PFG Provident Financial Group

Revenue, impairment and receivables example for a home credit loan

The simple examples below illustrate the calculation of the receivables balance within the home credit business of CCD and its interaction with revenue and impairment. Within the home credit business, loans are deemed impaired when two payments are missed within a 12-week cycle.

The following examples are based on a £100 loan with a total amount payable of £182 over 52 weeks which equates to a weekly payment of £3.50. The effective interest rate (EIR) applied to the loan is 2.5597% per week. In the first example, the customer pays in full in line with the loan agreement and in the second example the customer does not repay the full amount due.

	1. Customer pays to contract				2. Customer pays to contract for four weeks, misses two payments and then pays £2.00 per week for 50 weeks and nothing thereafter				
Week	Receivable B/F £	Revenue £	Collections £	Receivable C/F £	Receivable B/F £	Revenue £	Collections £	Impairment £	Receivable C/F £
Issue	–	–	–	*100.00*	–	–	–	–	*100.00*
1	*100.00*	*2.56*	*(3.50)*	*99.06*	*100.00*	*2.56*	*(3.50)*	–	*99.06*
2	*99.06*	*2.54*	*(3.50)*	*98.10*	*99.06*	*2.54*	*(3.50)*	–	*98.10*
3	*98.10*	*2.51*	*(3.50)*	*97.11*	*98.10*	*2.51*	*(3.50)*	–	*97.11*
4	*97.11*	*2.49*	*(3.50)*	*96.10*	*97.11*	*2.49*	*(3.50)*	–	*96.10*
5	*96.10*	*2.46*	*(3.50)*	*95.06*	*96.10*	*2.46*	–	–	*98.56*
6	*95.06*	*2.43*	*(3.50)*	*93.99*	*98.56*	*2.52*	–	*(45.03)**	*56.05*
7	*93.99*	*2.41*	*(3.50)*	*92.90*	*56.05*	*1.43*	*(2.00)*	–	*55.48*
8	*92.90*	*2.38*	*(3.50)*	*91.78*	*55.48*	*1.42*	*(2.00)*	–	*54.90*
51	*6.74*	*0.17*	*(3.50)*	*3.41*	*11.00*	*0.28*	*(2.00)*	–	*9.28*
52	*3.41*	*0.09*	*(3.50)*	–	*9.28*	*0.24*	*(2.00)*	–	*7.52*
55					*3.85*	*0.10*	*(2.00)*	–	*1.95*
56					*1.95*	*0.05*	*(2.00)*	–	–
Total		*82.00*	*(182.00)*			*59.03*	*(114.00)*	*(45.03)*	

Revenue less impairment = £82.00 *Revenue less impairment = £14.00*

* *Calculated as the difference between the receivable balance of £101.08 (£98.56 + £2.52) and expected cash flows of £2.00 per week over 50 weeks discounted at the weekly effective interest rate of 2.5597% which amounts to £56.05.*

Where the customer pays to contract, the revenue of £82.00 equals the service charge on the loan. In the second example, the customer pays to contract for four weeks, misses two payments and then pays £2.00 per week for 50 weeks but then nothing thereafter. Cash collected amounts to £114.00 compared with the contractual amount due of £182.00. Revenue in this example is £59.03 and impairment is £45.03 which results in revenue less impairment of £14.00.

The above are simple examples produced to show the mechanics of how revenue and impairment within home credit works and are for illustrative purposes only. They ignore the impact of early settlement rebates on the calculation of the EIR and are not based on actual impairment rates used by the home credit business.

The impairment charge and impairment to revenue metric in CCD do not represent what is usually considered as 'bad debt'. 'Bad debt' is often deemed to be the amount of principal that is not recovered on loans made. Within the home credit business, the service charge on a loan is fixed regardless of the time taken by a customer to repay a loan. There is no penalty interest or penalty charges. Due to their personal circumstances and the variability of their income streams, home credit customers often take longer than the contracted period to repay their loans. IFRS requires revenue to be recognised on the outstanding receivables at the original EIR set at the outset. The EIR assumes that a customer pays in line with the contractual term of the loan. Therefore, when a customer misses a payment, revenue continues to be recognised at the EIR as though penalty interest was being charged to the customer even though contractually it is not. Because this revenue is never going to be charged to the customer, a corresponding impairment charge is made.

This ‘gross up’ of revenue and impairment is illustrated in the following example.

The example is based on a £100 loan with a total amount payable of £182 over 52 weeks which equates to a weekly payment of £3.50. The EIR applied to the loan is 2.5597% per week. In this example, the customer pays to contract for four weeks, misses two payments and then pays £3.00 per week for the following 56 weeks. The total amount payable of £182 is received in full but over a total period of 62 weeks instead of 52 weeks.

Week	Receivable B/F £	Revenue £	Collections £	Impairment £	Receivable C/F £
Issue	–	–	–	–	*100.00*
1	*100.00*	*2.56*	(3.50)	–	*99.06*
2	*99.06*	*2.54*	*(3.50)*	–	*98.10*
3	*98.10*	*2.51*	*(3.50)*	–	*97.11*
4	*97.11*	*2.49*	*(3.50)*	–	*96.10*
5	*96.10*	*2.46*	–	–	*98.56*
6	*98.56*	*2.52*	–	*(12.34)**	*88.74*
7	*88.74*	*2.27*	*(3.00)*	–	*88.01*
8	*88.01*	*2.25*	*(3.00)*	–	*87.26*
61	*5.78*	*0.15*	*(3.00)*	–	*2.93*
62	*2.93*	*0.07*	*(3.00)*	–	–
Total		*94.34*	*(182.00)*	*(12.34)*	

Revenue less impairment = £82.00

* Calculated as the difference between the receivable balance of £101.08 (£98.56 + £2.52) and expected cash flows of £3.00 per week over 56 weeks discounted at the weekly effective interest rate of 2.5597% which amount to £88.74.

Revenue less impairment in this example is £82.00, consistent with a customer paying to contract. However, because the customer took 10 more weeks to pay their loan, revenue increases to £94.34 and is offset by impairment of £12.34. The ‘gross up’ of revenue and impairment is therefore £12.34.

The above is a simple example produced to show the mechanics of how the ‘gross up’ within the home credit business works and is for illustrative purposes only. It ignores the impact of early settlement rebates on the calculation of the EIR and is not based on actual impairment rates used by the home credit business.