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SOCIETY AND BANKS

Role of the Credit Bureaus in development of the financial sector of Georgia



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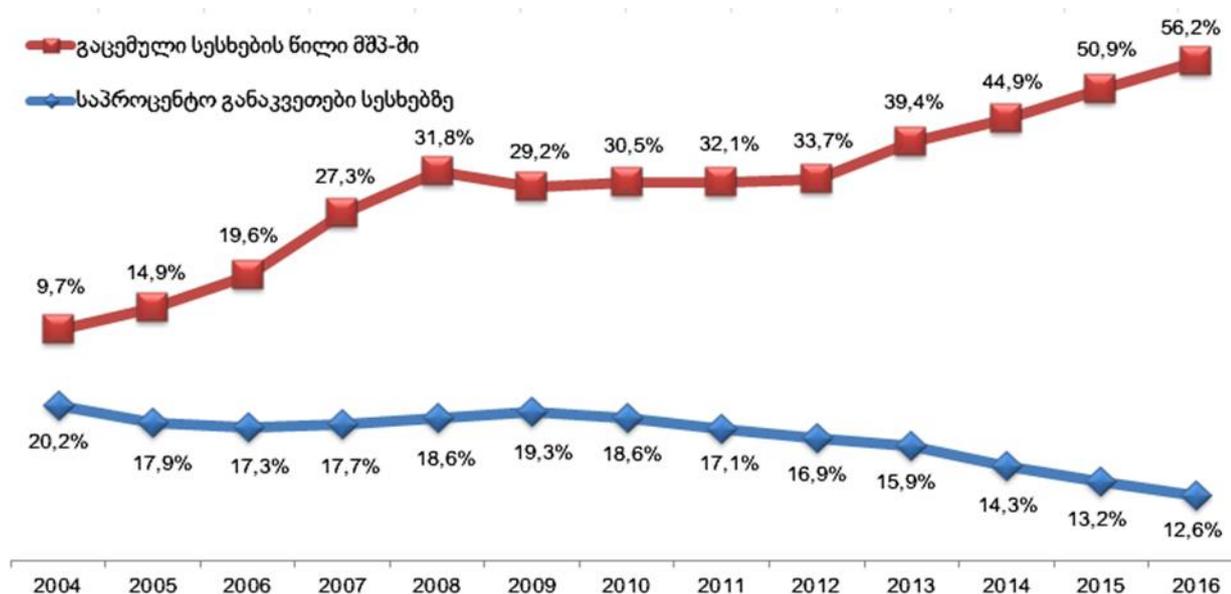
Role of the Credit Bureaus in development of the financial sector of Georgia

Asymmetry and deficient market in the modern world are the characteristics of the undeveloped and developing states mostly. Transparent financial system will facilitate to reduction of existing risks which will be reflected on the interest rates and will improve welfare of the business subjects and the consumers.

Currently, in most of the countries the Central Banks ensure financial stability. After dissolution of the Soviet Union, the National Bank of Georgia resumed independent activity without financial stability control mechanisms, which triggered hyper-inflation and failed to prevent notorious pyramid schemes of the banks. During the following years, the bank sector, along with development of the country, has restored confidence and started development, which as well was reflected on the interest rates and accessibility to the financial resources.

There were the organizations along with the Central Banks in various countries facilitating to transparency of the market and stability of the financial sector. These organizations constitute the credit bureaus. Their activity is directly reflected on accessibility to information and development of the financial sector. Capacity of overdue loans at the account of provision of information about insolvent debtors is reduced and the conferred rating points decrease the credit risks. As a result, we have the low interest rates and accessible financial resources.

Scale 1: ratio of the issued loans in GDP and average interest rates on issued loans.



Source: National Bank of Georgia, www.nbg.gov.ge.

