



The Western Hemisphere Credit & Loan Reporting Initiative (WHCRI)

Issues Related to Public and Private Databases relevant for the Credit Reporting Industry

Evaluation Workshop

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Strengthening Financial Sectors

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Content

- **Public Credit Registries (PCRs)**
 - What they are
 - Their objectives
 - Role in the CRS & interaction with PCBs
- **Other Public and Private Databases**

What they are?

- Credit information registries
 - databases with information on **borrowers of the financial system**
- operated by the **Central Bank or Bank Superintendency.**
- reporting is in general mandatory.
- their primary purpose is in general **bank supervision. Also.**
 - bank-prudential regulation
 - macroeconomic policy and control
 - competition
 - credit reporting



Purposes: bank supervision

- Support on-site inspections and off-site monitoring of credit risk
 - facilitates supervisory procedures
- Allows supervisors to.
 - construct indicators for individual banks and peer groups.
 - perform descriptive analysis of each banks' loan portfolio.
 - extract samples of the borrowers to be revised at the institutions. allowing to focus the sample in specific borrowers. regions or products.

Purposes: bank supervision

- Allows supervisors to monitor.
 - banks rating/scoring systems or the correct application of classification rules
 - validating them.
 - comparing the same borrower in different banks.
 - observing the deterioration of a bank's portfolio relative to other banks.
 - quality of banks' portfolios: static and dynamic
 - evaluate credit policies
 - connected lending
 - largest borrowers of the financial system



Purposes: bank supervision

- excessive concentrations of credit and risk
- the adequacy of banks' provisions and capital
- Induces banks to organize their information systems
- Permits banks to accurately assess the quality and risk of their loan portfolio
- Facilitates their compliance with prudential regulation



Purposes: bank supervision

- PCR data can be used to analyzing the credit risk profile of a bank's portfolio with.
 - scoring models and transition matrices (individual risk)
 - portfolio credit risk models (CreditRisk+, IRB, etc.)
- Those techniques provide economic measures of expected & unexpected losses useful to.
 - assess the degree of coverage of provisions and capital requirements
 - perform stress tests
- Basel II

Purposes: bank supervision. Example



- Carey. M.
 - “Credit Risk in Private Debt Portfolios”. The Journal of Finance. Vol. LIII. No. 4. August 1998.
 - “A Guide to Choosing Absolute Bank Capital Requirements”. Journal of Banking & Finance. 26. 2002
- Majnoni G., M. Miller y A. Powell
 - “Bank Capital and Loan Loss Reserves Under Basel II: Implication for Latin America and Caribbean Countries”. World Bank. mimeo. 2004.

Purposes: bank supervision. Example



- Resampling-based Monte Carlo simulation
- Mechanics
 - take a sample of **N** obligors
 - repeatedly resample with replacement samples **n** (**<N**)
 - compute loss rate in each simulated sample
 - approximate unknown loan loss distribution with resampled distribution
 - compute mean loss rate. and loss rate for relevant percentiles (i.e. 99.9%)
 - benchmark prudential regulation.

