

B A S I S



■ Collaborative Research
Support Program

Credit Bureaus and the Rural Microfinance Sector: Peru, Guatemala, and Bolivia

A joint project between
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Presentation

Credit markets are notably imperfect, and most notably for the rural poor. The result is that a vast majority of rural households are excluded from financial services, reproducing their lack access to sources of income and to sources of protection from income shocks. The imperfect nature of credit markets comes from the fact that loans are transactions over time occurring under imperfect information between lender and borrower. This creates four problems that need to be solved for a loan transaction to occur:

- Adverse selection in recognizing borrower types.
- Moral hazard in project choice and management by borrowers.
- Need for insurance by borrowers to limit personal exposure.
- Moral hazard in loan repayment.

The consequence of these difficulties is that formal lenders require the pledging of collateral. As a consequence, credit markets are both wealth constrained, which severely limits access for the poor, and risk constrained as the poor cannot expose collateral to risk even if they have collateral to pledge such as title over a house or a plot of land. With loans from formal lenders inaccessible, local money lenders have most often been the only source of credit available to the rural poor. The extraordinarily high cost of these loans has limited their use to emergency situations or to very short run and high return transactions.

The “microfinance revolution” has helped make substantial progress in overcoming this deadlock for the poor. It consisted in a set of institutional innovations aimed at resolving the four problems contained in loan transactions, without relying on wealth as required collateral, with some provision of insurance to reduce personal exposure, and offering loans at interest rates far inferior to those charged money lenders. This consisted mainly in microfinance institutions (MFIs) engaging in group lending with joint liability, village banking, and individual loans.

The microfinance revolution has opened access to financial services for millions of poor borrowers, including across Latin America. While we do not know enough about the true impact of these services on poverty, evidence on success stories abound. Yet, there are several problems that remain unresolved and there are new problems that emerge as the microfinance revolution comes to age. Most notable are the following:

i) Successful expansion of microfinance has been in sectors where money has a fast turnover and potentially high rates of return. This has been mainly in commerce and non-farm microenterprises. Use of microfinance services for agricultural investments remains limited by long turnovers and high costs.

ii) Graduation of successful borrowers from microfinance lenders to formal lenders remains limited by lack of information on reputation accumulated by borrowers through a long history of loans and timely repayments with a microfinance supplier.

iii) Increasing competition among microfinance suppliers (1) reduces the possibility for suppliers to use dynamic incentives (rising loan levels as the sequence of successful repayments extends) in reducing adverse selection and moral hazard; (2) increases the possibility for borrowers to take multiple loans without the knowledge of

suppliers, resulting in over-indebtedness; and (3) increases incentives for group default if alternative sources of loans are available for members of the group irrespective of past performance.

The “credit reporting revolution” has the potential of overcoming some of these problems, extending the reach and the benefits of the “microfinance revolution” among the poor. Indeed, in recent years, there has been an extraordinarily rapid penetration of credit bureaus that make borrowers’ histories publicly available. This has the potential to revolutionize the revolution. This is because reputation privately held by one microfinance institutions in which a particular client has been borrowing and repaying over time can now become a public good. On the supply side, it can increase competition among microfinance lenders as their best customers can now explore alternative sources of supply, capitalizing on the reputation they have gained in their borrowings with one MFI. It can also help microfinance lenders not only gain access to negative information about defaults by potential new customers, but also about positive information on their credit histories, reducing adverse selection and moral hazards in future loans transactions, and hence also lending costs. On the demand side, it can reduce ability by borrowers to be over-extended in debts without knowledge by suppliers, or to pledge collaterals with multiple lenders beyond their market value.

There are also risks for the poor associated with introduction of credit reporting systems. One is that poorer clients may be increasingly bypassed as MFIs can better identify more desirable borrowers and compete over those. The other is misinformation about past histories with weak rights for individuals to verify information and protect reputation.

To initiate an in-depth research project on these issues, the present report engaged into three country case studies of the development of the microfinance sector and the penetration of credit reporting systems in Peru, Guatemala, and Bolivia. These are three countries where credit reporting systems have already achieved extensive presence, and hence from which there is much to learn. Each country case study looked into:

- The evolution of the microfinance sector.

- The development of credit bureaus.

- The impact of credit bureaus on the microfinance sector.

- When possible, perceptions of the implications of credit reporting systems by microfinance clients.

Each case study presents an executive summary that summarizes findings. The overall perspective is one of extraordinary changes in microlending practices and in graduation to formal sector lending as a consequence of penetration of credit reporting systems. Yet, this development is chaotic and incomplete. In all countries, there exists a multiplicity of credit bureaus operating under different rules and offering different services. Regulation is uneven across institutions and countries. Client coverage is incomplete, in particular for many microfinance borrowers. And there is partial understanding among microfinance sector borrowers of implications for them of credit reporting. Hence, there is

still much to learn and much to do to capitalize on the promise offered by the “credit reporting revolution” in helping reduce rural poverty.

This report is the first step in a larger project on the impact of credit reporting systems on the microfinance sector and on access to financial services for the rural poor and, in particular, their agricultural operations. The next phase of the research is sponsored by BASIS through the project “Credit-Reporting Bureaus and the Deepening of Financial Services for the Rural Poor in Latin America”. This project is a joint undertaking between the University of California at Berkeley, the University of San Francisco, GRADE in Peru, and the FAO Office for Latin America.

PERU

INFORMATION SHARING AND MICROFINANCE IN PERU¹

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LIST OF ACRONYMS

CAC	Savings and Loans Cooperative (<i>Cooperativa de Ahorro y Crédito</i>)
CB	Credit Bureau
CCL	Lima Chamber of Commerce (<i>Cámara de Comercio de Lima</i>)
CEPES	Peruvian Center of Social Studies (<i>Centro Peruano de Estudios Sociales</i>)
CEPIR	Private Risk Information Center (<i>Central Privada de Información de Riesgo</i>)
CMAC	Municipal Savings and Loans Association (<i>Caja Municipal de Ahorro y Crédito</i>)
COFIDE	Financial Corporation for Development (<i>Corporación Financiera de Desarrollo S.A.</i>)
COFOPRI	Commission for the Formalization of Informal Property (<i>Comisión de Formalización de la Propiedad Informal</i>)
COPEME	Association of Private Organizations of Promotion and Development of Micro and Small Enterprises (<i>Consortio de Organizaciones Privadas de Promoción al Desarrollo de la Micro y Pequeña Empresa</i>)
CRAC	Rural Savings and Loans Association (<i>Caja Rural de Ahorro y Crédito</i>)
EDPYME	Organizations for Development of Small and Micro Enterprise (<i>Entidad de Desarrollo de la Pequeña Y Micro Empresa</i>)
ENNIV	National Household Survey for the Measurement of the Conditions of Living (<i>Encuesta Nacional de Hogares sobre Medición de Niveles de Vida</i>)
FENACREP	National Federation of Peruvian Savings and Loans Cooperatives (<i>Federación Nacional de Cooperativas de Ahorro y Crédito del Perú</i>)
FONCODES	National Fund of Compensation and Social Development (<i>Fondo Nacional de Compensación y Desarrollo Social</i>)
FONDEAGRO	Funds of Development of Agriculture (<i>Fondos de Desarrollo de la Agricultura</i>)
GDP	Gross Domestic Product
IFOCC	Institute of Support for Peasant Commercialization (<i>Instituto de Fomento a la Comercialización Campesina</i>)
INDECOPI	National Institute of the Defense of Competition and Protection of Intellectual Property (<i>Instituto Nacional de Defensa de la Competencia y de la Protección de la Propiedad Intelectual</i>)
INEI	National Institute of Statistics and Computer science (<i>Instituto Nacional de Estadística e Informática</i>)
MFI	Microfinance Institution
MIDE	Microcredit for Development (<i>Microcrédito para el Desarrollo</i>)
NGO	Non-Governmental Organization

LIST OF ACRONYMS

PETT	Special Project Land Titling and Rural Cadastre (<i>Proyecto Especial Titulación de Tierras y Catastro Rural</i>)
SBS	Superintendency of Banks and Insurance (<i>Superintendencia de Bancos y Seguros</i>)
SICOM	Consolidated System of Default (<i>Sistema Consolidado de Morosidad</i>)
SUNAD	National Superintendency of Customs (<i>Superintendencia Nacional de Aduanas</i>)
SUNAT	National Superintendency of Internal Revenue Administration (<i>Superintendencia Nacional de Administración Tributaria</i>)
USAID	United States Agency for International Development

EXECUTIVE SUMMARY

1. The microfinance (MF) sector has developed rapidly in developing countries over the last two decades, making credit available for many poor microentrepreneurs, although in most cases it has practically skipped the rural poor and most particularly their agricultural activities as smallholders.
2. This microfinance revolution has generated a number of studies on the sustainability and impact of the microcredit programs. One of the issues of growing concern in countries with a large microfinance sector is the effect of the increasing competition, among MFIs and with the commercial banks, on the sustainability of the sector. Higher competition improves the access to credit for small microentrepreneurs, but may also allow them to incur in over indebtedness, if credit histories remain private between the MFIs and their borrowers.
3. In Peru, like in many other developing countries, the MF sector has been growing significantly over the past two decades, especially in urban areas. At the same time, a risk information sharing system has been regulated by law since 1996, which allows for private providers, includes negative and positive information, but omits the unregulated microfinance sector.
4. This study discusses the mechanisms through which the credit bureau (CB) system has affected the performance of the microfinance sector in Peru, and searches for some insights on the kind of interventions that could improve the connection in a cost-efficient way. For that, we first revise the macro developments relevant for the microfinance sector and the CB system, including the recent regulatory adjustments. Then, we continue with a deeper analysis of the evolution of the two sectors in one region, the department of Cusco, which has a large MF sector, and a large agricultural sector. In Cusco, we also conducted some applied extensive interviews to a sample of credit officers and clients to receive further details on the situation of the MF sector, especially with respect to the financing of agriculture, and to the use and perception of the CB system.

Microfinance and Credit Bureaus in Peru

5. After the crisis of the late eighties, the Peruvian economy underwent a sharp process of stabilization and structural change that liberalized most goods and factor markets and reduce the participation of the state in productive activities while increased its regulatory role.
6. With respect to the financial sector the reform liberalized financial transactions and eliminated state development banks, which actually were already bankrupted by that time. It also strengthened substantially the regulatory power of the Superintendency of Banking and Insurance (SBS), and part of which included the development of a public credit bureau system and the regulation of private firms operating in the risk evaluation

and credit bureaus systems. Also, in an attempt to incorporate the growing number of NGOs offering financial services to small producers to the regulated sector, the law generated a special category, Entidades de Desarrollo de la Pequeña y Micro Empresa, (EDPYMES) with special tax and leverage incentives for formalization.

