

VISION2011

FHC&FABIO BARBOSA
MERCADO&POLÍTICA

Visões de valor para sua
decisão de negócios

Impacts of Full-File Credit Reporting

Evidence from Around the Globe

Realização

Serasa  Experian

A gente trabalha para você crescer.

Who is PERC?

PERC
RESULTS AND SOLUTIONS

A non-partisan, non-profit
policy research and development institute
devoted to increasing financial inclusion using
information solutions.

About PERC

PERC is dedicated to unleashing the power of information for asset building and wealth creation--a phenomenon we call *information led development*

Established in April 2002

- in 10th year of operation
- began as the Information Policy Institute

State, federal and international experience and capabilities in

- quantitative policy research--economic and social impact analysis
- education and outreach
- solutions and applications

Centrist, problem solving approach

About PERC

PERC is **R&D**

- Research feeds ideas for development of applications

PERC thinks like **double bottom line** firm

- ROI and social impact

All solutions must be **self-sustaining**:

- must be **in demand**
- users must be **willing to pay** for solution

Areas of Main Focus:

- Increasing access to **mainstream affordable credit** to the underserved
- Developing information solutions to development and other challenges

Impacts of Full-file and Comprehensive Credit Reporting

General Findings

Long history of investigation and study of information sharing.

- Results are full-file and comprehensive reporting:
 - **increases lending** to the private sector especially among lower social segments more than other reporting regimes; and,
 - results in **better loan performance** than segmented and negative-only reporting.
- Private bureaus with comprehensive data **increase lending** to the private sector.

General Findings

Three phases of economic investigation of information sharing in credit markets:

- **Phase 1:** Ownership structure matters - Private bureaus outperform public registries (Miller, et al.)
- **Phase 2:** Robustness of data matters - Positive and comprehensive reporting outperform negative and segmented systems (Barron and Staten, Turner, et al.)
- **Phase 3:** Participation rate matters - Growth in private sector lending is tied to the share of data that is fully reported (Turner and Varghese, et al.)

Consequences of Full-file Vs. Negative-only: US

Acceptance Rates for a Targeted Performance Level using Full-File versus Negative-Only Reporting		
Target default rate (%)	Full-file, comprehensive reporting (%)	Negative-only reporting (%)
3%	74.80%	39.80%
4	83.2	73.7
5	88.9	84.6
6	93.1	90.8
7	95.5	95

Source: John M. Barron and Michael Staten, "The Value of Comprehensive Credit Reports: Lessons from the U.S. Experience," in Margaret M. Miller ed., *Credit Reporting Systems and the International Economy*, 273-310 (Cambridge, MA: MIT Press, 2003).

Consequences of Full-file Vs. Negative-only: US

Acceptance Rates by Targeted Performance Level with Full-File versus Negative-Only Reporting (U.S. Commercial Scoring)

Target default rate (%)	Full-file, comprehensive reporting (%)	Negative-only reporting (%)
2%	41.90%	28.50%
3	49.2	40
4	55.6	47.2
5	60.4	55.5
6	63.7	60.4
7	66.4	64.1

Source: Michael Turner et al., *The Fair Credit Reporting Act: Access, Efficiency, and Opportunity* (Washington, DC: The National Chamber Foundation, June 2003).

Consequences of Full-file Vs. Negative-only: Argentina

Acceptance Rates by Targeted Performance Level with Full-File versus Negative-Only Reporting (Argentinean Loans in Excess of US\$21,000)		
Target default rate (%)	Full-file model (%)	Negative-only model (%)
3%	60.22%	49.50%
5	76.37	75.76
7	86.02	84.26
9	92.76	91.95
10	95.24	94.71
11	97.5	97.1
12	99.59	99.55

Source: Giovanni Majnoni, Margaret Miller, Nataliya Mylenko and Andrew Powell, "Improving Credit Information, Bank Regulation and Supervision." World Bank Policy Research Working Paper Series, No. 3443 (Washington, DC: World Bank, November 2004).