Purposes: bank supervision. Example

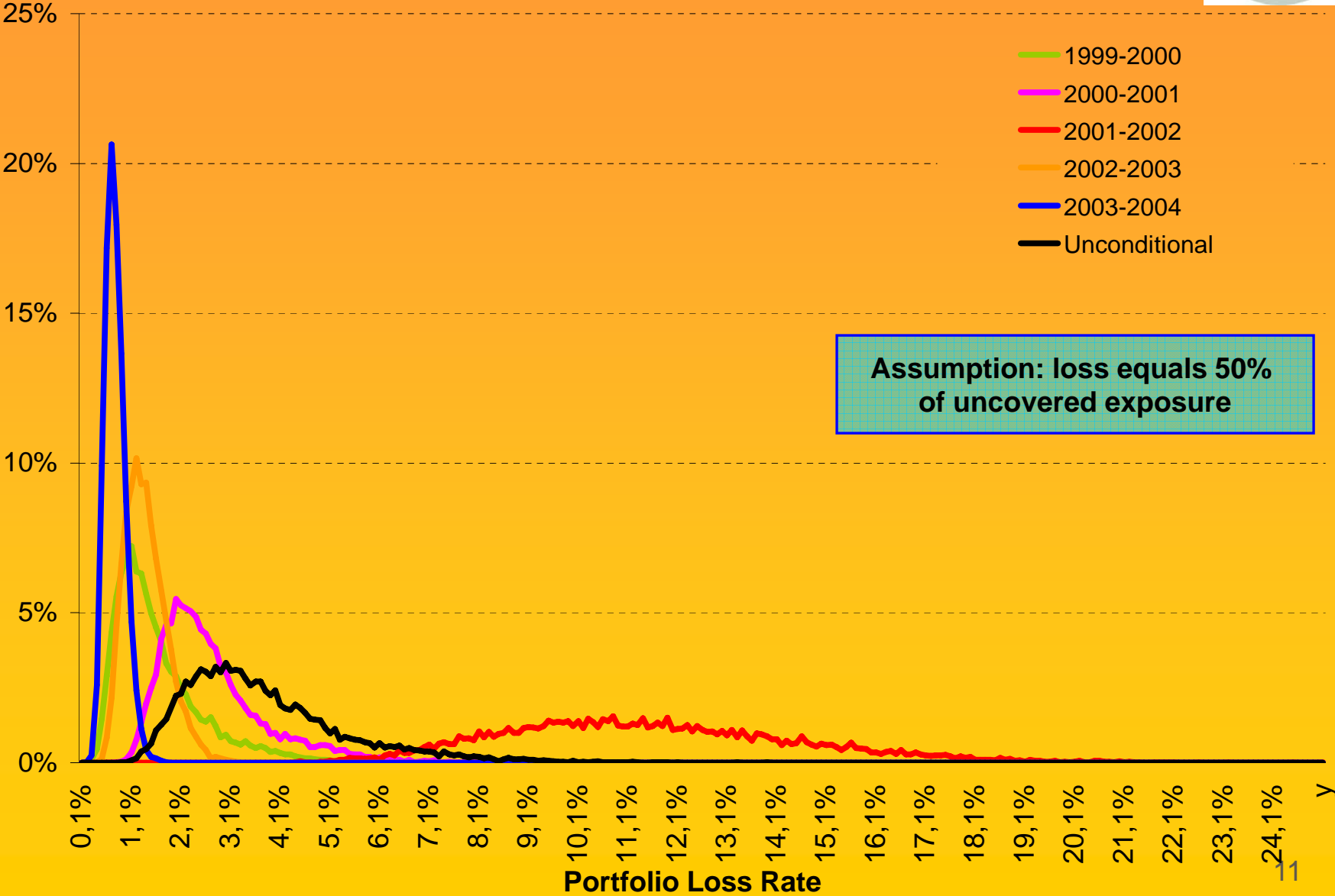


Large Retail Banks: Corporate Obligors

Period	Median	EL	95th	99th	99.9th
1999 – 2000	2.0%	2.3%	4.2%	5.5%	7.4%
2000 – 2001	3.5%	3.8%	6.4%	7.9%	9.6%
2001 – 2002	13.1%	13.4%	19.0%	21.5%	24.0%
2002 – 2003	1.8%	1.9%	2.7%	3.2%	3.9%
2003 – 2004	0.8%	0.8%	1.2%	1.5%	1.8%
Unconditional	4.3%	4.7%	8.4%	10.5%	12.8%

Assumption: Loss equals 50% of debt

Purposes: bank supervision. Example



Purposes: bank regulation

- Assists in drafting and modifying the prudential regulation regarding.
 - borrowers' risk classification
 - loan loss provisions
 - capital requirements for credit risk
 - concentration and connected lending
- Can be used in developing benchmark (supervisory) rating systems
- Basel II