7. The Peruvian financial sector has 7 different types of financial institutions: commercial banks, financial entities, cajas municipales (CMACs), cajas rurales (CRACs), cooperatives (CACs), EDPYMES and NGOs. The last five can be considered exclusive of MFIs, although there is one commercial bank (Mibanco) and one financial entity (Solución) that also have the microentrepreneurs as their target group. All of them, but CACs and NGOs, are regulated by the SBS. The CACs are only supervised indirectly by the SBS, through the Federation of CACs. NGOs are not regulated.
8. The MFI sector grew a lot during the nineties, especially the CMACs, in urban areas, and even after the recession. Still, this growth has not been able to compensate the reduction in loans by commercial banks after the crisis of 1998. Access to credit by Peruvian households increase from 17% to 32% in 1997, to decrease again for 2000. (19%) In rural areas, evolution of access to credit did not increase during the economic recovery, remaining constant at around 20%. This result is consistent with the fact that the agricultural sector has not been reached by the positive evolution of the financial sector during the nineties.
9. The growth of the MFI sector was supported by technical assistance from different sources, noticeably the German cooperation (CMACs) and the American cooperation through COPEME's Microfinance Initiative. This growth has definitely increased competition among MFIs, and with commercial banks, especially considering that the agencies of MFIs are concentrated in larger cities, pretty much like those of commercial banks.
10. The public credit bureau system dates back to 1968 but the process was not digitalized, it was very outdated, included only large loans from regulated banks who were the only ones with access to the system. Technological advances were gradually introduced improving the quality of the information, but it was not until 1996 that a major upgrade was achieved due to the new banking law and an IADB loan. Only in 1998, the system incorporated records on loans smaller than US \$ 4,500, and records from CMACs, CRACs and EDPYMES.
11. The 1996 law also regulated the activities of private credit bureaus (CEPIRS). CEPIRS could access the public CB by paying a fee, and complement it with information from other sources, provided they do not contain sensitive information, information that violates the bank secrecy, the tax reserve, or inexact information. They can then sell access to that information to risk information customers for a fee.
12. In practice, five CEPIRs appeared in 1995 as the result of the private initiative. They were Riesgo Cero, CERTICOM and Infocorp. CEPIRs provided the same products as the public credit bureau managed by the SBS, and offered additional information such as information on protests filed at the Chamber of Commerce, credit information from department stores, information about taxes, and unpaid bills from the telephone, electricity, and cable companies. The CEPIRs also make verifications of the legitimate address, employment, housing condition, business premises, identity card and civil status. Today, only Infocorp and CERTICOM remain in the markets, and

Infocorp controls 80% of the market with a database of more than 6 millions registries available to 1,200 clients. It offers to its clients 18 different products.

13. An interesting development is that Infocorp is actively working to incorporate the activities of the non-regulated MFIs into their database, for which they signed an agreement with COPEME's Microfinance Initiative. (1998) A goal for the medium run is to incorporate positive and negative information from non-regulated MFIs, but they have started by offering a corporate rate to all MFIs that are willing to register with COPEME. They plan to work with willing NGOs on adapting their registry system so that they can include their information in the Infocorp database.
14. Currently, more than 80 MFIs are registered with COPEME to use the Infocorp database, of which 34 are NGOs with financial operations. Of those, 20 are already providing the Infocorp database with their negative information on a systematic basis. Key constraints for NGOs to provide their credit information are the lack of an adequate registry system and a legal constraint in the case of village banks. The interesting thing is that the proportion of consultancies to the Infocorp database that return some information on the potential client is relatively high, (above 80%, on average) and in one out of four cases, they find some negative information.

Microfinance and Credit Bureaus in Cusco

15. Cusco is located in the southern highlands of Peru, has 1.2 million inhabitants that largely live in rural areas (54%) working in small farms, (48%) and has an extreme poverty rate (51%) that it is twice that for the whole country. In terms of income, the most important economic activity is tourism.
16. 60% of the rural plots are organized in peasant's communities, which has limited the titling and registration efforts by PETT in Cusco. According to the land law, individual transferable land property rights can be issued for communal land, but only after the community agrees to it. Clearly, this limits the ability of these farmers to offer their land as collateral to obtain credit.
17. As in the rest of the country, the MF sector has been growing in Cusco, especially the regulated MFIs and mostly in urban areas. The regulated MFIs are CMAC Cusco, the CRAC Quillabamba or CREDINKA, the EDPYME Crear Cusco, the Financiera Solución, and the Lima-based EDPYME Credivisión. The NGOs tend to work more in rural areas but have been gradually moving away from the agricultural sector.
18. CMAC Cusco is clearly the leading MFI in Cusco and has very low default rates. In terms of default rates, the ones with worst performance are the CRACs and the NGOs, precisely the ones more connected to the agricultural sector. These MFIs were clearly affected by the crisis in 1998-2001 that hit the agricultural sector particularly hard, but also by political distortions. In 1998-99 local politicians targeted the clients of one of the main NGOs operating in rural areas, IFOCC, and organize a local movement in favor of group default.
19. Access to credit by households in Cusco is still higher than in the rest of the country, even in rural areas. Nevertheless, we need to clarify that the main sources are

not MFIs, regulated or non-regulated, but other informal sources such as the local store, local traders, and relatives.

20. The agencies of the MFIs are highly concentrated in larger cities, especially regulated MFIs. In that sense, it is clear that the CMAC Cusco, for example, competes for clients not only with other MFIs but also with commercial banks. NGOs tend to work more in rural areas and there is some sort of segmentation in the sense that only one NGO operates in any given area.
21. The use of the information in the Infocorp database is relatively low in Cusco, although there is some indication that the Certicom database is also used. However, 3 regulated MFIs are registered: the EDPYME Credivisión, the CMAC Cusco and the CRAC Quillabamba, and the first two are the ones that use the database the most. Clearly, this indicates that the information provided by Infocorp that is not-SBS based is valuable for those institutions. Another indicator of the usefulness of the credit information is that 83% of the checks return some credit information.
22. Of the 19 NGOs identified as suppliers of microcredit in the department, only 3 are using the COPEME-INFOCORP agreement to access the Infocorp database. One can think that these institutions should benefit from getting access at the right price, but it may also occur that they expect lower hit rates since they tend to be located in smaller cities. It seems plausible to imagine that they would benefit more if their own information would be included in the database, as well as information from other previous sources including the Ministry of Agriculture's Fondegros.
23. The INFOCORP-COPEME agreement commissioned a document to explore the possibilities for improvement and expansion, and seems to be interested in gradually including the 16 identified NGOs that are not yet using it. That document also indicated that most MFIs would be interested in participating and even to share their own information when their registry system allows them. It would be very important to see what would be the effect of these additions on the use of the CB system and on the functioning of the MF sector in the department.

Perception and Use of Credit Bureaus in Cusco

24. For this section, interviews were conducted in and around the city of Cusco with staff of regulated and unregulated MFIs, as well as with urban and agricultural clients of some of these MFIs. A total of nine MFIs and eight clients have been interviewed. The MFIs interviewed were of different sizes, target groups, and status, to represent the variety of the department.
25. We interviewed four regulated MFIs and five unregulated ones; five operate in urban areas, two operate exclusively in rural areas, and two operate both in urban and rural areas. The interviews were conducted with general or executive managers in unregulated MFIs, and with risk managers and credit officers in regulated MFIs. The questions focused on five elements: the methods of evaluation of credit applicants, the rules of use of credit bureaus, the guarantee requirements, the loans supervision, and the procedures in case of default.

26. With respect to the evaluation of credit applicants, most credit officers from interviewed MFIs indicated that they combine their evaluation of the clients' repayment capacity with the checks of the CB system. The regulated MFIs use the public system consistently but they and the unregulated MFIs have varying rules for the use of the private CB databases, in particular the one from Infocorp. Many of the MFIs also indicated that they also use their personal contacts in other MFIs and banks, to check on the credit history of their applicants.
27. About the way they use the credit history, we did not find that all MFIs have a floor limit for the loan sizes for which they check the system. Also, the interviews suggested that regulated MFIs use it more strictly, in the sense that no loan is approved for a person that has a history of default. On the other hand, two NGOs indicated that they sometimes approve loans for applicants with a history of default, if they find other information that indicates to them that the applicant is trustworthy for the loan.
28. Another important finding of the interviews was that MFIs tend to find many applicants with standing debts with other financial institutions or with department stores. In the past, they had rules that prohibit approving loans to such applicants, but now have been forced to change those rules. Some of them indicated that the rules now state that for an applicant to receive a loan by them, they cannot have more than 2 or 3 standing loans with other institutions.
29. It is often argued that MFIs can reach the poor better because they better use reputation and credit histories, albeit private, to reduce their collateral requirements. The interviews with the credit officers in Cusco did not support such notion, as all of them indicated that all their loans are guaranteed with some collateral. In the case of agricultural loans, it is true that titling of agricultural land is low in Cusco, but they can put their houses as guarantee for a loan. Certainly, though, this rule limit agricultural credit to farmers with larger plots, that are closed to the larger cities, that have accumulated previously mainly through non-agricultural activities.
30. Another interesting point that showed up in the interviews is the problem with outdated information. Most MFIs indicated that often times they approve loans to an applicant after checking the Infocorp database, only to learn later that he/she did have a loan but had not been registered at the moment of the check. Apparently, the database tends to be 2 months old, on average.
31. Only eight MFI clients were interviewed, but still some interesting information showed up. First, we found that old urban clients tend to report higher growth in their loan sizes, compared to the ones they obtained when just started working with the corresponding MFI, than rural ones. This finding is consistent with the fact that agricultural lenders are limited in their growth by their plot sizes, especially in the context of limited tradeability of rural land.
32. Also, we found that, although geographical segmentation of MFIs limit rural farmers to have at most one alternative for access to credit at one point, they tend to have a credit history with different providers over time. Many of them indicated having received credit from previous NGOs, the old Banco Agrario, etc.
33. Urban lenders, on the other hand, perceive the increase in the number of providers of microcredit, and the competition between them. One way they learn about it is because it is more common now that they are visited by credit promoters from the

different MFIs, and even the commercial banks. Some of them also reported that competition has allowed them get better services from the financial institutions, although never lower interest rates.

34. All interviewees confirmed that they have to use their assets as collateral for the loans they get. Also, farmers confirmed that they have put their houses as collateral, rather than their agricultural land, often because the former does have a registered title but rural land does not.
35. Only half of the clients interviewed knew about the existence of credit bureaus, but it seemed that they had little notion on the way it could affect them and the MF sector. For instance, most of them understood that defaulting would have a negative impact on his/her possibilities to receive future credits from the same provider, but only one of them indicated explicitly that it would affect their creditworthiness with all possible providers of microcredit.

INFORMATION SHARING AND MICROFINANCE IN PERU

1. INTRODUCTION

The microfinance sector has developed rapidly in developing countries over the last two decades, making credit available for many poor microentrepreneurs. This expansion was possible mostly due to key technological innovations that allow microfinance institutions (MFIs) to offer small loans with an interest rate lower than the one charged by traditional local lenders, and with lower collateral requirements compared to commercial banks. In some cases, the technological innovation implied the use of information by peers on the credit worthiness of individual applicants through, for instance, group lending or village banking. In all cases, though, MFIs build a credit history with each borrower so that loans can gradually increase in size.

An important aspect of this microfinance revolution is that it has practically skipped the rural poor and most particularly their agricultural activities as smallholders. This exclusion could be seen as surprising considering that the rural poor tend to have more assets (land) to be leveraged into credit compared to the urban poor. A significant part of the explanation comes from the size and nature of risk associated to agricultural activities. In particular, weather shocks affect most farms in a village or region and thus limit the functioning of the joint-liability mechanism to isolate MFIs from credit risk. In addition, with high volatility of output, involuntary default is more common and makes it harder for farmers to establish a good reputation. Nevertheless, it also happens that with high correlated risk, risk-averse farmers may not want to demand credit because certain states of nature imply the loss of their assets. (Boucher and Carter, 2001)

This microfinance revolution has generated a number of studies on the sustainability and impact of the microcredit programs. (Morduch, 1999) One of the issues of increasing concern in countries with a large microfinance sector is the effect of the increasing competition, among MFIs and with the commercial banks, on the sustainability of the sector. Higher competition improves the access to credit for small microentrepreneurs, but may also allow them to incur in over indebtedness, if credit histories remain private between the MFIs and their borrowers. With more MFIs operating in the same village, selection costs and portfolio risk goes up because each one cannot observe if potential borrowers are simultaneously indebted with other MFIs, or have previously defaulted.