Consequences of Full-file Vs. Negative-only: Colombia

Acceptance Rates by Targeted Performance Level with Full-File versus Negative-Only Reporting Using Colombian Data		
Target default rate	Full-file, comprehensive reporting	Negative-only reporting
3%	10.00%	2.56%
5	41.35	5.15
7	58.82	13.6
10	73.06	54.97
12	77.8	72.26

Source: Michael Turner and Robin Varghese, *The Economic Impacts of Payment Reporting in Latin America* (Chapel Hill, NC: Political and Economic Research Council, May 2007), Table 5.

Consequences of Full-file Vs. Negative-only: Brazil

Acceptance Rates by Targeted Performance Level with Full-File versus Negative-Only Reporting (Brazilian Loans in Excess of US\$300,000)		
Target default rate (%)	Full-file model (%)	Negative-only model (%)
2%	65.08%	49.20%
3	82.27	55.84
4	91.53	84.81
5	96.23	94.36

Source: Giovanni Majnoni, Margaret Miller, Nataliya Mylenko and Andrew Powell, "Improving Credit Information, Bank Regulation and Supervision." World Bank Policy Research Working Paper Series, No. 3443 (Washington, DC: World Bank, November 2004).

Consequences of Full-file Vs. Negative-only: Equity

Effects on Acceptance Rates for a 3 Percent Targeted Default Rate between Full-file Reporting and Negative-only Reporting, by Demographic Characteristics (US Data)

	Negative-only (index = 100)	Full-file (index = 100)
Race-Ethnicity		
Caucasian, Non-Hispanic	100	121.8
African American	100	127.9
Latinos	100	136.8
All Minority	100	135.5
Gender		
Female	100	121.8
Male	100	123.0
Age		
<36	100	147.1
36-45	100	121.8
46-55	100	121.2
56-65	100	119.8
66-75	100	117.9
76+	100	119.9
Household Income (US\$)		
< 15,000	100	135.9
15,000-29,000	100	129.7
30,000-49,000	100	124.2
50,000-99,000	100	120.6
>100,000	100	117.8

Source: Michael Turner et al., *The Fair Credit Reporting Act: Access, Efficiency, and Opportunity* (Washington, DC: The National Chamber Foundation, June 2003).

Consequences of Full-file Vs. Negative-only: Equity

Results on demography using real credit files

- **Disadvantaged social segments gain greater access than others**
 - racial-ethnic minorities
 - young
 - low-income groups
- **These results were seen in US comparing full-file vs negative-only in general and full-file vs negative only (or non-reporting) of utility and telecom payment data**
- **Colombian simulations**
 - under negative-only, 33% of acceptances women
 - under full-file, 47% are women
 - under full-file, access to credit more than doubles for the young (<32)

More Information = Better Lending

Better lending decisions result from increased information sharing

- Positive data
 - Accounts (when opened/closed and types)
 - Timeliness of payments
 - Credit limits
 - Balances
- Inclusion of many sectors results in a more comprehensive credit and financial picture and increased coverage of a population
- Greater participation by data furnishers

Wider access to & fairer distribution of credit are indicators of a better functioning lending system, resulting from increased information sharing

Why Lenders Share Information with Credit Bureaus

Independent studies using credit file data from Asia, North America, and South America show:

- strong positive correlation between growth in lending to private sector and participation in credit reporting system;
 - study by Harvard and World Bank economists of 129 countries (for years 1999-2003)
 - private bureaus increase lending as a share of GDP by an estimated 20 percentage points
 - Similar PERC analysis found the same in addition to importance of data furnisher participation
- lenders experience sustainable growth in lending to new markets;
- loan portfolios perform better (impacts profits, reserves)

Why Lenders Share Information with Credit Bureaus

Positive credit reporting system has network characteristics:

- value of credit reporting system increases as number of participants increases; and
- cost of sitting on sidelines increases as growing number of competitors report customer data to credit bureau.

Lenders must overcome fear of competition. Requires leadership with vision and courage.

