Getting credit

Doing Business measures 2 types of institutions and systems that can facilitate access to finance and improve its allocation: credit information registries or bureaus and the legal rights of borrowers and lenders in secured transactions and bankruptcy laws (figure 1). These institutions and systems work best together. Information sharing helps creditors assess the creditworthiness of clients (though it is not the only risk assessment tool), while legal rights can facilitate the use of collateral and the ability to enforce claims in the event of default.

The 2 types of institutions are measured by 2 sets of indicators. The first set of indicators analyzes the legal framework for secured transactions by looking at how well collateral and bankruptcy laws facilitate lending. For example, does the law allow companies to use future crops as collateral? Does the collateral need to be described in detail in the loan agreement, or is a general description allowed? Do secured creditors have priority rights to the collateral in a bankruptcy procedure?

The second set of indicators looks at the coverage, scope and quality of credit information available through public credit registries and private credit bureaus. For example, do retailers or utility companies as well as financial institutions share credit information with public or private registries? Are data on both firms and individuals distributed in credit reports?

Rankings on the ease of getting credit are based on the sum of the strength of legal rights index and the depth of credit information index (table 1).

FIGURE 1 Do lenders have credit information on entrepreneurs seeking credit? Is the law favorable to borrowers and lenders using movable assets as collateral?

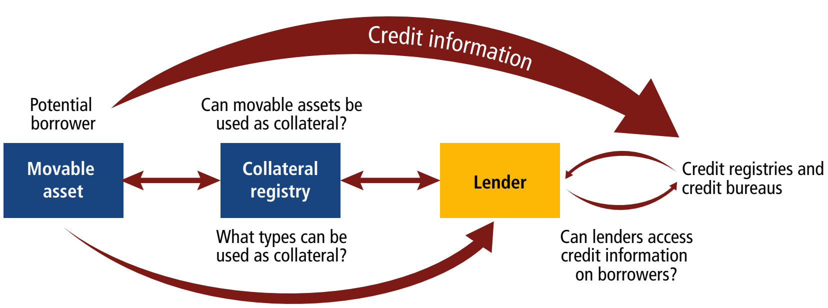


TABLE 1 Where are legal rights and credit information systems strong—and where not?

Strongest	RANK	Weakest	RANK
Malaysia[a]	1	Congo, Dem. Rep.	174
United Kingdom[a]	2	Iraq	175
South Africa[a]	3	Syrian Arab Republic	176
Hong Kong SAR, China[b]	4	Tajikistan	177
New Zealand[b]	5	Djibouti	178
United States[b]	6	Eritrea	179
Latvia[b]	7	Madagascar	180
Australia[c]	8	São Tomé and Príncipe	181
Bulgaria[c]	9	Venezuela, RB	182
Singapore[c]	10	Palau	183

Note: Rankings on the ease of getting credit are based on the sum of the strength of legal rights index and the depth of credit information index. See the data notes for details.

a. Malaysia, the United Kingdom and South Africa are tied in the rankings.

b. Hong Kong SAR, China; New Zealand; the United States; and Latvia are tied in the rankings

c. Australia, Bulgaria, and Singapore are tied in the rankings.

Source: Doing Business database.

LEGAL RIGHTS

In recent years access to finance has been considered one of the main obstacles to business in Africa, particularly for small and medium-size enterprises.[1] The Organization for the Harmonization of Business Law in Africa (OHADA) is doing something about it. After 3 years of debate and consultation with numerous agencies—including Juriscope, the World Bank Group, the Fondation pour le Droit Continental and the United Nations Commission on International Trade Law—the organization's council of ministers adopted amendments to the Uniform Act on Secured Transactions in December 2010. Among the objectives are to make the legal framework in the 16 member states more conducive to lending activities.[2]

The amended act allows for the creation of both possessory security interests (where the creditor has possession of the collateral) and nonpossessory security interests (where the debtor has possession) in all types of movable property (such as equipment, machinery and receivables) while harmonizing the legal framework in which they operate. That means greater legal protection for lenders in case of nonpayment. It also means that borrowers can use a broader range of assets as collateral, allowing them to obtain loans on better terms. With uniform implementation across all member states in the coming years, the changes could have a real impact on access to finance for businesses in those 16 African countries.

WHY DO SECURED TRANSACTIONS REGULATIONS MATTER?

Movable assets, not land or buildings, often account for most of the capital stock of private firms and an especially large share for micro, small and medium-size enterprises. In the developing world 78% of the capital stock of businesses is typically in movable assets, and only 22% in immovable property.[3] In economies with a modern secured transactions system, these movable assets could easily be used as collateral. But in most developing economies movable property would probably be unacceptable to lenders as collateral—either because the law does not recognize nonpossessory interests in movable collateral or because it does not provide sufficient protection for lenders accepting it. This constraint matters. Research shows that in developed economies borrowers with collateral get 9 times as much credit as those without it. They also benefit from repayment periods 11 times as long and interest rates up to 50% lower.[4]

Doing Business measures the legal rights of borrowers and lenders in secured transactions (or collateral) laws and bankruptcy laws—to describe how well these laws facilitate lending (table 2). A modern secured transactions system provides for the use of security interests in all types of movable assets—whether tangible or intangible, whether present, after-acquired or future assets, and wherever located—including both possessory and nonpossessory interests.[5] A modern legal framework for secured lending also establishes clear priority rules to resolve conflicting claims between secured creditors when a debtor defaults, whether in a bankruptcy procedure or not. One effective way to establish priority rights is to record the security interest in a centralized collateral registry.

TABLE 2 Who has the strongest legal rights for borrowers and lenders—and who has the weakest?

Strength of legal rights index (0–10)			
Strongest		Weakest	
Hong Kong SAR, China	10	Cape Verde	2
Kenya	10	Eritrea	2
Kyrgyz Republic	10	São Tomé and Príncipe	2
Latvia	10	Timor-Leste	2
Malaysia	10	Bolivia	1
Montenegro	10	Djibouti	1
New Zealand	10	Palau	1
Singapore	10	Syrian Arab Republic	1
South Africa	10	Timor-Leste	1
United Kingdom	10	West Bank and Gaza	1

Note: The rankings reflected in the table on legal rights for borrowers and lenders consider solely the law. Problems may occur in the implementation of legal provisions and are not reflected in the scoring. See the data notes for details.

Source: Doing Business database.

Creditor rights and access to finance

Research has shown that both legal protection for creditors and institutions for sharing credit information are associated with higher ratios of private credit to GDP. In developing economies with poorly functioning legal systems, credit markets might depend only on credit information sharing. But in developed economies with effective systems of bankruptcy, creditor rights can play a greater role.[6] Strong creditor rights expand the availability of loans. One reason is that when lenders have better legal protection during bankruptcy and reorganization of the debtor, they become more confident about the return of their investment in cases of default and therefore more willing to extend credit on favorable terms.