In this context, the development of credit bureaus appears as particularly important to facilitate the sustainability of the microfinance sector, but special efforts are required for credit bureaus to include the credit histories small microentrepreneurs develop with unregulated MFIs. Making credit histories public can help reduce selection costs and improve the quality of credit portfolios. A quick look at the information sharing system can help avoid incurring in costly selection mechanisms for those potential borrowers with previous histories of voluntary defaults (negative information). With positive information, we could also avoid approving loans that could raise their indebtedness beyond their repayment capabilities. But the development of credit bureaus can also enhance

microfinance as a mechanism to leave poverty, since it allows borrowers with good credit histories develop a reputation with commercial banks, so that they can eventually graduate to larger and cheaper loans.

In Peru, the development of the microfinance sector has been significant over the past two decades, especially in urban areas, as in many other developing countries. Several microcredit programs started working in rural areas after the agrarian development bank closed, but most of them have abandoned the sector now, because of a combination of factors. First, we had the macroeconomic crisis of 1997, accompanied by a weather shock, el Fenómeno El Niño, which generated huge regional defaults. Second, but not of less importance, we had the distortions generated in the rural credit markets by public initiatives such as the Cajas Rurales de Ahorro y Crédito (CRACs), the FONDEAGROS (rotating funds) and the recent creation of the Agrobanco. In any event, anecdotal evidence suggests competition has indeed increased for MFIs in both urban and rural areas.

The Peruvian congress gave a law to regulate the functioning of credit bureaus in 1996. Such law gave birth to a publicly funded credit bureau (CB) system, operated by the Superintendency of Banking and Insurance (SBS), while allowed the existence of private credit bureaus. Until recently, credit information services have been mostly used by banks and regulated MFIs, but the main private credit bureau, Infocorp, is currently working with the main apex institution, COPEME³, to extend the use of the system by MFIs, including non-regulated ones. This situation offers a good opportunity to study the effect of credit bureaus on the behavior of borrowers, the sustainability of MFIs, and in the graduation of borrowers into the Peruvian formal banking system.

This document pretends to describe the recent evolution of the microfinance sector and the CB system in Peru, with a special focus in Cusco. The Peruvian CB system has already been documented elsewhere, (IDB 1999; GTZ 2001) but this study will update and complement that work by:

- (a) focusing on the recent development of the legal environment and market structure of the CB system in Peru, including the agreement between COPEME and Infocorp;
- (b) exploiting previously unpublished data on the actual use of the Infocorp database at the national level and at the level of the department of Cusco⁴.
- (c) giving a specific attention to the relationship between the CB system and the agricultural microfinance market⁵;
- (d) documenting through interviews and focus groups the perception and actual use of credit bureaus by regulated and non-regulated, agricultural and non-agricultural organizations, and their clients.

³ Association of Private Organizations of Promotion and Development of Micro and Small Enterprises (Consortio de Organizaciones Privadas de Promoción al Desarrollo de la Micro y Pequeña Empresa).

⁴ Cusco was selected because the INFOCORP-COPEME agreement has chosen that department to start a series of case studies aiming at improving the way the Infocorp database helps the regulated and unregulated MFIs.

⁵ The key questions here refer to: (i) the factors that keep the microfinance sector away from the agricultural sector, and (ii) to evaluate whether the development of the CB system may play a role in facilitating the insertion of MFIs into the agricultural sector.

This document is structured in four sections, including this introduction. Section 2 presents background information on the Peruvian microfinance sector and CB system. Section 3 details this information for the department of Cusco. Finally, section 4 reports on interviews and focus groups done in the department with lenders and borrowers. It describes their perceptions on the general situation of the microfinance sector and on the role and usefulness of information sharing mechanisms for its development.

2. MICROFINANCE AND CREDIT BUREAUS IN PERU

Following the crisis of the late eighties, the Peruvian economy underwent a sharp process of stabilization and structural change in the early nineties that liberalized most goods and factor markets and reduce the participation of the state in productive activities while increased its regulatory role. The Peruvian economy grew strongly since 1993 with a strong dynamism from the local private sector and large inflows of foreign capital. The recovery stopped by 1998 with the conjunction of the effects of the international financial crises in Southeast Asia, Russia and Brazil, and the weather shock associated to El Niño. The recession lasted about four years in midst of a general confusion in the political arena that paralyzed further reforms in key markets⁶. The evolution of the agricultural sector during the past decade paralleled that of the global economy, despite a significant appreciation of the exchange rate. (GRADE, 2001)

The Peruvian economy is characterized by a proliferation of small firms both in urban and rural areas. Villarán (1998) estimates that microenterprises contribute about 42% of the GDP while Peruvian official statistics estimate that small and microenterprises employ about 75% of the urban economically active population. In rural areas, smallscale agriculture is also predominant. A significant proportion of these agents do not have access to credit by commercial banks, although many microfinance institutions have appeared in the last two decades to attend their credit needs.

2.1 Evolution of the Peruvian microfinance sector

Hyperinflation in the late eighties and early nineties together with the changes in the legal framework for the financial sector led to the disappearance of several financial institutions. The new regulations made all the state-owned specialized banks close, although by that time, their capital had already been consumed by low repayment and negative real interest rates.^{7,8} The network of cooperatives also collapsed. Of the more than 600 cooperatives that existed in 1991, only 176 were still existing in 1998 (Alvarado, et. al., 1998). Most of these do not grant new loans but focus on recovering the existing loans.

⁶ See Abusada et. al., 2000.

⁷ See Valdivia (1995)

⁸ The list includes Banco Agrario, Banco Minero, Banco Industrial, and Banco Hipotecario.

The structural reforms of the past decade did reach the financial sector and a new General Banking Law⁹ came out in 1996. The key points of the new financial system are:

- (a) Financial institutions became free to determine their interest rates and operations.
- (b) The state will no longer operate directly in the financial system. Still, they promote the development of the financial sector through the Financial Corporation for Development S.A. (COFIDE), a second-floor institution that channels public treasury and international funds through first-floor financial institutions for specific purposes. COFIDE has a special mission to attend the needs of regulated MFIs for support to small and microenterprises and small agricultural producers.
- (c) The mechanisms of supervision and control of the financial system have been strengthened, through the Superintendency of Banking and Insurance. All regulated financial institutions, including MFIs, have the obligation to report to the SBS, which can take measures to ensure their sound operating or even close them. Also, all regulated financial institutions have to report to the public credit risk information system managed by the SBS, and have the right to consult this system for free.

The structure of the financial system has not been significantly modified since the 1996 law. Still, the most important evolution is a return to state-supported mechanisms such as the Fondo Mi Vivienda and Agrobanco. The 'Fondo Mi-Vivienda' has been created in 1998 to offer subsidized housing loans. The new agricultural bank was created in 2001,¹⁰ and it is offering direct credit to agricultural producers that are enrolled in a Cadena Productiva, which means that they are connected to a market through a contract with an agro-industrial or an exporting firm.

Current actors of the Peruvian microfinance sector

Defining a microfinance institution as one that has a relatively large proportion of their operations dedicated to offering financial services to small microentrepreneurs, rural or urban, the Peruvian microfinance sector has regulated and non-regulated MFIs. Financial institutions in Peru can be organized in different 7 categories:

- Cajas Municipales de Ahorro y Crédito (CMACs),
- Cajas Rurales de Ahorro y Crédito (CRACs),
- EDPYMEs,
- Financial entities,
- Commercial banks,
- Cooperativas de Ahorro y Crédito (CACs),
- NGOs.

The main MFI categories are the CMACs, CRACs, EDPYMEs, CACs and the NGO sector. CMACs were created in 1980 with the following objectives: (i) to support the financial decentralization of the country, (ii) to participate in the creation of a local financial system aimed at the regional development, and (iii) to extend the offer of deposit and credit services to populations that previously did not have access to commercial banks.

⁹ Ley General de Banco numero 26702.

¹⁰ Ley de creación del Banco Agropecuario # 27603.

CMACs offer a wide range of savings and credit products, as well as some public services, mostly to urban clients. They are created and owned by municipalities with a participation of the civil society. CMACs have benefited from the experience of the German *Sparkasse* through a long international partnership, and have experienced a remarkable success that made them the main MFIs in Peru.

CRACs are decentralized for-profit private financial ‘entities’ created in 1994 to increase the supply of credit for small agricultural producers. The Peruvian Ministry of Agriculture played a decisive role in the creation of CRACs, encouraging the creation of ‘Caja’s organization’s committees’ and providing material for their start-up. Stakeholders of CRACs are typically agricultural cooperatives and private organizations. CRACs started offering loans to almost exclusively agricultural producers, but their portfolios only dedicate 33.5% agricultural credit.

The status of EDPYMEs was created in 1996 to offer a possibility for microfinance NGOs to graduate into the regulated sector. The incentives for NGOs to become EDPYMEs was that they would be exempt of the value added tax (IGV) and they would be able to manage funds from COFIDE, specifically addressed to microentrepreneurs. EDPYMEs are clearly oriented toward the financing of small and microenterprises, mostly in the urban context. EDPYMEs are not authorized to collect savings, but can offer a wide range of credit products.

Commercial banks are also called ‘multiple banks’, and there are 14 of them in Peru, with 783 agencies in the entire country. Multiple banks have the largest portfolio sizes but, with the exception of Mibanco, do not address the segment of small microentrepreneurs (**Table A. 2** in annex). Mibanco is a bank specialized in lending to microenterprises, it was created in 1998 from the NGO Acción Crediticia del Perú, with strong support from the government. The ‘Financiera Solución’, or financial company Solución, is a subsidiary of Banco de Credito, the largest commercial bank in the country, and also dedicates to making small loans to mainly microentrepreneurs and employees that cannot access banks.

Peru also counts with a network of cooperatives. CACs are registered with, but not regulated by, the SBS. CACs are linked through a national federation (FENACREP) that provides supervision, technical support, and an information reporting system. 168 cooperatives are currently registered with the FENACREP; their outstanding loan portfolio was \$197 million in March 2003. With the exception of CACs, all of these institutions are regulated by the SBS.

All regulated MFIs currently amount for a loan portfolio of US \$ 721 million, with the larger single MFI being Mibanco. This MFI is also very concentrated in the small and microenterprise sector, (65%) second only to the group of EDPYMEs. As a group, the CMACs are the largest group with a portfolio of US \$ 380 million. The crisis of the past recent years has clearly affected the sector generating a default rate of almost 6%. Clearly, CRACs are the ones with the largest default rate, (10%) followed by the EDPYMEs, although there are wide differences within these groups.

