Identifying Creditworthiness Criterions and Financing Approval Process of Islamic Banks in Indonesia

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Abstract. The study aims to identify the creditworthiness criterions and approval factors in providing financing facility to corporate and commercial clients of Islamic banks in Indonesia. It also explores the financing approval process in the Islamic bank for this segment. It employs qualitative study of in-depth and semi-structured interviews method via the available online tool. The study selects 3 (three) Islamic bank officers from the different banks as the respondents. The study finds that the 5Cs elements are all important by emphasizing in proper fixed asset collateral and sound capacity of the clients. There is a typical internal approval process with the timing is different between each bank. It highlights the importance of financial covenants and the requirement to use CASA products. The study also reveals that covid-19 pandemic has impacted the client’s business and its ability to repay the banks. The strategy is to conduct relaxation, reprofiling, and restructuring of the client’s facilities as per guideline from regulator.

Keywords: Creditworthiness · Corporate and commercial banking · Islamic banking · Qualitative study

1 Introduction

1.1 Background of Study

Financing evaluation and approval is a business process in the Islamic bank to review and evaluate the proposal from the clients. Providing financing facility by the bank depends on eligibility and creditworthiness. Creditworthiness is defined as how the banks determine the default probability and how worthy the potential clients to receive the credit facility (Feder et al. 1985 and Corazza et al. 2014). It considers moral character, history of trustworthiness, and capacity and ability to repay the financiers. To determine the creditworthiness of the clients, the bank’s credit department will use any relevant information available to assign the clients to a certain risk classification (Broecker 1990).

In assessing the risk and quality of the potential clients, the concepts of 5C’s of credit appraisal is often employed (Moti et al. 2012). The 5Cs elements are Character, Capacity, Collateral, Capital and Condition, where these are also considered by Islamic banks.
Character is focusing on disclosing of business affairs with the bank and use of funds for the purpose approved. Capacity is defining the ability of the business to generate sufficient cash flows to service the obligation. Capital represents the equity portion contributed to the project. Moreover, condition is related to the business surroundings and environment that have great impact to business. Collateral is security charged and pledged against the facility (Bhatt 2012).

According to Zairani and Zaimah (2013), there are several considerations for the bank to approve the financing request. Firstly, the clients need to provide reliable accounts on the financial activity, since the company’s financial statement is the principal factor that banks take into consideration. Secondly, the main purpose of the facility application as the consideration when deciding the approval. Thirdly, banks will consider businesses that are viable and can generate income in the long-term and appear likely to be successful in the market. Fourthly, the bank requires collateral to offset the risk of potential defaults. Lastly, the sound management structure, efficiency, profit potentiality, market strength, performance, and geographical location determinants.

Furthermore, Islamic banking has been developing significantly in Indonesia since the first inception in 1991. As of 30 April 2020, there are 14 Islamic banks, 20 Islamic windows and 163 Islamic rural banks (Financial Service Authority, April 2020). The total assets are recorded of IDR 534 trillion (eqv. USD 36.8 billion) with the total deposits of IDR 424 trillion (eqv. USD 29.2 billion). It is represented 6.07% of the national banking size in the country.

One of the important segments as a backbone in developing Islamic banking in Indonesia is corporate and commercial banking segment. From the total financing exposure of Islamic banks and Islamic windows of IDR 332 trillion (eqv. USD 22 billion) as of 30 April 2020, 33.49% are in the corporate and commercial portfolio. It is very interesting to explore what are the consideration for Islamic banks in providing financing approval of corporate and commercial clients.

There are several previous studies related to creditworthiness in the banking context (Savvides 2011; Zairani and Zaimah 2013; Osondu and Obike 2015; Grassa et al. 2020). However, to the best of author’s knowledge, there is no specific study with the case of corporate and commercial segment in Islamic banking. This study aims to fill this gap by using Indonesia as case study.

