

# **Strengthening credit bureaus to contain excess household debt in Moldova**

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## MFIs and household excess debt in Moldova: recap of the work by GET Moldova so far

In our presentation in February (PB/01/2019) we pointed out that microfinance institutions (MFIs) play a key role in fostering financial access for low-income households and micro-entrepreneurs in Moldova.

But the recent rapid growth of MFIs in Moldova, and of some MFIs with particularly risky lending practices, is a concern for financial system stability, in particular due to cross-defaults from excess household debt (also in PB/05/2018).

These risks should be monitored, and we recommended:

1. Strengthened enforcement of consumer protection
2. Unless implementation of the MFIs law of October 2018 leads to consolidation, higher capital requirements on MFIs, but for now no further measures such as DSTI limits or interest rate caps.
3. An insolvency code that covers households and micro-entrepreneurs. On that basis more predictable and cooperative private restructuring solutions should be facilitated.
4. **A strengthening of credit history bureaus to track proliferating borrowing relationships and complex borrower histories which are typical for this sector.**

This presentation delivers more detail and recommendations on this last point.

# **Strengthening credit bureaus to contain excess household debt in Moldova**

## **Outline**

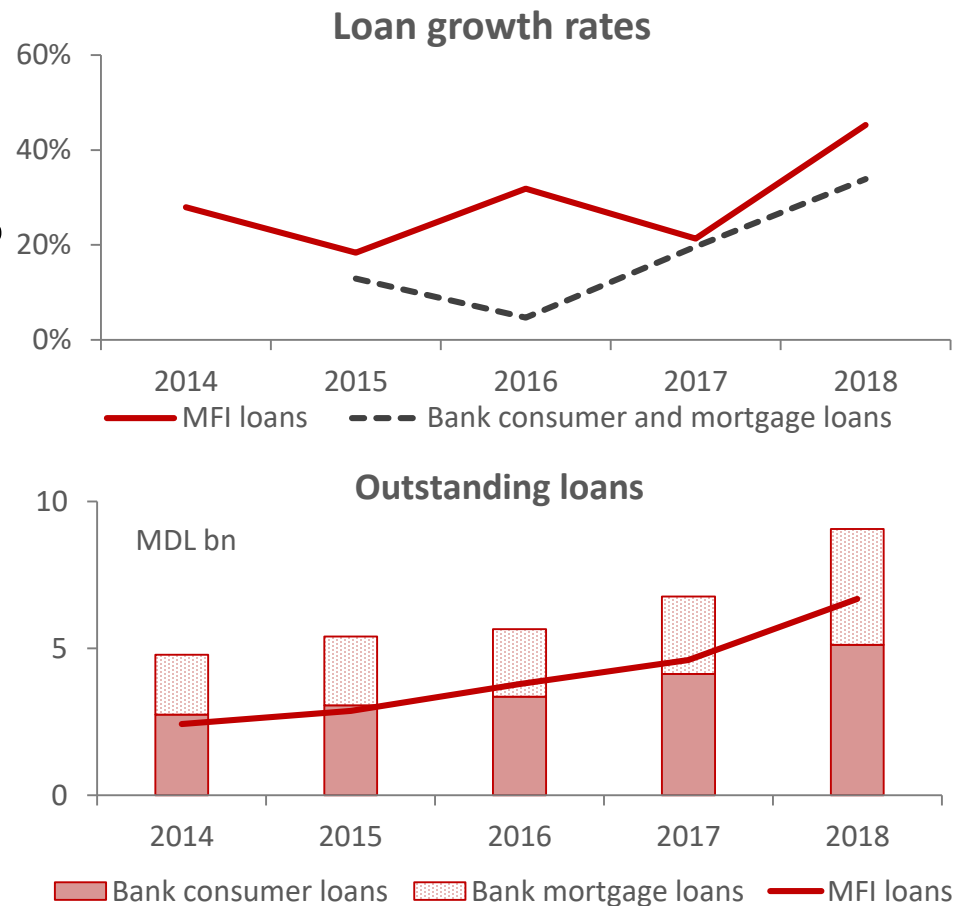
- I. Credit bureaus, household debt, and financial stability in Moldova**
- II. How to ensure comprehensive provision of credit information**
  - a. Inclusion of MFIs in the credit information system**
  - b. Use of non-financial information sources**
  - c. Facilitating the exchange of information**
  - d. Competition and a sustainable market structure**
- III. Conclusions and recommendations**

## **References**

# **I. Credit bureaus, household debt and financial stability in Moldova**

# The risk from excessive consumer credit growth in Moldova

- Consumer lending in Moldova has expanded on average by 29% yoy in the past 5 years
- MFIs now account for roughly 40% the retail loan stock
- More so than bank lending, MFI lending is prone to multiple, complex or excessive borrowing relationships
- This is due to inherently lighter regulation of non-deposit taking institutions, and inadequate information provision by borrowers