Table 1. Basic information on regulated MFIs, March 2003

	Number of MFIs	Outstanding loan portfolio (in million USD)	Loans to small and microenterprises, in % of total loans	Default rate
CMACs	13	380	47%	4.7%
CRACs	12	85	45%	10.0%
EDPYMEs	14	73	70%	8.6%
Financiera Solución	1	83	55%	2.0%
Mibanco	1	100	65%	3.0%
TOTAL or AVERAGE	41	721	56.4%	5.7%

Source: SBS

Finally, the size of the unregulated sector is impossible to estimate with precision. COPEME, a network of Peruvian microfinance institutions, both regulated and non-regulated, counts with 15 associates from the unregulated sector. These NGOs are from the entire country, use different credit methodologies (individual, solidarity groups, village banks), and are from different sizes.

The evolution of the microfinance supply during the nineties

The total supply of microfinance services has increased during the nineties due to the changes in the Peruvian financial infrastructure, and despite the disappearing of key institutions lending to small and microenterprises. The financing of agriculture, however, remains insufficient. Multiple banks, with the exception of Mibanco, are not considered in this section due to their limited role in financing small and microenterprises,

The size of the market grew strongly during the period. Although all the regulated MFIs participated in this growth, Mibanco had the largest growth rate with an average of 60% over the past 3 years. Still, the most surprising story is that the CMACs kept growing at a very fast pace, averaging a 29% over the same period, which has consolidated their leadership in the entire country. (Table 2)

Table 2. Evolution of the loan portfolio of regulated MFIs, in million USD

MFI	1995	1996	1997	1998	2000	Mar 2003
CMACs	25	65	84	90	179	380
CRACs	n/a	40	52	53	65	95
EDPYMEs	n/a	n/a	n/a	12	19 ^a	73
Financiera Solución	n/a	n/a	21	65	53	80
Mibanco	n/a	n/a	n/a	12	24	100

Sources: SBS, Mibanco, Trivelli (2002)

All information is at December of the year indicated, with the exception of (a) at June 2000.

The growth in loans has mostly addressed the commercial sector, while the agricultural sector has lost participation, even in the case of CRACs. With the movement of

liberalization in the Peruvian economy and financial sector, commercial banks were supposed to address the segment of agricultural credit. Commercial banks did increase their loans to agriculture during the recovery, although they were not able to fill the space left by the disappearing of the agricultural bank, and furthermore they left the sector with the recession (Table 3). The increase in the number of organizations and loan portfolio size for the microfinance sector did not reach the agricultural sector in a significant manner¹¹. Only 15% of the loans allocated to agriculture had the microfinance sector as the source.

Table 3. Loans of the regulated financial institutions to the agricultural sector, in million USD

	Dec. 1995	Dec. 1998	Mar. 2003
Commercial banks	256	441	300
CRACs	11	37	29
CMACs	3	12	18
EDPYMEs	n/a	n/d	3
Empresas financieras	3	5	2
TOTAL	273	495	352

Sources: SBS, Trivelli (2001)

In 2001, Agrobanco was created by law. Its level of transactions is still very low but it has already raised expectations among small farmers to access credit with low interest rates. Its major challenge is going to be to generate a sustainable operation in an environment of significant political pressure, and limitations for sectoral diversification.

In sum, the supply of microfinance services have greatly increased and improved in Peru since 1990. Still, this growth has not been able to compensate the reduction in loans by commercial banks after the crisis of 1998. Trivelli (2002) shows that access to credit by Peruvian households increase from 17% to 32% in 1997, to decrease again for 2000. (19%) In rural areas, evolution of access to credit did not increase during the economic recovery, remaining constant at around 20%. This result is consistent with the fact that the agricultural sector has not been reached by the positive evolution of the financial sector during the nineties.

The presentation of this regulated microfinance sector is the object of the next section, and will be done through four of its characteristics. First, a network of regulated MFIs, with the CMACs being particularly active, provides microfinance services now. Second, despite the increase in the supply, access to credit remains low and the sources of credit remain mostly informal. Third, anecdotal evidence suggests that competition between MFIs has increased. Finally, the low level of the supply of financing to agriculture will be highlighted.

¹¹ During the 1980's, the principal source of financing for the agricultural sector was the public agricultural bank. In 1989, last year of full operation, the agricultural bank lent \$538 millions, which in dollars of today amount to about US \$ 1,200 million. (Valdivia, 1995)

Competition among microfinance MFIs

Due to the expansion of MFIs in number and loan portfolio, the structure of the market is changing, and competition has increased among MFIs, regulated and non-regulated, and even with commercial banks. The increase in the number of MFIs is accompanied by an increase in the geographical overlap of their market zones (Table 4). MFIs indeed appear very concentrated, covering only 110 of the 1820 districts of the country in 2003. In 14 months, the number of agencies of CMACs, CRACs, and EDPYMEs has increased by 41%, when in the same period the number of districts in Peru where at least one CMAC, CRAC, or EDPYME is present increased only by 17%¹².

Table 4. Distribution of agencies of CMACs, CRACs, and EDPYMEs

	Dec. 1998	Dec. 2001	Feb. 2003
Total number of agencies	103	166	234
Number of districts with an agency ^a	-	94	110
Average number of agencies per district, in the district where agencies are present	-	1.76	2.12

Source: SBS

^a Peru counts a total of 1820 districts.

COPEME's 'Microfinance Initiative'

The growth of the Peruvian microfinance sector benefited from technical assistance of different kinds and from different sources. One example is the technical assistance offered by the German technical cooperation to the CMACs. Another very important example is the Microfinance Initiative, which is a joint program by COPEME and USAID designed to increase and strengthen the microfinance sector in Peru. It started in 1998 and the current round will last at least until 2006. This program comprises five parts:

1. Technical assistance for the management of MFIs. This technical assistance takes the form of cofinancing of audits of the specific needs of each MFI: strategic planning, microfinance technologies, marketing for MFIs, etc. This technical assistance is opened only to MFIs sharing their information in COPEME's system.
2. Training of the personnel of MFIs, through courses that are offered to any MFI with a corresponding fee.
3. 'Info Quality Training' is a comprehensive system of strengthening of the information systems of non-regulated microfinance organizations, with the objective of developing a form of supervision through shared information among the MFIs and microfinance NGOs.
4. The promotion of an information sharing culture among MFIs. This point is implemented through the agreement between COPEME and Infocorp, and through

¹² Also, many of the MFI agencies are located in districts where there are already agencies from commercial banks. Only 13% of these agencies are located in districts where there are no agencies from commercial banks.

the creation of an information sharing software among NGOs and EDPYMEs, called SINFONED.

COPEME's network includes all of the regulated MFIs, the association of CRACs, the federation of CMACs, and 18 unregulated MFIs. Nevertheless, their training courses, for instance, is offered to a much larger number of MFIs. Same occurs with the benefits of the agreement with Infocorp, for which 34 NGOs were already registered.

2.2 Credit bureaus in Peru

A credit bureau is an institution that gathers and distributes information about the credit history of natural and juridical persons. It may be public or private, and may contain positive and negative information. Negative information refers to unpaid or expired debts. Positive information refers to debts in good standing. Full information sharing refers to the exchange of both negative and positive information.

Evolution of public and private credit bureaus

As a risk information center, the Peruvian public Credit Bureau, operated by the SBS, began its operations in 1968. In 1992, the term "Central de Riesgos" (Risk Central) was introduced in the law. At the beginning, the public credit bureau published its bulletins quarterly, with 6 months of delay. In 1980, the format was changed to use magnetic tapes. Information on current and contingent debt, total debt, and the number of commercial banks with which the individual or enterprise had financial obligations was added. Whereas the original data delivered to each bank only included its own clients and those who had obligations with more than one credit institution, the public credit bureau started delivering information on all clients in 1992.

The growth of the microenterprise sector, and consumption credit, in Peru during the nineties generated pressures from risk information customers and the microfinance sector to include information on smaller loans into the information system. Until October of 1997, credit bureaus only managed information on loans larger than US \$ 4,500, mainly for technical reasons. In February 1998, information on loans smaller than \$4,500 was included into the new computerized system that notably allowed the distribution of information over the internet. At that time, there were 170,000 registries for loans over \$4,500, and over 2 millions for loans under \$4,500. In the information system, the information provided for the smaller loans contained less detail than the information provided for loans over \$4,500.

In the meantime, private credit bureaus (Central Privada de Información de Riesgos, CEPIRs) appeared in 1995 as the result of the private initiative. They were Riesgo Cero, CERTICOM and Infocorp. CEPIRs provided the same products as the public credit bureau managed by the SBS, and offered additional information such as information of protests filed at the Chamber of Commerce, credit information from commercial houses, information about taxes, and unpaid bills from the telephone, electricity, and cable companies. The CEPIRs also make verifications of the legitimate address, employment, housing condition, business premises, identity card and civil status.

Riesgo Cero went out of business in 2000 because of the price war among CEPIRs in the late nineties. Today, Infocorp controls 80% of the market with a database of more than 6 millions registries available to 1,200 clients. It proposes 18 different products.

CRACs, CMACs and EDPYMEs started being included in the public CB system in 1998. The information of banks and regulated MFIs is transmitted to the SBS in compliance of its supervision role, and is accessible to CEPIRs at a cost of \$5,000 a month. Unregulated NGOs are not included in the public CB system, although Infocorp is actively pursuing their inclusion, notably through its agreement with COPEME.

Legal environment

The current law for the regulation of the private credit bureaus is the law number 27489 from June 2001, modified in November 2002 by the law number 27863. Both aim at promoting sound exchanges of information in a framework of competition between private credit bureaus. They determine the following rules.

Any institution can access the public credit bureau, including commercial institutions, after paying the applicable fee. Institutions and individuals can access the information provided by CEPIRs, after paying the fee and having been previously identified. The users of the information provided by the CEPIRs are responsible of any illegal use of the information, notably in ways that harm the holders of the information.

The CEPIRs can collect risk information from public or private sources. This allows the CEPIRs to provide a full information sharing system about financial, credit, commercial and insurance risk. CEPIRs can also collect information from the holder himself or herself, after informing him/her about the CEPIR, the database, the possible uses of the information, and the facultative character of their answers. This information can never violate professional, commercial or industrial secret.

The information that appears in the informative reports must be licit, exact, and true, so as to reflect the real situation of the information holder. If not, CEPIRs have the obligation to correct it. By law, information collected by private credit bureaus cannot contain sensitive information¹³, information that violates the bank secrecy, the tax reserve, or inexact information.

Since CEPIRs are allowed to collect risk information from public and private sources without the authorization of the information holder, they are subject to specific rules of protection of the individual. The law guarantees the right of the information's holder, i.e. the person or organization whose data is gathered and distributed. The holders are protected by INDECOPI, the consumer defense institution, which is able to impose corrective measures to the CEPIRs, such as the modification or cancellation of their risk information. The following actions are considered as infractions: (i) to deny access to a consumer of its own information, (ii) to deny a rectification or revision request, or (iii) not to update the information in time. INDECOPI can also impose sanctions on the institutions

¹³ Sensitive information refers to information on ideological and religious affiliations, physical and emotional conditions on the applicant, etc.

that provide the information to the credit bureaus if the process involves any infraction of the law.

Every holder can access the information concerning themselves once a year, or whenever the information is rectified by the CEPIRs. He/she can check his/her data on screen for free, or receive a written copy for the cost of printing or copying. The holder can also have access to the identity of the sources of the CEPIR (when they were not public), the identity of the persons who received information about them, and the date of the report. Any holder has a right to demand the modification or cancellation of inexact information; this operation will be free of charge. If erroneous information is detected, the CEPIRs must send rectifying communications to everyone who received it from the moment of the detection back to twelve months before it.

