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PRIVATE CREDIT BUREAUS can improve access to credit in Vietnam

International experience shows that it is easier for businesses and individuals to borrow money in countries where credit information is readily accessible. It is believed that private credit bureaus, which are gaining in popularity worldwide, will improve small businesses' and individuals' access to credit by increasing the flow of data on loans and borrowers. This bulletin discusses the roles that private credit bureaus can play in Vietnam and the necessary operational conditions for such agencies.

Credit reporting agencies an introduction

It is clear that the information asymmetry between borrowers and lenders results in inefficient credit allocation and rationing. Lenders commonly require proof of collateral to overcome this constraint, but obtaining such evidence is problematic for many individuals and businesses, especially SMEs and new start-ups, which normally lack sufficient fixed assets that can serve as security. A much more efficient alternative for lenders is screening and monitoring a potential borrower's creditworthiness; in this case, the borrower's credit history record is the decisive factor in the granting and pricing of loans. Credit bureaus provide the systems and services that allow lenders to share and exchange information on borrowers with each other, thereby reducing the information asymmetry in the credit market. This, in turn, leads to a more efficient allocation of credit in the economy, facilitates larger lending volumes, and ultimately softens the financing constraints faced by firms as well as individuals.

In Vietnam, the concept of credit reporting is still rather new. The Credit Information Center (CIC), a public credit registry agency, was established by the State Bank of Vietnam (SBV) in the late 1990s. As of yet, there are no private credit bureaus in the country. Credit reporting is much lower in Vietnam, where only 1.1% of adults are covered, than in other countries that have private credit bureaus. For example, in Thailand credit reporting agencies cover 18.4% of adults, and in Australia the figure is 100%.¹

Private credit bureaus can significantly reduce the financing constraints faced by SMEs

Normally, central banks set up public credit registries for the main purpose of supervising banks, while market participants set up private credit bureaus to share information among lenders. As a result, public credit registries tend to focus on substantial credits that might have

systemic effects on the economy, and generally collect information only on large loan amounts. In addition, they usually collect information only from government-supervised institutions, which often results in the exclusion of non-bank financial institutions, such as leasing, financial and factoring companies, that are growing extensively. Finally, public credit agencies often provide just the current status of loans, not the payment history of borrowers.

In contrast, private credit bureaus which can either be private firms or non-profit organizations collect information on larger businesses, SMEs and individuals and on loans of any size. They provide lenders not only with potential borrowers' payment history but also with other value-added services, such as credit application processing and credit scoring tools. Therefore private sector credit bureaus are able to fulfill the lending community's requirements for information used in decision-making. A recent World Bank survey of over 5,000 businesses has found that while there is no conclusive evidence that public credit registries reduce perceived financing constraints, the existence of private credit bureaus does do so, and also improves small firms' chances of obtaining loans.² For instance, the percentage of small firms reporting financial constraints in countries without private credit bureaus is 49%, much higher than in countries that do have private credit bureaus, where it is 27%. In addition, the probability that such firms can obtain credit in countries without private credit bureaus is 28%, much lower than in countries with private credit bureaus, where the probability is 40%.

The strong market demand for private credit bureaus requires that the government undertakes timely actions to enable their operation

The rapid credit growth in recent years, especially for SMEs and individual consumers, has raised lenders' demand for credit

information to a level beyond what CIC, as a public credit registry, can satisfy. In a workshop on the development of private credit bureaus held early this year by the SBV and supported by IFC-MPDF and Visa International, over 150 local bankers agreed that Vietnam urgently needs private credit bureaus; reasons given included the fact that their demand for credit information on SMEs and individuals has exceeded CIC's capacity and also that the lack of private credit bureau services has negatively affected their businesses.

It is worth noting that credit information reporting is a very sensitive process, as it relates to not only the rights and obligations of credit institutions but also to the privacy of companies and individuals regarding their business and personal data. For many developing and transition economies, balancing these potentially competing interests is quite a challenging task, as it involves a complex set of factors, including: (i) an enabling legal framework; (ii) the buy-in of all relevant stakeholders notably the participation of all key financial institutions, (iii) a private-public partnership and broader social awareness; and, finally (iv) international know-how and expertise. For the past two years, the SBV has been studying this model and receiving advice from IFC on a strategic framework to develop private credit bureaus. It is an opportune time for Vietnam to speed up its efforts to create an enabling legal and regulatory environment for private credit bureaus.



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The "Business Issues Bulletin" provides those interested in business issues with a short summary and analysis of a particular topic affecting the business environment in Vietnam, and exposure to different opinions held by various stakeholders on the topic.

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(1) World Bank and International Financial Corporation (IFC), *Doing Business in 2006: Creating Jobs*, September 2005.