1.2 Problems Statement

Despite the vast development of Islamic banking in Indonesia as mentioned in the introduction, the trend of exposure in corporate and commercial segment is decreasing from 37.14% in April 2019 to 33.49% in April 2020 (Financial Service Authority, April 2020). Apart from shifting to consumer and retail segment, the other main reason is the decreasing level of creditworthiness in corporate and commercial segment due to the severe impact of covid-19 in Indonesia. As consequences, identifying creditworthiness criterions and approval process is crucial to understand the current strategy of Islamic banks for this segment.

Several previous studies mentioned that the relationship between creditworthiness and access to finance is significant to the business sector (Savvides 2011; Zairani and
1.3 Research Questions

Based on the above problem statement, there are 2 (two) questions can be raised as follows:

1) Does Islamic bank have a specific creditworthiness criterions and approval factors in providing financing facility to corporate and commercial clients in Islamic bank?
2) What are the processes of financing approval in Islamic bank for corporate and commercial clients?

1.4 Research Objectives

In general, this study purposes to identify the creditworthiness consideration and financing approval process for corporate and commercial clients in Islamic banking. Specifically, this study aims to achieve the following objectives:

1) To identify the creditworthiness criterions and approval factors in providing financing facility to corporate and commercial clients in Islamic bank.
2) To explore the financing approval process in the Islamic bank corporate and commercial clients.

1.5 Scope and Limitations

The study focuses to explore the perspectives and experiences of Islamic bankers in creditworthiness criterions and considerations as well as financing approval process. This study uses the sample from 3 (three) Islamic bank officers only in Indonesia. A qualitative approach will be used via in-depth and semi-structure interview platform.

2 Literature Review

2.1 Islamic Banking

Islamic banking is different from the conventional banking as it is interest free and operates under different principles and they have different risk profiles (Salman and
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Nawaz 2018). All products in Islamic bank have to comply with Shari’a requirement and approved by Shari’a committee member (Ayub 2019). Grassa et al. (2020) mentioned that the basic rules to govern the of Islamic banks’ operations are that it is forbidden to conduct interest-based (riba) transactions, not allowed to participate in uncertainty (gharar) or speculation, and proscribed from sinful financing and socially irresponsible activities. Unlike conventional banks that focus on debt-based and transfer of risk, Islamic banks adhere to profit risk-sharing and use tangible assets as collaterals in financial transactions (Radzi and Lonik 2016).

2.2 Credit Evaluation and Creditworthiness

Credit evaluation by financial institutions is used to measure the ability of client to repay their proposed credit facility. Credit risk evaluation aims to classify the clients with ‘good credit’ with proven repayment capacity and those with ‘bad credit’ with a high probability of default, where this is defined as creditworthiness (Genriha and Voronova 2012 and Bai et al. 2019). The key term of creditworthiness is “worthy”, whereby if the banks are confident that the potential clients will honor their obligations in timely manner, then the clients can be considered to be deemed creditworthy (Osondu and Obike 2015).

According to Nationalbank (2004), the client’s creditworthiness can be assessed through credit assessment criterions and measured by credit ratings. This is often assessed by the 5Cs elements namely Character, Capacity, Collateral, Capital and Condition (Moti et al. 2012). Credit risk can also be determined through cash flow projections based on proper financial model for corporate and commercial exposure (Savvides 2011).

Feschijan (2008) suggested that the need for checking the creditworthiness of companies arises when establishing credit relationship for the first time, special reasons occur, and regular monitoring. It is also suggested that creditworthiness depends on several major factors namely the borrower’s efficiency, reputation and key personal, capacity for profit making, the value of assets, capital, ability to repay, the state of the economic situation, profitability, and guarantee (Feschijan 2008 and Kousayri 2020).

Thus, it is important to ensure that the internal guidelines contain clear rule and direction in defining and measuring the creditworthiness criterions and credit evaluation process.

