Doing Business: Getting Credit and APEC

Submitted by: World Bank
Doing Business – Overview

- Doing Business measures the regulations applying to domestic small and medium-size companies through their life cycle
- 10 indicators in 183 countries
- The objective: well-designed, streamlined regulations, accessible to all
- Doing Business 2010 is the 7th report
Top 30 on the ease of Doing Business 2010 – Singapore tops the rankings 4th year in a row

<table>
<thead>
<tr>
<th>1. Singapore</th>
<th>16. Finland</th>
</tr>
</thead>
<tbody>
<tr>
<td>2. New Zealand</td>
<td>17. Mauritius</td>
</tr>
<tr>
<td>3. Hong Kong, China</td>
<td>18. Sweden</td>
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<tr>
<td>5. United Kingdom</td>
<td>20. Bahrain</td>
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<tr>
<td>6. Denmark</td>
<td>21. Switzerland</td>
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<td>7. Ireland</td>
<td>22. Belgium</td>
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<td>8. Canada</td>
<td>23. Malaysia</td>
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<td>10. Norway</td>
<td>25. Germany</td>
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<td>11. Georgia</td>
<td>26. Lithuania</td>
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<td>12. Thailand</td>
<td>27. Latvia</td>
</tr>
<tr>
<td>13. Saudi Arabia</td>
<td>28. Austria</td>
</tr>
<tr>
<td>15. Japan</td>
<td>30. Netherlands</td>
</tr>
</tbody>
</table>

How do APEC economies compare across regions?

Average Getting Credit ranking

<table>
<thead>
<tr>
<th>Region</th>
<th>Ranking</th>
</tr>
</thead>
<tbody>
<tr>
<td>High income: OECD</td>
<td>35</td>
</tr>
<tr>
<td>APEC</td>
<td>49</td>
</tr>
<tr>
<td>Europe &amp; Central Asia</td>
<td>51</td>
</tr>
<tr>
<td>Latin America &amp; Caribbean</td>
<td>76</td>
</tr>
<tr>
<td>East Asia &amp; Pacific</td>
<td>97</td>
</tr>
<tr>
<td>South Asia</td>
<td>100</td>
</tr>
<tr>
<td>Middle East &amp; North Africa</td>
<td>112</td>
</tr>
</tbody>
</table>
Methodology – Getting Credit

Getting credit has two separate sub-indices:

- Strength of legal rights: Index from 0 to 10
- Depth of credit information: Index from 0 to 6

Why Legal Rights?

- Affordable credit allows for the creation or expansion of businesses.
- Banks are more likely to lend — and at better rates — when a borrower can offer collateral.
- Types of collateral available: immovable and movable property.
- In developing economies: movable property is not accepted due to a lack of legal framework. However, most SME’s do not own real state.

“In Latin America, ‘Micro, small and medium size enterprises typically have 95% of their assets in movable property rather than real estate…Those owning no real estate or lacking formal title to their land do have assets: their movable property and land use rights. Under advanced collateral systems, this property could serve as collateral. Yet because of the defective legal system for using collateral, they cannot obtain such credit”
Movable property is not accepted as collateral

Why Legal Rights?

- The terms on which lenders make credit available depend on several factors: the lenders' cost of capital, the transaction costs to make the loan, and risks the loan will not be repaid.
- Higher costs and risks result in smaller, shorter loans at higher interest rates.
- Strong credit rights mitigates lender's risk and therefore help expand loan.
- If creditors have priority over other creditors or more bargaining power to force repayment or take control of the firm, they will extend credit on more favorable terms.

"In countries where security interests are perfected and there is a predictable priority system for creditors in cases of loan default, credit to the private sector as a percentage of gross economic product (GDP) averages 60% compared with only 30% to 32% on average for countries without these creditor protections"
What does the indicator cover?

Credit cycle: NPSI three main stages

Creation:
- Parties to a security agreement.
- Collateral and obligations that are allowed in a security agreement.
- Flexibility through the number of charges that can be used to secure a large number of assets.
- Flexibility of the agreement through a general description of its components.

Publicity:
- Third party effectiveness.
- Transparency of information.
- Speed of the process.
- Recommended approach: registration.