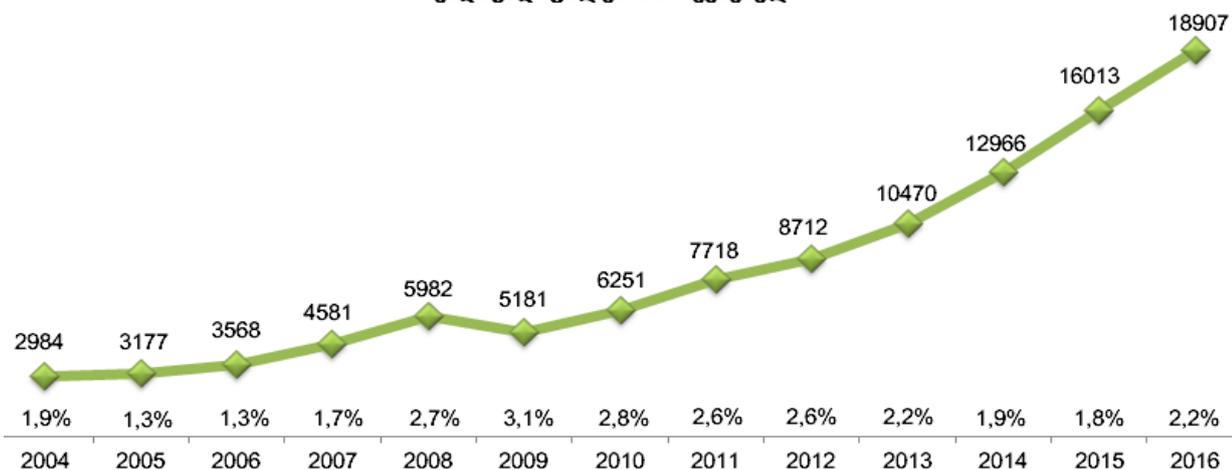
Scale 1 provides the share of the loans issued by the commercial banks in Georgia since 2004 in GDP and average interest rates. As we see, the ratio of the issued loans in GDP has drastically increased, evidencing increased insolvency of the consumers and business and underlining importance of crediting for facilitation to economic growth. At the same time, the interest rates are reduced indicating to the reduced credit risks. However,



the interest rates are not defined with the credit risks solely but there are the market risks, loan term, costs of attraction of financial resources and other factors affecting the interest rates.

Scale 2: Outstanding loans

კომერციული ბანკების მიერ გაცემული სესხები (მლნ ლარი) და სესხების ვადაგადაცილების მაჩვენებელი



Source: National Bank of Georgia, www.nbg.gov.ge.

Scale 2 reveals that the relative index of the outstanding loans along with growth of capacity of the loans issued since 2004 has minor changes. It indicates to an effective risk management by the bank sector and evidences development of the sector.

Meaning of the “credit history” has become even more relevant during the last years. It is important for us to know who formulates the credit history and how, who stores data and how the information is further provided to the party concerned. More than 120 countries worldwide apply the credit bureau services, which are chargeable. The tariffs vary according to the capacity of information and frequency of services. As a rule, the Companies shall pay from 0.05 cents to 5 USD per single inquiry.

We can find various forms of the credit bureaus according to the countries. There are the companies as under private so under state management, though they share the main principle of their activity – protection of financial sector from risky transactions.

Similar database was for the first time created 200 years ago on Manhattan. In the beginning of the XIX century, the employee of the Silk Factory dealing with the retail sales was registering the clients of the company. After several volumes of the register, the first company was established offering the information about solvency of the buyers to the persons concerned in exchange for certain fee. The credit bureaus in Europe have been established later, in 30s of the XX century. The first private company in Germany was established in 1927 and the state agency was established in 1934. Unlike the Western Europe, credit bureaus of the Eastern Europe were established later – in 1995 in Lithuania and in 1997 in Poland.

The credit bureau in Poland was established by the Bank Association. Unlike other countries, the banks, in view to upload information in and inquiry from Biuro Informacji Kredytowej did not need the permit of the client. The company is responsible for accuracy of the provided information. It is noteworthy that the all applications are directed to the Creditinfo base in Polish model regardless whether the loan has been issued. These factors



facilitate the financial sector to analyze and prevent the behavior of the customer as fraud, as well as excessive debts which is the pre-condition for growth of outstanding debts.

The databases in some countries are under state management. The credit bureau in France was delegated to the state by the private structures in 1946. Brazil and Argentina apply the two-level system. There as well are the countries where cooperation of the financial sector with the credit bureau is mandatory and is regulated under the law. In United States of America, the role of the state in development of the Credit Info was insignificant. It is noteworthy that the state agencies actively used the information about the bankrupted companies to manage the business register statistic. The Association was established in 1906 protecting the interests of the representatives of hereof sphere and as of present state, almost all the companies are the members of this Association.

Australia, Brazil, New Zealand and Norway change only the negative records. Austria, Argentina, USA, Great Britain and Japan apply the most improved models of the credit bureau where the obligations and information about the incomes are being altered.

In 90s, successful agencies started entering the European and Asian markets. Example of one of the hereof transactions is the strategic cooperation of credit bureau in Armenia ACRA Credit Reporting and the US Company Dun & Bradstreet. The credit bureau "ACRA" was established in 2004 in Armenia and activity thereof is regulated since October, 2008.

