ABSTRACT

Small business sector is the backbone of every economy. Its strong entrepreneurial nature contributes largely to the Gross domestic product, employment generation, exports, manufacturing and services. It is also a hub for innovation. Financial support is a key element in the growth and development of the sector. In developing countries like India, the status of financial support given to the sector is abysmal. One of the important reason banks are discouraged to lend to the small business sector is the perceived risk associated by banks in lending to the small business sector. Apart from the perceived risk, banks also find it difficult to appraise credit applicants based on limited information available regarding the applicant.

This study is an attempt to help bankers overcome the problem of credit appraisal of small business borrowers, with the help of the development of a credit scoring model. The credit scoring model does not take into consideration the accounting and financial information of the borrower. Therefore, the study assesses the borrower based on the information that is relevant to the business and personal information of the borrower that could evaluate the creditworthiness of the borrower.

Based on the literature available on determinants of repayment behaviour, bankers were asked to give their opinion on the importance of those variables in determining the creditworthiness of the borrower. Also information from select borrowers was gathered to examine the relevance of each of the selected variables in appraising the borrower. At the end of a series of statistical tests the determinants were finalised and a credit scoring model was formulated.