Legal and institutional differences may also shape the ownership and terms of bank loans around the world. Research finds that where creditor protection is stronger, loans have more concentrated ownership, longer maturities and lower interest rates.[7] Similarly, where secured creditors have priority over unsecured ones, the recovery rate for loans tends to be higher and the risks for secured creditors lower.[8] And some studies find that creditor rights can help prevent some effects of an economic crisis, since weak creditor protection and weak enforcement make credit markets more volatile.[9]

Legal reform, enforcement and economic growth

Reforming the legal framework for secured transactions can affect the behavior of lenders. Studies show that banks tend to increase their lending after amendments of collateral laws.[10] But for a legal reform to have a real impact, enforcement of the rights stipulated in laws needs to be possible in practice. The enforceability of contracts matters for the structure and pricing of loans.[11] Where enforcement of property rights is weak, lenders tend to offer short-term credit as a way to protect themselves from debtor behavior such as defaults.[12]

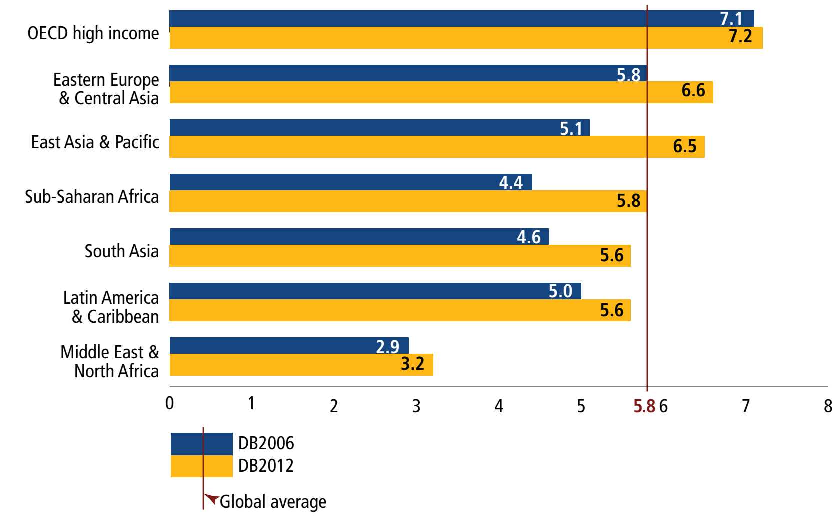
Secured transactions reforms are strengthening the legal rights of borrowers and lenders in economies around the world (figure 2). In Mexico secured lending picked up after reforms to its secured transactions system, as reflected in an increase in the lending activity recorded at the registry. The country introduced successive changes in the past 10 years to improve the system. The Law on Negotiable Instruments and Credit Operations was amended twice, in 2000 and in 2003, to introduce modern types of security interests. And a nationwide registry for movable collateral was created in October 2010. In the first 6 months of the registry's operation the number of filings almost tripled compared with the same period before the reform, and the registered loans amounted to a total of $70.9 billion in financing for Mexican firms.[13] By lowering the fees associated with registering security interests, the reform also led to savings for borrowers, estimated at $1.41 billion over the 6-month period.

Honduras enacted a new secured transactions law and launched a new collateral registry, which became operational in March 2011. The number of filings is encouraging. During the first 4 months of operation there were 1,689 filings, almost 3 times as many as in Guatemala during an entire calendar year—an impressive record considering that Honduras has a considerably smaller economy. Most filings relate to vehicles. But 19% involve commercial assets (and thus commercial loans), such as accounts receivable, retail and wholesale inventories, and agricultural, commercial, professional and industrial equipment. The low value of some of these assets used as collateral suggests growth in secured credit for micro and small businesses.[14]

Saudi Arabia continues to strengthen access to finance. In 2010 it amended its commercial lien law, improving its legal framework for secured transactions and providing for the creation of a unified lien registry. Saudi Arabia is now transferring information from the different existing registries to the new registry, which along with a unified database will soon be available to users.

FIGURE 2 East Asia & Pacific and Sub-Saharan Africa strengthened legal rights of borrowers and lenders the most

Average strength of legal rights index (0–10)

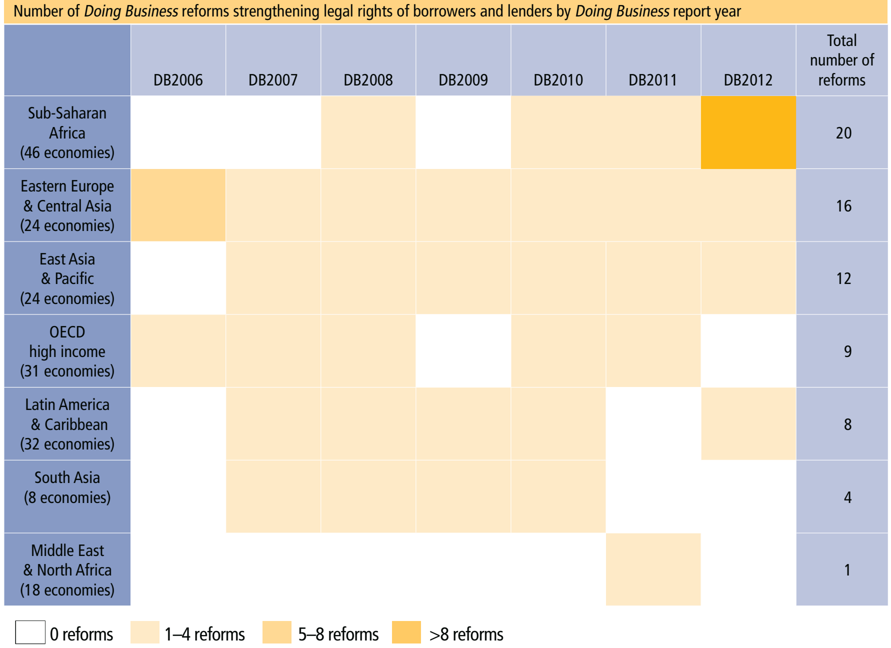


Note: The data sample for DB2006 (2005) includes 174 economies. The sample for DB2012 (2011) also includes The Bahamas, Bahrain, Brunei Darussalam, Cyprus, Kosovo, Liberia, Luxembourg, Montenegro and Qatar, for a total of 183 economies. DB2006 data are adjusted for any data revisions and changes in methodology and regional classifications of economies.

Source: Doing Business database.

FIGURE 3 Sub-Saharan Africa takes the lead in reforms providing stronger legal rights

Number of *Doing Business* reforms strengthening legal rights of borrowers and lenders by *Doing Business* report year



Note: An economy can be considered to have only 1 *Doing Business* reform per topic and year. The data sample for DB2006 (2005) includes 174 economies. The sample for DB2012 (2011) also includes The Bahamas, Bahrain, Brunei Darussalam, Cyprus, Kosovo, Liberia, Luxembourg, Montenegro and Qatar, for a total of 183 economies.

Source: Doing Business database.

WHO REFORMED SECURED TRANSACTIONS LAWS—AND WHAT HAS WORKED?

In the past 7 years *Doing Business* recorded 70 reforms strengthening the legal rights index, in 60 economies (figure 3). In 2010/11, 23 economies had such reforms, 16 of them African economies benefiting from the amendments to the Uniform Act on Secured Transactions (table 3).

Implementing a new secured transactions law and its corresponding collateral registry takes around 3 years on average. And the change may not have a noticeable economic impact right away. As with any legislative change, that may take some time—because the impact depends on users' awareness and adoption of the new mechanism. Yet a sound secured transactions system sets the stage for future benefits.

Through experience with collateral reforms in economies around the world, a number of good practices have evolved. Some have been used to develop model laws and guidelines, such as the Inter-American Model Law on Secured Transactions (box 1).

Allowing out-of-court-enforcement

Creditors are unlikely to extend loans secured by collateral if they must rely on long, costly and burdensome court proceedings to enforce their rights in case of a default. Quick enforcement is particularly important for movable property, which depreciates over time. One way to ensure quick enforcement is to allow parties to a security agreement to agree to out-of-court enforcement at the time the security interest is created. In this approach the security agreement is essentially considered to be an execution deed, allowing the secured creditor to seize the collateral or ask a nonjudicial official to do so if the debtor contests the enforcement.