Registration of the credit bureau requires the capital in the amount of 2 ml Armenian Drams and the partner companies are prohibited to hold more than 20% shares. The National Bank of Armenia issues the license on activity and supervises the credit bureau. The records to the "ACRA" databases are being reflected within 3 (three) business days and remain in the database during 5 years upon reflection. The client, on the basis of the personal application, is allowed updating the data, establishing limits on access and inquiring history free of charge once per year. Information shall be issued to the customer by means of SMS or postal service.

In Azerbaijan, the Special Register at the National Bank has been exercising the functions of the credit bureau since 2005, however currently the 15 representatives of the financial sector (13 commercial banks and 2 micro-financial organizations) strive to establish the private credit bureau. The company "Creditinfo" in Iceland is their partner and technical supporter. Enactment of database is scheduled for the next year.

According to the international experience, activity of the credit bureaus contributes significant economic benefits to the private sector:

- Accessibility to information facilitates the financial sector to tell solvent and high-risk customers apart entailing reduction of the index of outstanding debts;
- Accurate information about the bona fide customer allows business mitigating crediting policy and gradually alleviating loan issue procedure;
- Facilitates to growth of business liquidity and minimization of expenditures;
- Accessibility to database increases competition, which has positive impact on the retail, as well as business crediting. It reduces the interest rates;
- Reduces the problems entailed with excessive debts;
- Threat of aggravating of ratings stimulates the customer and business behavior to promptly fulfill the obligations assumed under the agreement.

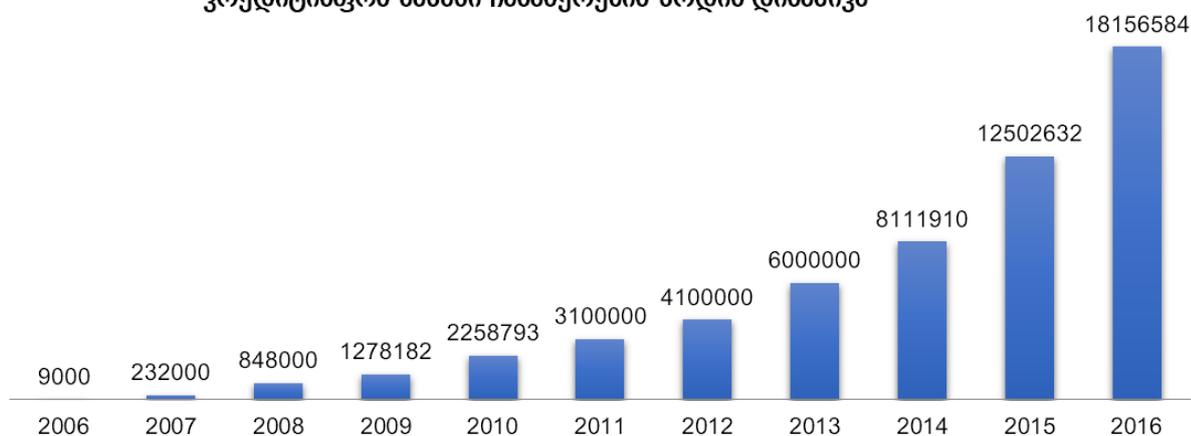


Till 2005, bank and financial sector of Georgia was at the initial stage of development, entailing deficit of bank products. In 2000-2003, the loss of the bank sector constituted 109 ml GEL. According to the World Bank reports, sustainability and transparency of the sector required establishment of the “Register of Debtors”. At present, JSC “Creditinfo Georgia” is the only credit bureau in Georgia established in 2005. The activity thereof covers processing/issue of the credit information and facilitation to activity of the financial institutions. Activity of the organization facilitates the bank sector to properly manage the credit portfolio and improves competitive milieu, which is reflected on the service quality rendered to the customers.

The database of the “Creditinfo” currently contains more than 18 ml records providing information about more than 2.5 ml natural persons and 70 000 companies. Hereof information is being updated in uninterrupted manner and is subject to monitoring by the Personal Data Protection Inspector.