(2) Inessa Love and Natalia Mylenko, "Credit reporting and financing constraints", World Bank Policy Research Working Paper, October 2003.

Viewpoints from international financial market development experts



● Private credit bureaus would complement Vietnam's public registry because they would maintain and investigate the borrowing histories of a much broader range of potential customers. Provided that the would-be borrowers first agree, their detailed credit histories will enable financial institutions to assess risk better and determine what interest rates to charge. As such, private credit bureaus could

significantly benefit banks, borrowers and ultimately, Vietnam's economy.

Banks would benefit because private credit bureaus would warn them of borrowers who are already heavily in debt and/or have a poor credit history. This could appreciably reduce banks' risks in lending and their losses from bad loans. As far as borrowers are concerned, experience in other countries shows that once banks begin to trust the services of credit bureaus, they will give borrowers with good credit history better interest rates, and even provide loans with less or no collateral.

*Mr. Adam Sack,
General Manager of IFC-MPDF*



● While private credit bureaus help to increase credit volume and improve access to credit, they cannot operate successfully without a strong legal system that oversees the operation of credit markets as a whole and credit bureaus in particular. This is why the role of the government is extremely important. Governments can promote a supportive environment for credit bureaus by enacting and enforcing laws that ease

the sharing of credit information while also protecting the legal rights of individuals and businesses.

The relevant laws include bank secrecy regulations, data protection laws and consumer protection provisions. The two main concerns that these types of legislation must address with regard to the collection and distribution of personal data are in the areas of access and privacy. Both access and confidence in secure, protected credit information are vital to create support for credit registry systems. At the same time, through unnecessarily severe penalties and sanctions or complicated and expensive procedures, overly restricted information sharing may discourage firms from entering the credit reporting business.

According to international best practices, the key legislative elements enabling the operation of private credit bureaus include: i) allowing not just financial institutions but also retailers, telecom companies, debt collectors, utility companies, etc., to report and access credit information; ii) including both positive (loans outstanding, assets, payment behavior on accounts in good standing) and negative information (defaults and arrears); iii) maintaining information on defaults from the system once debts have been repaid; iv) storing information for a period of 5-7 years; v) guaranteeing individuals the

right to check their own information and to report back to the bureau in case of erroneous data; and vi) ensuring that there is a mechanism in place for correcting mistaken information in the bureau.

*Ms. Nataliya Mylenko, Program Officer,
Global Financial Market Development,
International Finance Corporation*



● As a public credit registry, the CIC of Vietnam is already serving part of the market. However it does not have sufficient human resources or the technical capacity to deal with a volume industry like consumer credit. There should be a model that Vietnam can consider in which the public and private bureaus work together to serve the whole industry better and each have roles and functions in financial market

development. Malaysia, where the Bank Negara Malaysia runs the public registry and where a number of private bureaus actively operate in niche markets, can serve as an example.

Private credit bureaus change the way banks do business and help banks improve both operational efficiency and ultimately, their bottom line. In the U.K. or U.S., lenders no longer tend to collect information from the borrower's application; certainly there is not much information that they can get only from the application. For example, lenders can make credit decisions in three seconds based purely on customer names and their postal codes. This is because credit bureaus hold all the information that banks need for such decisions. The banks can be confident that such data is secure (obtained in accordance with consumer privacy laws), accurate (not easily changed by other parties), and reliable (available on a consistent basis). However, credit bureaus operate on the principle of reciprocity, which means that in return for these benefits, banks must commit to providing them with accurate information. Ultimately, the quality and quantity of information supplied determines the quality and quantity of information received, so both sides have a vested interest in ensuring that the other has access to correct data.

When establishing private credit bureaus in Vietnam, there needs to be careful consideration not only of the legal framework required to enable credit bureau operations and effectively to protect consumer privacy, but also of the issue of the credit bureaus' ownership and structure. A consortium model may be appropriate for Vietnam's context. This is a model in which a number of different parties can participate in bureaus, including the most important stakeholders: i) local providers who can serve market demand on the ground; ii) technical partners such as one of the leading international credit bureaus who not only bring in technology solutions required by the bureau but also have experience in setting up, operating, managing and promoting credit bureaus; and iii) lenders, who include banks as well as other subscribers such as credit card companies, insurance companies, etc.

*Mr. Tony Lythgoe, Credit Bureau and Risk Management Advisor,
International Finance Corporation*

* All viewpoints are from the workshop "Development of Private Credit Bureaus in Vietnam" which was co-organized by the State Bank of Vietnam, IFC-MPDF and Visa International in Hanoi, January 2006.

