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P2P Lending's Credit Risk in Vietnam: Determinants and Discussions

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ABSTRACT: The recent upsurge in information technology has created the automation of processes and the reorganization of the chain of financial business area. In a new trend technology application, peer-to-peer lending (P2P) model, a service that connects individuals to borrow and lend money is adopted by the new online platform along with advanced technology systems and many different purposes. Hence, this research explores the situation and draws on possible potential causes of peer-to-peer lending risk. The questionnaire surveys were launched in December of 2021 with arepresentative sample consisted of 205 participants, including the majority of Vietnamese who had stable incomes in major cities of domestic nation and some others abroad as well as in-depth interviews also took place with persons who have a clear understanding of peer-to-peer lending and its risks. Based on findings, some recommendations were proposed to reduce risk of a new form of credit provision.

INTRODUCTION

The development of the world has led to a series of new business forms. For instance, buying a car now makes it easier to take purchases through online payments. It is demonstrated that digitization has a dramatic impact on the financial services industry. The recent upsurge in information technology has created the automation of processes and the reorganization of the chain of business. Since then, the term "financial technology", also known as FinTech, has begun to appear. FinTech has made significant advances in the modern economy and had a great impact on the lives of human beings at this moment (Puschmann, 2017). In a new trend technology application, peer-to-peer lending (P2P) model, a service that connects individuals to borrow and lend money is adopted by the new online platform along with advanced technology systems and many different purposes. However, this model is increasingly trusted and used in a wide range country around the world. At low interest rates today, depositors do not get much profit if they bring money into the bank. In contrast, borrowers sometimes pay interest rates up to two digits, especially in the case of a credit card. This paradox creates a fertile market for those who want to associate surplus money with the needy persons (Downes and Goodman, 2014). For that reason, peer-topeer lending services attract so many users. On the other hand, similar to current forms of banks, P2P also includes collateral and unsecured loans. The only difference is that its appraisal will be conducted online and investors have many choices of partnering on P2P platform as well as monitoring all source of profits from the lender. Thus, without any transaction that is not accompanied by credit risk, peer-to-peer lending is no exception. There are many possible causes of peer-to-peer lending credit risk from P2P lending companies or P2P users. In three recent years, there has been some significant volatility in this particular lending market. As a result, customers of peer-to-peer lending are increasingly concerned that risks can occur at any time. Therefore, this study will show the inherent nature of P2P lending and the issues surrounding its credit risk