2.3 Previous Studies and Literature Gap

Several previous studies were conducted to measure the creditworthiness criterions and approval process in the banking sector. With regards to the creditworthiness criterions, Zairani and Zaimah (2013) indicated that there are nine factors identified as criteria associated with obtaining credit facilities from the banks in Malaysia namely good business record, viable industries and businesses, good and continuous relationships with banks, experiences in the sector, financial statement with convincing cash flow, collateral, and convincing project proposal. The study conducted interviews from officials of five banks in Malaysia. Meanwhile, Wasiuzzaman et al. (2020) reveals that the relationship between creditworthiness and access to finance is significant for both enterprises with and without links to large firms in Malaysia. The study employed 456 SMEs from
the manufacturing industry located in the Selangor and the Federal Territory of Kuala Lumpur areas are selected as the population. The collateral and condition factors are the most important factors for banks to provide the financing facility.

With regards to the credit risk control and selection criterions, Grassa et al. (2020) found that when compared to banks with lower credit rating scores, banks with high credit rating scores are likely to be more transparent when it comes to risk disclosure level. This study used samples of Islamic banks in twelve countries namely Bahrain, Egypt, Jordan, Saudi Arabia, Kuwait, Malaysia, Pakistan, Qatar, Tunisia, Turkey, UAE, and Oman. Moreover, Campanella et al. (2020) explained that large banks improved the process for assessing creditworthiness, while smaller banks worsened their own approach in the allocation of credits in Italy. The banks have the flexibility to select non-standardized measures in the decision-making process, however, the study finds that these criterions do not necessarily reduce the level of Non-Performing Loans (NPLs).

Credit risk assessment is the crucial aspect and the core of corporate financing as discussed by Savvides (2011). The quality of assessment managed by the credit risk officers will pave the successful implementation of the credit facility. Proper appraisal and evaluation of the risks during the credit risk assessment has strong impact to the quality of the portfolio during the tenure of facility. It provides the ability of the bank to recover in the case of default. Creditworthiness can be properly assessed is through the analysis of cash flow projection based on sound financial model and proper understanding of marketing and competitiveness aspects in business.

From the banking perspective, Alqallaf and Alareeni (2018) revealed the importance and relevance of Integrated Reporting (IR) practices with regards to managing the portfolio in the banking sector by considering a sample of 12 listed banks in Bahrain Bourse. Moreover, Ali et al. (2018) implied that with regards to the macroeconomic condition, oil prices, GDP and inflation were the most significant criterions to the Islamic bank profitability in Brunei by using Bank Islam Brunei Darussalam (BIBD) profitability from 2012 to 2016.

The previous studies provided the analysis to creditworthiness criterions and credit assessment process in the banking context. However, there were no specific studies in the context of Islamic banking, particularly in the case of corporate and commercial segment. This study, therefore, aims to add the literature by identifying creditworthiness criterions and approval process in the context of Islamic banking by using several Islamic bank officers in Indonesia as primary sources of evidence.

3 Methodology

This study uses qualitative approach to identify creditworthiness criterions and financing approval process in corporate and commercial segment of Islamic banks. The study employs in-depth and semi-structured interviews method through the available online tool. The aim is to explore the feedbacks from Islamic bank officers regarding their experiences, values, and various other aspects. The study develops a set of predetermined questions with other questions may be emerged from the dialogues with the interviewees (DiCicco-Bloom et al. 2006; Creswell 2009 and Showkat and Parveen 2017).

The study employs convenience and non-probability sampling for the interview purposes (Etikan and Alkassim 2016). Out of fourteen Islamic banks in Indonesia,
study selects three Islamic bank officers from the three different banks. The respondents represent the three positions as front office and investment arms of Islamic banks in the corporate and commercial segment namely Relationship Manager, Financing Analyst Head, and Business Manager. The interviews were conducted in Indonesian language via Zoom meeting on 15–17 September 2020.

The focus of the interview is as follows:

– The creditworthiness criterions and 5Cs elements;
– Internal financing approval process;
– Covenants and conditions from Islamic bank; and
– The impact of covid-19 and current challenges in managing corporate and commercial segment.

The list of questions is available in the Appendix 1.

4 Findings and Discussion

Following are the findings in this study and the detail of the interviews can be found in Appendix 2.

