IMPORTANCE OF CREDIT REPORT IN SANCTIONING LOANS

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ABSTRACT

A person's financial credibility is a crucial consideration when applying for a loan or a credit card. These days, a person's credibility is determined by his or her "credit score," which is a number based on how well the person has done in the past when it comes to repaying debts. This paper proposes a novel method for obtaining this information. Taking advantage of the fact that practically everyone now owns a smartphone, a smartphone app that collects all of this data and transmits it to the appropriate persons may exist. More than merely a person's transactions might be used to assess his or her credibility. According to this paper, you should look at social media data to learn more about a person's overall social status. Text messages are being used to deliver all transactions to bank and other institution customers. So, if you have access to SMS, you will be able to obtain information about all of these transactions. There will be a smartphone app that will send text messages including solutions to bank data and internet purchases. The usage of artificial neural networks will allow for the calculation of the final credibility score based on the many data points obtained. The major purpose of this paper is to provide a wealth of precise information regarding how your credit score and history affect your ability to obtain a loan.

INTRODUCTION

Your credit history includes all of the information from your credit report, such as the number of credit accounts you have, their outstanding balances, and the dates and times of your payments. Three reporting agencies collect and update data on a regular basis (Equifax, Experian and TransUnion). Bankruptcies and past-due debts to collection agencies are among the items on your credit report. Credit reports can only be obtained by submitting a financing or credit application (Insurance Information Institute) This is how inquiries appear on your credit report.

Your credit score, which is a numerical representation of your creditworthiness, is calculated using the information in your credit report. Lenders use your credit score, also known as your FICO score, to determine your creditworthiness. Your credit score is determined by a number of factors, including your payment history, account balances, and new credit inquiries, among others.

Your credit score and the information on your credit report have a direct impact on your ability to obtain a mortgage.

Your credit report and credit score are not the same thing. Your credit score is calculated using information from your credit report. Better credit histories and lower interest rates are linked to higher credit scores (Zeidan, et al. 2015).

There are several methods for calculating a person's credit score. The FICO score, on the other hand, is used by the majority of mortgage lenders. It doesn't matter which credit bureau is used to calculate your score depending on the circumstances. Most mortgage lenders use Equifax, Experian, and TransUnion, which are the three major credit reporting agencies. Preventing a negative impact on your credit score from inaccurate information on your report can save you money over time by lowering your overall interest rate and decreasing the amount of money in your bank account.

However, when it comes to deciding whether or not to lend you money, your credit score is just one of many factors that lenders consider. Other factors include:

- Credit report
- Credit history with that lender
- The amount of debt you already have
- How much you have in savings
- Your total assets
- Current income

AIM AND OBJECTIVES

AIM

"Importance of Credit Report in Sanctioning Loans"

OBJECTIVES

- To understand the basics of credit history and CIBIL report
- To acknowledge the role of credit report in process of loan
- To determine the ways that can help in enhancing credit score

LITERATURE REVIEW

CONCEPTS AND BASICS OF CREDIT REPORT

Good credit history is the result of timely debt repayment. Many organisations and even the government keep track of an individual's credit history, which is then summarised in a report called a credit report. A borrower's credit report and other sources of information are fed into an algorithm to predict future delinquencies, and the algorithm generates a credit score for the borrower.

In many countries, a customer's credit application is sent to a credit bureau when they apply for a loan from a bank, credit card company, or retailer. Credit bureau records are compared to those provided by the applicant, including their name, address, and other personally identifying information (PII). Based on the information gathered, the lending institution assesses a person's ability and track record of debt repayment. A borrower's willingness to repay a debt can be gauged by the promptness with which they have previously made payments to other creditors (Lee, et al. 2019). Overpayment may not be considered as a way to make up for missed payments because lenders value a consistent and on-time payment history.

The validity and reliability of consumer reports have been the subject of a long-running debate. Credit reports, according to industry insiders, are extremely reliable. Data from credit bureaus' analysis of 52 million credit reports serves as evidence. More than one-fifth of all consumer complaints ended in a dispute, according to the Consumer Data Industry Association, which testified before Congress. In spite of this, there is a widespread belief that credit report data can be inaccurate. There are now numerous laws in place to address the errors themselves as well as how they are perceived by people.

When it comes to consumer credit or loans, income is an important factor to consider. A consumer's income will be higher if they can get more credit, everything else being equal. When deciding whether or not to grant a loan, lenders take into account both the borrower's ability to repay a debt (income) and their willingness to do so (credit report).