Originally, CEPIRs were able to conserve information on unpaid obligations, administrative or other economic sanctions, and on state of insolvency and bankruptcy for a period five years after the obligation was paid or extinguished, the sanction was executed, or the state of bankruptcy or insolvency was declared. In 2002, the law set new limits of time for default information, differentiating between extinction and execution of the obligation. Expiration refers to the date when the obligation must be paid. Extinction refers to the elimination of the obligation. It occurs in case of death of the debtor, prescription, or amnesty. Since the modification of the law, CEPIRs are allowed to conserve and distribute the aforementioned information for a period of two years after its extinction, and for a period of five years after its expiration. In addition, the modification of the law established that CEPIRs could contain and distribute information about unpaid public service bills only for debts of six straight months or more. This adjustment was not based on technical but political reasons and has affected the system sizably. Infocorp, for instance, estimates that about 15% of their records were eliminated as a result of the law.

In addition, the time granted to source institutions to submit information to the CEPIRs about total or partial payments must not exceed the time to submit information about defaults. The CEPIRs, in turn, must update this information within the next two weekdays after receiving it. This will not apply in the case of protests, which are ruled by the Securities Law.

Information included

Infocorp, the main CEPIR, collects information from a wide range of sources, and is in the process of expanding it, notably to MFIs through its partnership with COPEME. At August 2003, 81 MFIs were affiliated at Infocorp through the partnership with COPEME. The current sources are: (i) the SBS, which distribute information on all the regulated financial institutions; (ii) the tax administration (SUNAT); (iii) the Chamber of Commerce of Lima (CCL); (iv) the Custom administration (SUNAD); and (v) Financial institutions, and commercial houses and firms.

Clients can consult Infocorp's products through a variety of means: by internet, by direct computer connection, by an automated phone service, and by going to an agency. Infocorp proposes 18 products, which provide the following type of information:

- General data (name, date of birth, ID Number, Address, Profession, Civil Condition, Phone Number), verified by Infocorp;

- Actual and historical operations in the financial system (SBS);
- Orders of payment and protests, collected from all departments by the Chamber of Commerce of Lima (CCL);
- Current debts expired or judicial *cobranzas*;
- Information about firms' bills;
- Closed bank account and cancelled credit cards;
- Credit card and consumption credit;
- Tax debts and directory of businesses registered in the SUNAT;
- International trade information: exports and imports made by the holder (SUNAD);
- Index of the number of consults realized to Infocorp during the last quarter, and the list of the companies who consulted.

2.3 Use of credit bureaus by MFIs at the national level

The level of consultation of credit bureaus depends on the quantity and type of information that they contain. Data on MFIs from the agreement COPEME-INFOCORP suggests that the departmental variations in amount of consultations and hit rate are related to the number and type of organizations sharing their client information.

Infocorp's database currently contains nationally available information. The information provided by the SBS on regulated MFIs is collected in the entire country, as is the information provided by the SUNAT and SUNAD. The Chamber of Commerce of Lima also consolidates data from all notaries in Peru. The inclusion of more sources will mainly be the result of a local-level strategy, through partnerships. Many organizations are indeed based at a regional or departmental level: most unregulated MFIs, public institutions (such as the Ministry of Agriculture and its agricultural credit programs), and a multitude of commercial, industrial, or service companies (such as electricity or water companies, wholesalers, medium-size vendors of agricultural products, etc.).

Figure 1: Consultations and hit rate in the agreement COPEME-INFOCORP, September 1st, 2001 – August 30th, 2003.



Source: Statistics administration of the COPEME-INFOCORP agreement.

The agreement between COPEME and Infocorp is a national-level partnership to include, at the local level, unregulated MFIs into Infocorp’s information sharing system. It was signed in 1998. One of the goals of COPEME’s Microfinance Initiative is to promote a culture of information sharing in the community of regulated and non-regulated MFIs. This aim is pursued by the creation of a network of information sharing between NGOs and EDPYMEs called SINFONED, and by the agreement with Infocorp signed in 1998. The terms of this agreement are that:

- COPEME will promote the use of Infocorp’s services and the sharing of client information in Infocorp’s database with the MFIs that it federates;
- Infocorp will grant reduced access price to the MFIs covered by this agreement, which will supply their own negative and positive client information to Infocorp’s database. The price reduction is of about 50%, and takes the form of a reduced entrance fee and the use of a minimum consumption price.

At August 2003, 81 organizations participated in this agreement. Detailed information on 70 of them shows there are 33 NGOs, 12 cooperatives, 11 EDPYMEs, 9 CMACs, and 5 CRACs.

The inclusion of non-regulated MFIs and non-financial organizations is in the interest of both regulated and non-regulated MFIs, and appears related to the number of consultations and the hit rate. With the increase in competition, regulated MFIs tend to lend to each other's clients, and to clients of unregulated MFIs. Unregulated MFIs, which target different clients from regulated MFIs, need a risk information database that takes into account their clients.

The number of consultations (**Figure 1**) appears related to the number of unregulated MFIs included in the information sharing system, and to the distribution of products consulted. Lima and Cusco are the two departments that use Infocorp most and the two departments in which most unregulated MFIs are included (20 and 6, respectively). In the five departments that use Infocorp less, only one or two unregulated MFI is present. Moreover, the departments that consult Infocorp more also globally consult the Consolidated System of Default (SICOM) more than the products made of SBS information. The SICOM is the product that consolidates all default information, including unregulated NGOs. In the departments of Loreto, Tumbes, Tacna, and Moquegua, where the numbers of consultations is lower, products based on SBS information are the most consulted.

A consultation of Infocorp's database typically involves a two-step process. First, the name, DNI or tax number (RUC) is provided and summary information is given indicating the number of products in which the person has information. Detailed information is usually consulted in a second step.

The analysis of the hit rate does not show any consistency with the inclusion of unregulated MFIs in each department. However, hit rates are strongly influenced by the policy of use of credit bureaus in each MFI.

3. MICROFINANCE AND CREDIT BUREAUS IN CUSCO

The department of Cusco is located in the southeast part of Peru. It covers about 70,000 sq km, most of which is in the Andes Mountains, at an altitude of more than 3000 meters above the sea level. One of its provinces, La Convención, is in the selva, or tropical rainforest region, at an average altitude of 1000 meters above the sea level.

The department of Cusco counts 1.2 millions inhabitants, which represents 4.5% of Peru's population. Table 5 shows summary information characterizing the population of the department of Cusco and of Peru.

Table 5. Characteristics of the population in Peru and Cusco

	Dept. Cusco	Peru
Population (2000, est.)	1,150,000	25,662,000
Average annual growth rate of the population (1981-1993)	1.7%	2%
Rural population (1993)	54%	30%

Source: INEI

3.1 The Cuzco economy

Economically and socially, the department of Cusco is doing worse than the national performance. Its economy, based on agriculture, is mostly informal and records a low level of productivity.

The GDP of the department of Cusco represents only 2.8% of the total Peruvian GDP. The primary sector is the principal economic sector of the department. The share of the primary sector in the GDP is much higher in Cusco than in the country (25.4% and 7.6% respectively). Although farming activities represent the second economic activity of the department in terms of contribution to the departmental GDP, they employ 48% of the economically active population. Manufacturing activities declined in the department during the nineties, while the service sector has been growing steadily, especially tourism (9.2% annually in the nineties).

Cusco is one of the poorest departments of Peru. With 75% of its population living in a situation of poverty¹⁴, the department is classified among the ‘departments with a generalized poverty’. According to the National Institute of Statistics and Information Technologies (INEI), 60% of the inhabitants have at least one unsatisfied basic need. The poverty in the department is also visible in the social indicators (Table 6). Departmental levels of education and literacy are worse than the national average. Several health indicators, such as life expectancy and infant mortality also place Cusco among the worst departments of the country.

¹⁴ The operational definition of poverty is based on per capita expenditures and the poverty line is defined by the cost of the Peruvian food basket.

Table 6. Social and poverty indicators in Peru and Cusco

	Dept. Cusco	Peru
Population living in extreme poverty (2001)	51.3%	24.4%
Share of the population aged 25 and older who completed primary education (2000, est.)	10.8%	14.9%
Illiteracy rate (2000, est.)	18.1%	9.3%
Malnutrition rate for children aged 5 and younger (1996, est.)	43%	25.4%
Life expectancy at birth (2000)	40.9 years	69.3 years
Underemployed population (2000)	74%	42.9%

Source: INEI

The agriculture in the department of Cusco

The agriculture in Cusco is largely marked by the characteristics of subsistence agriculture, organized in peasant's communities. The products are mainly targeted at local markets and cultivated with traditional technologies. Most farmers work land plot smaller than two hectares in 1994, and only 26% of the land is worked with modern machines. Most land is irrigated by rain, and the availability of irrigation infrastructure is well below the national average.

Most farmers are organized in peasant's communities. (*comunidades campesinas*) The 1994 Agricultural Census identified 1,018 peasant's and native communities legally registered. They represent 60% of the parcels and 52% of the surface. In peasant's communities, it is usual that the land in the valleys is individually assigned while pastureland in the mountains is managed collectively. In any case, land is non-transferable to outsiders, which limit the possibilities to use it as collateral. The new land law allowed the possibility of individual ownership of peasant communities' land, but with the approval of the community¹⁵. The Land Registration and Rural Cadastre Special Project (Proyecto Especial Titulación de Tierras y Catastro Rural, PETT) has been working in Cusco for 12 years, and has registered 76% of the 40,500 parcels presented to its office in Cusco but it has not been able to reach most of the communal land¹⁶.

The main agricultural products are potato, manioc, corn, and coffee. Potato is the main crop in the department and the base of the Andean alimentation. Its production has suffered from weather shocks the phenomenon El Niño, decreasing by 30% between 1995 and 1999. Cattle's breeding is also an important component of the primary sector in Cusco, especially sheep and *camelidos*. Coffee is the main export crop, cultivated in jungle areas.

In sum, the socio-economic situation of the department of Cusco situates it among the least developed departments of Peru. Although agricultural and tourism potentials exist,

¹⁵ Ley de Tierras 26505, 1991

¹⁶ The PETT was created by law in 1992 with the objective to update and improve the rural *catastro*, and to provide accurate property titles to rural landowners

the department suffers from a difficult environment, lack of basic infrastructure and human resources. Its economic activity is based on small traditional farming and informal entrepreneurship.

3.2 The microfinance market in Cusco

As it is in the rest of Peru, the microfinance market in Cusco is growing. Due to absence of data, especially in time, this section will only focus on the regulated MFIs. It is however clear that unregulated organizations and NGOs are an important lender, especially to the poor. Some have been providing credit in the department for more than 20 years. Table A.5 in annex provides information on all MFIs operating in the department.

The regulated MFIs operating in the department of Cusco are, by chronological order:

- the CMAC Cusco;
- the CRAC Quillabamba or CREDINKA;
- the EDPYME Crear Cusco;
- the Financiera Solución; and
- the Lima-based EDPYME Credivisión.

In April 2002, the CMAC Arequipa has received the authorization from the SBS to operate in Cusco but does not currently record any operation in Cusco. It will therefore not be considered in this study.