4.1 Profile of Respondents

| Respondents | B01 | B02 | B03 |
|-------------|-----|-----|-----|
| Gender      | Male | Male | Male |
| Education background | Master degree in islamic economics | Bachelor in industrial engineering | Bachelor in psychology |
| Age         | 35 years old | 37 years old | 34 years old |
| Years of experience | 6.5 years | 12 years | 12 years |
| Current position | Relationship manager (corporate and syndication) | Financing analyst head | Business manager of surabaya main branch |
| Current bank | Bank Muamalat Indonesia | Panin Dubai Shariah Bank | BNI Syariah |

The study uses coding of B01, B02, and B03 as the three selected respondents from different banks. Table 1 shows that the profile of respondents is diverse from Relationship Manager, Financing Analyst Head, and Business Manager. As it is shown, the respondents have strong background and experiences in managing the corporate and commercial clients.
4.2 Findings from the Interviews

Required Qualification for Corporate and Commercial Islamic Bank Officer
The study finds that there are two qualification sets to become the professional Islamic banking officer in the corporate and commercial segment namely soft skill and hard skill. The basic criterion of soft skill is the integrity as mentioned by B02 respondent. B01 respondent stated passion, awareness, communication, problem mapping and simplification, and solution provider. Meanwhile, B03 respondent advised the professional looks and manner are important since the segments are dealing with the corporations.

In terms of hard skills, B01 and B03 respondents mentioned regarding the strong analytical thinking in the quantitative aspects such as financial statement analysis. B03 respondent also implied the need of advance understanding of Islamic banking and the ability to explain Islamic corporate banking products vis-à-vis the conventional products to the external and internal parties in comprehensive manner.

Guideline for Creditworthiness Criterions
B01 respondent stated regarding the character and capacity since business is about trust and commitment. B02 respondent highlighted the need and the repayment ability. B02 and B03 respondents also emphasized the background checking of the principal owners of the clients and how strong they can provide the support in the worst-case scenario.

Furthermore, B03 respondent advised that his bank has its own standard guideline for creditworthiness criterions vis-à-vis the market norms. It provides clear direction in managing the corporate and commercial financing such as financial ratio, collateral value, and track records.

The Importance of 5Cs Elements
The study finds that all 5Cs elements are important as the creditworthiness criterions. Both B01 and B02 respondents highlighted that the most important aspect is currently the fixed asset collateral. B01 respondent mentioned the collateral value should be between 50%–70% of the total facility amount, while B02 respondent stated the minimum is 70% of the amount. B01 respondent suggested the concept of Islamic bank as asset-backed financing is also represented with the fixed asset collateral.

However, B03 respondent expressed that capacity is the most important element. He explained that his bank will not consider the client who does not have capacity even though he has good character. On the other side, if the clients have strong capacity but have limited fix asset collateral, then there is room for negotiation. With regards to character, B03 respondent described that the experience Islamic banker will use his/her intuition to define the client’s character.

Internal Procedures and Processes for the Financing Approval Process
There is a typical internal process based on the feedbacks from the interviews. There are two functions in the front office namely Relationship Manager as the marketing officer and client relationship management as well as Financing analyst for credit review assessment. Relationship Manager is responsible for data collection and client visit. Financing analyst will prepare the internal proposal to be submitted to the Risk Management function for review. B02 respondent added the proposal will also be reviewed by Financing Risk Analyst Division and Compliance Division.
Moreover, B03 respondent described that business unit is proactively hunting the clients in the market for on boarding process. B03 respondent also mentioned that his bank has preliminary discussion step for in principal clearance with the output is the indicative terms and conditions to be submitted and reviewed by the client before processing the internal approval.

The maximum financing amount is up to legal financing limit with some buffer between 70% to 90%. The final approval will be processed to the authorized party in the bank which is Board of Directors (BoD). B01 respondent mentioned that the process can go up to the Board of Commissioners (BoC) up to certain limit in his bank. If the proposal is approved, the next step is the bank will provide the Offer Letter for further process.

In terms of timing, B01 respondent mentioned that the internal process requires 2 to 4 months. B02 respondent said that the approval requires 1 month of process where the valuation usually takes 2 weeks. Meanwhile, B03 respondent said that it will take 1–2 months to process for the approval.