LITERATURE REVIEW

The significance of good credit risk management and how this could be attended by careful construction, credit risk policies, approval procedures and payment criteria. Having understood the objective and subjective factors that affect credit risk, the qualitative and quantitative knowledge that can best be applied is not difficult. In a nutshell, credit risk arises in the case of delayed payment of debt or the worse is insolvency. This is the inherent attribute of lending and contributing capital in the market. The risk that the borrower can not pay both the principal and the interest under the previous term in the credit agreement will lead to default and will have a significant impact on the financial situation of the relevant individuals or organizations. Moreover, many papers on credit risk of credit institutions, credit risk portfolio, but there has never been a serious problems with Peer-to-Peer Lending credit risk. Puschmann (2017) pointed out the important points when learning about FinTech, financial technology. More specifically, peer-to-peer lending, that kind of services through online technology equipment. Peer-to-peer model appeared first in the UK then spread to other countries, boomed in the US and peaked in China (Downes and Goodman, 2014). Until now, Lending Club, which was founded by Renaud Laplanche and based in San Francisco, America, is the largest P2P all over the world and takes the lead in companies listed on the stock market and offers secondary market loans. According to data from Lending Club's website, its average interest rate on a loan is currently 7.6%, its lowest rated loan is subject to interest rates of around 25%. There has been about $6 billion in loans financed through this company since it started operating in 2006 and has had $596 million interest paid. Lending Club's successes are seen as a positive signal for peer lending trends in the US amid the struggles of banks seeking higher returns amid low interest rates and consumer spending while it is difficult to convince banks to lend. Although human beings at that moment, when peer-to-peer lending just appeared, are aware of the impressive appearance and powerful influence of the Lending Club on the economy, Duarte et al. (2012) still decides to address the role of Peer-to-Peer Lending in financial transactions. Through a survey from potential borrowers, he wrote study Trust and Credit the Role of Appearance in Peer-to-Peer Lending, then analyzed the success of Prosper in particular and pointed out the potential resources in particular of other peer-to-peer lending. A catastrophic event made every customer of this lending model confused. Following an internal investigation at Lending Club, Renaud Laplanche, its founder and CEO at that time, resigned. Under the supervision and support of other advisors, the Lending Club conducted a review of an investment firm's issue with a $22 million loan within two months. This loan did not comply with the credit and regulatory requirements of the company. Although some employees are aware that this trade does not meet the criteria of the investor, this misconduct still occurs. The exchange of this great money through Lending Club investors generated a hidden profit. Soon after, three senior managers were laid off and resigned. The $22 million loan was also settled. Even so, the consequences it left were not modest. On the verge of development, this event was a blow to the Lending Club in particular and the peer-to-peer lending model in general. Furthermore, Lending Club's Monday trading session dropped 26% and continued to decline to 35% at the end of the day. Despite having discovered and dealt with this dangerous loan, Lending Club has also lost a long time to recuperate. Called the "old father" of peer-to-peer lending service, the company has played a significant role in the market. This was the first time a publicly traded P2P loan company had been exposed to credit risk. As such, it has attracted the attention of so many people, including major government officials as well as the finance ministry. All thing considered, peer-to-peer lending companies have lost confidence in their customers, and investment has fallen sharply. Finally, it leaded to closer scrutiny from government agencies and central banks. Beside Prosper, Lending Club, which is mentioned right up, others peer-to-peer lending also work with the same structure but an operation model is in many different sizes. Even so, every business method has certain credit risks, including large or small. Its level depends on lots of different factors as mentioned in the previous section. To investigate the issue, Cai et al. (2016) surveyed nearly 800 users of PPDai, the largest online peer-to-peer lending company in China. In addition, he did research Judging Online Peer-to-Peer Lending Behavior: A Comparison of First-time and Repeated Borrowing Requests and drew his own conclusions. To address the potential risk of peer-to-peer lending, users need to trust the trust created through it. This is the most important influence factor for both lenders and borrowers. In consequence, to create trust from the enemy, each individual to participate in peer-to-peer lending must provide high quality information. Only then, it could be safe and can grow in the long run.

According to Caroline Stern, Mikko Makinen and Zongxin Qian (2017), about 40% of young Chinese now make purchases through the Internet. At the beginning of 2014, peer-to-peer lending models entered the Chinese market and became a popular service in many major cities and provinces. Nevertheless, since late 2015, some fraudulent practices through P2P lending have begun to emerge, typically the famous all around the world Ponzi fraud model. Retailers in China had lost billions of dollars as peer-to-peer lending companies disappeared with investors' cash. Ezubao was accused of running away with more than $7.2 billion from about a million investors. Although the outstanding balance of peer-to-peer companies is still increasing, the average yield of P2P loans has declined significantly. Some senior leaders have called the Chinese peerto-peer lending market as "a fraudulent market". To summarize, investors have been becoming more sophisticated in this risky market. Besides, BitConnect is an open source community-based, allowing everyone to store and invest their capital in a non-governmental currency and even make a big profit from investing. BCC is considered an extension of P2P but connected to the Ponzi scheme. After its market launch in 2016, BitConnect's currency market share was rapidly rising and ranking high in the global electronic money index. But soon after, the rift began as many investors accused it of being a Ponzi model. As right predicted, in January 2018, BitConnect announced a formal halt to its loan service and temporarily closed its internal trading platform for five days. Next, the US court ordered the freezing of assets of this market. Many users have started a group lawsuit against BitConnect, offsetting their lost money. Additionally, according to the General Statistics Office, Vietnam has always been at the top of the list of whom entered the market. Hence, when the lending model collapses, Vietnam would be one of the countries suffering the most serious consequences. Many Vietnamese investors have worried about losing their assets. Although BitConnect promised to return all the money to investors in the form of BitConnect, the average price was about $350. Even so, as soon as the announcement ceased, the price of a copper BCC plummeted to $20. This means that investors have lost 90% of their assets.

