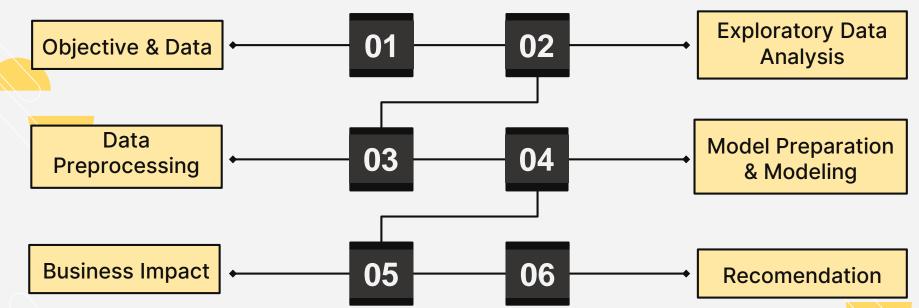


Predicting Loan Default Using Various Machine Learning Algorithms

Dery Purnama Saefudin

Outline





Business Understanding



Loan Default is a *PROBLEM* for Financial Industry.

The failure of a debtors to repay a loan according to the terms and conditions outlined in the loan agreement.





Objective

Current

6.188 debtors are current



22%

Default

22.313 debtors are default



78%

Obtain Insight of Loan Status

Create Machine Learning Prediction

Data

Before Cleaning

```
<class 'pandas.core.frame.DataFrame'>
RangeIndex: 32581 entries, 0 to 32580
Data columns (total 12 columns):
                                Non-Null Count
    Column
                                               Dtype
                                32581 non-null
                                               int64
    person_age
    person income
                                32581 non-null
                                               int64
    person_home_ownership
                                32581 non-null
                                               object
    person emp length
                                31686 non-null float64
    loan_intent
                                               object
                                32581 non-null
    loan grade
                                32581 non-null
                                               object
    loan amnt
                                32581 non-null
                                               int64
    loan int rate
                                29465 non-null float64
    loan status
                               32581 non-null int64
    loan percent income
                             32581 non-null float64
    cb person default on file 32581 non-null object
11 cb_person_cred_hist_length 32581 non-null int64
dtypes: float64(3), int64(5), object(4)
```

 Retrieved from https://www.kaggle.com/datasets/laots e/credit-risk-dataset/data

memory usage: 3.0+ MB

After Cleaning

```
<class 'pandas.core.frame.DataFrame'>
Int64Index: 28501 entries, 0 to 32580
Data columns (total 12 columns):
    Column
                                Non-Null Count
                                                Dtype
    person age
                                28501 non-null
                                                int64
    person income
                                28501 non-null
                                                int64
    person home ownership
                                28501 non-null
                                                obiect
    person emp length
                                28501 non-null float64
    loan intent
                                28501 non-null object
    loan grade
                                28501 non-null
                                                object
    loan amnt
                                28501 non-null
                                                int64
    loan int rate
                                28501 non-null float64
    loan status
                                28501 non-null int64
    loan percent income
                                28501 non-null float64
    cb_person_default_on_file
                                28501 non-null
                                                object
    cb person cred hist length
                                28501 non-null int64
dtypes: float64(3), int64(5), object(4)
memory usage: 2.8+ MB
```

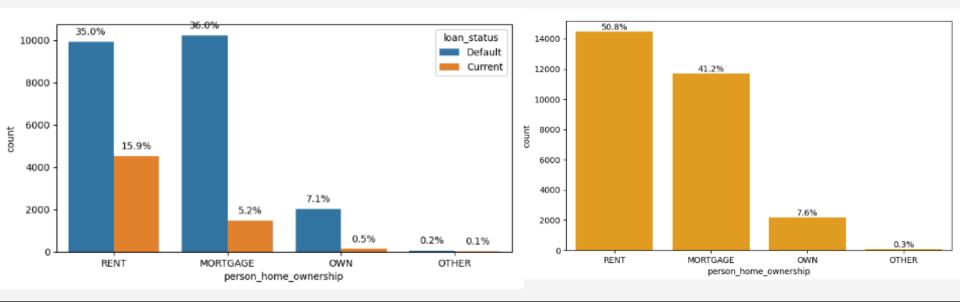
- The data has at most 32,581 rows and 12 columns before cleaning
- There are 28,501 rows and 12 columns after cleaning



