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# The Relationship of International Loans to Credit Wall (Worthiness): A Review

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***Abstract:*** *The creditworthiness analysis is based on preliminary research into the factors and the prerequisites that can influence the repayment of the credit in due course. The credit analysis is defined as a process of establishing the current creditworthiness of loan applicants and forecasting the trends in its development. Top priority goals and stages in the bank credit analysis are determined. Credit analysis is the method by which one calculates the creditworthiness of a business or organization. In other words, It is the evaluation of the ability of a company to honor its financial obligations. The audited financial statements of a large company might be analyzed when it issues or has issued bonds. Creditworthiness is how a lender determines that you will default on your debt obligations, or how worthy you are to receive new credit. Your creditworthiness is what creditors look at before they approve any new credit to you. Creditworthiness is determined by several factors including your repayment history and credit score. There are several ways you can improve your credit score to establish creditworthiness. The most obvious way is to pay your bills on time. Make sure you get current on any late payments or set up payment plans to pay off past due debt. Pay more than the minimum monthly payment to pay down debt faster and reduce the assessment of late fees. The principal aim, in this paper, is to investigate the factors that are considered in evaluating the creditworthiness of borrowers and lender countries by providing sufficient information about the credit undertaking and its risk level and the adoption of adequate measures for protection against credit risk.*

***Keywords:*** *International Loans, Creditworthiness, IMF, World Bank, Credit, Financial Stability, Global Financial Crisis.*

## Introduction

As a term, creditworthiness can be defined as the size of external loans that the state is able to obtain, and then repay them by the same agreed period, and through the financial surpluses that come from directing these loans to the productive investment fields leading to the creation of a new and diversified production structure and then increasing Exports on imports and then obtaining financial surpluses that enable the debtor state to repay the loan and the resulting benefits. In addition, Creditworthiness is an estimate of the experience of some specialized commercial agencies to estimate the validity or eligibility of a person to obtain a loan or a company wall or even a state to obtain loans, and in that it studies the financial capabilities of the company or the person or the state and the extent of their credit on the loan

The credit rating aims to determine the customer's merit and ability to obtain loans and financing, as these ratings examine the customer's suitability to pay those loans.

Furthermore, All countries strive to raise the level of their creditworthiness in order to obtain a high credit rating, to demonstrate the extent of their financial suitability and their ability to fulfill their obligations to others, as maintaining a high level of creditworthiness is a source of guarantee for the state and an important element in attracting capital that is focused in the form of investments that enhance Of economic growth and its continuation in the country. The client may request a rating agency to evaluate its credit score so that it will be a bond before going to financial institutions to obtain credit facilities - loans - bonds - bonds - bonds and other financing and facilities. It is indicated that the term customer means individuals, companies or countries.

A country may borrow abroad to diversify its currency denominations of debt or because its own country's debt markets are not deep enough to meet their borrowing needs. In the case of third-world countries, borrowing from international organizations like the World Bank is an essential option, as they can provide attractive lending rates and flexible repayment schedules. The World Bank, in conjunction with the International Monetary Fund (IMF) and Bank for International Settlements (BIS), gathers short-term foreign debt data from the Quarterly External Debt Statistics (QEDS) database. Long-term external debt data compilation is also collectively accomplished by the World Bank, individual countries that carry foreign debt, and multilateral banks and official lending agencies in major creditor countries.

One measurement of foreign debt burden is the amount of foreign exchange reserves relative to outstanding foreign debt. Foreign exchange reserves consist of foreign currencies held by a central monetary authority. They include banknotes, bank deposits, bonds, Treasury bill and other government securities denominated in other currencies. The U.S. dollar dominates most foreign exchange reserves of debtor countries, but the euro, British pound, Japanese yen and Chinese Yuan are also prominent in these reserves. Foreign debt as a percent of reserves indicates the level of credit worthiness of a country. Also tracked are foreign debt to exports (as many of the debtor nations rely on exports of commodities and goods to service loans) and foreign debt to gross domestic product.

## Literature Review

### China’s overseas lending

**Horn, S., Reinhart, C. M., & Trebesch, C. (2019)**

The purpose of this paper is to establish the size, destination, and characteristics of China’s overseas lending. The methods has based on identifying three key distinguishing features. First, almost all of China’s lending and investment abroad is official. As a result, the standard “push” and “pull” drivers of private cross-border flows do not play the same role in this case. Second, the documentation of China’s capital exports is (at best) opaque. China does not report on its official lending and there is no comprehensive standardized data on Chinese overseas debt stocks and flows. Third, the type of flows is tailored by recipient. Advanced and higher middle-income countries tend to receive portfolio debt flows, via sovereign bond purchases of the People’s Bank of China. Lower income developing economies mostly receive direct loans from China’s state-owned banks, often at market rates and backed by collateral such as oil. Our new dataset covers a total of 1,974 Chinese loans and 2,947 Chinese grants to 152 countries from 1949 to 2017. We find that about one half of China’s overseas loans to the developing world are “hidden”.