BOX 1 Bringing Latin America and the Caribbean in line with international good practice

The Organization of American States introduced the Inter-American Model Law on Secured Transactions in 2002. Since then 2 economies have adopted new secured transactions laws largely inspired by the model law—Guatemala (2008) and Honduras (2010). Others have followed a piecemeal approach by introducing successive legal reforms, such as Mexico (2000, 2003, 2010), or adopted just parts of the model law, such as Peru (2006)—with varying degrees of success. In 2010 Chile adopted new pledge registry regulations. These implemented a 2007 law that repealed earlier regulations on pledges and created a centralized registry. This change is consistent with the model law, though more remains to be done.

The momentum appears to be continuing. El Salvador has a new law in the draft stage, and Colombia and Costa Rica plan secured transactions reforms in the near future.

TABLE 3 Who strengthened legal rights of borrowers and lenders in 2010/11—and what did they do?

Feature	Economies	Highlights
Expanded range of revolving movable assets that can be used as collateral	Chile; Georgia; Liberia; OHADA member economies	The amended OHADA Uniform Act on Secured Transactions allows the creation of possessory and nonpossessory security interests on all types of movable property, present and future. It also harmonizes the legal framework for pledge mechanisms and introduces new types of security interests such as pledge of financial securities and the transfer of professional debts as security.
Allowed out-of-court enforcement of collateral	Honduras; OHADA member economies	In Honduras a new law allows out-of-court enforcement of collateral upon default as long as the parties have agreed to this. The parties also need to agree to the method of enforcement.
Created a unified registry for movable property	Chile; Honduras; Mexico; Tonga	In Honduras a new unified collateral registry became fully operational.[a] Users can perform online searches for registered liens by the debtor's name.
Allowed a general description of debts and obligations	Tonga	In Tonga a new secured transactions law permits secured obligations to be described specifically or in general terms.[b]
Gave priority to secured creditors' claims outside bankruptcy procedures	Tonga	In Tonga the new secured transactions law establishes priority for a security interest over the rights of a lien holder unless a notice of those rights is registered before the security interest is perfected or before a notice covering the collateral is registered and a security agreement is signed by the debtor.

a. Accessible at http://www.garantiasmobiliarias.hn.

b. The new law came thanks to the last of a series of secured transactions reforms sponsored by the Asian Development Bank in East Asia and the Pacific.

Source: Doing Business database.

TABLE 4 Good practices around the world providing strong legal rights for borrowers and lenders

Practice	Economies[a]	Examples
Allowing out-of-court enforcement	123	Australia; India; Nepal; Peru; Russian Federation; Serbia; Sri Lanka; United States
Allowing a general description of collateral	91	Cambodia; Canada; Chile; Nigeria; Romania; Singapore; Vanuatu; Vietnam
Maintaining a unified registry	68	Bosnia and Herzegovina; Guatemala; Honduras; Marshall Islands; Federated States of Micronesia; Montenegro; New Zealand; Romania; Solomon Islands

a. Among 183 economies surveyed.

Source: Doing Business database.

This has the added benefit of reducing dependence on the courts and thus freeing up court resources.

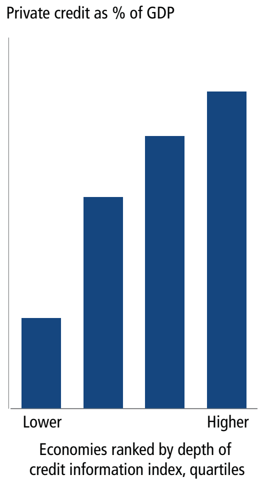
Today 123 economies allow some sort of out-of-court enforcement (table 4). But not all extrajudicial procedures are efficient. In some economies, for example, the law requires notarization of the agreement. This can protect unsophisticated debtors from abusive creditors. But if not managed well, notarization might also imply an added cost for credit. In other economies the law overprotects the debtor, making the procedure expensive and unappealing to secured creditors. When legal reform introduces a system of out-of-court enforcement, it needs to strike the right balance—to protect the rights of all those affected, including the debtor and other creditors. In the past 7 years *Doing Business* has recorded 39 legal reforms in this area.

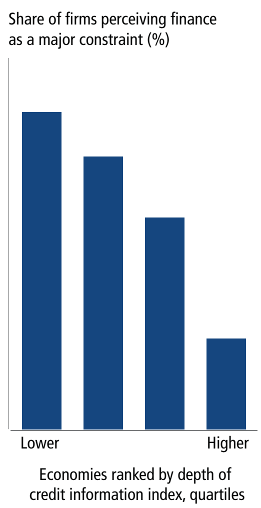
Allowing a general description of collateral

Some collateral laws require a specific description of the assets in the security agreement. This increases transactions costs when revolving assets such as inventory are used as collateral—because every time inventory is purchased or sold, the security agreement needs to be updated and perhaps even reregistered. Allowing a general description of the collateral makes security agreements more flexible and increases access to finance.

Laws providing the most flexibility allow security interests in all types of movable property and permit a generic description of the assets to secure a loan as long as these assets are identifiable—for example, allowing the contract to stipulate as the collateral "inventory of general merchandise as of [date] and for [amount]." Such contracts typically obligate the debtor to maintain the same aggregate value of inventory and the same type of goods. For nonpossessory security interests to be effective, the debtor needs total freedom to use the assets as long as proper care is taken to preserve their commercial value. Today 91 economies allow a general description of collateral in a single category and in combined categories.

FIGURE 4 More credit information is associated with more credit and lower perceptions of finance as a constraint





Note: Relationship is significant at the 5% level after controlling for income per capita.

Source: Doing Business database; World Bank, World Development Indicators database (2010 data); World Bank Enterprise Surveys (2010 data).

Maintaining a unified registry

Before accepting collateral, creditors need an effective way to find out whether the potential borrower has already granted a security interest in the collateral and, if so, what priority those rights have. A central collateral registry—unified geographically and recording interests in all types of movable assets—supports the use of movable collateral to secure loans. If registries are not unified across regions, a creditor will have no way of knowing whether a security interest in an asset has already been registered in another jurisdiction. And a need to search multiple registries increases transactions costs. But where registries are unified and computerized, a creditor can immediately check all the registries in an economy from one location, by searching the debtor's name.

Today 68 economies have some sort of centralized registry for movable property used as collateral by companies. But only 15 of these can be characterized as modern, notice-based collateral registries. These registries offer online access for registration and searches, register all types of encumbrances, establish clear parameters for priority and maintain a central database searchable by the debtor's name or a unique identifier. Once registered, security interests immediately have effect against third parties.

CREDIT INFORMATION

In Bhutan many small and medium-size businesses have difficulty accessing formal credit and must rely on personal funds. Women, who are more likely to run small businesses, face the biggest hurdles.[15] But the situation is starting to improve thanks to a new credit information bureau that started operating in 2009. Imagine Charlotte, a young Bhutanese entrepreneur who runs a small confectionery business in Thimphu. She wants to expand her profitable catering business and has new customers lined up—but she needs more funds. Charlotte approaches Sonam, a loan officer at her bank, for a line of credit. Because of the new bureau, Sonam can review her credit history—and determine that Charlotte qualifies for a low-interest loan program for small businesses.