Enforcement:
- Priority rules outside/inside bankruptcy.
- Secured creditors protection during reorganization/bankruptcy processes.
- Out of court enforcement.

Legal Rights Index (0-10)

<table>
<thead>
<tr>
<th>Strength of legal rights index (0-10)</th>
<th>10</th>
</tr>
</thead>
<tbody>
<tr>
<td>Can any business use movable assets as collateral while keeping possession of the assets?</td>
<td>1</td>
</tr>
<tr>
<td>Does the law allow businesses to grant a non possessory security right in a single category of movable assets, without requiring a specific description of the collateral?</td>
<td>1</td>
</tr>
<tr>
<td>Does the law allow businesses to grant a non possessory security right in substantially all of its assets, without requiring a specific description of the collateral?</td>
<td>1</td>
</tr>
<tr>
<td>May a security right extend to future or after-acquired assets, and may it extend automatically to the products, proceeds or replacements of the original assets?</td>
<td>1</td>
</tr>
<tr>
<td>Is a general description of debts and obligations permitted in collateral agreements, so that all types of obligations and debts can be secured by stating a maximum amount?</td>
<td>1</td>
</tr>
<tr>
<td>Is a unified collateral registry in operation?</td>
<td>1</td>
</tr>
<tr>
<td>Do secured creditors have absolute priority to their collateral outside bankruptcy procedures?</td>
<td>1</td>
</tr>
<tr>
<td>Do secured creditors have absolute priority to their collateral in bankruptcy procedures?</td>
<td>1</td>
</tr>
<tr>
<td>During reorganization, are secured creditors’ claims exempt from an automatic stay on enforcement?</td>
<td>1</td>
</tr>
<tr>
<td>Does the law authorize parties to agree on out of court enforcement?</td>
<td>1</td>
</tr>
</tbody>
</table>
Legal rights in APEC economies

Percent of APEC economies

- Movable assets can be used as collateral: 100%
- General description of debts and obligations permitted: 95%
- Non-possessory security rights allowed in all assets: 71%
- Non-possessory security rights allowed in a single category of revolving movable assets: 67%
- Parties can agree on out of court enforcement: 67%
- Security right extends to future assets: 57%
- Secured creditors have absolute priority outside of bankruptcy: 52%
- Secured creditors' claims exempt from an automatic stay: 48%
- Secured creditors have absolute priority during bankruptcy: 43%
- Unified collateral registry exists: 38%

Legal Rights in APEC

Legal Rights Index

- New Zealand: 10
- Singapore: 10
- Malaysia: 10
- Hong Kong, China: 10
- Australia: 10
- United States: 10
- Vietnam: 10
- Japan: 8
- Korea, Rep.: 8
- Peru: 8
- Brunei Darussalam: 8
- Canada: 7
- China: 7
- Mexico: 7
- Papua New Guinea: 6
- Taiwan, China: 6
- Chile: 5
- Thailand: 5
- Russian Federation: 4
- Indonesia: 4
- Philippines: 4
- Taiwan, China: 3
- Indonesia: 3
- Philippines: 3

9/22/2010
Reforms that improved legal rights in APEC

- New Zealand: Personal Property Securities Act (1999)
  - A wider range of movable assets, including future property, can be used as collateral.
  - General description of assets.
  - Wider range of obligations secured and maximum amount of debt.
  - Unified collateral registry is operational and is searchable by debtor's name.
- Peru: The Bill on Guarantees Based on Moveable Property (2006)
  - Secured creditors have priority to their collateral outside bankruptcy procedures.
  - Allow out of court enforcement by law.

Getting Credit (Credit Information)

**Public credit registry:**
Database managed by the public sector, usually by the central bank or the superintendent of banks that collects information on the creditworthiness of borrowers (persons or businesses) in the financial system and facilitates the exchange of credit information amongst banks and financial institutions.

