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A Conceptual Study On Credit Information Sharing: A Literature-Based Approach

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ABSTRACT

This literature survey explores the evolution of credit information sharing, credit information bureaus in contemporary financial systems that support well-informed lending choices and improve credit market efficiency, and their effects on borrowers. The research looks at credit information exchange and credit bureaus in India and other nations. The results demonstrate the growing significance of credit information bureaus as a result of the widespread use of credit reports. Employers use it to find information about a candidate's credit history, and insurance companies, car manufacturers, landlords, and employers use it to assess a client's credit worthiness. Therefore, it is evident that the current financial system depends on the exchange of credit information. The results show that for high-quality borrowers, exchanging credit information lowers loan duration and the interest rate spread. It was discovered that credit information bureaus had a favourable and substantial effect on banks' credit performance, globally.

Keywords: Credit Information Bureaus, Credit Information Sharing, Credit Score, Banks

Jel code: G21, G28, D14

Introduction

Society has transitioned from an agrarian to an industrial society, now becoming a knowledge society. Information literacy is crucial for this, and Credit Information Companies (CICs) play a vital role in disseminating credit information, influencing future business growth (Chakrabarty, 2013). According to a global survey of credit information systems, developing nations are rapidly realising the value and benefits of information sharing, and the deployment of these systems has grown significantly over the past ten years, especially in Asia and Latin America (Luoto, McIntosh, & Wydick, 2007). Consumer credit bureaus have

existed for a while in the majority of industrialised nations, including Europe in the 1960s, the US in the 1970s, Hong Kong, and Australia in the 1980s and 1990s. Singapore's infrastructure and market for credit information are very young. it is started in 2002 (Mingyue).

A private credit bureau improves credit data quality for creditors, focusing on retail and MSME lending markets. Public credit registries support prudential supervision and improve credit portfolio quality by enabling access to data from regulated financial institutions, typically owned by central banks (ICCR, 2022). Equifax, Experian, and TransUnion are the three largest nationwide providers of credit reports, sometimes called nationwide consumer reporting agencies (Cooper, 2023).

According to Jappelli and Pagano (2002), credit information sharing is the sharing of data on a client's financial history, including credit history, credit worthiness, and the borrower's current debt level. For the credit market to operate effectively, credit information bureaus are necessary. They limit excessive debt, assist excellent borrowers obtain financing, and enable lenders to better identify and manage risks (Mylenko, 2008). The adoption of a high-quality system for gathering and processing credit information will have long-term consequences that encourage the creation of constructive impulses for the growth of the credit market (Bielova & Savchenko, 2016). In addition to determining credit eligibility, credit reports are employed in other decision-making processes. These include determining (together with previous account history) eligibility for checking accounts, determining rates for car and other property and casualty insurance when allowed by law, and qualifying for rental accommodation. A potential employer may review a candidate's credit record when they apply for a job, if the candidate gives permission (CFPB, 2012).

Review of literature

2.1 Evolution of credit information bureaus

Credit bureaus emerged in the United States in the late 1800s to support merchant lenders in extending credit to local businesses and individuals. Before these lists, local merchants used personal knowledge of borrower's character to make credit decisions (CFPB, 2012). Credit bureaus and credit scoring have existed for many decades in advanced nations like the U.S. and Europe, but in India, they only gained legal recognition in 2007 when laws forcing banks to provide data to bureaus were established (Mishra, Prabhala, & Rajan, 2019). In August 2000, State Bank of India and HDFC formed Credit Information Bureau (India) Ltd. (CIBIL), with a 40 percent equity stake each and two foreign technology partners, M/s. Dun & Bradstreet Information Services (India) Pvt. Ltd. and TransUnion International Inc., U.S.A., splitting the remaining 20 percent equity stake. It was developed in response to the changing demands of a financial market that was developing (Chakravarti & Chea, 2005). Equifax, Experian, CRIF High Mark, and TransUnion Credit Information Bureau (India) Limited (TransUnion CBILI) are the four private credit information companies (CICs) in India. All licensed credit institutions are required by RBI to provide all CICs with borrower credit information (Paul, 2018) National markets also vary; in the UK and Italy, two or three businesses share the majority of the market, but in most countries, such as Germany, Finland,

Ireland, France, or Sweden, a single big credit bureau dominates the industry. Additionally, in other economies, like Belgium, state and private credit bureaus coexist (RIESTRA, 2002). (Rothemund & Gerhardt, 2011) shows that the majority of credit bureaus in Europe are subsidiaries (11), meaning they are owned entirely or in the majority by another business, which is often another credit agency. It is noteworthy that Experian (UK) operates subsidiaries in Denmark, Italy, Norway, and Spain under this category. Additionally, the Italian business CRIF S.P.A. owns the Czech Credit Bureau A.S. and the Slovak Credit Bureau.

Financial institutions' demand for information and bank supervisors' pressure to improve risk management led to initiatives in Africa to develop credit bureaus (Mylenko, 2008). The cost of credit information has continuously decreased over the past 10 years due to greater investment and innovation, partly because of the emergence of new data sources and heightened competition among credit rating agencies (Dunkerley, et al., 2021). both traditional (logistic regression and decision tree) and more advanced (support vector machines, ensembles, i.e. bagging and boosting, and neural networks) techniques appear to be the most widely used credit scoring approaches (Markov, Seleznyova, & Lapshin, 2022).