The regulated microfinance sector in Cusco is clearly dominated by the CMAC Cusco, which increased its leadership in terms of geographical expansion, number of clients, and loan portfolio (**Table 7**). With five agencies in four districts, the CMAC has the most extended network of agencies of the department, even with respect to commercial banks. Between March 2001 and March 2003, the CMAC has more than doubled its outstanding loan portfolio, while the average progression of the other regulated MFIs was of 5% (**Table A. 4** in Appendix A). Remarkably, the CMAC Cusco kept its default rate to reasonable proportions.

Obviously, there are no official records on the activities of the unregulated MFIs. Fortunately, COPEME's Microfinance Initiative ordered a study of the sector in Cusco, as part of their agreement with Infocorp to expand information sharing among MFIs. Velasco (2003) identified 19 unregulated MFIs in the department of Cusco. They are two cooperatives, one public microfinance program (National Fund of Compensation and Social Development, FONCODES), and 16 NGOs. The unregulated MFIs in Cusco lend on average smaller loans, and have a higher default rate.

Table 7. Indicators of MFIs in Cusco, 2003^a

Organization	Number of borrowers	Loan portfolio, in million USD	Default rate
CMAC	25,073	25.6	4.2%
CRAC	5,513	4.4	11.4%
EDPYMEs	1,021	2.0	7.3% ^b
Financiera Solución	1,636	2.5	2%
Total regulated MFIs	33,243	34.5	6.6%
Unregulated organizations ^c	23,157	10.0	17.4%
Total department of Cusco	56,400	44.5	10.5%

Sources: SBS, Velasco (2003)

^a The information is at January 2003 for unregulated organizations and at March 2003 for regulated MFIs.

^b The default rate of the two EDPYMEs is very distinct by organization: 4.6% for Crear Cusco, and 11% for Credivisión.

^c Based on the information of the 19 unregulated MFIs identified in Velasco (2003).

The higher default rate of the unregulated MFIs is partly explained by the recession that affected the Peruvian economy, and the agricultural sector in particular. Nevertheless, another important factor is the relatively wide practice of default that result from a history of political distortions that has affected the development of a microfinance sector in the department. A well-known recent example is the repayment crisis that affected the department of Cusco at the end of the nineties, which hit particularly hard to IFOCC, a microfinance NGO that operated mostly in rural areas. This crisis had its roots in the economic crisis of 1998-99, which moved local politicians to organize a local movement in favor of default, arguing that interest rates were too high and oppressive. Still, the movement also built on intrinsic weaknesses of some organizations such as a bad adaptation of credit methodologies to the target groups, and bad management of their portfolio growth. Today, IFOCC and two other unregulated organizations present a default rate of 100% (**Table A.6** in annex), i.e. they only focus on recovering past loans but do not grant new loans. IFOCC has also changed its target group by developing its urban credit operations.

Access to credit in Cusco

The access to credit is currently better in Cusco than in the rest of the country, including the rural areas (**Figure A.1** in Appendix A). For the entire department, the rate has even increased from 15% to 24% from 1997 to 2000. In 2000, the percentage of rural households of the department that reported having access to credit (21%) was higher than the rate for Andean rural households at the national level (15%).

However, these numbers are tempered by the importance of informal sources of credit. In 2000, more than 70% of rural households relied on informal sources. This data also suggests that most MFIs do not reach agricultural producers.

Table 8. Sources of credit for households in Cusco, 2000

	Rural areas	Total
Family/Friend	20%	16%
Bank	4%	13%
Caja Municipal	11%	17%
Cooperative	2%	2%
Private company	5%	3%
Local store	54%	45%
Other	4%	3%

Source: ENNIV

Competition among MFIs in Cusco

The microfinance market in Cusco is highly segmented, with different levels of competition in each segment. The most competitive segment is the one in urban areas, which is also segmented in different layers. In the first layer operate the CMAC, the CRAC, and the Financiera Solución, in competition with each other and with the commercial banks, and focuses on small and medium entrepreneurs. The second layer is where EDPYMEs and unregulated NGOs operate, and is constituted of the poorer microentrepreneurs. Competition among these organizations is lower than in the first layer. However, the EDPYMEs partly compete with the CMAC, the CRAC, and the Financiera Solución. Globally, the urban areas, especially the city of Cusco, are the areas where competition is more acute. Of the 13 MFIs agencies in the department, eight are in the city of Cusco, which extends over the districts of Cusco and Wanchaq.

On the contrary, rural areas are poorly covered by regulated MFIs. Only six of the 109 districts in the department have an agency of a regulated MFI. Unregulated MFIs are the main providers of microfinance services in the rural areas, with a marked geographical specialization for each NGO. With the exception of the most productive and profitable areas, few rural areas count with the presence of an unregulated MFI. In the others, informal sources of credit are the only sources available.

This situation has been evolving toward a greater concentration in urban areas. (**Table A. 3** in annex for regulated MFIs). Between January 2002 and March 2003, the number of agencies went up by 40%, but the number of districts in which MFIs are present increased only by 20%.

The market of microfinance services in Cusco is centered on the leadership of the CMAC Cusco, but smaller MFIs could grow faster than the CMAC and increase the level of competition. The CMAC currently grants almost 60% of the loans of regulated MFIs in the department, and concentrates half of the clients. In an in-depth analysis of the structure of microfinance markets in Peru, Portocarrero (2003) describes this situation in several departments. Comparing the different departmental markets, he foresees a next phase in which competition will reach a maximum due to the saturation of the market. In this context, the importance of risk information sharing will grow.

Microfinance credits to agriculture in Cusco

The volume of loans to agriculture from MFIs is very low in the department. On average, regulated MFIs present in Cusco only dedicate 4% of their loan portfolio to agriculture (Table 9). Few COPEME-affiliated non-regulated MFIs lend to agriculture. Agricultural loans represent 30% of the total loans of MIDE, 7% of those of Cáritas del Perú, and 0% of Adra Ofasa¹⁷.

Table 9. Agricultural credit of regulated MFIs operating in Cusco at March 2003, in US \$^a

	Amount	Share of their portfolio
CMAC Cusco	322,000	1%
CRAC Quillabamba	1,265,000	26%
EDPYME Crear Cusco	85,800	7%
EDPYME Credivisión	30,000	2%
Financiera Solución	0	0%
TOTAL/AVERAGE for regulated MFIs	1,702,800	4%

Source: SBS

^a The amounts and shares are for the entire organizations, and not necessarily correspond to operations in the department of Cusco.

Using national averages, it can be inferred that the microfinance supply to agriculture does not total more than US \$ 2 millions in the department of Cusco. The total financing to agriculture, including commercial banks, regulated MFIs, and the three mentioned MFIs, does not exceed US \$ 4 million. Due to their small average loan size, unaccounted for unregulated MFIs do modify this estimation. In comparison, US \$ \$16.8 millions are estimated necessary to the financing of traditional cultures only, excluding export crops and investments (CEPES, 2001).

3.3 Use of Credit Bureaus in Cusco

The national-level partnership between COPEME and Infocorp has been applied in the department of Cusco since 1998. The penetration strategy of Infocorp in the department presents three characteristics (Velasco, 2003):

1. To date, eight organizations are client of Infocorp through the agreement COPEME-INFOCORP: three regulated MFIs, the two cooperatives, and three NGOs.
2. The reduced price available to microfinance organizations through the agreement with COPEME has been a powerful incentive to enter Infocorp's information sharing system, especially for NGOs. The reduction has taken two forms: the use of corporate prices, and the possibility for several organizations to share the fees and minimum price.

¹⁷ These percentages are given for the entire organization, at the national level.

3. None of the identified unregulated MFIs share their information with COPEME, although they all know Infocorp and its services, and have indicated being ready to share their own client information. (Velasco, 2003)

The actual and potential demand of risk information by MFIs in Cusco

The actual use of Infocorp's database in the department of Cusco is globally low in terms of the number of institutions that are registered to use it. Also, the SBS-based risk information plays a center role in the sense that they are the most consulted and generate some of the highest hit rates. (Velasco, 2003)

All regulated MFIs benefit from a free and unlimited access to the public credit bureau, with which they share their own information. As a result, they use it extensively, relying on private credit bureaus when additional information is necessary and according to rules specific to each MFI. On the contrary, unregulated MFIs depend on private credit bureaus for their risk information; they however also have access to the SBS information through both Infocorp and CERTICOM. Data on the consultation of the SBS and CERTICOM credit bureaus are not available. Therefore, this section will focus on the use of credit bureaus through the agreement COPEME-INFOCORP.

Due to the multiplicity of the products offered by Infocorp to its clients and the low number of consultation of some of them, this section will focus on the most used and relevant ones. A complete list of the available products and their number of consultations in Cusco is provided in **Table A.7** in Appendix A. The estimations of the relative importance of each product are computed using the total of existing products.

Consultations of the CB databases are made using the National Identification Number (DNI) and the name of the client. The use of the DNI is very widely spread in all databases of the MFIs in Cusco, and in all sectors in general. The most-used Infocorp products in Cusco are:

- (a) The 'Consolidated SBS information by borrower' presents all the debts contracted in the regulated financial system by the individuals or organizations that borrowed from two or more institutions. This product indicates the total amount of direct and indirect debts, the amount of defaulted debt, and the name of the institutions that reported the client as defaulting.
- (b) The 'Consolidated credit report', issued by the SBS, gives detailed information on each borrower and all its financial obligations in the regulated financial sector: direct and indirect debts, guarantees used, investments, all lines of credit in the regulated sector, goods used as collateral, unpaid bills for sale of goods and products, etc. If one debt is reported as defaulted, this product provides a detailed analysis of all debts by institution using the SBS' classifications of debts (five-element scale from 'normal' to 'lost').
- (c) The Consolidated system of default (SICOM) has a much wider coverage: it consolidates all the default information known to Infocorp in the financial, commercial, industrial, and service sectors, such as unpaid checks, payment orders, consumer credit, etc. Any document can be registered in this system.
- (d) The orders of payment registered by a notary: records of the orders registered by drawers and debtors.

Between November 1st, 2001 and September 30th, 2002, eight MFIs consulted regularly the Infocorp's database, taking advantage of the preferential treatment under the COPEME-INFOCORP agreement (Table 10): three regulated MFIs, the two cooperatives operating in the department, and three unregulated NGOs (Adra Ofasa, Cáritas del Perú, and Asociación Arariwa)¹⁸. All of them made, on average, 910 consultations per month. Of these, 759 have returned information, which equals to an average consultation hit rate of 83%. The average number of products consulted is seven.

Table 10. Consultation of Infocorp's database by type of MFI in Cusco, Nov 2001 – Sept 2002

Type of organization	Minimum-Maximum of		
	Number of consultations ^a	Number of products consulted ^a	Ratio consultations/ credit operations
Regulated MFIs	0-429	0-2,429	0%-143.0%
Non-regulated MFIs	0-212	0-979	0%-71.7%
TOTAL or AVERAGE	910	6,097.5	19.0%

Source: Velasco (2003)

^a *Average number per month in the period considered.*

A more detailed analysis of the actual use of risk information services in these eight organizations shows that the number of consultations of Infocorp's database is low, with an unequal number of consultations and number of products consulted among organizations. The reasons and methods of consultation are not related to the size or the type of the organization, but are the result of specific credit approval procedures. The CMAC Cusco, for instance, consults Infocorp's database only for loans larger than US \$ 1,500, but collects high quantities of information on each consultancy (16 products on average).