Scale 3: Dynamics of growth of records into the Creditinfo database in 2006-2016

კრედიტინფოს ბაზაში ჩანაწერების ზრდის დინამიკა



Source: JSC “Creditinfo Georgia”

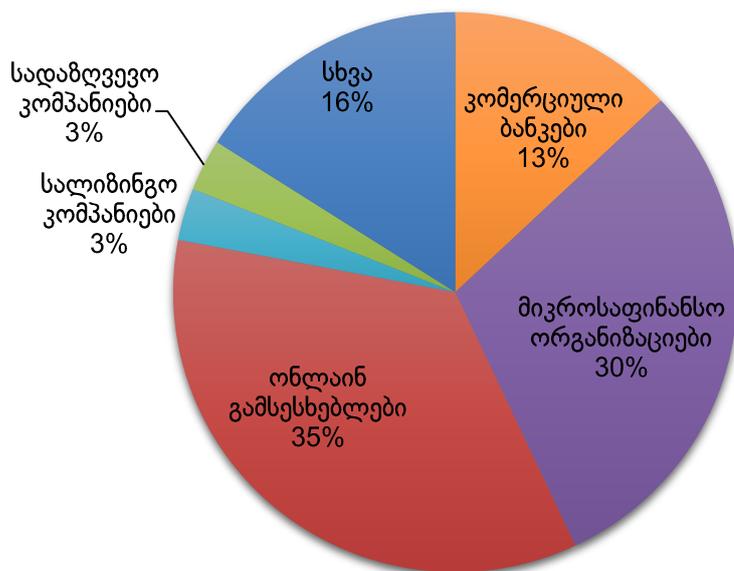
Scale 3 provides the dynamics of record growth from 9000 in 2006 to 18 ml in 2016. The pace of the record growth is in direct relation with increase of the crediting level and evidences necessity of inquired information. One of the factors of growth of crediting level was entry of the credit bureau to the market entailing simplification of procedures and risk reduction. For instance, if approval of the loan required a couple of days in the past, now it is possible to obtain in a couple of minutes. The number of credit products has also increased becoming more diverse. However, it had yet another reasons as well.

“Creditinfo Georgia” conducts its activity in financial sector. It provides the commercial banks, micro-financial organizations, online credit companies, leasing companies and other organizations with data. Estimation of the financial institutions being the customers of the credit bureau would be interesting.



Scale 4: Number of Records of the Joint-Stock Company "Creditinfo" according to the actors of the financial sector

ჩანაწერების რაოდენობა საფინანსო სექტორის მონაწილეების მიხედვით



Source: JSC "Creditinfo Georgia"

Scale 4 provides that the share of the commercial banks (13%) is lower compared to the micro-financial (30%) and online credit organizations (35%). It may evidence that the hereof organizations operate with smaller resources and are oriented to the short-term loans while the commercial banks are capable to provide the customers with the long-term financial resources. The natural persons and business subjects also refer to the micro-financial organizations and online credit companies the income structures of which fail to allow them referring the commercial banks.

Creditinfo Georgia offers various types of services to the financial sector customers. All the persons are allowed once per year being cognizant with the credit history free of charge. The company renders the chargeable services as well enabling registration of the customers allowing them track the changes of the data in the extracts of the credit history. It is a good opportunity for the natural persons to track their credit history and manage their portfolio.

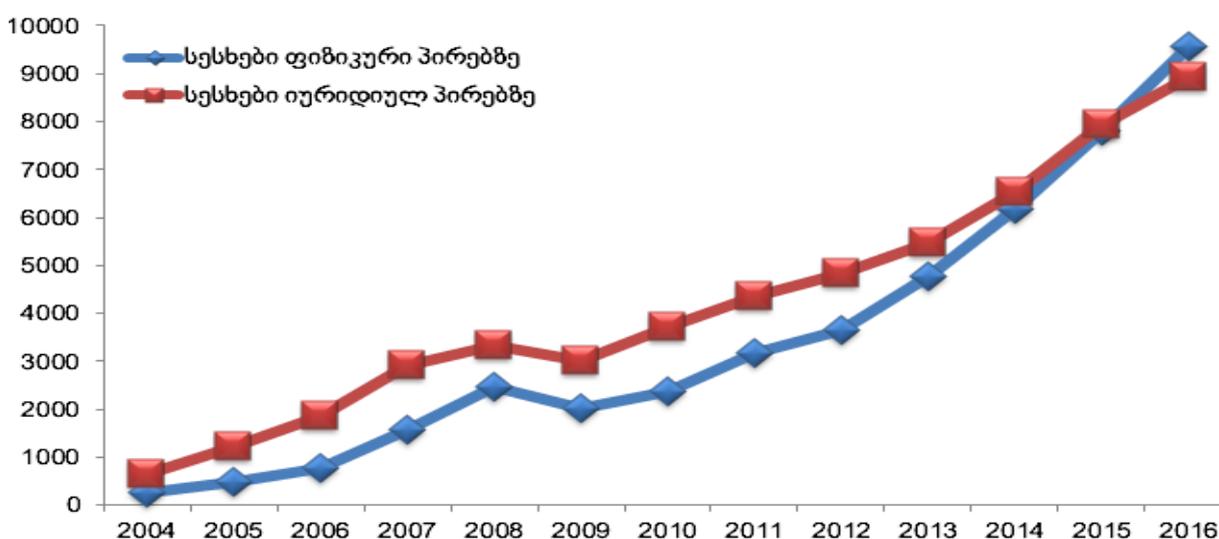
Recently, "Creditinfo Georgia" and distribution companies started cooperation. Distribution companies will have access to the information about the outstanding debts and will be allowed uploading information about business subjects into the uniform database. It is an important factor upon concluding the deals if we take the resonant examples of the trade networks into account when the insolvent trade networks have entailed grave problems to the distribution companies and established unhealthy practice on the market. We can state that this cooperation