2.2 Impact of credit information sharing on credit institutions

(Chakravarti & Chea, 2005) All financial institutions in the United States and maybe a few other industrialised nations rely on credit bureaus as their magic wand to stay afloat in the fiercely competitive lending and profit-making market of today. (P.K, 2016) Because bank loans are predicated on a mutually beneficial relationship between the borrower and the lender, banks will evaluate the borrower's creditworthiness by obtaining a credit report from the credit bureaus. (Hachinohe University Research Institute (HURI), Daiwa Institute of Research (DIR), 2008) The information's theories imply that financial institutions will typically turn into intermediates.

(Bielova & Savchenko, 2016) The quality of a credit portfolio is crucial for a bank's reliability and financial stability, but in Ukraine, low information collection and use contribute to high credit risks. (Mungiria, James, Ondabu, & Ibrahim, 2019) The study proves that credit reference bureau checks have a part in Kenyan commercial banks' financial intermediation of non-performing loans. The study also discovered a negative association between credit reference bureau checks and non-performing loans. Thus, it can be said that there is a connection between the amount of financial intermediation demonstrated by non-performing loans in Kenyan commercial banks and information from credit reference bureaus. (Pauline & N, 2022) The research showed that commercial banks' credit performance was positively and significantly impacted by credit information bureaus, with this effect being particularly noticeable in the Mwanza area. The impact of non-performing loans on commercial banks' credit performance was beneficial but not statistically significant.

The findings show that Serbian creditors base their credit choices on accurate and high-quality information, which significantly reduces risk and, in turn, interest rates on loans that are authorised (Simovic, Vaskovic, & Poznanovic, 2010). Regardless of whether the information sharing method is private or public, we find that bank lending is higher and credit risk is lower in nations where lenders exchange information (Jappelli & Pagano, 2001). Since credit scoring provides banks with a tool to more precisely price risk, it may also promote additional lending. However, there is a lot of flexibility in loan conditions due to the normal bank-borrower relationship, which is developed over years of lending (Mester, 1997). It is determined that credit rating has a favourable effect on the credit risk of India's banking industry (G & Madhav, 2021). Since bilateral banking partnerships punish borrowers, it is possible for borrowers and lenders to engage in recurrent interactions. Additionally, the incentive impact of credit reporting is minimal. The capacity of lenders to collect rents from relationships is weakened by information sharing, which nonetheless influences market outcomes (BROWN & ZEHNDER, 2007).

2.3 Effects on Borrowers and Credit Access

The credit bureau is one among those instruments that may aid in managing excessive debt. There is a significant risk of excessive debt in an economy where the credit information index value is zero, or in a nation without a credit bureau. (Simovic, Vaskovic, Rankovic, & Malinic, 2014). Sharing information about borrowers' characteristics and indebtedness improves banks' understanding, enables accurate repayment predictions, reduces informational rents, acts as a borrower discipline tool, and eliminates over-indebtedness by drawing credit from multiple banks (Jappelli & Pagano, 2005).

(Fosu, Henry, & Ciftci, 2023) study into how sharing credit information affects debt costs, paying special attention to the establishment of credit bureaus in emerging nations. Using the DID technique and a sizable dataset of more than 7200 businesses from 28 developing nations between 2004 and 2019, it was discovered that when credit bureaus were established, businesses' average cost of debt drastically decreased. (OECD, 2010) The theory underlying the beneficial effects of credit information sharing as well as the operational and legal framework of registries in both OECD and non-OECD nations are reviewed in this study. It was discovered that in the absence of a credit registry, borrowers tended to only pay back loans when they intended to keep up their existing lending arrangement. (Son, Khanh, & Liem, 2020) Public credit registries and private credit bureaus help alleviate information asymmetry, reduce adverse selection, increase credit, and reduce corruption's negative effects on financial sector development.

(Alvarez-Botas & Gonzalez, 2024) The findings indicate that sharing credit information reduces loan maturity and the interest rate spread for high quality borrowers. If credit information bureaus never kept the credit information, consumers would pay more and get less credit overall (Avery, Calem, & Canner, 2004). Enhanced credit information sharing has a positive impact on borrower's investment efficiency (Hou, Mengistu, Ng, & Zhang, 2024). Research from both domestic and international sources indicates that an investor's credit score will be higher and more favourable if their credit history is excellent. Additionally, loan collection would be quite convenient (G & Madhav, 2021). having a low credit score

can have a number of serious drawbacks, such as trouble getting credit, higher interest rates, fewer credit options etc.. (Mishra M. , 2023).