Viewpoints from international credit bureaus



● Thailand's example is very interesting, as it illustrates how legislation can support or hinder the work of credit bureaus. Two private credit bureaus started services in early 2000, a couple of years before the Central Bank finalized the Credit Information Business Act that went into effect on March 14, 2003. During the drafting period (2000-2003), Parliament spent a great deal of time changing the law's

contents, specifically: turning the Act into a consumer protection law, tightly regulating how bureaus do business and imposing heavy criminal penalties (five to ten years in jail) on members and bureaus for small and likely mistakes.

After the law was passed, the two existing credit bureaus were faced with a number of legal issues. Both had to suspend operations for three months to undergo a compliance review and ensure that systems were in place for complying with the new law. They reopened for business only after a comprehensive consultation process between the government and international experts took place and the regulation was revised. Now credit bureaus need to follow a code of conduct to assure consumers of their privacy. With this new law, both regulators and the credit bureaus have committed to protect consumers' personal information.

*Mr. Leon Chee, Director, Credit Bureau Solutions,
Dun & Bradstreet*

● Credit cards were widely used in Hong Kong, especially between 1998 and 2001. As banks competed for a share in the market and eased their lending standards, some borrowers were able to obtain several credit cards from different banks and the credit limits they were granted far exceeded their repayment capability. As a result, there were a large number of cardholder bankruptcies and this caused banks many problems. One reason for the high number of credit card delinquencies in Hong Kong during this period was the banks' inability to accurately assess the financial position of individual borrowers. Although lenders in Hong Kong had been sharing credit data through a private credit bureau since 1985, participation in the credit bureau was not compulsory and banks did not cooperate. As a result, there was no comprehensive database of credit information.

In 1998, the banks finally reached consensus on sharing

consumer credit data, but only regarding negative information (as they were restricted by the Code of Practice on Consumer Credit Data). Positive data, including the level of debt and repayment records, could not be exchanged. The sharp increase in credit card delinquencies in 2001 highlighted the need for positive credit data sharing. In March 2002, relevant industry organizations submitted joint proposals on the issue to the Privacy Commissioner for Personal Data. After consultations, the Commissioner revised the Code to allow lenders to share positive consumer credit information from June 2003 onwards.

*Ms. Galina Ho, Senior Manager,
Sales & Marketing, TransUnion Hong Kong*



● When establishing a credit bureau a few years ago, Singapore faced the same problems that Vietnam is facing now. Should the credit bureau be public or private? What is the best way to ensure that banks share information with the bureau? It took over a year for Singapore to come up with a model in which 75% of the credit bureau was owned by a private company and 25% by the industry association; this

meant that all banks would have a stake in the bureau and thereby ensured their commitment. In the meantime, it was necessary to have the Central Bank of Singapore (MAS) behind the process to set up the bureau and help it move forward. Since the credit bureau had custody of very sensitive data, the Central Bank also played an important role in making sure that the credit bureau followed strict procedures so as to prevent data abuse and privacy violations. Now the Central Bank is more comfortable with allowing the private bureau to lead. Most of the initiatives now come from the bureau, after discussion at the Board level and consultation with the Central Bank.

The most important challenge in establishing a credit bureau is to persuade banks to share information, even though they may be aware that they all have a stake in the bureau. In the end, banks understand that running a credit bureau is not their core business, so they basically let the private credit bureau run the show.

*Mr. William Lim, Executive Director,
Infocredit Holdings Pte., Ltd.*

Viewpoints from the public financial sector



● In Vietnam there is a legal framework for credit information reporting, specifically in regulations about the exchange and provision of information services regarding monetary and banking activities among financial institutions, organizations, individuals and the SBV. The CIC was set up under this legal framework as a public registry, started operations as part of the SBV's Credit Department, and became an independent unit in 1999. CIC's main

functions include the collection, analysis, forecasting, processing and provision of information on enterprises and their monetary and banking

operations to relevant parties.

However, given that the market demand for credit and related information is growing very rapidly and that we urgently need to meet the global requirements for integrating and reporting credit information, CIC cannot work alone. Vietnam's credit information reporting industry is small and starting from a basic level. There is major informational asymmetry that negatively affects the development of our financial markets. It is estimated that there are potentially over 25 million individual customer files, credit card accounts and consumer loans, which CIC alone cannot serve. By 2010, the forecast is that CIC will only be able to satisfy only 10 million clients, of whom 500,000 will be corporate customers, and the rest individuals. It is time to consider private credit bureaus that can better serve the rest of the market. ▶

- ▶ From now to 2010, CIC intends to cooperate with private credit bureaus to better serve this high volume industry. We must closely work together to create a sound credit environment in Vietnam.

