



19th International Conference Enterprise and Competitive Environment 2016, ECE 2016, 10–11
March 2016, Brno, Czech Republic

Social lending and its risks

Martina Pokorná^{a,*}, Miroslav Sponer^a

^a*Masaryk University, Faculty of Economics and Administration, Department of Finance, Lipová 41a, 603 00 Brno, Czech Republic*

Abstract

Czech companies discover alternative non-banking financing of their business. Social lending known as peer to peer (P2P) financing has started to appear on the Czech market. P2P lending is a new platform of financial transactions that bypasses traditional intermediaries by directly connecting borrower and lenders. But there is an information asymmetry between lenders and borrowers to which online P2P lending platforms have to face. As many loans are not secured by collateral, the assessment of the borrower's creditworthiness is very important. The aim of this article is to define risks of investments to P2P loans and propose the elimination of these risks. We went through studies focused on default of corporate entities which were done in different countries and selected some of them. We have chosen these studies because their research is focused not only on financial indicators assessment but also on non-financial indicators assessment and use econometric models to measure probability of default. These studies also confirmed well known basic relations which should be taken into consideration by lenders – higher profitability, higher liquidity and higher volume of assets means lower risk of default, while higher indebtedness and higher leverage means higher risk of default.

© 2016 The Authors. Published by Elsevier Ltd. This is an open access article under the CC BY-NC-ND license (<http://creativecommons.org/licenses/by-nc-nd/4.0/>).

Peer-review under responsibility of the organizing committee of ECE 2016

Keywords: peer-to-peer financing; peer-to-peer lending platforms, risk; corporate entities; risk assessment

World trend on lending markets is so called peer-to-peer platforms in several last years. P2P lending platforms bring to lending market a speed and efficiency thanks to rapid progress of modern IT technologies and easy accessibility of data and their processing. Platforms create their marketing image as progressive, effective and low cost alternatives of traditional financing.

First P2P lending platforms were established in the United Kingdom and in the United States. Their concept is to connect directly small investors with borrowers. There are also several P2P lending platforms in Czech Republic.

* Corresponding author.

E-mail address: m.pokec@seznam.cz

Seemingly attractive offer of progressive financial products should be critically considered. What are the differences in reality between services offered by a bank and P2P lending platforms' offers, what are advantages and risks.

Although P2P lending platforms are relatively new, many researches have studied the P2P lending market. Most of them have focused on finding factors that affect the probability of funding success and default rates in P2P lending. Avery et al. (2004) showed that a borrower's financial strength is crucial in ability to obtain secured and unsecured credit from financial institutions. Similarly, a borrower's financial strength plays an important role in the P2P lending market (Iyer et al. 2009, Herzenstein et al. 2008).

The aim of this article is to define risks of investments to P2P loans and propose the elimination of these risks. First part is focused on the benefits and risks of P2P lending. We introduce what P2P lending is, what is its progress and what are the advantages and disadvantages of online lending. We describe how the credit risk is evaluated by different investors in second part. The possibilities of credit risk elimination are proposed in the third part.

1. The benefits and risks of P2P lending platforms

P2P lending is a type of financial transactions concluded directly between individuals or between individuals and a company without the intermediation of a traditional financial institution. It has a short history but it has rapidly grown in last years. P2P lending platforms offer to borrower lower interest rates than banks usually offer. They are more flexible, more quick and transparent.

The first online P2P lending company was Zopa, launched in United Kingdom in 2005, next platforms were Prosper and Lending Club, established in the United States in 2006. P2P online exchanges are growing as alternative platforms to traditional savings and investments. Zopa is the UK's largest peer-to-peer lending service. They have lent £1.23 billion to over 150,000 people since 2005[†]. Prosper arranged loans in amount over 5 billion USD[‡]. Lending Club arranged business loans in amount over 11 billion USD at the end of 2015[§] and successfully entered into the stock exchange. Also British government invests through P2P lending platforms.

There are also several P2P lending platforms in Czech Republic. Intereson.cz was established in 2008 as the first P2P lending platform in Czech Republic. It is a part of Ferratum Group. Next P2P lending platform were Bankerat operating from 2010, pujcmefirme.cz (2014), Kreditní klub (2014) and Symcredit.cz operating from 2015. But only two of them – pujcmefirme.cz and Symcredit provide loans to corporate entities.

There are many advantages of P2P lending compared to loans transactions made through traditional lending institutions. The main advantage of P2P lending is that borrower can get a loan at a lower rate without collateral, while lender can obtain a higher return on his investments (Magee 2011). Despite the fact that high returns on investment from microfinance has been questioned, P2P lending has attracted a huge entry of investors who have been discouraged by the stock market returns and lower interest rates offered by banks (Brennan 2009). The Wall Street Journal has reported that the leading P2P platforms have provided investors with 10% or higher annual returns at a time of historically low interest rates (Haewon et al. 2012). The next big advantage of P2P lending platforms are transparent, flexible conditions, quick decisions and lower costs because operational costs of P2P lending platforms are not so administrative and hierarchic overloaded.

On the other hand, no investment is without risk, nor the investment to P2P loan is. In the online P2P lending market, the traditional role of credit risk assessment is left to individual lenders rather than financial institutions. Thus, there is possibility of misrepresentation for borrowers in terms of their creditworthiness (Haewon et al. 2012). Most of the requested loans are from borrowers which are not able to get a loan in a bank. If a borrower does not pay the loan back than is necessary to prosecute a claim with risk that the full amount of a loan will not be recover.

P2P loans are regulated only as so called "Providers of small sized payment services" in the Czech Republic. Because of that P2P lending platforms do not have an obligation to contribute to the "Fund of deposit's insurance" and investors do not have their investments insured.

[†] <https://zopa.com>

[‡] <https://prosper.com>

[§] <https://lendingclub.com>

Download English Version:

<https://daneshyari.com/en/article/1107249>

Download Persian Version:

<https://daneshyari.com/article/1107249>

[Daneshyari.com](https://daneshyari.com)