METHODOLOGY AND DISCUSSIONS

Primary data will also be displayed by quantitative methods. A survey was launched along with the questionnaire to assess the factors surrounding peer-to-peer lending credit risk. There were 250 questionnaires distributed but the results were totally composed of only 205 people. Besides, in-depth interviews have taken place with 10 persons who really care about and want to share their views on peer-to-peer lending. The purpose of these interviews is to show specific and accurate views of P2P users. Based on the credit risk issues that have occurred and relevant scientific papers, the interview questions were designed to fit the interviewee. The results have also revealed many clear points about P2P credit risk in Vietnam in particular and in the world in general.

Sources of Peer-to-Peer Lending

What causes such great risks? Investment types have not been thoroughly tested; credit card debt still appears. In addition, long-term investment has also made loan repayments slower and returns are not fixed during a period of time. After the loan, the lax supervision makes the return on capital less. According to the user experience in the survey, an interviewee claimed that the peer-to-peer lending user management information system was lacking in transparency, which was difficult to assess for collateral. This has led to cases of misbehavior and mischief among users. Technology development also means that online crime cases are on the rise. It would be easier for criminals to cheat online lenders by applying for a loan that has stolen identity information than in traditional banks. The criminals will try to persuade and prove to the lender that they are the one who stole the information. Only with such a case could it affect the many aspects of P2P lending and other companies in general. In addition, the government and state-owned banks have not had strong moves to introduce specific regulations to peer-to-peer lending companies. Therefore, a few start-ups can use the trick to circumvent the law when dealing. When there is a risk from customers or P2P owners, the parties are difficult to deal with each other as well as the authorities also lack legal basis to resolve disputes. Some companies have commitments on the web trading floor is not really detailed, the interests of customers have not been mentioned when the dispute occurred. The survey found that 79% of peer-to-peer lending users think there is a lot of lack of transparency in the handling of customer information. Some customers still have high ratio of bad debt, bad debt and overdue debts, which makes them feel unsure when making investment decisions. Moreover, 94.6% persons said that the collateral was not specified so the risk of P2P credit can not be avoided. All figures are shown in the table below:

According to the data in the chart below, from the primary data, more than 70% of users agree that the management and monitoring information before and after the investment is not very tight. There are a number of vulnerabilities created so that scammers can circumvent the law and commit misconduct to make money. The fact that the information is not thoroughly tested regularly contributes to opportunistic causes of credit risk for other peer-to-peer borrowers.

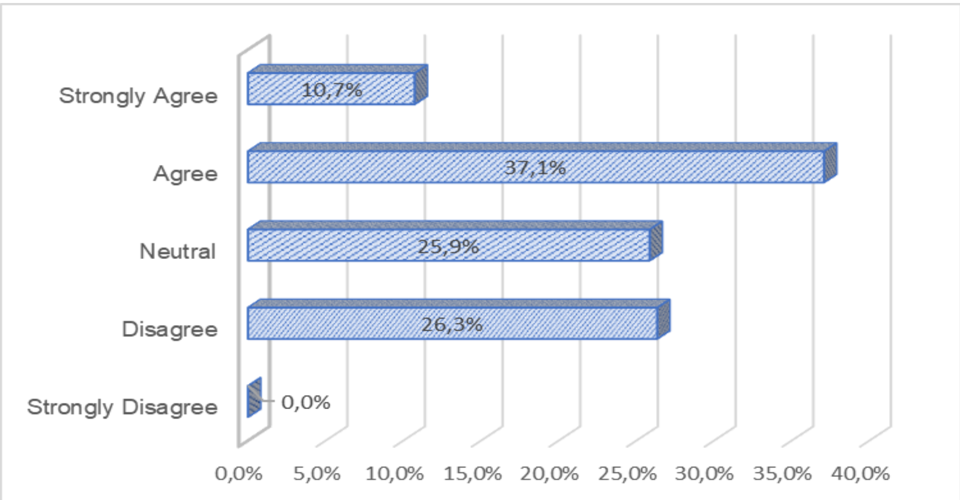

Figure 2: Supervision before and after loan contracts become bad debts

Source: Primary Data

The Collapses and Potential Appearance of Peer-to-Peer Lending

Although there are strong points for users, peer-to-peer lending service still has potential credit risks that investors have to be afraid of. According to the survey, more than 70% of users are afraid of using P2P lending. There are many bank credit risks in the world and peer-to-peer lending credit risk is no exception. The case of the Lending Club, one of the leading peer-to-peer lending companies in the United States, has caused quite a stir. After creating the "whirlwind" of peer-to-peer, Lending Club has earned millions of dollars and raised the stock market quite strong. To minimize credit risk, the Lending Club focuses on high credit score borrowers and increases interest rates for high risk loans. According to the data from the World Bank Data, only those borrowers with a FICO score of 660 or more will be approved at its website. Therefore, around the beginning of 2016, Lending Club and other P2P lending companies are having a hard time attracting investors. While Lending Club shares are on the downward trend. In April 2016, the Lending Club faced a scandal. CEO Laplanche was forced to leave the company after being accused of fraudulent loans and refused to cooperate in an internal investigation. This news shocked the market because Laplanche was considered a pioneer in the industry and one of the earliest.