A credit history is no substitute for risk analysis. But when banks share credit information, loan officers can assess borrowers' creditworthiness using objective measures. And access to credit information not only benefits creditors. It also benefits deserving borrowers, by increasing their chances to get credit. Where credit registries or bureaus are present, allowing easier access to borrowers' credit histories, banks are more likely to extend loans (figure 4).

Besides providing credit information in the form of credit reports, the more advanced credit bureaus offer other services, including credit scoring. Credit scores, assigned to borrowers on the basis of their ability and capacity to repay debt, are calculated using information from various sources, including credit reports. The scores make borrowers aware of how they are affected by the data that credit bureaus collect. Some banks use credit scores in their loan approval process.

A growing number of credit bureaus calculate credit scores. Today, among 89 private credit bureaus around the world, 46 report that they provide credit scores. Not surprisingly, 16 of them are based in OECD high income economies; the other 30 are spread across regions. Sub-Saharan Africa has the least credit scoring because public credit registries, which typically do not provide credit scores, far outnumber private credit bureaus in the region.

WHY DOES CREDIT INFORMATION SHARING MATTER?

Credit bureaus and credit registries are essential parts of the financial infrastructure that facilitates access to formal finance. By sharing credit information, they help reduce information asymmetries, increase access to credit for small firms, lower interest rates, improve borrower discipline and support bank supervision and credit risk monitoring.

Reducing information asymmetries

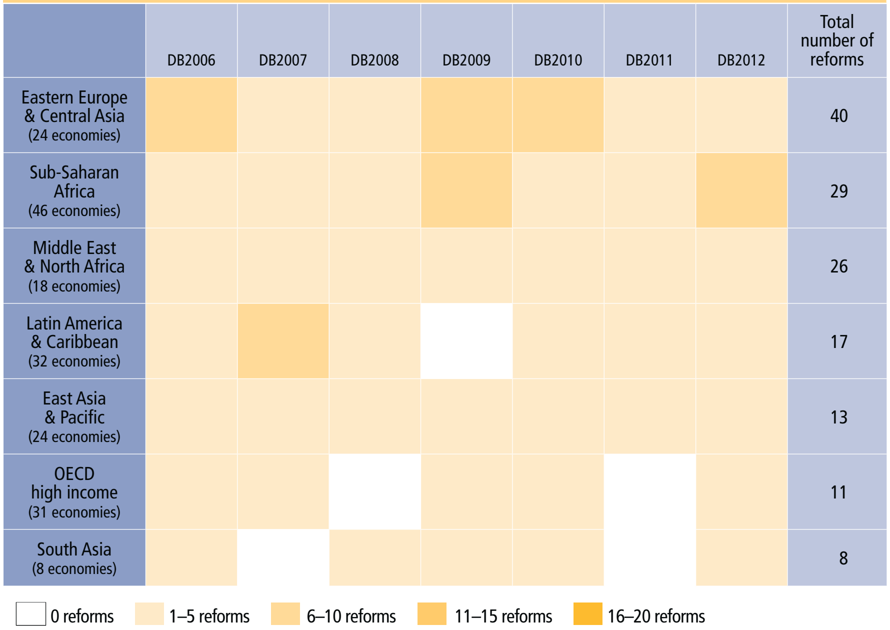
Borrowers typically have more information about their financial situation and investment opportunities than lenders do. This information asymmetry in credit markets affects the relationship between lenders and borrowers, especially borrowers that are small and medium-size enterprises. Banks are more likely to lend to larger firms, which typically are more transparent and use international accounting standards.[16] Sharing information on borrowers through credit registries or bureaus is one way to overcome these asymmetries. Credit reporting systems help lenders learn about borrowers' characteristics, past behavior, repayment history and current debt exposure.

Increasing access to credit for small firms

Credit bureaus and credit registries are one way of increasing access to finance for individuals and small firms.[17] With better,

FIGURE 5 Eastern Europe and Central Asia still leading in credit information reforms

Number of *Doing Business* reforms improving credit information systems by *Doing Business* report year



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Source: Doing Business database.

cheaper and faster access to credit information, lending officers can use accurate and objective data to make unbiased decisions in offering loans. And when they can assess the risk of default, banks have more incentive to lend to individuals and small firms. Supported by credit reporting systems, banks can base their credit decisions on past borrower behavior and therefore sensibly extend credit to smaller firms.[18] Research shows that basing credit decisions on objective information may improve the availability of credit to the poor and increase entrepreneurs' opportunities for success, supporting the development of micro and small businesses in developing economies.[19] A recent study found that after the introduction of new credit reporting systems in developing economies, access to credit grew twice as fast for small firms as for large ones.[20]

Research in 27 transition economies shows that introducing a credit reporting system is associated with an increase of 4.2 percentage points in firms' reliance on credit.[21] Such an effect would be welcome in the Middle East and North Africa, where banks cite lack of transparency among small and medium-size enterprises and the weak financial infrastructure (credit information, creditor rights and collateral infrastructure) as the main obstacles to lending more to such enterprises.[22] Since 2005 about three-fourths of the region's economies have reformed their credit information systems. Yet on average less than a quarter of the adult population in the region is covered by a credit reporting system. And only 7 of 18 economies in the region have a private credit bureau.

Sharing credit information reduces banks' uncertainty about borrowers' total debt exposure, decreasing the costs of screening and lowering interest rates.[23] By aiding the exchange of information among lenders, registries and bureaus help creditors sort good borrowers from bad ones and price loans correctly.

Using data on loans in Mozambique in 2000–06, researchers found that a better and more intense bank-borrower relationship improves the likelihood that a loan will be approved by 4.2% and reduces the time for processing a loan approval by 0.6 days. With the existence of data on repayment behavior, banks required 11.6% less in collateral value for each additional loan a firm took.[24]

Improving borrower discipline

Credit information sharing can act as a disciplinary device for borrowers. When creditors are known to share information about customers' credit records, borrowers know that defaults on loans from one lender may disrupt future access to credit from all other lenders. So borrowers have greater incentive to repay.[25] Research has shown that repayment rates can increase by up to 80% when a credit registry starts operation.[26] According to a recent study surveying 70 utility companies in the United States, 72% reported that the benefits of credit reporting amounted to at least 2–5 times the costs. Half of all customers said that they would be more likely to pay their bills on time if those payments were fully reported to credit bureaus and could affect their credit score.[27]

Supporting bank supervision and credit risk monitoring

For regulators, credit information systems provide a powerful tool for supervising banks and monitoring credit risk and credit trends in the economy. Regulators often use information from credit bureaus to assess whether current provisioning is adequate and to analyze developments in credit markets and interest rates. The results may guide changes in the legislation governing financial institutions. Research in Argentina, Brazil and Mexico found that credit registries played a valuable role in credit risk evaluation and in supervision, including in calculations of credit risk for capital or as a check on a bank's internal ratings.[28]

Credit information systems also support competition in the credit market. As more credit information becomes available, competition among banks and nonbank financial institutions should increase. Research in the Middle East and North Africa found that lack of credit information systems may curtail competition in the banking sector.[29]

WHO REFORMED CREDIT INFORMATION SHARING—AND WHAT HAS WORKED?