To determine whether or not to extend a loan, lenders use these factors. As a result of a shift to risk-based pricing in the financial services industry, this report has become even more relevant. FICO is the most widely used credit scoring model in the United States, Canada, and other countries. The factors are similar and may include:

- A person's credit rating or score can be affected by their payment history, which accounts for 35 percent of the FICO score. Many common negative events are taken into account when calculating a company's risk. These include charge-backs; collections; late payments; repossession; foreclosure; settlement; bankruptcy; liens and judgments. A FICO score is influenced by a variety of factors, including the severity, age, and frequency of negative items. A delinquent or unpaid debt that is only a few years old is considered to be worse. As the severity of the condition worsens, it becomes increasingly difficult to cope. As a result, having too many people is even more detrimental than having too few.
- Credit card debt accounts for 30% of an individual's FICO score. Credit reports show a person's total debt as well as the types of debt they have. The credit utilisation ratio measures how much of your credit limit you are actually using. Three different kinds of debt are taken into account in this calculation.
- Revolving debt: Credit card debt, retail credit card debt, and petroleum credit card debt are all examples of revolving debt. For the most part, the revolving debt that was examined was not secured by real estate and instead came from credit cards. Revolving utilisation, or "open to buy," is the most important metric in this category because it depicts the relationship between a customer's total credit card debt and the available credit limit. To calculate the utilisation percentage, take the total amount of credit card debt and divide it by the total amount of available credit. Higher percentages lower the credit score of the cardholder. If you're working hard to improve your credit rating, don't close your credit cards. If a cardholder does not pay off their outstanding debts at the same pace as they close credit card accounts, their total available credit limits will be reduced, and their utilisation percentage will most likely rise.
- Instalment debt: Debts that are paid in instalments are known as instalment debts. With a car loan, a good analogy is that the cardholder typically makes the same monthly payment for a length of time (such as 36 to 60 months). In terms of risk scoring systems, instalment debt is a distant second to credit card debt. For a loan secured by an asset, like an instalment debt, a car, house, or boat can all be used as collateral. In order to avoid having their property repossessed by the lender, customers will go to great lengths to pay their bills on time.

- Open debt: Open debt can be classified as either unsecured or secured. Every month, you must pay this recurring monthly bill in full. "Pay in full" products include any of the numerous credit cards currently on the market. A good example is the American Express Green card. Older versions of the FICO scoring system treat open debt as revolving credit card debt, but newer versions exclude it from the revolving utilisation calculation.
- It contributes 15% of your FICO score to the age of your credit file. The older a person's credit report is, the more secure it is. It's expected that this will raise their credit score. Cardholder's credit file age and average account age are used to determine this "age" for the cardholder's credit file. People's credit files are judged by the oldest account's "opening date," which is the date the account was opened. All open and closed accounts on a consumer's credit report are averaged to determine the average age of the accounts on the report.
- One of the best ways to raise a credit score is to have a wide variety of accounts on one's credit report. A person's credit score improves if they are able to handle a wide range of financial situations by managing multiple accounts.
- Ten percent of your FICO score is based on the number of credit inquiries you make. Requests for information from credit files result in an inquiry being made by the company. A person's credit score can be affected by a variety of different types of inquiries. There are two types of "soft inquiries": those that have no bearing on a consumer's ability to repay and those that are recorded on a consumer's credit report for six months.
- According to predetermined standards, credit bureaus can sell the contact information of individuals to lending institutions for the purpose of issuing credit cards, loans, and insurance.
- On the other hand, a creditor conducts regular credit checks on its customers. Account management, maintenance, or review is the term used to describe this process.
- A credit counselling agency can obtain a client's credit report if the client gives their permission.
- It does not affect an individual's creditworthiness to review their personal information. This type of investigation is known as a "consumer disclosure" investigation.

  Checks on potential employees' criminal records.
- Concerns about insurance
- Negative feelings about utility service

- Lenders and credit scoring models can see a "hard inquiry," or request for credit or a loan in response to a legitimate request from a customer. A lender may "pull" a customer's file if the Fair Credit Reporting Act permits it in order to provide credit to a customer. However, credit scores aren't always affected by hard inquiries. A person's credit score can be improved by limiting the number of credit inquiries he or she makes. Because of a person's recent history of multiple inquiries on their credit report, a lender might consider them a high-risk borrower because of their recent financial difficulties. (Ryan, S. G,2012).

