

# Sector specific expert SME rating models streamline processes and ensure Basel II compliance for a leading domestic bank in UAE



## Client Profile

The client is one of the leading domestic banks in UAE with more than AED 1 billion in profits last year, offering a variety of retail and corporate products. The Bank is jointly owned by the Governments of Abu Dhabi and Dubai and is growing to become one of the key players not just in UAE but in the entire Middle East region. The Bank has a healthy SME book and is focusing more on structured lending to the SME sector through various facilities.

## Summary

The project aimed at developing rating models for the client's SME portfolio to support both parameterised and non-parameterized loans that will enable the risk department to streamline the lending process and also comply with Basel II requirement of IRB approach for SME lending. The models were developed using qualitative and quantitative parameters that reflects the Bank's policies, loan type, management and business factors, socio-economic consideration and the regions' regulatory framework.

## Insights

The rating models streamlined the credit approval process for SME lending and provided sufficient controls in assessing a borrower through standard parameters. The rating model allowed to uniformly apply lending criteria across the SME portfolio, thereby improving overall portfolio quality and also meet Basel II compliance.

## Client Benefits

- D&B Expert models provided a jump-start to finalize SME assessment parameters
- Standard assessment of all SME borrowers allowing enforcement of risk policies
- Ability to provide flexible pricing based on score value

## Business Challenge

**Rating models:** The bank had two broad categories of SME lending, parameterised and non-parameterized loans differentiated on loan size, availability of SME financial statements and the type of guarantee provided. The Bank required different models to recognize these two broad loan type segments.

**Sector specific:** The Bank also differentiates its SME customers based on their area of business under three broad sectors.

**Standardization:** The client was unable to create a uniform process as there were many deviations based on data availability leading to inconsistent and time-consuming underwriting process.

**Flexibility:** The Bank required a certain degree of flexibility for external factors that may have a varying impact on SME customers based on their areas of operation.

**Overrides:** The client also has a specific process to override the final score based on additional findings or parameters that are not part of the rating model and very specific to the borrower.

## D&B Solution

D&B has considerable experience in developing SME rating models by virtue of being one of the largest data and rating provider of SME in the region. D&B Expert rating models for SME is widely used by various banks and institutions to rate and assess their SME borrowers.

To meet the requirements and overcome the challenges of the client, D&B provided its Expert models for both parameterized and non-parameterized lending. Upon review of the expert models, the below 5-step process was followed:

- D&B base SME rating models
- Evaluate and agree on Importance of Risk drivers
- Finalize data elements for each model
- Assign Weightages
- Define and finalize Rating scales

The outcome of this exercise allowed to develop three sector specific SME rating models (manufacturing, trading and services) defined to meet the requirements and specifics of these individual sectors. The model parameters considered and allocated corresponding weightages to both qualitative (balance sheet, profit & loss, financial ratios, cash flows, etc.), and quantitative (business, management, industry and economic) factors.