Challenges During the Approval Process from Credit Risk Perspective

The responses from the respondents in terms of challenges during approval process are vary. B01 respondent mentioned regarding different understanding, assumption, and appetite between internal stakeholders of the bank in the client business. He also highlighted on the limited comparison in client business, particularly for the client with unique business.

B02 respondent revealed that the challenges come post the approval especially to ensure that the approved facility is utilized as per the original purpose. Monitoring is the key aspect in this regard to ensure the facility can be realized as per initial projection.

B03 respondent suggested that the main challenge is how to convince internally that the business unit conduct comprehensive risk mitigation to the client since it faced the overwhelming risks from all aspect of the client business. He recommended that to get back to the basic principle of credit in terms of business aspect, character, and collateral. However, this is not an easy task to find such client profile in the current market.

Covenants and Conditions in Providing the Approval of Financing

The study finds that the same requirement and covenant to use CASA (current account and saving account) products and cash management of their banks as the main transaction account for the client’s business. There is also a standard financial covenant such as current ratio and debt to equity ratio. B03 respondent mentioned other terms such as to become the first option if the client requires additional financing and no new investment and change in shareholders without the bank’s prior consent. B02 respondent highlighted that the covenants are designed to ensure that the repayment to the bank is conducted in timely manner.

The Impact of Covid-19 and the Current Challenges in Managing the Corporate and Commercial Segment of Islamic Bank

Covid-19 pandemic has impacted the client’s business and its ability to repay the banks. To cater this challenge, the strategy is to conduct relaxation, reprofiling, and restructuring of the client’s facilities as per the guideline imposed by the Indonesia’s Financial Service Authority (OJK).
OJK has issued credit stimulus policies for Indonesian banks, relaxing credit scoring requirements and providing special treatment for loan restructuring (Herbert Smith Freehills 2020). The policy is available to commercial banks, Islamic banks, rural credit banks (BPR), Islamic rural credit banks (BPRS) and foreign bank branch offices in Indonesia. COVID-19 Credit Stimulus Policy issued through OJK Regulation No.11/POJK.03/2020 dated 16 March 2020 is valid until 31 March 2021. All clients of Indonesian banks are eligible for this credit stimulus as long as the client’s business condition has been affected by the COVID-19 pandemic based on the bank’s internal assessment.

In this regard, B01 respondent implied that covid-19 has impacted the decline in client’s revenues. However, some clients who are refocusing to enhance the new business line needed during this time, somehow, can cope with this challenge. The bank provided relaxation by deferring the repayment schedule and some adjustment in the covenants. The other challenge is moral hazard of the clients and the issue of corporate governance. B01 respondent also added that 60% of the business of the bank are in the corporate client.

B02 respondent informed that his bank anticipated the covid-19 impact by processing the restructuring particularly to the business sector that is directly impacted. The good thing is that the regulator is very supportive in this regard by providing stimulus for restructuring and relaxation of payment. His bank treats the issue on case by case basis with the maximum is up to one year till March 2021. He also advised that non covid-19 aspect is directly impacted by covid-19 condition.

Furthermore, B03 respondent explained that covid-19 has impacted the bank if compared to other peers, because this is the first time his bank is experiencing the decline in revenue and profit since the spin-off. Although the non-performing financing ratio is still manageable, however, the ratio of financing at risk is increasing significantly. For corporate segment, the bank is conducting reprofiling of short-term financing facility by easing the repayment schedule. For some of big investment, restructuring is the alternative solution provided.

In terms of non covid-19 impact, B03 respondent advised that the corporate segment is actually sound. With the support and incorporation from the parent bank, the bank has been refocusing the corporate segment into more on standing corporation clients since our cost of financing is considered attractive due to the CASA is almost 60%.

5 Conclusion and Suggestion for Further Studies

The study concludes that the 5Cs elements are all important and considered by the three Islamic banks in providing the approval of financing facility to the corporate and commercial segment. Specifically, proper fixed asset collateral and sound capacity of the clients are the two most important aspects.