ROLE OF CREDIT HISTORY AND CREDIT REPORT IN LOAN APPROVAL

A person's credit score is taken into account by all financial institutions when approving a loan application. A borrower's ability to pay back the loan in the time allotted is evaluated using this score by banks. A person's ability to borrow money in the future is strongly influenced by their credit score. Most people have a credit score between 300 and 900. Applicants with a credit score of at least 750 are preferred by lenders. People's credit scores used to be based solely on the information banks kept on file. Banks provide this information to the credit scoring agency on a monthly or yearly basis. The vast majority of the time, this data is gleaned solely from transactions involving money. People's credit scores are determined solely by their banking and loan history, as a result. Non-financial factors that have a significant impact on a person's financial credibility are not taken into account, despite the fact that it is somewhat accurate. (Chaudhuri, K,2012)

PROCESS OF LOAN APPROVAL

In the current economic climate, getting a loan is more difficult than it used to be. For many people, it's a long and arduous process. Because it is so important to lenders, they base loan approval on a borrower's CIBIL score. Lenders may reject your loan application or charge you a higher interest rate if you don't have a credit history.

Loan Approval Process

When you apply for the loan, this is what happens:

- You fill in the loan application form.
- You hand it over to the bank or lender.
- A low credit score makes a loan application unlikely to be approved.
- CIBIL is used by banks and lenders to check a person's credit score and credit report.
- Your credit score and the documents you've submitted determine your eligibility.
- If the applicant is ineligible, the application will be rejected.
- If you meet the lender's or bank's eligibility requirements, your loan will be approved.79% of the loans that are disbursed are to the individuals who have a Credit score that is greater than 750.

What do the lenders check for in your CIBIL report?

The banks or lenders look for the following in the CIBIL Report:

- There should be a note on the Credit Information Report if a debt has been written off. The Account Status section of your credit report contains this information.

- In addition, the lender will look at your payment history. Check to see if you have any unpaid debts and how much you owe. Days Past Due is a field on a credit report where you can find this information.
- The profile of the company is then examined by the lenders. Most banks keep a list of borrowers who have been pre-approved for loans.
- Lenders and banks will also look at the EMI to income ratio. If your current EMI is more than half of your monthly salary, you have a very low chance of getting a loan.

For example let's take two cases:

Case 1: If you earn $50,000 per year and pay Rs.10,000 in monthly EMIs, your EMI payment ratio is 20% of your gross income. You can afford an EMI of Rs.25,000- Rs.10,000 = Rs.15,000 per month if you can borrow 50% of Rs.50,000. At a ten percent interest rate, Rs. 15,00,000 can be borrowed for 20 years at Rs. 15,00,000. If this is the case, the bank or lender is likely to grant you a loan.

Case 2: The EMI to income ratio is 50000/100000 percent because the total income is Rs.1,00,000 and the EMI is Rs.50,000. To put it another way, you can borrow half of the $50,000 you have available, and an EMI that fits into your budget is a reasonable amount of money to spend. As a result, you're eligible for a Rs.0 loan with a ten percent interest rate for the next two decades. If this is the case, your loan application will most likely be rejected by the bank or lender.

Follow these suggestions to improve your credit score.

How to Improve CIBIL Score?

Having a bad credit score isn't the end of the world. The following tips will assist you in achieving a higher GPA at the end of the semester. Significant changes in your credit score and "improvements" to your credit report can be seen in as little as six months (Weston, 2011).

Avail your recent credit report

This will assist you in determining where you went wrong and what needs to be done to correct it. There are many ways to improve your credit score, but paying your bills on time is the most important. You can use this tool to correct a mistake or set a new goal if you've made one (it has to be at least six months).

Never postpone payments

As technology has advanced, so has the number of people who procrastinate. This will anger CIBIL, so make sure to pay all of your bills and obligations on time. Your grade will suffer as a result if you don't. It's best to automate your payments to avoid unintentional delays.

Have a diverse credit-folio

Lenders will be able to see that you can handle a wide range of credit as a result. This can be accomplished with the right combination of unsecured and secured loans. Taking out unsecured loans rather than secured loans is frowned upon.

Don’t have unused credit cards

It is never a good idea to have an unused credit card or a collection of credit cards. If you're worried about exceeding your credit limit, avoid using a credit card. Rather, purchase groceries or gas and pay it off at the start of the next month. If you haven't used your credit card in a while, it might be time to close it.