The information provided by the SBS is the key element of the departmental credit information system (Table 11). Two products based on SBS information are among the four most consulted summary products, and are the two most consulted detailed products. The same also generate the third and fourth higher hit rates of all products offered by Infocorp in the department. The two other most consulted products correspond to additions by Infocorp, and have the advantage of including more information, captured from unregulated exchanges in all sectors of the economy. Their position underlines the informality of the economic and financial sectors in Cusco. More information is needed on the sequence in which the four products presented in Table 11 are consulted to draw more precise conclusions on the relative advantage of each product, and the impact of their differences in hit rate.

¹⁸ This is a low number considering that Velasco (2003) already identified 19 NGOs that offer financial services to microentrepreneurs and the poor.

Table 11. Hit rate and Most consulted products in Cusco, Nov 2001 – Sept 2002

Products	Consultations	Product hit rate
SICOM	865	22.7%
Order of payments	865	12.3%
Consolidated SBS by borrower	864	49.1%
SBS' Consolidated credit report	608	44.7%
ALL PRODUCTS	6,097	19.9%

Source: Velasco (2003)

The potential demand for Infocorp's services concerns one regulated MFI (the EDPYME Crear Cusco) and 16 unregulated MFIs. At the current rate of consultation and without considering the effect of the increase of coverage of Infocorp's database, the inclusion of all of them would produce an increase of the number of consultations of 29%. (Velasco, 2003)

The actual and potential supply of risk information by MFIs in Cusco

The information supplied to the SBS and Infocorp by the participating organizations represents the majority of the information generated in microcredit transactions in the department, despite the fact that no unregulated MFI currently shares its information. Their contribution is potentially important, for it would include in the system a new segment of the microfinance market.

The institutions currently included in the Infocorp database through the legal mechanisms of supervision by the SBS are the five commercial banks and the five regulated MFIs present in the department. Leaving aside banks, the five regulated MFIs represent about 55% of the microfinance clients in the department, and concentrate more than 65% of the amounts lent (Table 12). These high rates are partially explained by the presence of the CMAC in the system of information sharing; the CMAC Cusco itself records almost 60% of the loans and almost 50% of the clients in the department.

Table 12. Indicators of the supply of microcredit information in Cusco, January 2003

Organizations (detail in Table A.6 in annex)	Loan portfolio size ^a	Number of clients	Default rate
Total already provided to Infocorp	29.8	27,836	5%
Total potential to provide to Infocorp	10.0	23,157	13.5%
TOTAL GENERAL	39.8	50,993	8.9%

Source: Velasco (2003)

^a *In million USD.*

The characteristics of the target groups of the potentially supplier organizations are important elements of their inclusion. All are unregulated organizations, mostly NGOs, and reach clients that do not access regulated MFIs. Their average loan size is \$430 (against \$1,000 for regulated MFIs), and their average default rate is more than double the rate of

regulated MFIs. Their sharing of information would also more than double the number of defaulting borrowers for which information is recorded and shared.

Elements of the future evolution of Infocorp's presence in the department of Cusco

In the context of the national agreement between COPEME and Infocorp, they commissioned a paper to establish the current situation of the use of the CB system and to evaluate potential for improvement and expansion. An independent consultant, Alejandro Velasco, elaborated that document, and he identified the following axes of expansion of Infocorp in Cusco¹⁹:

- (a) Priority must be given to the inclusion into the system of the identified non-regulated organizations and their information. Infocorp has already expressed its interest in including new microfinance organizations in their program with COPEME, and would also benefit from any inclusion of new information, as well as from new clients.
- (b) There is evident interest of these microfinance organizations in consulting and sharing negative information. Positive information should also be included in the information system to increase the impact and possibilities of credit bureaus.
- (c) The quantity of consultations made by each organization can be increased. This phenomenon should come as a consequence of the introduction of new information; however, it is possible and would be profitable for Infocorp to take actions to promote an increased use of its products through more flexible price schemes.

In sum, the inclusion of all unregulated organizations into Infocorp would have a large systemic effect on the market of risk information in the department of Cusco. Conjugating the incorporation of new organizations into the system and the adoption of specific measures by Infocorp aimed at promoting its services, it is reasonable to estimate an increase in the number of checks of about 50%, and an increase in the number of positive checks of more than 50%. The newly included organization would also share extremely useful information, extending the impact of the credit bureau to new categories of borrowers.

4. PERCEPTION AND USE OF CREDIT BUREAUS IN CUSCO

The use of Credit bureaus in the department of Cusco has been documented statistically in the previous section. This section will focus on the procedures and practices set up in MFIs regarding the use of credit bureaus in the evaluation of credit applicants. Clients' perceptions of credit bureaus have also been documented through interviews.

¹⁹ See Velasco (2003).

4.1 Structure of the interviews

Interviews were conducted in and around the city of Cusco with staff of regulated and unregulated MFIs, as well as with urban and agricultural clients of some of these MFIs. A total of nine MFIs and eight clients have been interviewed.

The MFIs interviewed are of different sizes, target groups, and status, to represent the variety of the department. Their names and basis characteristics are presented in. It is to be noted that the NGOs IFOCC and MIDE recently became clients of Infocorp, through the opportunity that COPEME grants them. They are not included in the statistics on the use of credit bureaus in Cusco in the previous section, which is up-to-date as of January 2003. We interviewed four regulated MFIs and five unregulated ones; five operate in urban areas, two operate exclusively in rural areas, and two operate both in urban and rural areas. The interviews were conducted with general or executive managers in unregulated MFIs, and with risk managers and credit officers in regulated MFIs. The questions focused on five elements:

- The methods of evaluation of credit applicants;
- The rules of use of credit bureaus;
- The guarantee requirements;
- The loans supervision; and
- The procedures in case of default.

Of the eight clients that were interviewed, three are urban microentrepreneurs and five are agricultural producers. Agricultural clients were both small producers practicing traditional agriculture and modern producers of export crops. Two clients borrowed from unregulated MFIs, and six from the Caja Municipal or the Caja Rural. The questions to clients focused on their credit history, their use of guarantees, and their perception of the consequences of defaulting or having defaulted on loans. Clients were explicitly asked about credit bureaus at the end of the interview only.

4.2 Information sharing and its use in MFIs interviewed

Information sharing is based on formal and informal mechanisms. Informal mechanisms of information sharing include: (i) the sharing of lists of potential clients, for whom the receiving organization warns if they have a bad record in their file, and (ii) personal contacts between credit officers of regulated and unregulated MFIs. These personal contacts are known and accepted by the management staff of all interviewed organizations. The use of these informal mechanisms has increased between unregulated MFIs after the repayment crisis of 1998-99, which promoted a culture of generalized information sharing. Currently, informal mechanisms of information sharing are the only ones used in the two small NGOs interviewed. The formal mechanism of information sharing is the use of centralized databases maintained by a credit bureau.

The evaluation of credit applicants

Credit bureaus are used in the evaluation of credit applicants, but the importance given to the information they provide varies. In all interviewed MFIs, the evaluation of credit applicants is made using two criteria: the capacity to repay, and the willingness to repay. The capacity to repay is assessed by similar ways: socio-economic information about the client and its family (for agricultural loans) or business associates (for loans to small- and microenterprises), credit application forms which always include questions on the credit history, and visits to the enterprise of agricultural unit. The willingness to repay is by nature subjective, and its evaluation is one of the main tasks of the credit officer. Credit bureaus and informal information sharing mechanisms constitute ways to objectively evaluate applicants' willingness to repay.

The relative importance given to the two criteria of evaluation and the importance given to the credit bureau check to evaluate the willingness to repay vary in each MFI. Non-regulated MFIs can give only relative importance to the information obtained from credit bureaus. Two out of five NGOs interviewed allow their credit officers to continue the evaluation of applicants even when the information from the CB is unfavorable. They declared giving more importance to the evaluation of the applicant's capacity to repay and using the credit bureau information more as an aid to the decision than as a requirement. They also emphasized the importance of personal contacts with credit applicants and clients over their strict economic and financial evaluation.

On the other side, all regulated MFIs interviewed set limits to distinguish between acceptable and unacceptable credit histories, and they systematically refuse to lend to clients whose debts are classified as Deficient, Doubtful, or Lost²⁰. Regulated MFIs also reported refusing to lend if the applicant already has more than two other outstanding loans.

Rules for the use of the credit risk information

The rules of use of credit bureaus are the guidelines given to and/or used by credit officers regarding which credit bureau to check, for which loans, and for which persons. In this section, we explore whether the interviews to credit officers in Cusco can help us identify any patterns of use of the credit risk information provided by Infocorp based on legal status, size, lending methodology or sectoral concentration. We found only two clear patterns.

The first pattern of use identified is based on the specificity of regulated MFIs in Peru and their free access to the public credit bureau (Section 3.3 page 30). All regulated MFIs interviewed check the credit history of all their clients in the public credit bureau, but have differing procedures of consultation of private credit bureaus. Moreover, only two of the biggest MFIs in the department, use both private credit bureaus. These two elements could explain why some regulated MFIs have a low amount of consultations of Infocorp, from the statistics of COPEME. Credit officers of some MFIs are indeed free to choose the CEPIR they use, provided they use one when indicated. All other MFIs use either Infocorp or do not use private credit bureaus.

²⁰ These categories are the SBS' classification of debts: Normal, with potential problems, Deficient, Doubtful, and Lost.

The second identified pattern relates to the type of loans granted. Agricultural lenders consult Infocorp's database less than their urban counterparts. This pattern is consistent with the lower availability of financial services in rural areas, and the globally lower level of competition among financial institutions in agricultural areas.

Consultations of the databases of credit bureaus are made by the national identification number (Documento Nacional de Identificación, DNI) and by the name of the client. The use of the DNI is very widely spread in all databases of the MFIs in Cusco, and in all sectors in general.

Guarantee requirements

Credit bureaus have the potential to allow good borrowers to use their credit history as a guarantee of their loans, thus lowering or deleting the requirements for material guarantees. However, this mechanism cannot be identified in any of the interviewed MFIs. Despite the differences in use of credit bureaus, all interviewed MFIs require guarantees. Loans made in productive agricultural zones with well-established land titles seem to be the only loans for which borrowers can use their land as collateral. All other loans of other MFIs, regulated or not, are guaranteed by other property. The most commonly used asset is the house of the borrower, because these property titles are much better established than land titles. Some MFIs also require additional guarantees such as household items of value, and/or co-signers.

Procedures in case of default and loan supervision

The procedures in case of default of the borrower are similar in all interviewed MFIs. They involve a two-step process: first, warnings are addressed to the clients, before legal action is taken to recover the loan with the good(s) used as guarantee. All MFIs declared having already engaged such procedures, but recognize that the delays necessary to effectively recover the loan weaken this option.

Prevention of loan default in the form of loan supervision is not that common among MFIs in Cusco. The only MFIs that reported monitoring the use of the loans are the EDPYMEs. However, all the MFIs except one accept to negotiate solutions with defaulting clients for the recovery of the loans. These solutions are quasi-exclusively a change of the term of the loan; one MFI only agrees to modify the interest rate. Of all interviewed institutions, only one regulated MFI said running a credit check at this moment. The institution that refuses to modify the conditions of the credit does so by experience: in the past, such solutions have never functioned for it. Such credits are considered as lost and provisioned for as soon as the client is late in his/her payments.