As a result, Lending Club shares fell below $5, down nearly 70% compared to their IPO price. The scandal has led some investors to be skeptical about this lending model. Prior to the loan options, users are suddenly afraid of the unforeseen risks of peer-to-peer lending service.

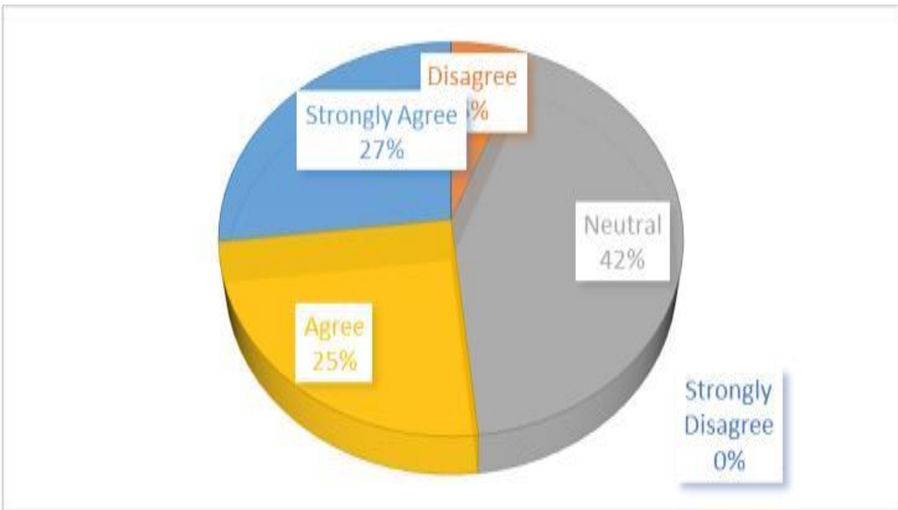

Figure 3: Fear of using peer-to-peer lending model
Source: Primary Data

As a result of the survey, only 6% of users are not concerned about the potential credit risk of this model. Some figures show disappointment after the big scandal of the world's leading peer-to-peer lending company. The fact caused P2P lending to drop significantly in the market. The success of the Lending Club as well as the peer-to-peer lending model are considered to be the symbol of the FinTech wave - a new trend in the banking industry in which the technology will create breakthroughs for traditional banking operations that have existed for hundred years. However, like the pioneers, the road ahead is not easy. After the departure of the CEO, Lending Club has struggled to make a profit in 2017 despite gaining market share from traditional lenders in some areas. Net loss fell by $5 million in the fourth quarter and revenues were about $160 million.

Moreover, BitConnect announced on January 17 that it would stop lending service and temporarily close its internal trading platform for five days. BitConnect has become one of the most successful ICOs in history with a value that is more than 3,000 times that of a year. According to the data from the General Statistics Office, from the starting price of $0.12 at the ICO, at the end of 2017, BitConnect has reached a record level of nearly $400 a copper. This information has shocked the world and made a lot of investors panic as they could lose almost all of their money. As a lending model similar to peer-topeer lending, the MLM lending BitConnect incident was collapsed by the Ponzi model, the most famous island fire model in history, which made more people confused about the reliability of the lending. As the chart below, although the number of people who do not want to continue to use peer-to-peer lending service is just 14%, this is a significant figure for getting the full trust from customers.