Smart handling of debts

Repaying your debts is a good way to improve your credit score. Revolving credit on our credit cards can quickly spiral out of control if we're not careful. This is something we've all experienced. Personal loans can be used to pay off credit card debt. As a result, you can save money on interest while also resolving a problem quickly (Weston, 2011).

No maxing out the credit

Make use of the Rs.2 lakh credit card limit, but don't rely on it solely. Your debt-to-income ratio should be in good shape.

Not prolonging tenures

The length of the loan or credit you have taken out can also have an impact on your credit score. If you take out a three-year personal loan and then extend it halfway through for a lower monthly payment, your CIBIL score may suffer.

METHODOLOGY

SOURCES FOR DATA FOR THE PROJECT

Secondary data collection yields information and data that can be used to manage a variety of organisational activities. By learning about this process, you can gain a better understanding of how a person's credit history affects future financing.

RESEARCH TECHNIQUE

By incorporating both internal and external secondary data into the study's basic process, the study's objectives can be met in a variety of ways. Primary research techniques are less useful than previously researched data when it comes to managing various activities.

METHODS FOR GATHERING DATA

Using government publications, such as government-issued journals, articles, books, and research papers; public records; and the most important business documents, data management and organisational processes can be better linked.

DATA RECORDING

Records of previous communications, decisions, and actions must be preserved for both historical and future evidence purposes. The month and day of the month must be represented consistently in the computer structure.

DISCUSSION AND FINDINGS

As a result of their poor credit histories, hundreds of millions of people in low-income countries are unable to obtain credit or bank accounts. Instead of using credit history, alternative data such as income can be used to predict a new account's credit risk. Along with the more common demographic data, there is a wealth of other information available. According to Santos et al., demographic variables play a significant role in credit scoring (2019). Traditional scoring models will be put to the test to see if they can be improved by using alternative data.

Many people are unaware that they have a FICO score until they try to buy a house, get an SBA loan, or make a large purchase like a new car. Lenders use a three-digit number system to determine whether you are eligible for a loan and the interest rate you will be charged. When you apply for a loan, your credit score gives the lender a quick snapshot of your creditworthiness There is no such thing as a universal credit score. If they are both co-signers, each co-score signer's will be checked separately. Your credit costs will increase if you are denied credit because you appear to be a higher risk to a lender. Borrowing money, to put it another way, will cost you more money.

Without credit, the modern economy would collapse. If you need to borrow money for a variety of reasons, such as a home mortgage or a student loan to help you pay for college, you'll need a line of credit. It will also be necessary to demonstrate your ability to repay the debt. Your three-digit credit score is critical to your financial future because of your creditworthiness. Your credit score is important when applying for a mortgage, a car loan, or a student loan. People with bad credit will have a harder time finding credit cards with low APRs, raising borrowing costs.

Even if you don't plan on applying for a loan, having a good credit score can help you with your finances. Credit information is typically used by landlords, insurers, and employers to determine whether or not a person is trustworthy and responsible. Because of your poor credit rating, you may be considered a high-risk investment, regardless of what appears on your credit report. Your personal and financial well-being may be improving if you have good credit. Your insurance premiums, your ability to rent an apartment, and even whether or not you are hired for a new job are all affected by your credit score.

To take advantage of the benefits of good credit, you must first establish it, but you must also maintain it. With today's best credit cards, you can earn cash back rewards and enjoy luxury travel benefits. Do you know how to keep your credit score in good standing? Maintain your current good credit habits, and your credit score should improve. Paying all of your bills on time and in full is essential. To keep your utilisation ratio low, never use more than 30% of your available credit at any given time. Avoid closing out-of-date credit accounts to demonstrate a long history of good credit. Don't be fooled by the fact that maintaining a high credit score is easier than establishing one. Your credit score may suffer if you don't pay your bills on time or accumulate debt that you can't afford to repay.

CONCLUSION

If you manage your credit well, the lower your credit costs are, the better off you will be. Budgeting your expenses, responsibly paying off credit cards, and paying all of your bills on time, even the smallest ones, are all examples of good financial management. Saving and investing more money is a great way to improve your credit score and lower your loan interest rates, and they can assist you in doing so. If you have a good or excellent credit score, you can save hundreds of thousands of dollars over the course of your life. For someone with good credit, every financial transaction is more affordable. Banks are lowering interest rates, fees, or both to entice customers with better credit ratings. Because lenders are less likely to compete for a person with a low credit score, they can charge higher APRs (APRs). If your credit score is low, you may have trouble renting an apartment, getting a car, or even getting life insurance. The reason for this is that your credit score has an impact on your insurance score.

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