Exploratory DataAnalysis

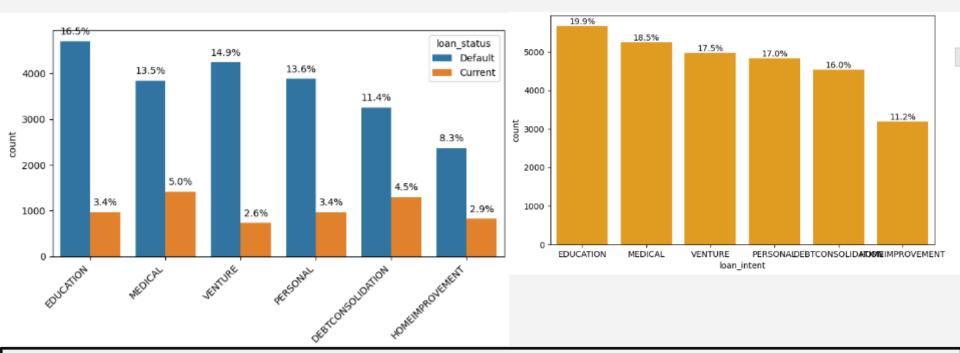


Home Ownership by Loan Status



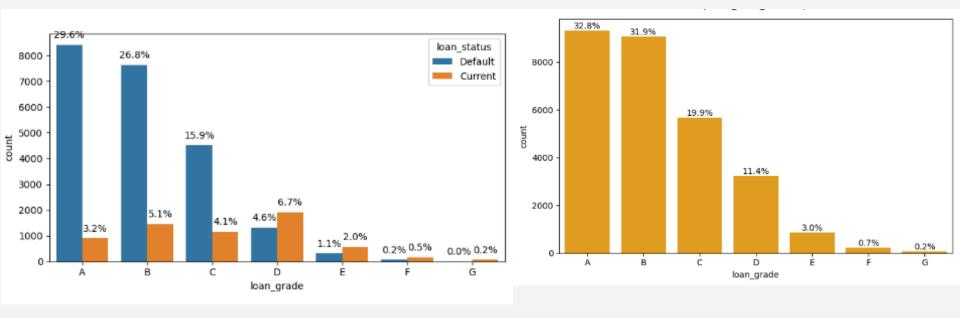
- Most of Debtors' home ownership are Rent (50.8%)
- Debtors who default the most are Occupier (15.9%)

Loan Intent by Loan Status



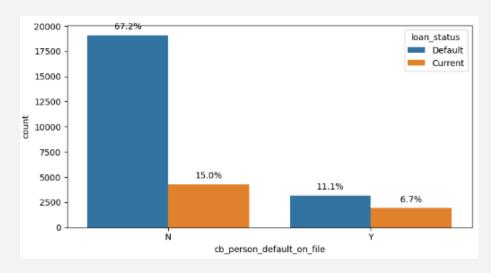
- The most common purpose of loan is Education (19.9%).
- Debtors who the most default are those with Education as the purpose (16.5%)

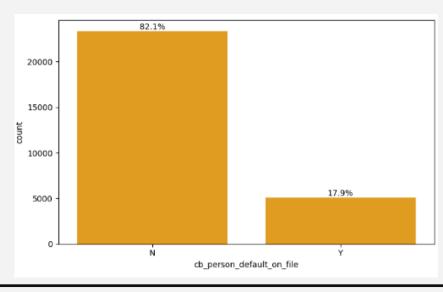
Loan Grade by Loan Status



- The most common loan grade is Grade A (32.8%).
- Debtors who the most default are those with Loan Grade A (29.6%)

Default History by Loan Status

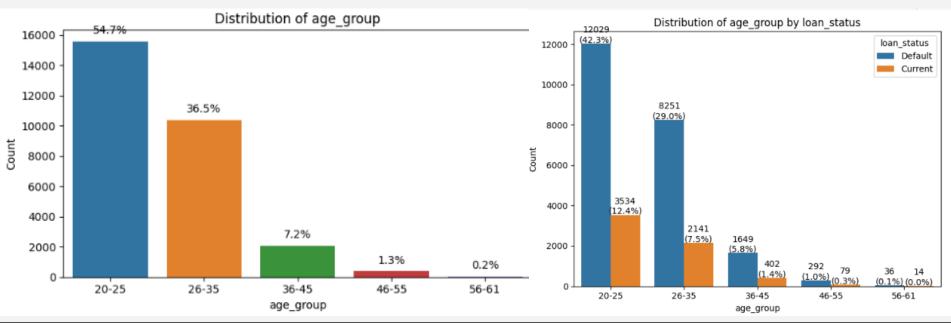




- The most debtors do not have loan default history (82.1%)
- Debtors who the most default are those without loan default history (67.2%)