### International Institutions and Political Liberalization: Evidence from the World Bank Loans Program

**Carnegie, A., & Samii, C. (2019).**

The purpose of the study is to investigate how do international institutions affect political liberalization in member states? Motivated by an examination of the World Bank loans program, this article shows that institutions can incentivize liberalization by offering opportunities for countries to become associated with advanced, wealthy members. In the

World Bank, when a loan recipient reaches a specified level of economic development, it becomes eligible to graduate from borrower status to lender status. The study demonstrates that this incentive motivates states to improve their domestic behavior with respect to human rights and democracy. Combining qualitative and quantitative evidence, the results suggest that the desire to become a member of this elite group is responsible for motivating member states to reform due to the belief that such membership brings diffuse international and domestic benefits.

**Banking credit worthiness: Evaluating the complex relationships**

**Bai, C., Shi, B., Liu, F., & Sarkis, J. (2019)**

In developing economies agriculture and farming play crucial roles for economic sustainable development. Farmer credit risk evaluation is an important issue when determining financial support to farmers, improving agricultural supply chain performance, and ensuring profitability of financial institutions. Credit risk evaluation, or creditworthiness, is not a trivial exercise due to various complexities. Honoring complexity is necessary to effectively evaluate and predict farmer creditworthiness. A methodology using fuzzy rough-set theory and fuzzy C-means clustering is used to evaluate and investigate the complex relationships between farmer characteristics, competitive environmental factors, and farmer credit level. The methodology is detailed using actual bank data from 2044 farmers within China. This empirical methodology generates decision rules that provide insight to more complex relationships than can be found through standard econometric multivariate approaches. A rule-based methodological outcome can be used to predict the creditworthiness of farmers and to aid in agricultural loan decision making. Prediction accuracy of the rule-base was 81.16%. A central finding is that education and skills related characteristics are important for determining farmer credit-worthiness.

**Credit Worthiness and Repayment Performance among Small – Holder Farmers in Sri Lanka: Application of Probit Model**

**B. Sivatharshika and A. Thayaparan (2019)**

The objective of the study is to examine the factors which determine the credit worthiness and loan repayment performance among the small-holder farmers in Vavuniya district in Sri Lanka. A sample of 113 small –holder agricultural loan borrowers from five villages who get the loans from SANASA TCCS served as the respondents in the study. A set of structured questionnaire was used to collect the primary data from the respondents who lives in the five villages located in Marukkarambali GS division in Vavuniya district, Sri Lanka during the period of 2018/2019. The dependent variable is the credit worthiness measured as binary variables where it takes as one for defaulters and zero for non - defaulters and the selected demographic characters, farming characters and farmers' attributes were taken as explanatory variables in the study. To identify the above characters on the credit worthiness of the farmers' descriptive statistics, and binary probit model were employed.

The results of the descriptive statistics revealed that, 43.4% of the respondents belonged to the defaulters while 56.6% of them belonged to the non – defaulters in the study. Estimated results of the probit model suggest that among the demographic characteristics, age of the farmers, levels of education, number of family members positively influenced the loan repayment performance of smallholder farmers, while among farming characters, income, farm size, land ownership, farming experience, off-farm activities, purpose of loan and possibility of crop failure were positively impact on credit worthiness and repayment performance at different significant levels. On the other hand, knowledge about the loan and responsible guarantors were the major factors of farmers' attributes influencing the repayment performance in the study. The overall findings of the study may help to the farmers as well as to the micro finance institutions to predict the repayment behaviour of the new loan applicants and to make the decision to grant loans in future.

**The political economy of International Finance Corporation lending**

**Dreher, A., Lang, V., & Richert, K. (2019)**

Much of the International Finance Corporation's (IFC) lending benefits private companies from rich countries and supports projects in middle-income countries. Large corporations such as Lidl or M€ovenpick have received its loans for highly profitable investments. This contrasts to some extent with the IFC's official mandate, which is to finance poverty-reducing projects for which private capital is not available on reasonable terms. Investigating a potential driver of this mismatch, (Dreher, A. et al. 2019) argued that some governments can influence the allocation of IFC loans to the benefit of private companies in their countries. Using new data for more than 3000 IFC projects over the 1995–2015 periods. Dreher, A. et al. 2019 showed that (joint) IFC Board membership of countries where borrowing companies are based and of countries where the projects are implemented increases the likelihood that these countries receive IFC loans. This has implications for the debate on leveraging private-sector investments for development.