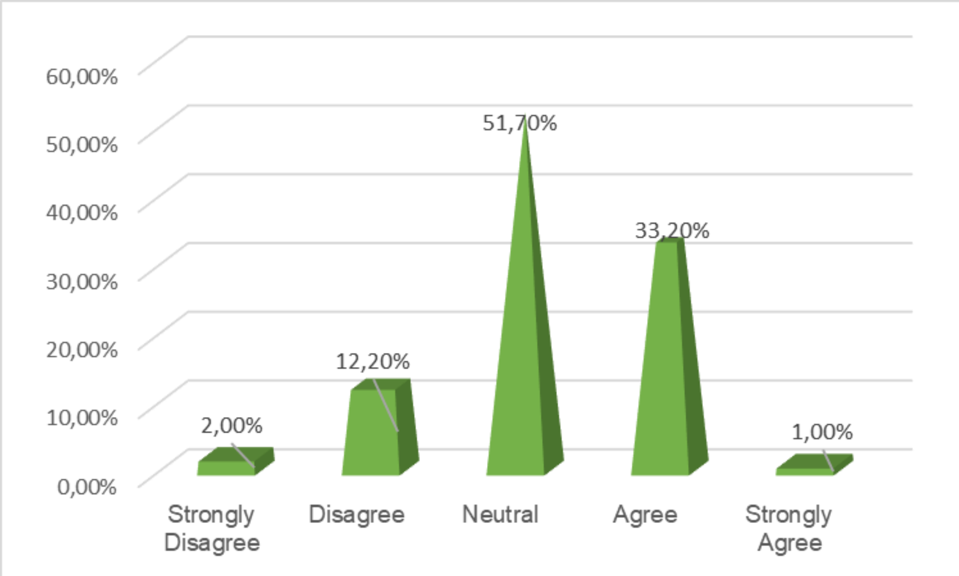

Figure 4: Ability to continue to use peer-to-peer lending service
Source: Primary Data

At Superior Court of California, from 2006 to 2008, a class action lawsuit has occurred about the issue of revolving around this lending model. Prosper, the nation's first peer-to-peer lending company and one of the market's top movers, was accused of selling unqualified and unregistered securities in violation of state securities laws during that time. Until 2013, the new lawsuit ends when Prosper pays the plaintiffs $10 million.

Loan bubbles are likely to occur in the future, causing peer-to-peer lending to become more confused. Without a positive transition, these patterns can fall off immediately and collapse.

RECOMMENDATIONS

Suggestions for Peer-to-Peer Lending Companies

To avoid undue risks, peer-to-peer lending companies must be more aggressive in avoiding risks. The errors identified from the cause of credit risk are the basis for the leaders to make sound policies.

The first of the peer-to-peer lending companies is to make requirements on limits not be limited. This reduces the risk of not recovering capital and avoiding debt. Users who have a bad debt ratio on total outstanding loans and a high rate of overdue debt should also be eliminated immediately. Technology systems installed on the websites of the trading floor also need to be improved and updated continuously. In addition, the collateral assessment should be made explicit and clear both before and after the loan.

Additionally, the related information of borrowers and lenders on the peer-to-peer lending platform should be managed and publicly disclosed to further enhance transparency. Once credibility has been established, the user is excited and feels safe to continue using the model.

Table 4: Evaluation of some measures taken to mitigate the peer-to-peer lending credit risk (unit: percent)

Criteria	SD	D	N	A	SA
Enhance the authentication of the users' information and financial situation.	0.0%	0.0%	9.3%	31.7%	59.0%
Make transparent the peer-to-peer lending companies' policy and financial status.	0.0%	0.0%	20.0%	43.9%	36.1%
Assess the financial situation periodically.	0.0%	0.0%	49.3%	24.9%	25.9%

Source: Primary Data
(SD: Strongly Disagree; D: Disagree; N: Neutral; A: Agree; SA: Strongly Agree)

Based on the results of the survey, all users of the peer-to-peer lending model agree that P2P companies enhance the authentication and financial status of P2P clients. This is to increase the tightness and safety, to ensure equity for investors. In addition, the policies and financial position of peer-to-peer lending services need to be transparent so that customers can mushroom and anticipate possible credit risks. Furthermore, the regular financial assessment of the company should also be done regularly to ensure the fraud and loss would not occur.

Suggestions for the Government and Central Bank

Although it is highly competitive with traditional banks, the Government and the Central Bank are constrained or relaxed with this business model. If bad debt increases or low liquidity, peer-to-peer lending model collapse leading to the economy also affected no small.