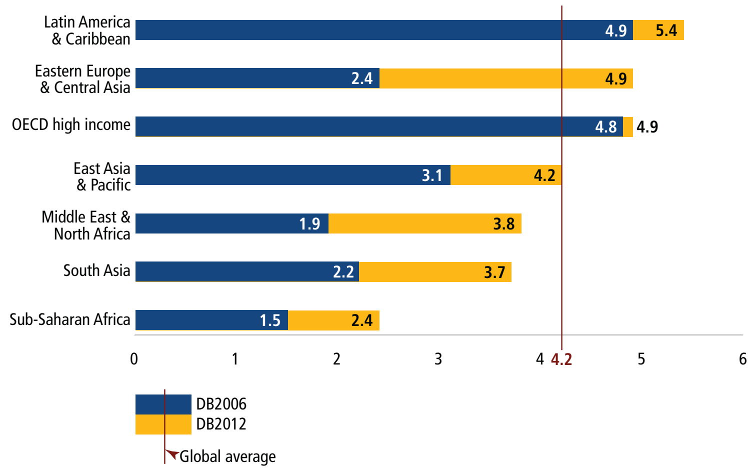
In the past 7 years 87 economies, more than half of those with a credit reporting system as recorded by *Doing Business* (142 economies), implemented 144 regulatory reforms to improve credit information systems (figure 5).

More than half of these regulatory reforms were aimed at expanding the set of information collected by existing credit registries or bureaus, such as by removing the threshold for loans to be reported or collecting information from retailers or utility companies. Others established new credit bureaus or registries or implemented a regulatory framework that allows the sharing of data and fosters trust in the system by both banks and borrowers. Since 2005, 20 new credit registries or bureaus have been established in economies that previously had no reporting system.

Doing Business measures both public credit registries and private credit bureaus. Public credit registries are defined as databases managed by the public sector, usually by the central bank or the superintendent of banks that collect information on the creditworthiness of borrowers and facilitate the exchange of credit information among banks and financial institutions. Private credit bureaus are set up in response to commercial opportunities and market conditions.[30] Although they are private entities and operate in the private commercial sphere, private credit bureaus are regulated by laws that allow the sharing of data between banks and borrowers. Regulations on privacy, bank secrecy and data protection stipulate the type of information that may be shared between banks and private credit bureaus. Regulations on access to credit information specify which data can be available to banks and borrowers. Some economies, such as Jordan, Kazakhstan, Kenya, Uganda and the United Arab Emirates, even mandate by law that data be shared with private credit bureaus. Economies such as Ecuador and Morocco have established a public credit registry in the central bank with the clear objective of building a credit information database that can later be transferred to a private credit bureau.

FIGURE 6 Better credit information systems in all regions

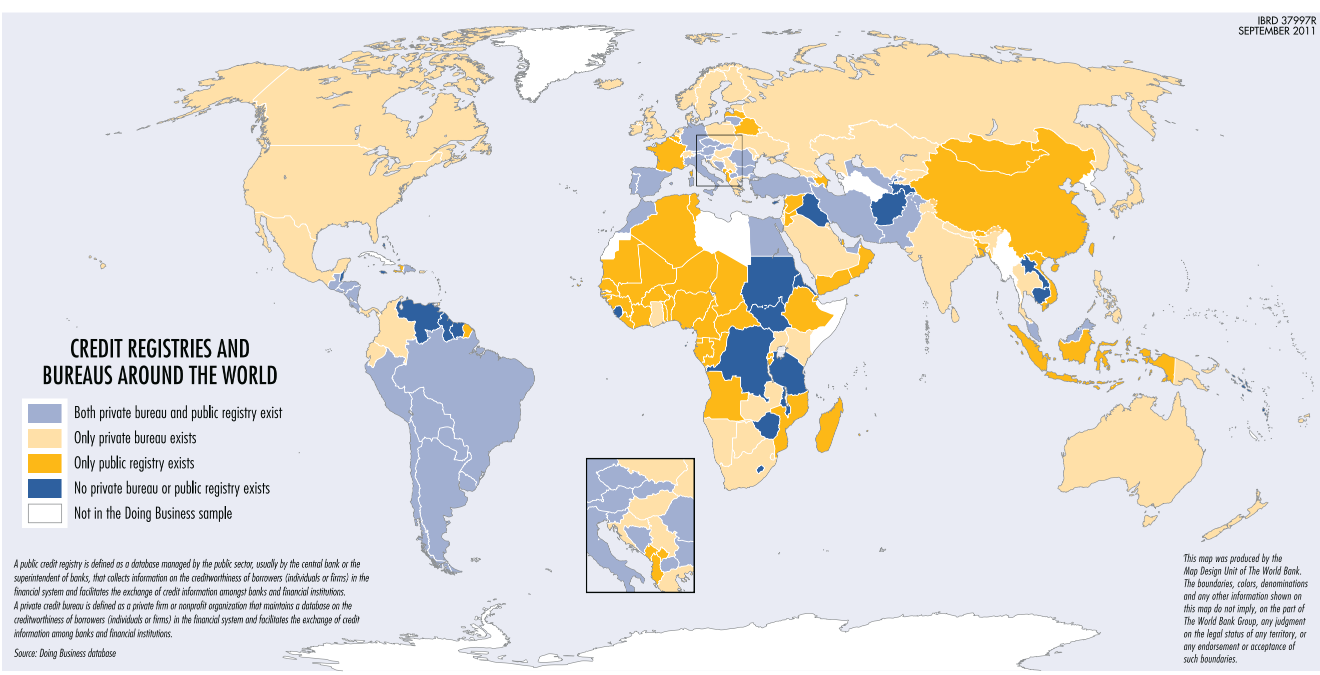
Average depth of credit information index (0–6)



Note: The data sample for DB2006 (2005) includes 131 economies. The sample for DB2012 (2011) also includes Bahrain, Cape Verde, Equatorial Guinea, Gabon, Guinea-Bissau, Kosovo, Liberia, Montenegro, Qatar, Swaziland, and Trinidad and Tobago, for a total of 142 economies. DB2006 data are adjusted for any data revisions and changes in methodology and regional classifications of economies.

Source: Doing Business database.

FIGURE 7 Credit registries and bureaus around the world



Globally, coverage by credit registries and credit bureaus increased from an average of 21% of the adult population in 2005 to 38% in 2011. The average depth of credit information index increased from 3.0 in 2005 to 4.2 in 2011 (figure 6).[31]

But 41 economies around the world, mainly in Sub-Saharan Africa and the Middle East and North Africa, still lack any kind of credit information system (figure 7). And in many that do have one, the credit bureau or registry covers only a tiny fraction of the adult population.

In 2010/11, 22 economies strengthened their credit reporting system. Improving the regulatory framework for sharing credit information was the most popular feature of credit information reforms (table 5).

Specific practices help increase credit coverage and encourage the use of credit information systems. Among the most common measures have been expanding the range of information shared, collecting and distributing data from sources other than banks and lowering or eliminating minimum loan thresholds (figure 8).

Reporting good as well as bad

Credit information can be broadly divided into 2 categories: negative and positive. Negative information covers defaults and late payments. Positive information includes, for example, on-time loan repayments and the original and outstanding amounts of loans.

A credit information system that reports only negative information penalizes borrowers who default on payments—but it fails to reward diligent borrowers who pay on time. Sharing information on reliable repayment allows customers to establish a positive credit history and improves the ability of lenders to distinguish good borrowers from bad ones. Sharing more than just negative information also ensures that a credit information system will include high-risk borrowers that have accumulated significant debt exposure without yet defaulting on any loans.

