by local and foreign scholars (Table 2).

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Table 2 Composition and classification of financial indicators used in creditworthiness analysis

| № | Indicators | Classification of financial indicators |
|---|---|---|
| 1. | **Liquidity indicators** | 1.1. Current liquidity ratio |
| | | 1.2. Fast liquidity ratio |
| | | 1.3. Absolute liquidity ratio |
| | | 1.4. Cash ratio |
| 2. | **Rotation indicators** | 2.1. Rotation coefficient of TMZs |
| | | 2.2. Accounts receivable turnover ratio |
| | | 2.3. Private capital turnover ratio |
| | | 2.4. Asset turnover ratio |
| | | 2.5. Net working capital turnover ratio |
| | | 2.6. Circulation period |
| 3. | **Operational profitability indicators** | 3.1. Profit margin ratio |
| | | 3.2. Return on investment ratio |
| | | 3.3. Capital return ratio |
| | | 3.4. Earnings per share |
| 4. | **Indicators of business risk** | 4.1. Leverage operation |
| | | 4.2. Financial leverage |
| | | 4.3. General leverage |
| 5. | **Indicators of financial risk** | 5.1. Debt to equity ratio |
| | | 5.2. Percentage coverage ratio |
| | | 5.3. Debt recovery ratio |
| 6. | **Financial stability ratio** | 6.1. The ratio of fixed assets to invested capital |
| | | 6.2. The ratio of current assets to non-current assets |
| | | 6.3. The ratio of share capital to total tangible assets |
| 7. | **Indicators of interest coverage** | 7.1. Fixed interest rate recovery ratio |
| | | 7.2. Fixed dividend recovery ratio |

Since the definition and characteristics of these indicators are given in many literatures, we will focus on quality indicators, while limiting them to this classification.

## Conclusions and suggestions.

Credit is an integral part of the modern economy and the global financial system. The increase in credit is an important factor influencing global economic development. Credits are also one of the main sources of income for commercial banks, and loans are a necessary financial tool for commercial banks to achieve high profitability through the expansion, development and modernization of their activities. Therefore, it is advisable to organize and conduct a creditworthiness analysis on the basis of a comprehensive approach.

In conclusion, it should be noted that the methods currently used in the analysis of creditworthiness of business entities are not fully in line with international practice and are subject to rapid changes in the global economy. Therefore, we consider it necessary to take into account the following suggestions in improving the analysis and assessment of creditworthiness:

- When organizing a creditworthiness analysis, it is advisable to first identify the most important principles and fully implement them..
- Business and financial risk indicators are listed separately, as well as interest rate and operating profitability indicators, while listing the quantitative (financial) indicators used in the creditworthiness analysis.
- A comprehensive approach to the analysis process is needed when considering creditworthiness analysis and assessment as a holistic system.
- Extensive use of the scoring model in assessing the creditworthiness of the borrower based on the results of the analysis. When scoring, it is necessary to develop procedures for relying on accurate mathematical calculations, industry characteristics, the main type of activity, methods for determining quality indicators and evaluation of the reliability of all data by cross-checking.

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