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IDENTIFY THE FACTORS INFLUENCING ON GRANTING CREDIT IN LENDING INSTITUTIONS

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Declaration of the Candidate

I declare that this is my own work and this dissertation does not incorporate without acknowledgement any material previously submitted for a Degree or Diploma in any University or other institute of higher learning and to the best of my knowledge and belief it does not contain any material previously published or written by another except where the acknowledgment is made in the text.

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Declaration of the Supervisor

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To my Parents and Husband

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ABSTRACT

Credit scoring system based on various criteria is widely used analysis technique of measuring customer credit worthiness by the Credit Information Bureaus (CIB) in many developed countries. However, such a system is not available in Sri Lanka. The aim of this study is therefore to identify the factors that influencing on granting credit in lending institutions in Sri Lanka and to recommend a criteria to identify potential borrowers. The required variables for the study were identified from the Bureau point of view and secondary data were collected from customer credit reports. Further, 75 customers who obtained credit were selected randomly and based on their credit profile eight important variables were derived.

The combination of Principal Component Analysis (PCA) and Factor Analysis (FA) was carried out to develop factors. The suitability of data for PCA was confirmed using Bartlett's Test (X^2= 206.092, p= 0.000) and suitability for FA was confirmed by KMO statistic (KMO=0.532). The results of FA showed that the initial system of 8 variables can be reduced to 2-D system which account for nearly 52% of the initial variability. Of the identified two principal components, first component came from the, "own credit history" and the second was came from "guaranteed credit history". In order to have better interpretation the results obtained from PCA were rotated using orthogonal factors namely Varimax, Equimax and Quatimax and found that the results obtained were invariant on the type of rotation. Thus it can be concluded that, own credit history and the guaranteed credit history are the influential factors on credit granting. Depending on the variance representing by each factor, it can be concluded that the own credit culture component is more significantly influence on the credit evaluation process than the guarantee component. However, in order to have the accurate credit decision on granting credit, it is required to consider both factors together by indentifying the importance depending on the representing variance. The finding in this study could be effectively employed to develop a suitable credit scoring system for the lending institutions. The study further showed the benefit of using multivariate techniques to solve some problems in lending institutes.

Key words: Principal Component Analysis, Factor analysis, Orthogonal rotations

TABLE OF CONTENTS

	Page
Declaration of the candidate	i
Declaration of the Supervisor	ii
Dedication	iii
Acknowledgement	iv
Abstract	v
Table of Contents	vi
List of Figures	ix
List of Tables	ix
List of Abbreviations	x
Chapter 1: Introduction	1
1.1 Back Ground of the Study	1
1.2 Role of Credit Information Bureau of Sri Lanka (CRIB)	2
1.3 Contend of the Credit Report	3
1.4 Current Procedure of Credit Evaluating	6
1.5 Importance of Identifying the Factors for Customer Credibility	6
1.6 Objective	8
1.7 Limitation of the Study	8
Chapter 2: Statistical Methodology	9
2.1 Overview	9
2.2 Standardized the Data	9
2.3 Principal Component Analysis (PCA)	9
2.3.1 Eigen value one criteria	11
2.3.2 The scree plot	11
2.3.3 Proportion of variance account for	12

2.3.4 The interpretability criteria 12
2.4 Mathematical Frame of the PCA 12
2.5 Factor Analysis (FA) 13
2.5.1 Factor extraction method 14
2.5.2 Factor rotation methods 14
2.5.3 Mathematical frame of factor analysis 15
2.5.4 Determining the number of factors 16
2.5.5 Criteria for selecting items 16
2.5.6 Bartlett's test of Sphericity 17
2.5.7 Kaiser-Mayer-Olkin(KMO) measure of sample adequacy 17
2.6 Selection of Variables 18
2.7 Gathering the Data for the Selected Variables 20
2.8 Data Analysis 21
Chapter 3: Results and Discussion 22
3.1 Preliminary Analysis of Data 22
3.1.1 Descriptive analysis 22
3.1.2 Test for normality 23
3.1.3 Association between variables 24
3.1.4 Test of correlation matrix 25
3.2 Identification of Principal Components to Retain 25
3.2.1 Eigen value one criteria 25
3.2.2 The scree plot 26
3.2.3 Proportion of variance account for 27
3.3 Eigen Scores of Selected Principal Components 27
3.4 Conformity for the Factor Analysis 28
3.5 Factor Extraction Using Principal Component Analysis (PCA) 29
3.6 Identify the Weights for Factors 32

3.7 Discussion 34

Chapter 4: Conclusions and Recommendations 36

4.1 Conclusions 36

4.2 Recommendations 37

References 38

Appendix 39

1.1 The Secondary Data 39

1.2 Probability Plots of the Selected Variables 42

LIST OF FIGURES

		Page
Figure 2.1	Steps of Principal Component Analysis	10
Figure 2.2	Geometric representation of PCA	12
Figure 2.3	Geometric representation of q- Factor Model	15
Figure 3.2	Scree plot	26

LIST OF TABLES

		Page
Table 2.1	Description of the variables	20
Table 3.1	Descriptive statistics of observed variables	22
Table 3.2	P-Values of Anderson- Darling Test	23
Table 3.3	Correlation matrix among the selected variables	24
Table 3.4	Results of Bartlett's Test	25
Table 3.5	Eigen value analysis of the correlation matrix	26
Table 3.6	Eigen scores of the selected Principal Components	27
Table 3.7	Results of KMO Test	28
Table 3.8	Rotated Factor loading and Communalities via Varimax Rotation of 3- Factor Model	29
Table 3.9	Rotated Factor loading and Communalities via Equimax Rotation of 3- Factor Model	31
Table 3.10	Rotated Factor loading and Communalities via Quartimax Rotation of 3- Factor Model	31
Table 3.11	Identified variables for the selected 3- Factor model	32
Table 3.12	Factor Score Coefficients via Varimax Rotation of 3- Factor model	33

LIST OF ABBREVIATIONS

Abbreviation	Description
CF	Credit Facility
CRIB	Credit Information Bureau
FA	Factor Analysis
GRT	Guaranteed
KMO	Kaiser-Mayer-Olkin
NDIA	Number of Days In Arrears
NIC	National Identity Card
PCA	Principle Component Analysis
SD	Standard Deviation
SPSS	Statistical Package for the Social Sciences