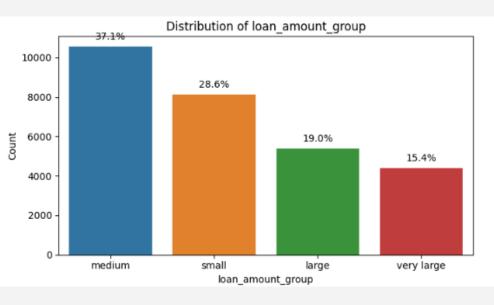
Age Group by Loan Status

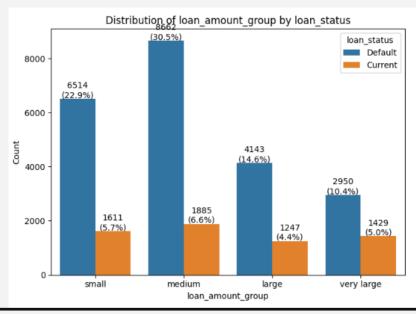


- The mostdebtors fall within the 20-25 age range (54.7%)
- Debtors who the most default are those within the 20-25 age range (42.3%)



Loan Amount Group by Loan Status

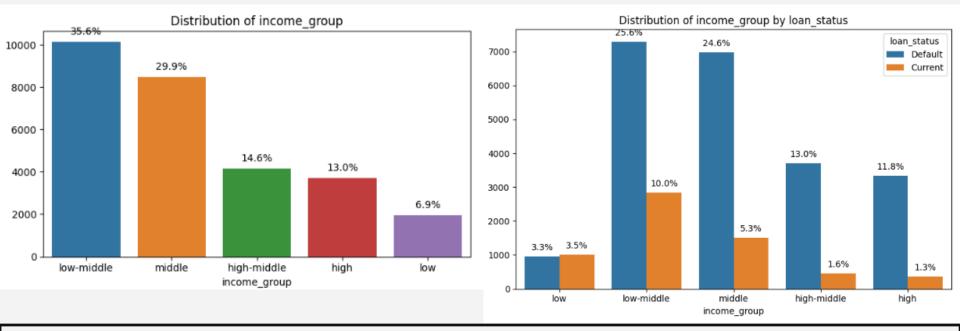




- The most common debtors are those with loan in the range of 5,000 10,000 / medium (37.1%).
- Debtors who the most default are those with loan in the range of 5,000 - 10,000 / medium (22.9%)



Income Group by Loan Status



- The most common debtors are those with income in the range of 5,000 10,000 / medium (35.6%).
 - Debtors who the most default are those with loan in the range of 5,000 10,000 / medium (25.6%)