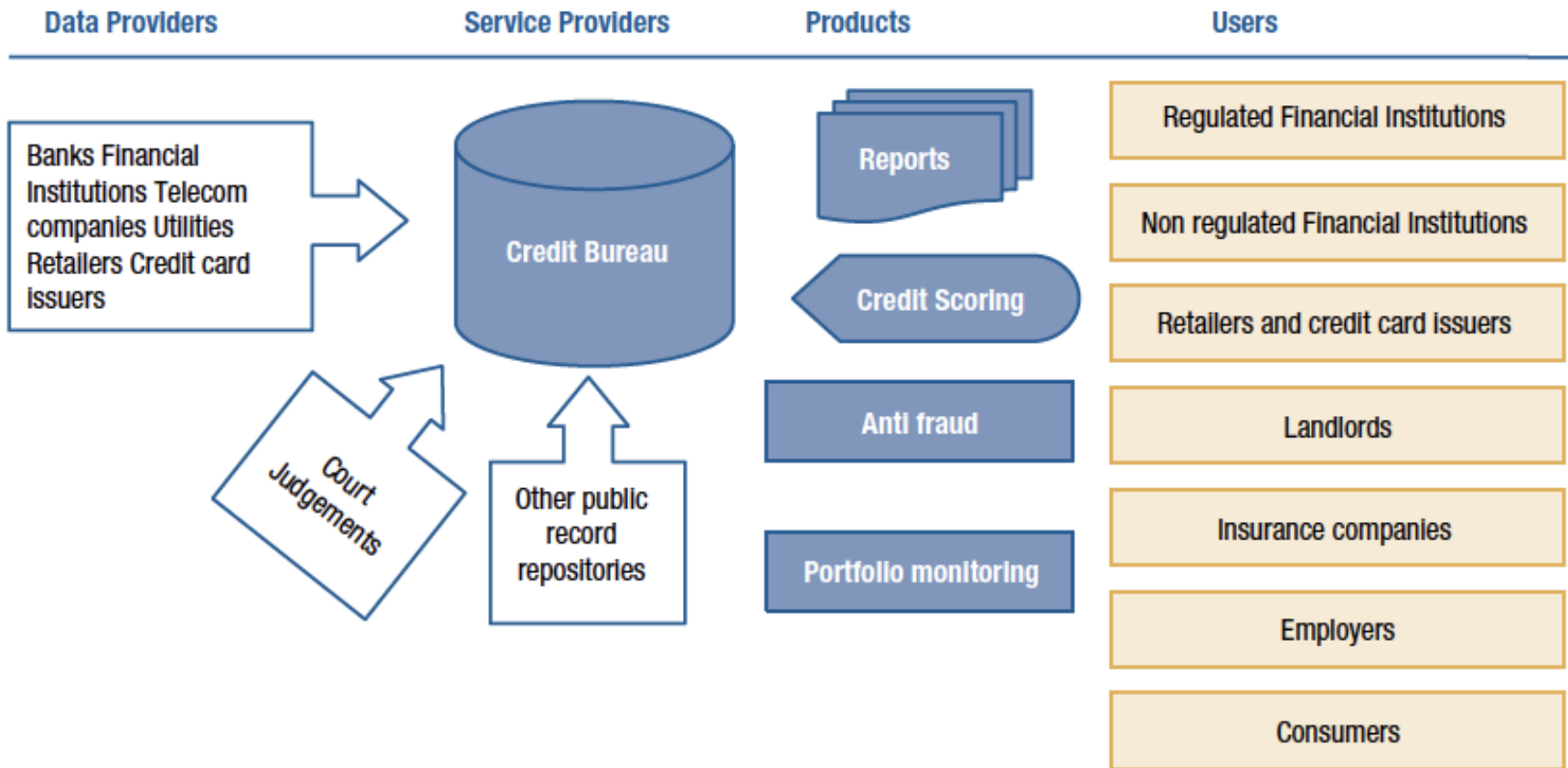
Sources: NBM, NCFM

Note: MFI loans include mortgage loans and loans to companies

## The role of credit bureaus in stemming MFI over-lending

Credit history bureaus provide information on exposures and repayment records of both individuals and SMEs/microentrepreneurs. They overcome the inherent problem of 'asymmetric' information between lenders and borrowers and are hence essential for financial stability. Credit bureaus:

- collect information from bank and non-bank financial institutions, and also from utility companies and retailer (which may later become bureau clients themselves)
- along with defaults, also disseminate 'positive' information on repayment records. This is helpful for loan approval and reduces default rates of borrowers with a short credit history, widening access to credit
- Some bureaus also provide additional services, such as credit scores
- operate largely on a subscriber basis (each lender reports to and consults one bureau)
- As a typically private business, bureaus differ in pricing, data sources and data systems used, and hence rarely exchange information



Source: World Bank (2011).