The Government should introduce specific legal policies to avoid clashes between peer-to-peer lending and bank loan services. It is necessary to avoid cases like Uber in Southeast Asia, for low profits and inadequate policies with countries in the region should have left the lucrative market. When P2P lending organizations are too weak and on the brink of collapse, there is a need for support from the central bank to restore or merge. Moreover, the specific policies will avoid the spleen of the bad sectors when operating on the peer-to-peer lending platform.

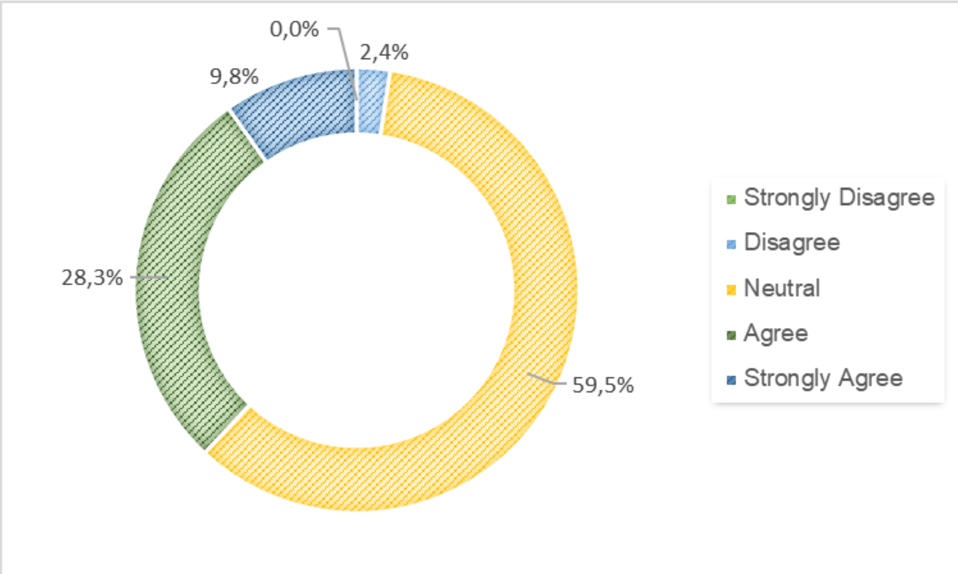

Figure 5: The Government provides specific legal policies for the P2P companies

Source: Primary Data

The Government has also added specific legal policies to this type of loan, which is always the top priority that P2P clients always expect. Only the compliance of the law to avoid the "black market" and scam tips scaled. In addition, when it comes to credit risk, having legal protection also makes customers feel more secure.

Suggestions for Peer-to-Peer Lending Users

When it comes to avoiding risks from investors or P2P lending companies, users also need to take measures for themselves. First, before investing, users need to look up information and history of the company and partner on the exchange. The liquidity of the company was not overlooked during the review process. Each company has its own pros and cons, users need to wake up to see the error of them.

Next, when starting to participate, it is necessary to operate slowly, follow up to keep track of the operation of the company selected. Without hurrying into the market and lending or borrowing a large amount of money, slowly create your foundation in small increments. Each transaction object has different characteristics, which is why users have to be careful when deciding to join.

In addition, the user must know the extent of his own risk is. Everyone needs to think carefully about the amount of money they are trading to avoid damaging themselves. Once you know what your strengths and weaknesses are, the user should thoroughly investigate and invest in that area. When diversifying loans, the user will reduce the risk locally. Profits will therefore be higher than the user defaults.

Finally, P2P lenders must have a certain emergency fund to ensure they can cover their personal expenses. Investing with a P2P loan platform is a simple process, but it requires careful measures in the first place.

CONCLUSIONS

Once the problem is thoroughly and thoroughly researched, the reader not only understands peer-to-peer lending model but also knows the problems surrounding its credit risk. From there, individuals, companies, organizations can easily decide whether to invest in P2P or not, choose P2P or banks ... This is not the old, not the new, the study of it quite reasonable in the present time.

Based on studies from the quantitative and qualitative datasets, this paper outlines the causes for potential peer-to-peer lending credit risk. Peer-to-peer users as well as P2P companies must learn from and experience these causes. It can be very damaging to the assets and profits of peer-to-peer clients. Although peer-to-peer lending credit risks have already been resolved, P2P users are left with constant anxiety. To meet these limited needs, peer-to-peer companies as well as customers need to accurately see their risk exposure to self-regulatory measures. Besides, the government should pay more attention and have policies to ensure the interests of the people.

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