**The Determinants of Sovereign Credit Ratings: Indonesia and Its Neighborhood Countries 1998-2016**

**Gerry Michel, Akhmad Solikin (2019)**

The aim of this research is to study the determinants of sovereign credit ratings of Indonesia and its neighborhood countries in the period of 1998-2016. Using secondary data and analyzed using ordered probit, it is found that every credit rating agency has its own variables influencing to its published credit ratings.In general, for Indonesia and its neighborhood countries, the variables with significant and positive relationship are fiscal balance and current account deficit to GDP, freedom index, and GDP per capita; while the variables with significant and negative relationship are external debt to GNI and real exchange rate. Gross domestic savings to GDP influences credit ratings in both ways. Interestingly, inflation does not affect the credit ratings. Indonesia and neighborhood governments could use this information to manage their macroeconomic indicators in order to get favorable ratings from credit rating agencies.

**Global horse trading: IMF loans for votes in the United Nations Security Council**

**Dreher, A., Sturm, J. E., & Vreeland, J. R. (2009)**

The purpose of this paper is to investigate whether temporary members of the United Nations Security Council receive favorable treatment from the International Monetary Fund (IMF) using panel data for197countries over the period from 1951 to 2004. The results indicate a robust positive relationship between temporary Security Council membership and participation in IMF programs, even after accounting for economic, political, and country-specific factors. There is also evidence that Security Council membership reduces the number of conditions Included in IMF programs. IMF loans seem to be a mechanism by which the major Shareholders of the Fund can win favor with voting members of the Security Council.

**Enhancing the Role of Regional Development Banks**

**Griffith-Jones, S., Griffith-Jones, D., & Hertova, D. (2008).**

Access by emerging market countries to private capital markets can be unreliable, limited and costly, and thus lending through multilateral development banks (MDBs) needs to continue playing an important role in the international development architecture. At the same time there are a number of important reasons why lending by regional and sub-regional development banks (RDBs, SRDBs) can and should play an important and valuable complementary role to multilateral lending and institutions. The main issues and conclusions discussed in our paper are the following. Firstly we analyse the successful experiences of the European Investment Bank (EIB) and the Andean Development Corporation (CAF). European integration offers very valuable precedents and lessons; the EIB was central to the process of European integration since the beginning, as it was especially created to support this process. An interesting question is whether EIB lending to developing countries could not be expanded more. The CAF on the other hand is unique in being almost exclusively owned by developing countries. A noteworthy feature is also the exponential growth of its loans since 2000 and the great average speed, at which their loans are approved, with an average period of around 3–4 months. These and other positive features of the CAF provide very good lessons for potential new development banks.

**The effects of IMF and World Bank lending on long-run economic growth: An empirical analysis. Butkiewicz, J. L., & Yanikkaya, H. (2005).**

The International Monetary Fund and the World Bank, frequently, and often repeatedly, extend loans to developing nations. These loans have been blamed for generating adverse economic outcomes. The aim of this paper is to assess the growth impact of Fund and Bank loan programs by using an empirical growth model that controls for other determinants of growth. A unique feature of this study is the use of the value of loans rather than the number of programs. The results indicate that Bank lending stimulates growth in some cases, primarily by increasing public investment. Fund lending is either neutral or detrimental to growth. The channel for this effect is a negative impact of Fund lending on public as well as private investment.

**The Economic Content of Indicators of Developing Country Creditworthiness**

**Haque, N. U., Kumar, M. S., Mark, N., & Mathieson, D. J. (1996).**

This paper analyzes the economic determinants of developing country creditworthiness indicators for over 60 developing countries for the period from 1980 to 1993. The main results indicate that economic fundamentals – the ratio of non-gold foreign exchange reserves to imports, the ratio of the current account balance to GDP, growth, and inflation – explain a large amount of the variation in the credit ratings. All developing country ratings were adversely affected by increases in international interest rates, independent of the domestic economic fundamentals. A country's regional location and the structure of its exports (such as whether it is primarily an exporter of fuel products or manufactured products) were also important.