# Credit bureaus in Moldova: market structure

## **Biroul de Credit**

- Founded in 2008, at the initiative and with support of the banking sector
- Holds credit information from all 15 banks, representing 100% of banking portfolio, and about 30% of the non-bank credit portfolio. Also some savings and loans institutions

## **Infodebit Credit Report**

- License since 2017. Prior to that a simple credit scoring bureau
- Covers about 15 per cent of banking portfolio, though 70 per cent of non-bank credit portfolio

## **A third bureau was licensed in early 2019**

- Unclear that a market as small as Moldova can sustain three credit bureaus
- Differing data standards and IT systems
- Bank ownership of largest bureau may undermine incentives for information sharing
- The two original bureaus have not agreed on an information exchange



## Credit bureaus in Moldova: information content

In the World Bank's 2018 Doing Business assessment, Moldova currently scores relatively well, meeting 6 out of 8 standards of credit information :

- Data on firms and individuals are distributed.
  - Both positive and negative credit information are distributed.
  - At least two years of historical data are distributed.
  - Data on loan amounts below 1% of income per capita are distributed.
  - By law, borrowers have the right to access their data in the largest credit bureau or registry in the economy.
  - Banks and other financial institutions have online access to the credit information.
- **But important gaps remain:**
- Data from retailers or utility companies are not distributed in addition to data from financial institutions
  - There are no additional services provided, such as credit scores to help banks and other financial institutions assess the creditworthiness of borrowers

## Credit bureaus in Moldova: coverage is quite low

Indicator	Moldova	Europe & Central Asia	OECD high income	Best Regulatory Performance
Strength of legal rights index (0-12)	8	7.2	6.1	12 (5 Economies)
Depth of credit information index (0-8)	6	6.6	6.7	8 (42 Economies)
Credit registry coverage (% of adults)	0	25.3	21.8	100.0 (4 Economies)
Credit bureau coverage (% of adults)	15.8	43.4	65.3	100.0 (25 Economies)

Coverage	Credit bureau
Number of individuals	393,852
Number of firms	18,900
Total	412,752
<b>Percentage of adult population</b>	<b>15.8</b>

Source: World Bank Doing Business Indicators, 2019

## Credit bureaus in Moldova: regulatory basis

- Credit bureaus are regulated by the Law establishing the National Commission on Financial Markets of 1998, and various implementing regulations, the latest being from 2009
- The National Commission is responsible for licensing and supervision of services provided, sources of credit history information and equal access to credit information for all users
- An **amendment** is proposed which will:
  - Make it mandatory for MFIs to report new loans to at least one bureau;
  - Make it mandatory to report defaults (negative credit events);
  - Provide rights for bureaus to draw on non-financial information such as utility companies and telecoms

## **II. How to ensure comprehensive provision of credit information**

## a. Inclusion of MFIs in the credit information system

In many low income and emerging markets there has been a deterioration of MFI credit portfolio quality over the last ten years, due to inadequate risk management, poor internal organisation, and overly aggressive lending practices in the MFI industry

A range of countries (e.g. Armenia, Cambodia) underline that inclusion of MFIs in the regular credit reporting can be in the interest of the industry as a whole due to:

- Improved risk management
- Efficiency in borrower screening and approval process
- Incentives for responsible borrower behaviour

However, MFIs individually will not have incentives to supply sufficient credit information, due to: costs of IT infrastructure to set up reporting, delays in loan approval etc.

## MFI inclusion in Moldova

Mandatory reporting by MFIs in Moldova, as envisaged in the amendment, will likely lead to positive structural changes in the industry:

- A further consolidation of the industry, reducing the number of providers further from currently about 150, due to MFI-specific costs in setting up reporting capacity
- We previously identified two types of business strategies in the industry: poor due diligence/high default rates, and more in-depth approval procedures. Mandatory reporting will strengthen the latter strategy
- It could define a role for an industry association in fostering reporting procedures and IT standards, and an industry body could also become a counterpart for National Commission and NBM
- A MFI-specific database, as used in other countries and subject to different pricing, does not seem to be offered by bureaus in Moldova at present

## **b. Use of non-financial information sources**

The use of information from outside the financial system is common though not standard

It will strengthen credit discipline, as providers such as retailer or utilities may more quickly flag debt distress, than would be evident in e.g. loan defaults

It is particularly important in markets with low financial inclusion, as in Moldova, as first-time borrowers can more easily document credit quality

### **Situation in Moldova:**

- The amendment confirms the bureaus' right to draw on non-financial sources, which is welcome
- Privacy rights should not pose a problem, under European legal standards (GDPR)
- Processing can be challenge (e.g. due to absence of ID numbers). The two smaller bureaus with more adaptable IT systems are more likely to overcome these challenges