will facilitate to reduction of the risks of the distribution companies and thus, we will prevent unhealthy business model in long-term perspective in this sector.

It would be preferable for other legal entities which need to hold the certain information about the partner organizations to follow the example of the distribution companies. As a result, we will prevent the fraud behavior. Besides, it is possible simultaneously with so-called negative database to create the database of the certain type where the positive rating is conferred to the bona fide tax-payer business subjects, simplifying use of low-interest loan products for them.

Scale 5: Loans issued by the commercial banks according to the legal entities and natural persons (million GEL)



Source: National Bank of Georgia, www.nbg.gov.ge.

Scale 5 provides that the loans issued to the legal entities within 2004-2015 exceeded the loans issued to the natural persons. As of the end of 2016, the loans issued to the natural persons constituted 9.6 ml GEL, while the loans issued to the legal entities were in the amount of 8.9 ml GEL. One of the factors entailing hereof index was that the sole entrepreneurs are as well accounted in the natural persons since 2015. As expected, the crediting level for the legal entities in the event of development of the loan market will exceed the crediting level for the natural persons.

Taking the international experience into account, Creditinfo should preferably improve the database. The database may contain the record about incomes as of the legal entities so of the natural persons. It will facilitate not only the financial sector but the debtors to obtain the loan in simplified manner without necessity of submission of the additional documents, such are: salary certificate, bank extract of income certificate. In the event of the natural persons, any financial institution shall be able to study the hereof data. As to the legal entities, information about their incomes will be accessible for the commercial banks and micro-financial organizations (as these institutions solely offer business loans). It will facilitate the financial institution in the shortest period to study the company incomes and taking the lowest as possible credit risks into account, approve the loans. It is recommended to ensure strict monitoring of data protection mechanism to prevent disclosure of the information



about the financial state of the legal entities to other organizations. The record on incomes of the legal entities and natural persons shall be uploaded into the database on the basis of their consent solely.

Most of the consumers without registered or sufficient income, resorts to the private usurer for the loans. In the event of improved financial state, the commercial banks evade repayment of such type of liabilities. It is entailed with the fact that the consumers fail to prove how good faith he/she had in repayment of the liability of the private usurer. Correspondingly, this sector as well shall be involved and on intermittent-basis update information in the database of Creditinfo. It is as well preferable to enclose the database on socially vulnerable persons to the database. It will facilitate us to prevent past negative experience when the loans of certain types were issued to the socially vulnerable population.

Conclusion and Recommendations

The study revealed the role of the credit bureaus, in case of Georgia of JSC “Creditinfo” development of the financial sector:

- Stability of the financial sector;
- Transparent credit risks;
- Reduced interest rates;
- Accessibility to financial resources;
- Monitoring of the level of excessive debt and frauds;
- Improvement of investment milieu of the country.

At present, the activity of the credit bureaus in Georgia is monitored by the Personal Data Protection Inspector. It is noteworthy that the information about the legal entities and natural persons is protected from unauthorized access. However, increased importance of the credit bureaus in the future may entail necessity of regulation.

It is noteworthy that the credit bureaus play an important role in reduction of credit risks. As a result of the study of the current state, NGO “Society and Banks” has developed the recommendations ensuring development of the financial system and facilitating to protection of consumers’ rights and improvement of service quality.

- Swifter update of the information about the credit records is preferable (currently, the term constitutes 15 days);
- If demanded by the consumer, accumulation of the information about the incomes in the credit bureau will simplify issue of the loans;
- We will hail cooperation of the credit bureau with the legal entities. Accessibility of the legal entities to the information of the credit bureaus will prevent fraud problems and facilitate to stability.