There is a typical internal approval process based on the feedbacks with Relationship Manager and Financing Analyst as the front office. The new proposal is also reviewed by the Risk Management Division before processing the final approval to the Board of Directors. The challenges during the approval process from credit risk perspective are vary. The respondents highlight the importance of financial covenants and the requirement to use CASA products and cash management of their banks. The internal approval process is vary between 1 to 4 months.
The study also finds that covid-19 pandemic has impacted the client’s business and its ability to repay the banks. The solution presented is by conducting relaxation, reprofiling, and restructuring of the client’s facilities as per guideline from regulator.

This study has limitation since it uses the sample from 3 (three) Islamic bank officers only. Further studies can consider more samples from other Islamic banks, so that it will get broader perspective and feedbacks in terms of creditworthiness criterions form other Islamic banks in Indonesia. It will also be interesting if further studies can analyze the feedback from the corporate and commercial clients with regards to the Islamic financing facility.

Appendix 1. List of Questions

1. What are the profiles of respondents in terms of the experiences in managing corporate and commercial segment in Islamic bank?
2. What are the classifications required to become Islamic bank officer in corporate and commercial segment?
3. What are the guideline and criterions of creditworthiness classification during the financing assessment process?
4. Are 5Cs elements be considered by the Islamic bank in considering the new application from the clients? What are the most important elements in 5Cs?
5. What are the internal procedures and processes for the financing approval process? How long is the process?
6. What are the challenges during the approval process from credit risk perspective?
7. What are the covenants and conditions in providing the approval of financing request from clients?
8. What are the impact of covid-19 and current challenges in managing the corporate and commercial segment of Islamic bank?

Appendix 2. Interviews Result

1. What are the Profiles of Respondents in Terms of the Experiences in Managing Corporate and Commercial Segment in Islamic Bank?
   B01: “35 years old Corporate Relationship Manager with 6.5 years of experience in Syndication and Corporate Banking segment of Islamic banking. Holding master degree in Islamic Economics and highly experience in managing various portfolio sectors from oil and gas, mini hydro, LPG power plants, aviation, fuel trading, and currently focusing state owned companies in infrastructure that focus in airport management and toll road”.
   B02: “Islamic Banker with 12 years of Experience in Corporate and Commercial Banking. The First 7 years Was with Other Islamic Bank and 5 years with the Current Bank. Current Position is Financing Analyst Head. 37 years Old and Holding bachelor’s Degree in Industrial Engineering.”
   B03: “34 years old with 12 years’ experience in Islamic banking with the first 7 years as the Corporate Account Manager in my previous bank. I then joined my current
bank as Senior Account Manager then promoted as Team Leader. Currently as the Business Manager in Surabaya Main Branch with the main role to supervise all the financing business. Holding the bachelor degree in Psychology from Gajah Mada University.”

2. **What are the Classifications Required to Become Islamic Bank Officer in Corporate and Commercial Segment?**

**B01:** “The first is to have strong passion and awareness in business for account engagement. Quantitative skills are obviously needed and can be developed during the time. Other skills are communication, problem mapping and simplification, and able to provide solution.”

**B02:** “The basic criterion is integrity because Islamic banker is always assumed to have a sound integrity in the market. In particular, there is always temptation to do the harmful in corporate and commercial segment when dealing with external.”

**B03:** “The difference between the retail banking with corporate and commercial segment is the counterpart, and the clients are usually demanding our capacity to deeply understand the segment. The officer must have an advance understanding of Islamic banking and the ability to explain Islamic corporate banking to the external and internal parties in comprehensive manner. Strong analytical thinking in dealing with annual and financial reports as well as horizontal and vertical analysis. Professional looks and manner are also important as we are dealing with high level people.”

3. **What are the Guideline and Criterions of Creditworthiness Classification During the Financing Assessment Process?**

**B01:** “5Cs are the standard where character is very important. Capacity to handle the project (qualitative aspect) is also another vital aspect. Business is about trust and thus commitment and integrity are vital.”

**B02:** “Creditworthiness is Assessed Based on Relevant Regulation. We Are Measuring that the Client Needs the Financing Facility and Has the Ability to Repay the Bank. We Have the Tools to Determine Whether the Clients Have the “need” and “ability to Repay”.