**Relative Importance of Political Instability and Economic Variables on Perceived Country Creditworthiness**

**Lee, S. H. (1993).**

This paper examines the relative importance of political instability and economic variables on perceived country creditworthiness. Overall, the results indicate that both political instability and economic variables are taken into account in evaluating country creditworthiness; however, it appears that bankers assign larger weight to economic variables. Hence, it seems that the country creditworthiness perceptions are largely based on a country's economic performances, which we except to reflect longer term political stability. In addition, the frequency of changes in the regime and armed conflict, both proxying for political instability, also affect the credit ratings.

**Politics and Perceived Country Creditworthiness in International Banking**

**Thomas L. Brewer Pietra Rivoli (1990)**

The purpose of this paper is to test for the effects of political instability on perceived country creditworthiness. The central questions are (1) Do international bankers and financial markets respond to these political phenomena in their assessments of countries' creditworthiness? and (2) What types of political instability affect creditworthiness perceptions? The determinants of credit- worthiness perceptions are of central importance because these perceptions affect both the supply and cost of capital flows to developing countries. The paper represents a departure from most previous studies of country creditworthiness in international banking, such as those by Feder, Just, and Ross (1981) and Shapiro (1981), because it incorporates political as well as economic phenomena. Our results suggest that political variables are at least as important as economic variables in explaining perceived creditworthiness. Therefore, the failure to include measures of political stability in models of country creditworthiness will result in misspecification.

**International lending, long-term credit relationships, and dynamic contract theory. International Finance Section, Department of Economics, Princeton University.**

**Crawford, V. P. (1987).**

This study considers to what extent dynamic contract theory has been, or could be, used to explain several phenomena often observed in modern international capital markets—notably credit rationing, rescheduling of loan payments, the predominance of short- and medium-term credit over long term credit, and restricted access of poor countries to commercial loan markets. This study has provided an introduction to dynamic contract theory and a survey of dynamic contract models dealing with credit relationships.

**The determinants of international creditworthiness and their policy implications**

**Feder, G., & Uy, L. V. (1985).**

The present paper utilizes an empirical measure of creditworthiness based on bankers' perceptions to estimate the effect of various variables hypothesized to influence assessments of countries' debt-servicing capacity. The data pertain to a cross section of countries within the period 1979–1983. Such estimates necessarily employ a ceteris paribus assumption, which prevents a realistic assessment of the effects generated by policy changes. The second part of the paper develops, therefore, a dynamic simulation model of a hypothetical average economy. The simulations allow analysis of changes in macroeconomic variables and creditworthiness over time within a system that maintains accounting identities and behavioral constraints. Several changes in policy variables are considered that highlight the importance of export expansion. The latter is, of course, an often suggested policy objective, but the present paper demonstrates its effectiveness in terms of a somewhat nonstandard criterion.

**The Long-Run Creditworthiness of Developing Countries: Theory and Practice**

**Kharas, H. (1984).**

This paper analyzes the determinants of developing country long-run creditworthiness, focusing on the process of capital accumulation relative to external debt. Creditworthiness depends on the actual capital stock compared with a critical level, representing the gross wealth just sufficient to ensure that interest payments to foreigners never exhaust national output given expected gross inflows and existing outstanding debt. Hence, the probability of rescheduling is linked to debt service-capital, net inflows-capital, investment rates, and income levels. The empirical results, based on a probit analysis of historical rescheduling incidents, are quite robust and supportive of the theoretical framework.

## Conclusions

There was a significant impact of proximate country instability as indicated by the frequency of governmental regime change on perceived country creditworthiness. The frequency of regime change appears to be at least as important as economic variables in explaining lenders' risk perceptions. This was true for both instability in the head of government and instability in the governing group. These results were consistent for the two measures of perceived creditworthiness. Moreover, this research has presented that a reduction in credit quality should be recognised at an early stage when there may be more options available for improving the credit. Banks must have a disciplined and vigorous remedial management process, triggered by specific events, that is administered through the credit administration and problem recognition systems. A bank's credit risk policies should clearly set out how the bank will manage problem credits. Banks differ on the methods and organisation they use to manage problem credits. Responsibility for such credits may be assigned to the originating business function, a specialized workout section, or a combination of the two, depending upon the size and nature of the credit and the reason for its problems.

In addition, effective workout programs are critical to managing risk in the portfolio. When a bank has significant credit-related problems, it is important to segregate the workout function from the area that originated the credit. Finally, the paper has presented the international lending organisations which were adopted in the context of the comprehensive revision by the IMF and World Bank of their policies on debt limits conditionality for non-concessional borrowing.

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