Sharing full information makes a difference for lenders. A study in the United States simulated individual credit scores using only negative information and then using both negative and positive information. The negative-only model produced a 3.35% default rate among approved applicants, while the use of both positive and negative information led to a 1.9% default rate.[32]

Experience in Hong Kong SAR, China, provides another example. Between 1998 and 2002 credit cards became popular. Perhaps too popular: many consumers were able to accumulate several credit cards because positive credit information was not shared at the time. There were many credit card defaults, and in 2002 Hong Kong SAR, China, was hit by a severe credit card crisis. Lenders

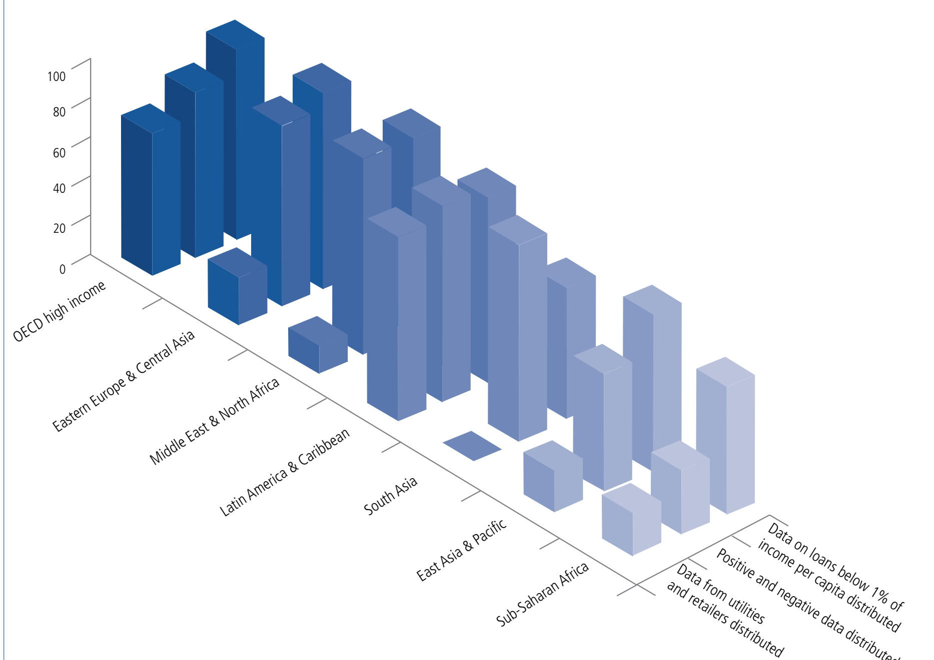
TABLE 5 Who improved the sharing of credit information in 2010/11—and what did they do?

Feature	Economies	Some highlights
Improved regulatory framework for sharing credit information	Angola; Brazil; Cambodia; Madagascar; Malawi; Sierra Leone; United Arab Emirates	Sierra Leone adopted a legal framework for the creation of a public credit registry.
Expanded set of information collected in credit registry or bureau	Armenia; Cape Verde; Croatia; Oman; Rwanda	Armenia began requiring national utility companies to provide credit data to the credit bureau. Croatia's private credit bureau started collecting positive and negative information on firms.
Created a new credit registry or bureau	Bhutan; FYR Macedonia; Moldova; Timor-Leste	Bhutan's first public credit registry started operations, covering 30,000 individuals.
Provided online access to data at credit registry or bureau	Cape Verde; Oman; Paraguay; Uruguay	Oman introduced a new online platform for sharing credit information. In Uruguay 540,000 firms and individuals can now access the public credit registry online.
Lowered or eliminated threshold for loans reported	Cape Verde; Madagascar; Mongolia; Qatar	Madagascar eliminated the minimum threshold for loans included in the database.
Expanded historical data distributed	Cape Verde; Oman; Qatar; Rwanda	Qatar's credit registry expanded the historical data available for distribution.
Guaranteed by law borrowers' right to access data	Algeria; Angola; Slovak Republic	In Algeria a new ordinance gave borrowers the right to inspect their credit data.

Source: *Doing Business* database.

FIGURE 8 Worldwide, reporting data on small loans is the most common feature of credit information sharing

Share of economies where type of data is distributed (%)



Source: *Doing Business* database.

TABLE 6 Good practices around the world in sharing credit information

Practice	Economies[a]	Examples
Distributing data on loans below 1% of income per capita	119	Brazil; Bulgaria; Germany; Kenya; Malaysia; Sri Lanka; West Bank and Gaza
Distributing both positive and negative credit information	100	China; Croatia; India; Italy; Jordan; Panama; South Africa
Distributing credit information from retailers or utilities as well as financial institutions	54	Fiji; Lithuania; Nicaragua; Rwanda; Saudi Arabia; Spain

a. Among 183 economies surveyed.
Source: Doing Business database.

wrote off nearly 13% of their total card receivables, compared with 7.5% for lenders in the United States. Since then the credit bureau has shifted to a full credit reporting system.[33]

A study of Latin American economies suggests that where private credit bureaus distribute both positive and negative information and have 100% participation from banks, lending to the private sector is greater (at least 47.5% greater).[34] Another study also looked at the effect of providing positive and negative information in Latin America.[35] In Brazil it found that having access to positive information would reduce the default rate from 3.37% to 1.84%—equivalent to about a 45% reduction in portfolio losses for Brazilian banks. The study also showed the gains in terms of access to credit. While 56% of the sample population would get credit if only negative information is used, more than 82% would if full information were available.

There is good news for potential borrowers in Brazil. After 10 years of work to create an appropriate legal framework for sharing positive credit data, a new law entered into force on June 9, 2011, that allows private credit bureaus to collect positive information.

Today 16 of the 142 economies with a credit reporting system as recorded by *Doing Business* share only negative information. Over the past 7 years only 7 economies moved to a full information sharing system (table 6).

One of these is Oman. On December 20, 2010, its central bank launched the Bank Credit and Statistical Bureau System. This new system collects positive and negative information on firms and individuals, including information on any type of credit facility and on both performing and nonperforming loans. Georgia started distributing positive and negative information in the summer of 2007. This was in response to banks' demand for a better understanding of customers' payment patterns. The banks wanted to improve their risk management tools as their lending grew. The largest banks participated actively in sharing positive information. The positive credit reporting system contributed to a 20-fold increase in coverage compared with the previous year, from 8,000 borrowers to 160,000.

Collecting and distributing data from retailers and utility companies

One effective way to expand the range of information distributed by credit registries is to include credit information from retailers and utility companies, such as electricity providers and mobile phone companies. Providing information on payment of electricity and phone bills can help establish a good credit history for those without previous bank loans or credit cards. This represents an important opportunity for including people without traditional banking relationships. A recent study across 8 global mobile money operators found that 37% of their customers lacked a bank account.[36]

But including this information can be challenging. Utilities and retailers are regulated by different institutions than financial companies are. They also might have to be convinced that the benefits of reporting bill payment outweigh the costs.

A utility in the United States has clearly benefited. In August 2006 DTE Energy, an electricity and natural gas company, began full reporting of customer payment data to credit bureaus. DTE customers with no prior credit history—8.1% of the total, according to a recent study—gained either a credit file or a credit score. And customers began to make payments to DTE a priority. Within 6 months DTE had 80,000 fewer accounts in arrears.[37]

A study in Italy looked at the effect of providing a credit bureau with payment information from a water supply company.[38] The credit bureau, CRIF, set up a credit scoring model, the "water score," which took up to 3 years of payment of water bills into consideration. More than 83% of water customers who previously had no credit history now have a positive one thanks to paying their water bills. This has made it easier for them to obtain credit. Those benefiting most include young entrepreneurs and families with only one income, 2 of the groups that tend to lack bank accounts in Italy.

Today credit bureaus or registries in 54 economies around the world include credit information from sources other than banks,

TABLE 7 Who has the most credit information—and who the least?