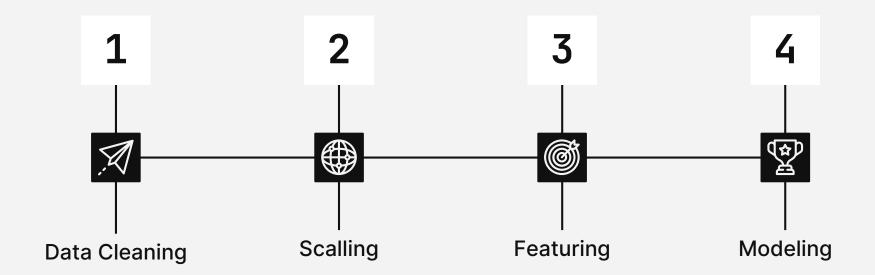
Features Engineering

After Encoding

RangeIndex: 28441 entries, 0 to 28440 Data columns (total 44 columns): # Column Non-Null Count Dtype Operson_age 28441 non-null int64 1 person_income 28441 non-null int64 2 person_emp_length 28441 non-null int64 4 loan_int_rate 28441 non-null int64 5 loan_status 28441 non-null int64 6 loan_percent_income 28441 non-null int64 8 loan_to_income_ratio 28441 non-null float64 8 loan_to_income_ratio 28441 non-null float64 10 int_rate to_loan_amt_ratio 28441 non-null int64 10 int_rate_to_loan_emratio 28441 non-null float64 10 int_rate_to_loan_emratio 28441 non-null int64 10 int_rate_to_loan_emratio 28441 non-null int64 10 int_rate_to_loan_emratio 28441 non-null int64 11 person_home_ownership_MORTGAGE 28441 non-null int64 12 person_home_ownership_MORTGAGE 28441 non-null int64 13 person_home_ownership_MORTGAGE 28441 non-null int64 14 person_home_ownership_MORTGAGE 28441 non-null int64 15 loan_intent_DEBTCONSOLIDATION 28441 non-null int64 16 loan_intent_DEBTCONSOLIDATION 28441 non-null int64 16 loan_intent_EDUCATION 28441 non-null int64 17 columns (total 44 columns): 22 loan_grade_B 23 loan_grade_C 28441 non-null int64 26 loan_grade_E 28441 non-null int64 27 loan_grade_G 28 cb_person_default_on_file_N 28441 non-null int64 29 cb_person_default_on_file_Y 28441 non-null int64 29 cloan_grade_E 28441 non-null i									
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Model Preparation





Modeling

Random Forest

Logistic Regression

K-Neighbour

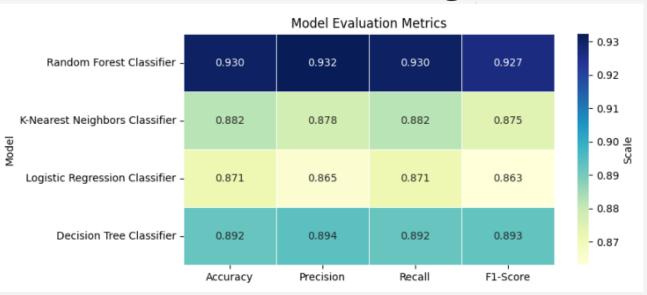
Decission Tree

Base Model

Hyperparameter Tuning (Grid Search)

Model

Before Tuning



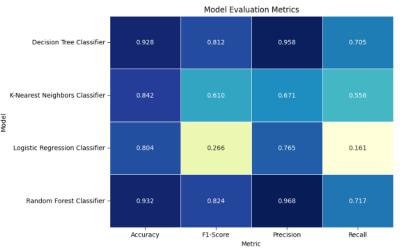


Random Forest
Precision (0.932)
Recall (0.892)





After Tuning



96 %

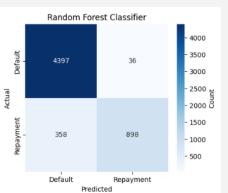


0.4

- 0.2

Model can predict the true default debtors correctly

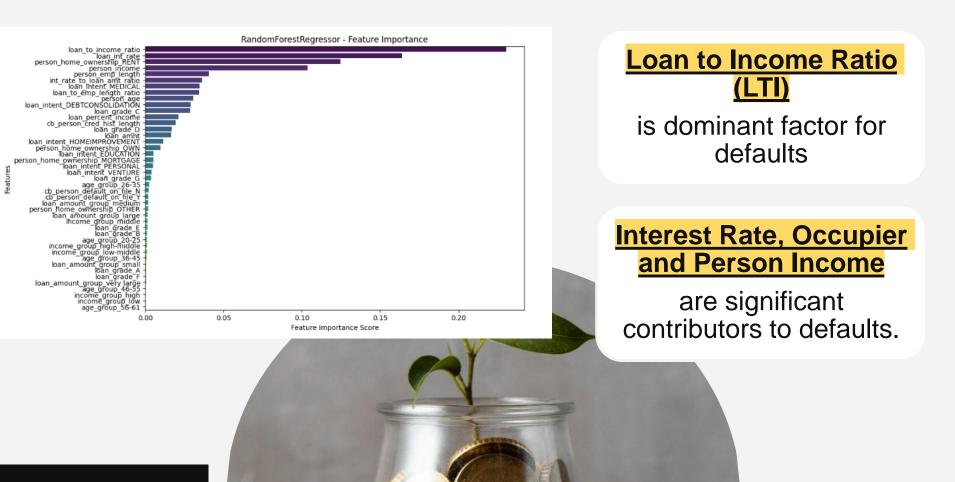




Business Impact

- The model can correctly predict 96 of the 100 default case and 29 default case can not be predicted correctly.
- If on average the bank's loss due to the default case is Rp 100 million per case & month, then using this model, the total potential losses that could be prevented are Rp 4.2 billion.

Feature Important





Business Recomendation

Improved risk management strategies:

- Adjusting loan principal limits (LTI < 35%)
- Adjusting interest rates
- Requesting additional documentation
- Adding additional approval processes
- Targeting Low Risk Market Segment