Purposes: credit reporting

- Some PCR's have a direct role in the CRS producing "credit reports".
 - on-line queries and batch requests
- Main features.
 - limited to bank financings
 - limited to reporting institutions
 - basic services
 - limited resources
 - negative information summarized by risk classification and amounts past due
 - floor for reporting

Purposes: developing the PCB market



- PCR can reduce entry costs into the PCB market. making a set of basic credit information available to eligible PCBs.
 - PCBs would compete adding additional information and developing value-added services.
 - the PCR could redirect its services towards its natural purposes: supervision & regulation.
- PCR can solve coordination problems when creditors refuse to “first-move” in sharing positive data.
- or upon misleading interpretations of bank secrecy.

Purposes: develop the PCB market – expected benefits



- By playing this subsidiary role in the CRS. expected outcomes:
 - more transparency and information in the credit market. with all its implications (less moral hazard. adverse selection and over-indebtedness. and easier acces to credit).
 - more efficient allocation of resources
 - PCR: supervision
 - PCB: credit reporting
 - better PCB services: reports. scorings. Basel II. etc.

Purposes: economic policy

- Useful information to understand the tendency of credit in the regulated financial sector:
 - number of borrowers: firms (SME and corporate) and individuals.
 - number of credits in each type of credit.
 - average interest rate and maturity.
 - credit by geographic region and business sector.
 - access to credit & over-indebtedness.

Other considerations

- Cost of technology to handle large volumes of data (hardware and software)
- Cost of human resources needed to handle the data (validations)
- Regulatory overkill: the cost of burdensome reporting demands for banks vs. once-and-for-all catch up.
- The lower the floor, the larger the size of the PCR
 - should be set balancing its objectives and the abovementioned costs.

Considerations regarding their feasibility



- Many countries don't have a PCR
- PCRs and PCBs can coexist

Region or Economy	Legal Rights Index	PCR coverage (% adults)	PCB (% adults)
OECD	6.3	8.4	60.8
Latin America & Caribbean	4.5	7.0	27.9
East Asia & Pacific	5.0	3.2	10.1
Europe & Central Asia	5.5	1.7	9.4
Middle East & North Africa	3.9	3.2	7.6
Sub-Saharan Africa	4.2	1.5	3.8
South Asia	3.8	0.1	1.3



Other public and private databases relevant for the CRS

- Rejected cheques databases
 - relevant in countries where are used for short term financing,
 - particularly by SMEs,
 - usually kept/operated by CB or BS.
- Balance-sheet databases
 - useful to assess corporate obligors,
 - kept by CB or BS, chambers of commerce, stock exchanges, departments of the public administration (s.a. firms' superintendency).



Other public and private databases relevant for the CRS

- Collateral registries
 - real estate and vehicles (automobiles, vessels, aircraft)
 - contain information of property and charges
 - which complements a borrower's "human collateral".
- These registries may be more or less efficient
 - possibility to perform remote on-line queries
 - information/certificates delivered on-line
 - the output may be a scanned image or typed data
 - interconnection of departmental/provincial registries
 - this allows to query only once across the country
 - is crucial when on-line queries are not possible



Other public and private databases relevant for the CRS

- This data is,
 - useful in the credit granting process,
 - useful in handling and prosecuting default obligors,
 - and otherwise costly to obtain (time and \$).
- Streamlining access to this data should at least,
 - facilitate a borrower's capacity to secure credit (access to credit),
 - reduce banks' administrative costs (hiring of attorneys to get this data, etc.),
 - which may be more burdensome for smaller banks.



Other public and private databases relevant for the CRS

- Other important databases
 - Civil Registry
 - marital status
 - IDs issuer
 - importance of a unique and unequivocal identification of individuals,
 - difficult to forge.
 - Court records (Civil & Commercial)