Depth of credit information index (0–6)

Most		Least	
Argentina	6	Burkina Faso	1
Canada	6	Burundi	1
Germany	6	Djibouti	1
Japan	6	Guinea-Bissau	1
Korea, Rep.	6	Liberia	1
Lithuania	6	Mauritania	1
Malaysia	6	Niger	1
Mexico	6	Guinea	0
United Kingdom	6	Madagascar	0
United States	6	Nigeria	0

Borrowers covered by credit registries or bureaus (% of adults)

Most		Least	
Argentina	100	Liberia	0.65
Australia	100	Algeria	0.35
Canada	100	Burundi	0.28
Iceland	100	Nepal	0.26
Ireland	100	Djibouti	0.24
New Zealand	100	Ethiopia	0.20
Norway	100	Mauritania	0.16
Sweden	100	Nigeria	0.09
United Kingdom	100	Madagascar	0.05
United States	100	Guinea	0.02

Note: The rankings on borrower coverage reflected in the table include only economies with a public credit registry or private credit bureau (142 in total). Another 41 economies have no credit registry or bureau and therefore no coverage. See the data notes for details.
Source: Doing Business database.

including those where coverage is 100% (table 7). In these 54 economies coverage of borrowers is 17.6 percentage points higher than in those where credit bureaus or registries do not include information from retailers or utility companies. These economies include 10 where credit bureaus or registries started collecting and distributing alternative data in the past 7 years. Kazakhstan's first credit bureau broadened its sources of credit information in 2007 by including information from the national gas company (KazMunayGas) and from retailers such as furniture companies. This shift, along with a boom in consumer credit lending, led to an 80% increase in coverage by January 2008, from 1.62 million borrowers to 2.92 million. In Rwanda 3 utility companies—2 mobile phone companies (MTN and Tigo) and an electricity and gas company (EWSA)—started providing credit information to the private credit bureau in April 2011.

Lowering or eliminating minimum loan thresholds

Where thresholds for the loans included in a credit bureau's database are high, retail and small business loans are more likely to be excluded. This can hurt those that benefit the most from credit information systems—such as female entrepreneurs and small enterprises, whose loans are typically smaller. Credit bureaus and registries that collect and distribute data on microfinance loans are more likely to support female entrepreneurship by enabling women to build credit histories—because women make up 76% of all borrowers from microfinance institutions.[39] Public credit registries usually set relatively high thresholds for loans, $34,260 on average, since their primary purpose is to support bank supervision and the monitoring of systemic risks. Private credit bureaus tend to have lower minimum loan thresholds, $418 on average.

Today 119 economies have minimum loan thresholds below 1% of income per capita. And over the past 7 years 17 economies eliminated their minimum loan threshold. On average in these economies, this more than quadrupled the coverage.

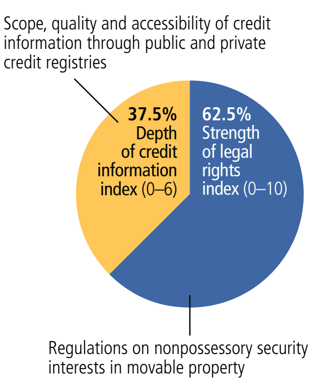
Pakistan's public credit registry eliminated its loan threshold of 500,000 rupees ($7,605) in 2008. Now all loans are reported to the registry. Among those demanding this change was the Pakistan Banks' Association, whose members were facing rapid growth in consumer lending and thus in the need for credit data. Indonesia, Tunisia, and West Bank and Gaza also eliminated loan thresholds in 2008. Azerbaijan eliminated 3 thresholds in 2009: 1,000 manat ($1,314) for individuals, 5,000 manat ($6,572) for firms and 10,000 manat ($13,144) for credit cards. This action was spurred by the rapid growth in consumer loans, which had led banks to request more detailed information on a larger group of borrowers.[40]

DATA NOTES ON GETTING CREDIT

Doing Business measures the legal rights of borrowers and lenders with respect to secured transactions through one set of indicators and the sharing of credit information through another. The first set of indicators describes how well collateral and bankruptcy laws facilitate lending. The second set measures the coverage, scope and accessibility of credit information available through public credit registries and private credit bureaus. The ranking on the ease of getting credit is based on the percentile rankings on its component indicators: the depth of credit information index (weighted at 37.5%) and the strength of legal rights index (weighted at 62.5%) (figure A.1).[41]

FIGURE A.1 Getting credit: collateral rules and credit information

Rankings are based on 2 indicators



Note: Private bureau coverage and public registry coverage are measured but do not count for the rankings.

LEGAL RIGHTS

The data on the legal rights of borrowers and lenders are gathered through a survey of financial lawyers and verified through analysis of laws and regulations as well as public sources of information on collateral and bankruptcy laws. Survey responses are verified through several rounds of follow-up communication with respondents as well as by contacting third parties and consulting public sources. The survey data are confirmed through teleconference calls or on-site visits in all economies.

Strength of legal rights index

The strength of legal rights index measures the degree to which collateral and bankruptcy laws protect the rights of borrowers and lenders and thus facilitate lending (table A.1). Two case scenarios, case A and case B, are used to determine the scope of the secured transactions system. The case scenarios involve a secured borrower, the company ABC, and a secured lender, BizBank. In certain economies the legal framework for secured transactions means that only case A or case B can apply (not both). Both cases examine the same set of legal provisions relating to the use of movable collateral.

Several assumptions about the secured borrower and lender are used:

- ABC is a domestic, limited liability company.

TABLE A.1 What do the getting credit indicators measure?
Strength of legal rights index (0–10)
Protection of rights of borrowers and lenders through collateral laws
Protection of secured creditors' rights through bankruptcy laws
Depth of credit information index (0–6)
Scope and accessibility of credit information distributed by public credit registries and private credit bureaus
Public credit registry coverage (% of adults)
Number of individuals and firms listed in a public credit registry as percentage of adult population
Private credit bureau coverage (% of adults)
Number of individuals and firms listed in largest private credit bureau as percentage of adult population

- The company has 100 employees.
- ABC has its headquarters and only base of operations in the economy's largest business city.
- Both ABC and BizBank are 100% domestically owned.

The case scenarios also involve assumptions. In case A, as collateral for the loan, ABC grants BizBank a nonpossessory security interest in one category of movable assets, for example, its accounts receivable or its inventory. ABC wants to keep both possession and ownership of the collateral. In economies where the law does not allow nonpossessory security interests in movable property, ABC and BizBank use a fiduciary transfer-of-title arrangement (or a similar substitute for nonpossessory security interests). The strength of legal rights index does not cover functional equivalents to security over movable assets (for example, leasing or reservation of title).

In case B, ABC grants BizBank a business charge, enterprise charge, floating charge or any charge that gives BizBank a security interest over ABC's combined movable assets (or as much of ABC's movable assets as possible). ABC keeps ownership and possession of the assets.