- practically, though, reciprocity systems limit threat of poaching
- scale of competitive challenge also shaped by whether prescreening/marketing permitted

Movement Toward Full-File Reporting

Moved Toward Full-File 2007-2010 (N=15)



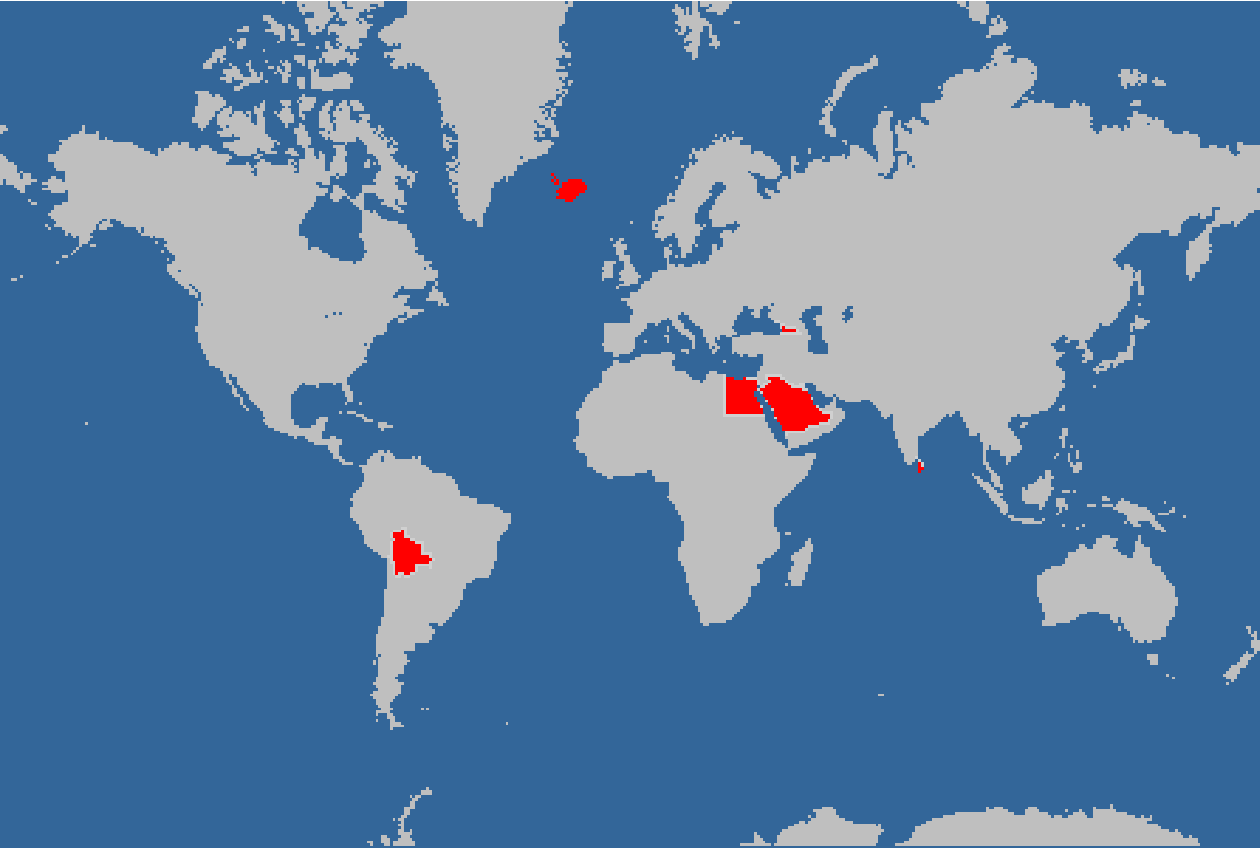
- Albania
- Brazil
- Croatia
- Georgia
- Ghana
- Kenya
- Latvia
- Morocco
- Russian Federation
- Tunisia
- Uganda
- Ukraine
- United Arab Emirates
- Uzbekistan
- Zambia

Moved Toward Full File 2004-2010 (N=30)



- Albania
- Bahrain
- Belarus
- Brazil
- China
- Costa Rica
- Croatia
- Czech Rep.
- Egypt
- Georgia
- Ghana
- India
- Kenya
- Kosovo
- Latvia
- Morocco
- Nigeria
- Panama
- Pakistan
- Qatar
- Russia
- Rwanda
- Saudi Arabia
- Slovak Rep.
- Sri Lanka
- Tunisia
- Uganda
- UAE
- Uzbekistan
- Zambia

Changed to Legally Include Retailers/Utilities 2007-2010 (N=9)



- Bolivia
- Egypt, Arab Rep.
- Georgia
- Iceland
- Kuwait
- Papua New Guinea
- Saudi Arabia
- Sri Lanka
- Trinidad and Tobago