We are also focusing on background checking in terms of the principal owner of the clients and how strong the goodwill of the ultimate owner. In the worst case scenario, how far the owner can back up the client. We also checked the track record to the business community and from other banks.”

**B03:** “Yes, we have the guideline namely *Buku Panduan Pembiayaan* (Financing Guideline Book). It provides clear direction in managing the corporate and commercial financing. Firstly, we have our own standard in the financial ratio vis-à-vis the market standard. For example, the standard of current ratio of 100% and debt to equity ratio of 2x. Secondly, we look at the growth ratio and the bottom line has to be profit. Thirdly, we are also very strict in collateral value for commercial segment, but we have some adjustment on corporate segment on case by case basis. Lastly, the owner and company track records are the vital aspect.

4. **Are 5Cs Elements be Considered by the Islamic Bank in Considering the New Application from the Clients? What are the Most Important Elements in 5Cs?**

**B01:** “Yes, 5Cs are important and all aspects are urgently considered. However, currently one of the main considerations is fixed asset collateral with the market
value of 50%–70% from the total financing offered for corporate segment and 125% for commercial segment. New business segment is more on State Owned Companies (SOEs) portfolio like airport management, toll road, and energy except IPP.”

B02: “5Cs are usually employed in all banks and all factors are important. However, we are currently focusing on fixed asset collateral due to asset-based financing. Financing to value of fixed asset collateral is minimum at 70%.”

B03: “5Cs are good for the guidance in assessing the client. Personally, the most important aspect is Capacity particularly during this pandemic period. Capacity in terms of people and business whether the clients are able to repay the financing facility. If the clients have good character but they do not have capacity, we are not considering their proposal. On the other side, if the clients do have the capacity, but have limited fix asset collateral then we have room for negotiation. For the experience banker, however, there is another aspect called intuition particularly in dealing with the character.”

5. **What are the Internal Procedures and Processes for the Financing Approval Process? How Long is the Process?**

B01: “The process requires 2–4 months of internal process. Once the request comes, the proposal will be assessed by Financing Analyst for 4-eyes control purpose. The next stage is that the proposal will be assessed by Risk Management before going to the final approval process to the Board of Directors and Board of Commissioners. The maximum amount is 70% from the bank’s legal financing limit.”

B02: “Standard documentation of legality aspect, financial statements, and collateral. Relationship Managers are responsible for data collection and conducting business visit to the client. Based on the visit, RMs then prepared the internal report regarding all aspects of the clients. After that, the process is coming to our part as Financing Analyst and then we prepare the internal proposal. If needed, the Financing Analyst also conduct the site visit. From our end, the proposal is processed to 3 (three) different divisions namely Financing Risk Analyst Division, Risk Management Division, and Compliance Division. Furthermore, these divisions provide the review memo for further submission to the Financing Committee for internal approval. The committee consists of several layers up to the Board of Directors. We apply 90% of legal financing limit as the maximum amount that can be processed. The approval requires 1 month of process where the valuation usually takes 2 weeks within this period.”

B03: For corporate and commercial clients, we are proactively hunting the clients in the market as first step and we call it as on boarding process. We consider that the marketing aspect is successful whenever the new client that we approached submits the official proposal to us. Second step is data collection from the client and we are mainly focusing on the business and budget plan as well as the financial statement. We are then preliminary discussed in our division for in principal clearance. After this, we provide the indicative terms and conditions to the client. If the client is fine with this, then we process the credit review and assessment to the Risk Management Division. After the green light from this division, we are processing for final approval to our Board of Directors since all corporate and commercial proposals are approved only by the board. After the approval, then we provide with the Offer Letter and subsequently with the signing of financing agreement and disbursement. Normally, it will take 1–2 months to process for the approval.
6. **What are the Challenges During the Approval Process from Credit Risk Perspective?**
   **B01:** “The first challenge is there is a different understanding from internal stakeholders in the client business. Site visit is often jointly conducted to bridge the knowledge. There are often different assumptions between RM, Financing Analyst, and Risk Management Department, where the last two parties usually adopt conservative approach. The next aspect is regarding limited comparison in the client business particularly for the client with unique business. The other challenge is the appetite between business unit, Risk Management, and BoD are sometimes different.”
   **B02:** “From the credit risk perspective, we need to ensure that the approved facility is utilized as per the original purpose. If we provide the working capital facility, we need to ensure that the client does not use this for new investment. It will affect the cashflow ability of the client. Monitoring is the key aspect in this regard to ensure the facility can be realized as per initial projection.”
   **B03:** “The main problem during this pandemic is that we faced an overwhelming risk from all aspect of the client business. We faced an increasing risk profile of our clients. Therefore, the challenge is how we convince internally that we conduct comprehensive risk mitigation to our client. The guidance from our board during this period is to get back to the basic principle of credit so long as the client business is sound, have a good character, and equipped by sound collateral. However, this is not an easy task to find such client profile in the current market.”