Findings

Over the last twenty years, a number of nations have implemented credit information-sharing programs, driven by the desire to increase credit availability. From 2004 to 2018, around 75 developing nations implemented credit information-sharing programs (Fosu, Henry , & Ciftci, 2023). The banking industry is known for being a trustworthy and confident one. Actually, the word "credit" indicates confidence. Banks will evaluate a borrower's creditworthiness by obtaining a credit report from credit information agencies since bank loans are predicated on a reciprocal connection between the lender and the borrower (K, 2016). By encouraging lending transparency, credit information systems contribute to the development of an efficient financial system. They are also useful instruments for reducing moral hazard and adverse selection in credit markets, and they have been shown to increase the number of borrowers in formal credit markets and decrease interest rates and default rates overall (Luoto, McIntosh, & Wydick, 2007).

The credit bureau is the magic wand that all of the financial institutions in the United States and maybe a few other industrialised nations utilise to stay afloat in the fiercely competitive lending and profit-making market of today. Credit bureaus, also called credit reporting agencies (CRAs), gather data from merchants, lenders, landlords, and other sources about bill payments, loan repayments, credit availability, monthly debt, and other types of information. They then sell the report to businesses so they can conduct credit assessments, determine whether a credit risk is good or bad, and determine the appropriate interest rate to charge (Chakravarti & Chea , 2005).

It is feasible to draw the conclusion that indebtedness per capita (IPC) is significantly influenced by the Credit Bureau Functional Index (CBFI). It demonstrates the existence of a broad pattern that debt decreases as the CBFI value rises. (Simovic, Vaskovic, Rankovic, & Malinic, 2014). It is clear that credit bureaus are advantageous to both lenders and borrowers. Maximising the amount of favourable loan agreements given and rejecting the unfavourable ones are goals shared by both partners. For lenders, the secret to guaranteeing the success of fund management is optimising the credit that is given and denied. Repayment of credit will guarantee a spotless record on the register and permit further borrowings from the credit market since, from the standpoint of the borrower, there is an interest in gaining access to credit in order to fund purchases (RIESTRA, 2002).

Credit information registries, often known as bureaus, are responsible for gathering and maintaining credit data in a database. Sometimes people make a distinction between "credit bureaus," which are information brokers, and "public credit registries," which are often run by the central bank and require participation from a smaller group of financial firms (Hachinohe University Research Institute (HURI), Daiwa Institute of Research (DIR), 2008). Governments should make sure that the establishment of private credit bureaus won't be impeded when they want to establish a public credit register to provide credit information (OECD, 2010).

The 3 large CRAs in the United Kingdom (UK) are Equifax, Experian and TransUnion (FCA, 2023). Positive and negative data are gathered by the KSV private credit bureau in Austria. Before the establishment of a public registration by the National Bank of Belgium (NBB), private registries were in place in Belgium. Currently in France, the Bank of France is in charge of the public record of negative information. In Germany the Bundesbank owns and runs this nation's first public registry, which was created in 1934. Italy is home to two established credit bureaus: CRIF and CTC (Consorzio per la tutela del credito). In the Netherlands, in 1965-founded Dutch Bureau Krediet Registratie, or BKR, is a great illustration of a positive central registry. In Portugal, in 1995 founded Credinformações as a joint venture between Equifax and ASFAC (Associação das Financeiras por Aquisição a Crédito), Credinformações is the primary credit bureau in this nation, same like in Spain. UC AB, a Swedish company, gathers both positive and negative data, including credit type and demographic data in Sweden. Currently, there are just three major credit bureaus in the United Nation: Equifax, Experian, and Transunion (RIESTRA, 2002). Transunion CIBIL, India's oldest bureau, was founded in 2000 (Mishra, Prabhala, & Rajan, 2019) At the moment, there are four private Credit Information Companies (CICs): Equifax, Experian, CRIF High Mark, and TransUnion Credit Information Bureau (India) Limited (TransUnion CBIL) (Paul, 2018).

Conclusion

Prior to the last 20 years, providing credit information was not important. However, it is an important topic of conversation worldwide right now. Everyone needs money to live in peace, thus when money is in shortage, credit options should be available. Numerous banks and other credit organisations exist, and they provide clients with a range of credit plans. However, bad debt is additionally a challenge for the lender. What happens if the borrower defaults on the loan? In order to decide whether or not to give credit, banks and other organisations should ascertain the creditworthiness of their clients before making any loan offers. Therefore, credit information bureaus assist the lender in determining the borrower's credit worthiness. They serve as an intermediary between the borrower and the lender. Both the borrower and the lender benefited from the bureaus sharing this credit data. By determining the borrower's credit quality, the lender can make the best choices and increase revenue by preventing bad debt. Customers with a solid credit history will benefit from good loan agreements, such as reduced interest rates and a greater loan duration, among other things.

Credit information is now used by insurance firms, automobile companies, employers, and landlords to determine a client's credit worthiness, as well as by employers to learn about a candidate's credit history. Thus, it is clear that exchanging credit information is crucial to the modern financial system. Therefore, raising awareness of this is essential. Simultaneously, the data's accuracy and quality should be improved. Additionally, consumer dispute resolution must be sufficiently robust.

Sharing credit information will increase borrowers' awareness of their creditworthiness, improve their credit behaviour, and increase the profitability of credit institutions, all of which will contribute to the expansion of the economy as a whole.

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