**Private credit bureau:**
Private firm or nonprofit organization that maintains a database on the creditworthiness of borrowers (persons or businesses) in the financial system and facilitates the exchange of credit information amongst banks and financial institutions.
Methodology – Getting Credit (credit information)

Depth of credit information: (Index from 0 to 6)
1. Data on both firms and individuals are distributed
2. Both positive and negative credit information is distributed
3. Data from retailers, trade creditors or utilities as well as financial institutions are distributed
4. 2 years or more of historical data are distributed
5. Data on all loans below 1% of income per capita are distributed
6. By law, borrowers have the right to access their data

- Public registry coverage: number of individuals/firms as a % of adult population
- Private bureau coverage: number of individuals/firms as a % of adult population

→ Impacts score if the coverage is less than 0.1% of adult population

What type of information do credit bureaus collect?

1. Positive and negative data

- Positive information:
  • Amount of loans (original, outstanding, installments)
  • On time repayment patterns

- Negative information:
  • Arrears
  • Defaults (normally after a certain time it is considered a default, and the bank may cancel the loan)
  • Court judgments, bankruptcies
What type of information do credit bureaus collect?

2. Individuals and Firms

- Are individuals and firms listed in the database?
- Please note that we count sole proprietors as individuals and not firms.

From where do the bureaus get their data?

3. Sources of data

- Many sources of data, to target various segments of the population:
  - Bank loans, mortgages
  - Leasing companies
  - Credit cards
  - Utilities (telephone-cell-, electricity, garbage collection, fines, etc…)
  - Retailers (consumer credit for white goods, furniture: Carrefour, Walmart, JC Penney)
  - Trade credit (firms like Nestle or a big distributor such as Coca-cola giving extended terms of payment to its clients-companies)
  - Microfinance institutions
4. Historical data

“Past behavior is a good predictor of future payments”

-Mr. A. Banker

- At least 2 years of data are distributed
  - What happens to a default & arrear when it is repaid: is it deleted?

5. Minimum loan amount to distribute loans

The minimum loan amount required to be included in the registry:
  - for loans, for defaults, etc.
  - We give one point if threshold is lower than 1% of income per capita
What type of information do credit bureaus collect?

6. **Is it guaranteed by law that borrowers can verify their data?**
   - It has to be written in the law

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### Credit Information Index (0-6) in Chile

<table>
<thead>
<tr>
<th>Depth of Credit Information</th>
<th>Private Credit Bureau</th>
<th>Public Credit Registry</th>
<th>DB score (5)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Are data on <em>both firms and individuals</em> distributed?</td>
<td>Yes</td>
<td>Yes</td>
<td>1</td>
</tr>
<tr>
<td>Are both <em>positive and negative data</em> distributed?</td>
<td>No</td>
<td>Yes</td>
<td>1</td>
</tr>
<tr>
<td>Does the registry distribute credit information from <em>retailers, trade creditors or utility companies</em>?</td>
<td>Yes</td>
<td>No</td>
<td>1</td>
</tr>
<tr>
<td>Are <em>more than 2 years</em> of historical credit information distributed?</td>
<td>No</td>
<td>No</td>
<td>0</td>
</tr>
<tr>
<td>Is data on <em>all loans below 1% of income per capita</em> distributed?</td>
<td>Yes</td>
<td>Yes</td>
<td>1</td>
</tr>
<tr>
<td>Is it <em>guaranteed by law</em> that borrowers can inspect their data in the largest credit registry?</td>
<td>Yes</td>
<td>Yes</td>
<td>1</td>
</tr>
<tr>
<td><strong>COVERAGE (% of adult population)</strong></td>
<td>33.9</td>
<td>32.9</td>
<td></td>
</tr>
</tbody>
</table>
Credit information in APEC

Depth of Credit Information Index

People's Republic of China (2006): established credit registry

Indonesia: increased scope of credit information / lowered thresholds on loans being reported

Papua New Guinea (2008): new private credit bureau

Philippines (2008): new act setting regulations for credit information

Vietnam (2010): Decree on Credit Information Operations

- Improved scope of credit information that is distributed (ex: historical data, positive and negative information)
- Low minimum threshold (or none) for loans being reported
- Data from non-regulated institutions is distributed (ex: retailers, utilities)
- Borrowers can access their credit report
- Allow out of court enforcement by law.
Thank you. For more information: www.doingbusiness.org