

## Supporting the Development of Private Credit Information Bureaus *IFC increases technical assistance and invests in regional credit bureau initiatives*

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Sharing information on borrower credit histories allows lenders to improve risk management and expand lending to new market segments. Correlation between existence of credit information registries and depth of credit markets is widely documented. There is also evidence that the private sector is better suited to serve the needs of lenders by providing detailed credit history information and value-added services, such as credit scoring, while public credit registries, run by bank supervisors, should focus on monitoring systemic risks.

**Rational for IFC involvement.** Consumer and small business finance is of great significance to IFC, given its substantial portfolio of mid-sized banks and commitment to increasing access to financial services for the underserved. More than 40 percent of IFC's financial markets portfolio is held in financial institutions that are doing business primarily with micro, small and medium-sized enterprises. Growing retail and SME lending requires that client banks introduce adequate risk management and loan approval processes to ensure that growth remains healthy.

The use of credit bureau information and the introduction of credit scoring can significantly reduce risks of default and enable banks to lend to new segments of the market. Thus support for the development of private credit bureaus through technical assistance and investment is a core part of IFC's work in the financial sector.

While the IFC is providing support for credit bureau development to small and big countries alike, particular attention is paid to those countries where IFC's exposure to banks is significant. In almost all of these markets, growth in retail and small business finance is outpacing commercial lending with the respective risks and constraints imposed in the case of non-existing or poor credit bureaus. Of IFC's top 10 country exposures to banks at the end of 2004, six out of 10 either did not have a credit bureau or had a credit bureau that recorded negative data only. IFC is now involved in the development of credit reporting in Russia and China and supports efforts to introduce positive information sharing in Romania and Brazil.

IFC closely collaborates with the World Bank to coordinate policy advice and joint interventions, for example in the reform of the legal and regulatory framework for credit reporting, as well as consumer education and training activities. IFC also continues to work with Project Development Facilities (PDFs) and regional development banks during technical assistance implementation and for local support.

**Technical Assistance.** IFC is managing its technical assistance for credit reporting under the Global Credit Bureau Program funded from different donors. To-date, US\$2 million have been approved in donor financing, of which about 73 percent had been committed and/or disbursed as of February 2005. Given the long development cycles for credit bureaus, effective support requires a combination of on-going support and specialized assignments. To provide the necessary on-going support, IFC has hired dedicated regional credit bureau advisors for Eastern Europe and for Latin and Central America, who work on the ground for the period of at least two years. Africa, the Middle East and Asia are currently covered on a case-by-case basis.

Credit bureau advisors work together with IFC staff to develop private credit bureaus. Key challenges in the development of credit reporting are mostly concentrated in three areas: (1) legal and regulatory issues, (ii) concerns of financial institutions about making their information available to competitors, and (iii) lack of adequate public policy in the sector.

IFC provides assistance on legal and regulatory issues in coordination with the World Bank and other donors. For example, in Ghana and in Costa Rica donor funding was used to prepare legal opinions on credit information sharing which are now used to engage government in discussions on legal reform.

To overcome lenders' unwillingness to share information, an important part of building the ground for the establishment of private credit bureaus is to explain the benefits of sharing data and the ways lenders can integrate credit bureau information into their loan approval processes. IFC has organized roundtable discussions among potential credit bureau participants in Nigeria, Egypt and Morocco, supported conferences on these issues in Kazakhstan and Russia, among others, and is currently in active consultations with large lenders in about 30 countries. IFC also provides assistance to individual institutions to develop credit scoring solutions and is working on shared scoring solutions for banks in East Africa. In countries where credit bureaus operate,

IFC focuses on the introduction of positive information, for example in Brazil and Pakistan, and the development of credit scoring, by developing a microcredit bureau score in South Africa for example.

In some countries the development of the private credit reporting industry is hampered by misguided public policy. For example, expansion of public registries to cover all retail loans issued by regulated institutions is costly and undermines private sector initiatives. Empirical research and international practice have demonstrated that private registries are better suited to serve the needs of lenders.<sup>1</sup> Public registries may play an important part in improving banking supervision and monitoring systemic risks, but they should not serve as the main information providers to commercial institutions. Mandatory collection and provision of information-- often at subsidized prices--distorts market incentives for financial institutions to develop a private registry. A case in point is the expansion of the public registry in Bulgaria, which put on hold the development of a private registry that was almost ready to start operations. Discussions of public registry expansion in Armenia make banks unwilling to commit to joining a private credit information-sharing enterprise. While the development of a public registry might appear to be an effective means to fill the gap of available credit information, in the medium to long term it undermines private initiatives and thus hurts creditors who will not have access to a broad set of credit data, including the information from non-banks that is usually collected by private bureaus. Creditors who rely on public registries will not be able to benefit from value-added services such as bureau scores, moreover, which allow them to maximize the value of credit information. At the same time, the public sector could play a very important role in supporting the development of private credit reporting by providing an adequate legal and regulatory framework, and by making information from public registries available to private sector operators as, for example, in Chile.

**Investment projects.** IFC can complement its TA work by financing the creation or expansion of private credit bureau operations. In 2002 IFC completed its first investment in a consumer and SME credit bureau, Trans Union Central America (TUCA), which is the first regional credit bureau. TUCA currently operates in Guatemala, Honduras, El Salvador and Costa Rica, and plans to expand its operations to Nicaragua by mid 2005. Managing data from several small economies within one information technology system allows economies of scales and improved efficiency and profitability for the credit bureau. Product standardization across countries in the region will also facilitate cross border financial service offerings in Central America.

Another investment project currently being considered by IFC is supporting Experian in the creation and operation of credit bureaus and the provision of value-added products and services, such as scoring and fraud detection tools, in several countries in South Eastern Europe and the Middle East. Experian is one of the leading international players in the sector with credit bureau operations in 16 countries and clients for its decision support solutions in more than 50 countries. By bringing to the table its expertise and experience in developing business in emerging markets, Experian will partner with IFC in promoting the development of needed credit information infrastructure in the target countries. Moreover, introduction of state of the art credit scoring systems will allow financial institutions to improve their underwriting processes for consumer and small business lending.

Overall, the IFC does not view investing in credit bureaus as its main role in the sector. Its primary objective is to develop credit reporting in the private sector, principally through technical assistance.

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<sup>1</sup>*Doing Business report 2004, Love and Mylenko "Credit Reporting and Financing Constraints", World Bank 2003.*