*Mr. Pham Cong Uan, Deputy Director,
Credit Information Center (CIC)*

- In recent years, Vietnam's banking sector has undergone tremendous reform and made great achievements towards regional and international integration. Credit, especially for SMEs and consumers, has demonstrated sustained growth at average rate of 20% per year. This rapid credit growth in both product diversification and volume has presented commercial banks and non-bank financial institutions with great challenges, particularly in terms of improving credit appraisal skills, speeding up credit decision making processes, and ensuring good risk management practices to maintain and improve the quality of loan assets.

By collecting and sharing credit information from and among lending institutions, the CIC, under the SBV, has significantly helped Vietnam's

banking sector improve the quality of its credit activities in terms of safety, efficiency, sustainability and risk management. However, the very fast growth of consumer credit, particularly credit cards, has raised the demand for credit information to a point where it outstrips CIC's current capacity and structure as a public credit registry.

Recently, the SBV has been receiving technical assistance from the International Finance Corporation in mapping out a strategy framework for developing private credit bureaus. The SBV is considering how to coordinate the activities of both the public credit registry and private credit bureaus so as to best serve the increasing demand of Vietnam's banking sector in a sustainable manner. However, credit information activities are a very sensitive area; they are related not only to the rights and responsibilities of credit institutions, but also to the privacy and secrecy of businesses and individuals. This is a fairly new area for Vietnam, so we need to understand and refer to international best practices as we select a model that is suitable for both our country's context and global standards.

*Mr. Phung Khac Ke, Deputy Governor,
State Bank of Vietnam*

Viewpoints from the commercial financial sector



- In Australia and New Zealand, ANZ has already been using the information from private credit information bureaus to make decisions on increasing the number and amount of loans for current clients as well as on extending loans to new clients for several years. Based on "scorecards" (information about borrowers' ages, professions, incomes, past credit status, assets and advantages), we classify clients into different groups for the purposes of

establishing appropriate credit limits.

Private credit bureaus can benefit banks in a number of ways. First, their concentration of accurate information helps banks enhance the quality of their credit services and minimize future risks of non-payable loans. Also, it is easy for banks to access this information (for example, a credit report can be downloaded from the bureau's website in just few minutes or seconds), which significantly reduces the cost of finding such data. In the future, ANZ Vietnam will develop some new products, such as car loans or housing loans. If such credit bureaus exist, the bank will not have to spend a lot of time and expense collecting information about a loan applicant from multiple sources before making a decision. Having relatively accurate and timely information on the bank's clients from such center is very useful for us.

*Mr. Chu Viet Cuong, Senior Manager
Electronic Banking Services Vietnam, ANZ*



- Visa is committed to extending the efficiencies of electronic payments to communities and economies around the world. Electronic payments reduce underground economies, bring greater transparency, and attract capital and consumers to the banking system. When coupled with the judicious use of credit, electronic payment systems can play a critical role in helping small business grow and stimulate macroeconomic growth by as

much as two percent. The development of strong private credit bureaus

is vital to that process. Credit bureaus are at the heart of sound lending practices and benefit not just lenders but also borrowers. The growth of Vietnam's economy depends largely on lenders' abilities to sustain financing while managing risks efficiently and effectively. Our experience, along with the IFC's, teaches us that while it is valuable to transfer knowledge between markets, solutions have to be sensitive to local circumstances. For this reason, we will work closely with the Vietnamese Government, regulators, banks and other stakeholders to ensure that this project delivers exactly what Vietnam needs.

*Mr. Stuart Tomlinson, Country Manager for Vietnam,
Cambodia and Laos, Visa International Asia Pacific*



- Credit cards have been present in Vietnam since 1996. However, to date there are only 100,000 credit card users. This number is very small, especially when compared to the number of users of bank cards (the majority of which are debit cards), which is about two million people. Moreover, 70% of the 100,000 credit card holders use a collateral-based credit card. The two main explanations for the slow development of the credit card industry in Vietnam are: (i)

lenders' lack of necessary information on borrowers and (ii) the collateral requirements for loans.

Private credit bureaus may help retail banking services develop further in the future. Sharing credit information is essential for this. Vietcombank commits to immediately participating in credit bureaus and for as long as they are available in Vietnam, provided that a legal framework enabling the operation of private credit bureaus is in place.

In my opinion, Vietnam can learn from the credit bureau model in Singapore, where all banks are shareholders and the central bank plays an important supporting role. This model is good in ensuring commitment from all banks in the market; as shareholders, banks will be more responsible in providing and using information. These efforts towards providing transparent and clear information will not only contribute to each bank's business development but also towards establishing a sustainable financial market.

*Ms. Nguyen Tu Anh, Director of Card Center,
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