The strength of legal rights index includes 8 aspects related to legal rights in collateral law and 2 aspects in bankruptcy law. A score of 1 is assigned for each of the following features of the laws:

- Any business may use movable assets as collateral while keeping possession of the assets, and any financial institution may accept such assets as collateral.
- The law allows a business to grant a nonpossessory security right in a single category of movable assets (such as accounts receivable or inventory), without requiring a specific description of the collateral.
- The law allows a business to grant a nonpossessory security right in substantially all its movable assets, without requiring a specific description of the collateral.
- A security right may extend to future or after-acquired assets and may extend automatically to the products, proceeds or replacements of the original assets.
- A general description of debts and obligations is permitted in the collateral agreement and in registration documents; all types of debts and obligations can be secured between the parties, and the collateral agreement can include a maximum amount for which the assets are encumbered.
- A collateral registry or registration institution for security interests over movable property is in operation, unified geographically and by asset type, with an electronic database indexed by debtors' names.
- Secured creditors are paid first (for example, before general tax claims and employee claims) when a debtor defaults outside an insolvency procedure.
- Secured creditors are paid first (for example, before general tax claims and employee claims) when a business is liquidated.
- Secured creditors either are not subject to an automatic stay or moratorium on enforcement procedures when a debtor enters a court-supervised reorganization procedure, or the law provides secured creditors with grounds for relief from an automatic stay or moratorium (for example, if the movable property is in danger) or sets a time limit for the automatic stay.[42]
- The law allows parties to agree in a collateral agreement that the lender may enforce its security right out of court.

The index ranges from 0 to 10, with higher scores indicating that collateral and bankruptcy laws are better designed to expand access to credit.

CREDIT INFORMATION

The data on credit information sharing are built in 2 stages. First, banking supervision authorities and public information sources are surveyed to confirm the presence of a public credit registry or private credit bureau. Second, when applicable, a detailed survey on the public credit registry's or private credit bureau's structure, laws and associated rules is administered to the entity itself. Survey responses are verified through several rounds of follow-up communication with respondents as well as by contacting third parties and consulting public sources. The survey data are confirmed through teleconference calls or on-site visits in all economies.

Depth of credit information index

The depth of credit information index measures rules and practices affecting the coverage, scope and accessibility of credit information available through either a public credit registry or a private credit bureau. A score of 1 is assigned for each of the following 6 features of the public credit registry or private credit bureau (or both):

- Both positive credit information (for example, outstanding loan amounts and pattern of on-time repayments) and negative information (for example, late payments, and number and amount of defaults and bankruptcies) are distributed.
- Data on both firms and individuals are distributed.
- Data from retailers and utility companies as well as financial institutions are distributed.
- More than 2 years of historical data are distributed. Credit registries and bureaus that erase data on defaults as soon as they are repaid obtain a score of 0 for this indicator.
- Data on loan amounts below 1% of income per capita are distributed. Note that a credit registry or bureau must have a minimum coverage of 1% of the adult population to score a 1 on this indicator.
- By law, borrowers have the right to access their data in the largest credit registry or bureau in the economy.

The index ranges from 0 to 6, with higher values indicating the availability of more credit information, from either a public credit registry or a private credit bureau, to facilitate lending decisions. If the credit registry or bureau is not operational or has a coverage of less than 0.1% of the adult population, the score on the depth of credit information index is 0.

In Lithuania, for example, both a public credit registry and a private credit bureau operate. Both distribute positive and negative information (a score of 1). Both distribute data on firms and individuals (a score of 1). Although the public credit registry does not distribute data from retailers or utilities, the private credit bureau does do so (a score of 1). Although the private credit bureau does not distribute more than 2 years of historical data, the public credit registry does do so (a score of 1). Although the public credit registry has a threshold of 50,000 litai, the private credit bureau distributes data on loans of any value (a score of 1). Borrowers have the right to access their data in both the public credit registry and the private credit bureau (a score of 1). Summing across the indicators gives Lithuania a total score of 6.

Public credit registry coverage

The public credit registry coverage indicator reports the number of individuals and firms listed in a public credit registry with information on their borrowing history from the past 5 years. The number is expressed as a percentage of the adult population (the population age 15 and above in 2010 according to the World Bank's *World Development Indicators*). A public credit registry is defined as a database managed by the public sector, usually by the central bank or the superintendent of banks, that collects information on the creditworthiness of borrowers (individuals or firms) in the financial system and facilitates the exchange of credit information among banks and other regulated financial institutions. If no public registry operates, the coverage value is 0.

Private credit bureau coverage

The private credit bureau coverage indicator reports the number of individuals and firms listed by a private credit bureau with information on their borrowing history from the past 5 years. The number is expressed as a percentage of the adult population (the population age 15 and above in 2010 according to the World Bank's *World Development Indicators*). A private credit bureau is defined as a private firm or nonprofit organization that maintains a database on the creditworthiness of borrowers (individuals or firms) in the financial system and facilitates the exchange of credit information among creditors. Credit investigative bureaus and credit reporting firms that do not directly facilitate information exchange among banks and other financial institutions are not considered. If no private bureau operates, the coverage value is 0.

The data details on getting credit can be found for each economy at http://www.doingbusiness.org by selecting the economy in the drop-down list. This methodology was developed in Djankov, McLiesh and Shleifer (2007) and is adopted here with minor changes.

NOTES

1. Africapractice 2005.
2. The OHADA member states are Benin, Burkina Faso, Cameroon, the Central African Republic, Chad, the Comoros, the Republic of Congo, Côte d'Ivoire, Equatorial Guinea, Gabon, Guinea, Guinea-Bissau, Mali, Niger, Senegal and Togo. The Democratic Republic of Congo will soon become the 17th member state.
3. Alvarez de la Campa and others 2010.
4. Alvarez de la Campa and others 2010.
5. World Bank 2011.
6. Djankov, McLiesh and Shleifer 2007.
7. Qian and Strahan 2007.
8. Djankov and others 2008.
9. Galindo and Micco 2007.
10. Haselmann, Pistor and Vig 2010.
11. Bae and Goyal 2009.
12. Diamond 2004.
13. The data on the number of filings and volume of loans were provided by the Mexican government. Other factors in addition to the institutional and legal reforms might have contributed to the increase in the filings and loan volume.
14. National Law Center for Inter-American Free Trade 2011.
15. World Bank 2010.
16. Jappelli and Pagano 2002; Behr, Entzian and guettler 2011; Brown, Jappelli and Pagano 2009.
17. Brown, Jappelli and Pagano 2009; Jappelli and Pagano 2002.
18. Brown, Jappelli and Pagano 2009; Petersen and Rajan 2002; DeYoung, Frame, Glennon and Nigro 2010.
19. Luoto, McIntosh and Wydick 2004; Brown, Jappelli and Pagano 2009
20. Brown and Zehnder 2007.
21. Brown, Jappelli and Pagano 2009.
22. Rocha and others 2010.
23. Brown and Zehnder 2007; Luoto, McIntosh and Wydick 2004; Brown, Jappelli and Pagano 2009; Behr, Entzian and Guettler 2011.
24. Behr, Entzian and Guettler 2011.
25. Padilla and Pagano 2000.
26. Brown and Zehnder 2007.
27. Turner and others 2009.
28. Powell and others 2004.
29. Anzoategui, Martinez Pería and Rocha 2010.
30. Jappelli and Pagano 1993.
31. Straight average of percentages across economies.
32. Barron and Staten 2003.
33. Bailey, Chun and Wong 2003.
34. Turner and Varghese 2007.
35. Powell and others 2004.
36. CGAP and World Bank 2010.
37. Turner and others 2009; Turner 2011.
38. Preliminary findings of an ongoing internal study at the credit information services firm CRIF SpA, Italy.
39. World Bank 2010.
40. Interview with a private credit bureau in Azerbaijan.
41. The ranking is based on a straight average of points from the strength of legal rights index and depth of credit information index.
42. The scoring on this aspect was revised this year to bring it into line with UNCITRAL (2004, 2007) and World Bank (2011).

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