7. **What are the Covenants and Conditions in Providing the Approval of Financing Request from Clients?**
   **B01:** “Standard financial covenant in current ratio and debt service coverage ratio. Fixed Asset collateral. Deposit transaction in the bank is other challenge to be implemented due to the clients often contest this term.”
   **B02:** “Pretty much standard covenant is considered. From our end and for the purpose of monitoring, we need to ensure that the bank is protected through the covenant so that the client can repay the bank in timely manner. As an example, cash flow payment and proceed are managed through our bank account. We are monitoring the use of financing facility is directly transferred to the suppliers of the Client to avoid side streaming.”
   **B03:** “We have tailor made terms and conditions depending on the type of business and the client profile. However, we are normally requesting the clients to use cash management products in our bank as sole banking partner. Other term is that we have the first option if the client requires additional financing. We also request the client not to perform new investment and change in shareholders without our prior consent. Waiver of the covenants is usually happening usually for the corporate action and change in the management structure.”

8. **What are the Impact of Covid-19 and the Current Challenges in Managing the Corporate and Commercial Segment of Islamic Bank?**
   **B01:** “Due to covid-19, the client’s revenues are declining. However, some clients who are shifting to enhance the new business line can cope with this challenge. As an example, I have a client in paper and printing business who are refocusing to sale the tissue and packaging are somehow faced an increasing trend. Covid-19 has also impacted the decline in production of the client, but at the same time the
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selling, general and administrative (SGA) expense is still the same. Thus, there is a dilemma between maintaining the salary and obligation to its employees and to meet the bank’s repayment obligation. As solution, we often offer relaxation by deferring the repayment schedule and some adjustment of the covenants such as sinking fund (reserve amount). The other challenge is moral hazard of the clients and the issue of corporate governance.

The interviewee also added that 60% of the business of the bank are in the corporate client.”

B02: “Due to covid-19 impact, most of the clients proposed for restructuring particularly to the business sector that is directly impacted. Property sector is the example. All parties are currently facing significant delay in receivables payment. The good thing is that the regulator is very supportive in this regard by providing stimulus for restructuring and relaxation of payment. We treat the issue on case by case basis with the maximum is up to March 2021 (1 year) as per regulator’s stimulus. Non covid-19 aspect is directly impacted by covid-19 condition.”

B03: “Covid-19 has impacted our bank if compared to other peers, because this is the first time we are experiencing the decline in revenue and profit since the spin-off of our bank. 60% of our business is in consumer banking and covid-19 has hit our business. Although the non-performing financing ratio is still manageable, however, the ratio of financing at risk is increasing significantly. Our revenue and net profit are corrected due to restructuring process. For corporate segment, we are focusing on the state-owned companies and we are conducting reprofiling of our client facility by easing the repayment schedule during this period. We are providing the extension of short-term financing through this reprofiling exercise. For some of big investment, restructuring is unavoidable.

Furthermore, in terms of non covid-19 impact, our corporate segment is actually sound. With the support and incorporation from our parent bank, we are now refocusing our corporate segment into more on big corporation clients since our cost of financing is considered attractive due to the CASA (current account and saving account) is almost 60%.”

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