# Use of non-financial information sources in European credit bureaus

	AT	BE	HR	CY	CZ	DK	FI	DE	EL	HU	IC	IT	PL	XK	RO	RU	RS	ES	SK	SW	CH	NL	UK
Banks	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Credit unions	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Debt collectors / debt purchasers	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Leasing	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Credit card suppliers	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Retail credit suppliers	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Health insurance	Not answered	Not answered	Not answered	Not answered	Not answered	Not answered	Not answered	Not answered	Not answered	Not answered	Not answered	Not answered	Not answered	Not answered	Not answered	Not answered	Not answered	Not answered	Not answered	Not answered	Not answered	Not answered	Not answered
Other insurers	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Energy	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Water	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Telecommunication companies	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Television suppliers	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Internet providers	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Mortgage providers	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Home rental companies	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Brokers/Intermediaries	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Courts	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Government departments	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Crowd-funding platforms	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Payment services providers	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Tax authorities	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Police	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Central banks	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Acquirers of credit portfolios	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Investors	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Others	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes

Yes, organisations supply data to CRA  
 In discussions  
 No, organisations doesn't supply data to CRA  
 Not answered

Source: ACCIS



## c. Facilitating the exchange of information

- *Private* credit bureaus in Moldova compete to provide what is in effect a public good for the financial industry. Experience in Europe suggests that as a financial system becomes more mature, private bureaus will access similar information
- Regulation cannot force the bureaus to share information but can:
  - require that lenders consult all relevant information (possibly two bureaus if this seems warranted), a principle in line for instance with the EU Mortgage Credit Directive;
  - ban anti-competitive practices (e.g. should a bureau owned by banks demand exclusivity that prevents banks from consulting or reporting to competing bureaus);
  - require that fraud detected by one bureau is reported to the other two (possibly through a joint database);
  - facilitate the use of common information sources (e.g. court records), for instance by convening regular meetings between the bureaus;
  - give consumers/borrowers rights to have erroneous information corrected (for instance through access to an ombudsman), even though credit quality assessments may well differ;
  - set high standards for the quality of information accessed and for the reports that are produced

## d. Competition and a sustainable market structure

### Ownership

- The majority of credit bureaus in emerging markets are owned by banks or bank associations, which ensures reciprocity in information sharing
- Recently, more ‘challenger’ credit bureaus have emerged, based on access to IT
- Competition among private providers gives incentives to improve data quality, lower prices and provide additional services, such as credit scores

### **But the market is normally highly concentrated. This is due to:**

- Network externalities: the value of information will grow with a wider participation by financial institutions
- Economies of scale arising from fixed costs of data systems

### **Implications for Moldova**

- A credit bureau owned by banks warrants particularly close supervision, as it is less likely to include information from non-banks, and may have an incentive to erect barriers to information flows
- Three credit bureaus are unlikely to be economically viable
- There should be no regulatory preferences for now (e.g. use of one bureau for supervisory purposes)

## **III. Conclusions and recommendations**

## Conclusions

- Moldova's credit information system is at present not equipped to track the rapid rise of the microfinance industry
- There is a risk of a segmented credit information system: one bank-supported incumbent, and two much smaller though more innovative bureaus which cater to the microfinance institutions
- Other countries demonstrate that as the financial system matures credit bureaus access similar information. Competition between the three Moldovan bureaus will identify the most efficient processes, and give incentives for innovation, e.g. in producing credit scores
- Scale economies and network effects in the industry are such that ultimately at most two bureaus seem viable
- Fostering a wider set of financial institutions to report to credit bureaus will likely lead to a further consolidation in the MFI industry: MFIs incur fixed costs in IT systems and reporting, and predatory lending practices based on light borrower information are less practical

## Recommendations on regulations and enforcement

- Mandatory reporting of new exposures by MFIs, as in the proposed amendment, is sensible. NCFM should support this through engagement with individual large MFIs (or an industry association) to foster common platforms and IT systems for reporting
- Pilot studies may demonstrate the value of credit reports for MFI asset quality, and for first-time borrowers gaining access to credit
- Access by the bureaus to non-financial information (also in the amendment) could be supported by defining data provision by state bodies (e.g. courts, collateral registry), and guiding private enterprises towards more open data standards (e.g. telecoms, utilities)
- **A data exchange** between bureaus can only be mandated for specific circumstances, e.g. fraud or AML violations. Otherwise, NCFM should engage the three bureaus to work towards use of a common database, and similar quality of reports
- Any anti-competitive practices by individual bureaus (e.g. exclusivity requirements) should be checked. High standards for data quality should be applied, as three credit bureaus may not be viable in a small market in the long run

## References

- ACCIS (2018): 2017 Survey of Members: Analysis of credit reporting in Europe.
- World Bank (2012): Credit Reporting Knowledge Guide.
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