1% per capita GDP or lower Loan Floor, 2007-2010 (N=25)



- Albania
- Armenia
- Azerbaijan
- Belarus
- Bulgaria
- Croatia
- Egypt
- Ghana
- Indonesia
- Kenya
- Mauritius
- Montenegro
- Morocco
- Mozambique
- Oman
- Papua New Guinea
- Russian Federation
- Rwanda
- Sri Lanka
- Syrian Arab Republic
- Tunisia
- Uganda
- Ukraine
- UAE
- Uzbekistan
- West Bank and Gaza
- Zambia

Also largely accounted for by expansion of credit reporting into microlending

Expansion of Consumer Rights of Access 2007-2010 (N=27)



- Albania
- Belarus
- Colombia
- Croatia
- Egypt
- Georgia
- Guatemala
- Honduras
- Indonesia
- Iran
- Kenya
- Kyrgyz Rep.
- Macedonia
- Mauritius
- Morocco
- Russian Federation
- Rwanda
- Serbia
- South Africa
- Sri Lanka
- Tunisia
- Uganda
- Ukraine
- United Arab Emirates
- Vietnam
- Yemen
- Zambia

Some like Egypt as part of comprehensive CR development, others like Indonesia as registries become oriented towards risk assessment

Including Firms as Well as Individuals 2007-2010 (N=10)



- Ghana
- Greece
- India
- Montenegro
- Papua New Guinea
- Russian Federation
- Syrian Arab Republic
- Uganda
- Uzbekistan
- Zambia

Examples of Impact of Shift to Full-file Reporting

Hong Kong: information sharing a response to rising credit card bankruptcies

- Bankruptcy filings rose from 893 in 1998 to 4,606 in 2000 to 25,328 in 2002.
- Opened credit bureau with positive information 2002.
- Info sharing reveals large numbers servicing debt with debt.
- Bankruptcies spiked as lenders became increasingly aware of borrowers using loans to service other loans.
- Two-year recovery time--but lending is now broader, deeper, and more sound.

But such patterns are not identical across economies that shift to full-file reporting

Examples of Impact of Shift to Full-file Reporting

ECUADOR'S FINANCIAL SYSTEM CRISIS 1990's

- Reckless lending characterized by loans to 'ghost' clients, personal relations, dummy corporations
- Central bank concerned, incentivizes with Basel Committee's 3rd pillar on reserve provisioning
- Financial institutions bad risk assessment techniques consequences:

Liquidity shortage

Accumulation of structural problems

Lack of good administration

Weak supervision

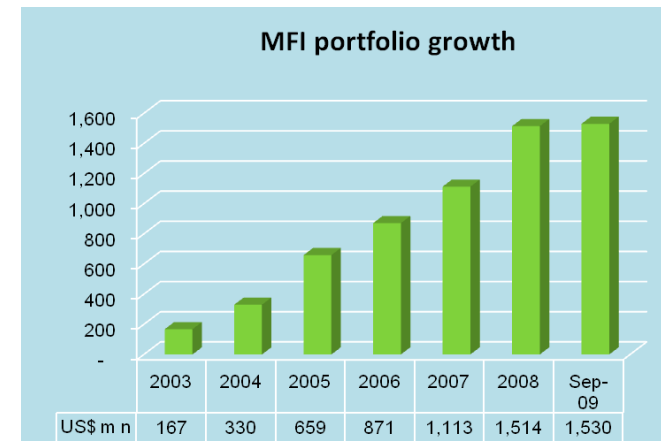
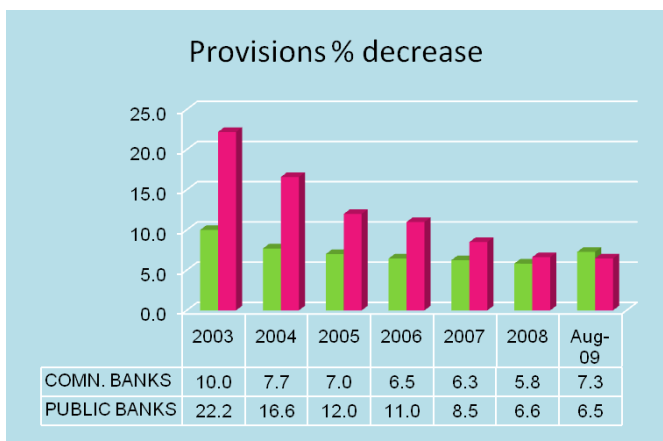
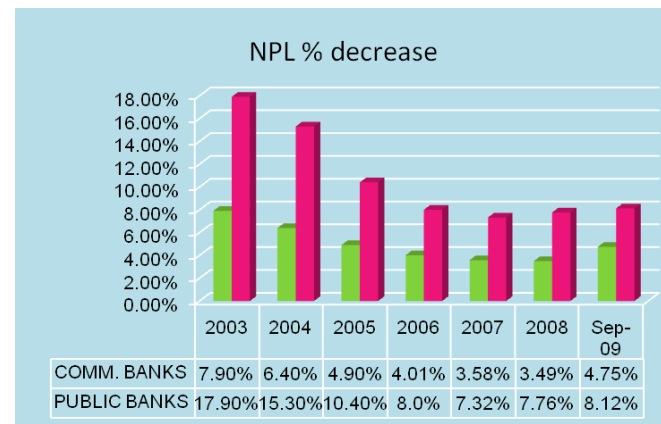
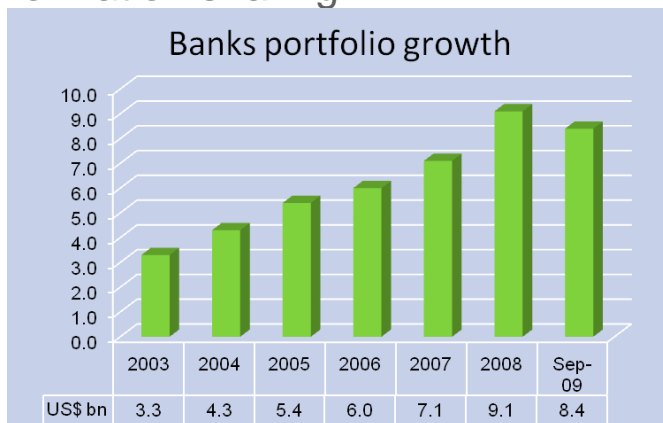
Macroeconomic chaos

- US\$ exchange rate from 6.7 to 19.8 in one year, in a market where 80% of transactions were in US\$!!

Examples of Impact of Shift to Full-file Reporting

ECUADOR'S FINANCIAL SYSTEM POST-PCB

- Beginning in early 2000's, Ecuador with help of IFC enacts credit reporting reform (culminated in 2005 law) and begins implementation of bureaus → better performance as banks take up information sharing



Examples of Shifts to Full-file Reporting

Mandatory full-file reporting:

China

Ecuador

Morocco

Kenya (negative only data mandated, full file encouraged)

Russia

Mandatory use:

Ecuador

Morocco

Mexico

Russia

Other Benefits of Full-File Reporting

Data Security Issues

All else being equal, the fact of more data being “out there,” that is, in more databases, increases the chances of data in unauthorized hands.

BUT all else is NOT equal: more data also available to fight identity theft.

- Negative-only data is events based and not good at identifying fraud until well after the fact
- Payment patterns and account information available via positive data helps identify fraudulent activity.
- Truth databases to verify identity and simply to identify fraud.

Data Security Issues: The Role of Disclosures

But most importantly, the reporting of new account information to a centralized third party allows a data subject to review regularly what, if any, new accounts have been opened in her/his name.

Free disclosures serve as instruments to reduce ID theft and ID fraud. Key is to engage the data subject

Declining number of ID theft cases and declines in total losses in recent years in US

Data Quality Issues: More Data Can Mean Better Data

Two ways in which more, positive data can improve data quality:

1. Positive systems are more likely to be automated, i.e., less manual and therefore less human error
2. Positive data—like account balances, credit limit data, etc.—allow for internal tests of consistency

Bureaus should institute tests as they acquire more, positive data

Value-Added Products

Positive reporting witnesses new value added services opportunities. More consumer information means more potential products and tools

But the new data takes time to gather, test and deploy

Disincentive to continue developing tools based on older limited information, leads to transition phase to new tools

The new products will take some time to be brought to market and optimized

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