In the case of interviews with MFIs that currently use CBs, the interviews were ended by asking the credit officers how this could be improved. Several MFIs complained that they did not encounter most of the clients whose information they verify, but the increase of the coverage of the credit bureaus was not the most desired improvement. Most MFIs, of all type and size, wished for a more frequent update of the information in the

databases of the CBs. The information currently provided is on average two months old, and has proven wrong many times for some MFIs.

4.3 Perception of the credit bureaus by clients

The clients interviewed have been chosen by the MFIs upon request of the investigators. Their distribution is indicated in **Table 13**.

Table 13. Types of clients interviewed					
	Unregulated MFI (MIDE)		Regulated MFI		TOTAL
	New client	Old client	New client	Old client	
Urban client (SME)	-	-	1	2	3
Agricultural client	1	1	1	2	5
TOTAL	1	1	2	4	8

MIDE is a medium-size microfinance NGO operating in the province of Anta, about 30 km from the city of Cusco. It provides microfinance to small farmers organized in solidarity groups. The organization is the only one providing microfinance services in the region, mostly for agricultural activities, but also for traditional other rural activities (cattle ranching, commerce of agricultural products, etc.). We interviewed two clients, one with two years of credit and the other one with five years of credit experience. Both did not change the type of activities they practice: agriculture and commerce of different agricultural products and cattle.

Clients of regulated MFIs are agricultural and microenterprise clients. They borrowed from the Caja Municipal and the Caja Rural. They have between one and 30 years of borrowing experience, with several lenders, almost always from the regulated sector. Agricultural clients of the Caja Rural come from a fertile valley of the department, where the borrowers are specialized in the production of corn, exclusively for exportation. This valley has been well provided in credit for the last decades. Small- and microentrepreneurs are urban merchants or small factory managers.

The perception of credit bureaus by the clients was investigated through a two-step process. First was asked their perception of the consequences of defaulting on a loan, from their own experience or their observation of other clients' experience. In a second time was asked whether they know credit bureaus, and what they know about them. This information is placed in the context of their credit history, and the guarantees that they used.

Credit histories

Credit bureaus can have a stronger impact when borrowers are able to build themselves a credit history, possibly borrowing increasing amounts from several lenders. In the department of Cusco, it appears that the possibilities and practices of clients are very different for rural and urban clients.

The progression in terms of loan size appears stronger for urban clients than for the rural ones. The former reported current loans on average ten times bigger than their initial

loan. Agricultural clients have a more limited progression, for different reasons. Due to their unique activity, modern agricultural clients have high but relatively fixed needs of credit. Traditional agricultural clients have also not progressed as fast as urban clients, due to the traditional type of activities they practice and the limited financial resources available to them in the area.

The weakness of the financing supply to agriculture lowers the need for a credit bureau, and prevents rural clients from building themselves a credit history in different organizations, thus moving up the lending ladder from unregulated MFIs to regulated ones and to banks. Most agricultural clients of the department, for example, have no alternative lending organization to turn to in their region, with the exception of informal lenders. Modern agricultural clients that were interviewed, situated in a profitable modern agricultural region, had the opportunity to borrow from different lenders, but never at the same time. Cooperatives, Banco Agrario, or more recently AgroBanco followed each other but did not compete.

The experience of urban clients is entirely different. These clients have had choices of lenders in the past, and perceive the increase in the number of lenders and the competition between them. The Caja Municipal, the Caja Rural, the Financiera Solución, and the banks have all adopted policies of active recruitment of clients. They go towards the clients in commercial areas and in their business. One urban microentrepreneur client of a regulated MFI that was interviewed reported being visited by different MFIs and banks.

Urban clients interviewed recognized benefiting from the competition between lenders. However, they do not enjoy lower interest rates, but rather additional and/or better services. An old client, with a 30-year-long history of credit with nine different lenders, answered staying with his current lender for the quality of their service and the flexibility of their loan products.

Use of guarantees

As reported by the personnel of the MFIs, all borrowers have to use their assets to guarantee their loans. The asset reported as most commonly used as guarantee was the house for urban borrowers. Only the modern agricultural borrowers, which have titled land, used their land as collateral; traditional agricultural clients used their house.

The fact that guarantees are mandatory to obtain a loan does not bother the borrowers, although the majority of them would value being able to borrow without guarantee. However, all the borrowers interviewed do not envision the possibility to do so. A modern agricultural borrower reported for instance that “*banks do not value good character*”.

Perception of the consequence of defaulting on a loan

During the interview, clients were asked if they have ever defaulted or knew any person that has already defaulted, and if this event makes it harder for them/the person to receive new loans. These questions were used as an indicator of the extent to which borrowers’

repayment behavior is shaped by middle- and long term credit perspectives and the mechanisms of information sharing.

The general level of knowledge of the mechanisms of information sharing and their impact on every borrower is low. Although most of the clients interviewed recognize that defaulting on a loan is harmful to them, only one declared that it would make it more difficult to receive other loans from all lenders. The other borrowers interviewed had only a vague understanding of the mechanisms by which defaulting could harm their capacity to be granted more loans: an agricultural client observed that defaulting makes the interest rates go up, and another underlined the impossibility to use the same guarantee with another lender.

The knowledge of the impact of defaulting on a loan does not vary consistently with the different categories of borrowers. One MFI systematically informs its clients during the loan approval process of the existence of information sharing mechanisms between all lenders in the country; of its clients interviewed, only one clearly remembered that the institution would not lend him/her if he/she defaulted. Other clients from regulated MFIs also only reported the difficulties to borrow from the same MFI in case of default, not considering automatically the transfer of information between lenders.

Knowledge of the credit bureaus

The explicit and precise knowledge of credit bureaus, the information that they contain, and their use in MFIs is low among MFI borrowers in Cusco. It is lower than the perception of the harm that defaulting can do. Of the eight clients interviewed, four had some knowledge of credit bureaus, but only two realized the extent to which information can be shared and used by all lenders.

This knowledge is higher among urban clients than among rural ones. The two clients that reported knowing what a credit bureau is are both urban clients. Only one of the five rural clients interviewed had a limited knowledge of credit bureaus, while all the others did not know anything about it.

Table 14. Characteristics of the MFIs interviewed

MFI	Position if contact person	Loan portfolio^a	Number of clients^b	Credit methodology	Rural credit
NGO Runamaki	Director	73	160	Solidarity groups	100%
NGO Imagen	Executive Director	80	60	Individual and Solidarity groups	n/a
NGO Caritas del Perú	Director of Credit	230	1,050	Solidarity groups and Village Banks	0%
NGO IFOCC	Executive Director	348	850	Individual	0%
NGO MIDE	Manager	260	3,050	Solidarity groups	100%
EDPYME Credivisión	Agency manager	770	1,630	Individual and Solidarity groups	0%
EDPYME Crear	Risk manager	1,130	1,000	Individual	0%
CRAC	Risk manager	3,900	5,200	Individual	23%
CMAC	Risk manager	24,000	20,000	Individual	1.3%

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APPENDIX A

Table A.1: Number of regulated MFIs

	1990	1995	2003
CMACs	10	13	13
CRACs	0	10	12
EDPYMEs	0	0	14
Financiera Solución	0	0	1
Mibanco	1 ^a	1 ^a	1
TOTAL	11	24	41

Sources: SBS, Portocarrero et al. (2002)

^a Mibanco existed as an NGO before its incorporation as a commercial bank in 1998.

Table A. 2: Summary information on the commercial banks, March 2003

	Multiple banks (without Mibanco)	Mibanco
Average number of clients	125,974 ^a	77,942 ^b
Total outstanding loan portfolio, in million USD	10,500	100
Average loan portfolio, in million USD	810	100
Average default rate	8.61%	3%
Loans to small and microenterprises, in % of loans	2%	65%

Sources: SBS, Mibanco

^a Including Mibanco

^b At December 2001

Table A. 3: Evolution of the geographical distribution of some regulated MFIs in the department of Cusco

	Number of agencies		Number of districts with an agency	
	Dec. 2001	Mar. 2003	Dec. 2001	Mar. 2003
CMAC	4	6	4	5
CRAC	3	4	3	3
EDPYMEs	2	2	1	2
Financiera Solución	1	1	1	1
TOTAL	9	13	5	6

Source: SBS

Table A. 4: Evolution of the loan portfolio of regulated MFIs in Cusco

Organization	2001	March 2003
CMAC Cusco	10,716 ^a	25,610
CRAC Quillabamba	4,542 ^a	4,380
EDPYME Crear Cusco	945 ^b	1,171
EDPYME Credivisión	720 ^b	829
Financiera Solución	2,258 ^c	2,510
TOTAL	-	34,500

Source: SBS

^a *At March 2001.*

^b *At June 2001.*

^c *At January 2002.*

Table A.5: Basic information on microfinance organizations in the department of Cusco

Organization's name	Start of operation in the department of Cusco	Personnel in the department	Provinces of operation
CMAC Cusco	March 1988	150 ^a	Cusco, Canchis, Calca, La Convención, Espinar
CRAC Quillabamba	November 1994	55 ^a	Cusco, Canchis, La Convención
EDPYME Crear Cusco	December 1999	16 ^a	Cusco
EDPYME Credivisión	April 2000	13 ^a	Cusco
Financiera Solución	February 1998	35 ^a	Cusco
CAC Santo Domingo de Guzman		25 ^b	Anta
CAC Quillabamba		18 ^b	Anta
ONG IFOCC			
PEJ PA Sicuani			
CIUR INTI			
Imagen			
ONG Runamaki			Chincheros, Calca, Ollantaytambo, Cusco, Urubamba, Oropesa, Anta, Pisac, Taray, San Salvador, Quispicanchi, Yucay, Canas, Canchis, Espinar
Caritas Sicuani			
IPID Sur Sicuani			
Centro Desarrollo Rural Yanapay			
Guaman Poma			
Adesa			
ONG ADRA OFRASA		31 ^b	
ONG Carit�s del Per�			
ONG Carit�s Sicuani			
ONG MIDE		14 ^b	
FONCODES Cusco			Valle Sagrado, Anta, and Paucartambo

Sources: SBS, Velasco (2003), Ministry of Agriculture

^a At March 2003.

^b At December 2002.

Table A.6: Indicators of the microcredit information supply in the department of Cusco, Jan 2003

Organization	Loan portfolio size ^a	Number of clients	Default rate
CMAC Cusco	24,000	20,000	4.2% ^b
CRAC Quillabamba	3,900	5,200	11.4% ^b
EDPYME Crear Cusco	1,130	1,000	4.6% ^b
EDPYME Credivisión	770	1,636	11% ^b
Financiera Solución	n/d	n/d	n/d
Total already provided to INFOCORP	29,800	27,836	5%
CAC Santo Domingo de Guzman	3,800	4,900	13.5%
CAC Quillabamba	1,800	2,316	30%
Asociación Arariwa	1,220	4,600	3%
ONG IFOCC	348	850	13%
PEJ PA Sicuani	348	930	4%
Microcredito para el Desarrollo	260	3,051	5%
Cáritas del Perú, Cusco	230	1,050	15%
Cáritas del Perú, Promesa Sicuani	230	800	4%
PAC Hormiga Sicuani	145	800	5%
CIUR INTI	140	320	2%
Imagen	80	60	4%
ONG Runamaki	73	160	13.5%
Caritas Sicuani	69	322	1.6%
IPID Sur Sicuani	53	163	29%
Adra Ofasa	39	442	0.1%
Centro Desarrollo Rural Yanapay	290	700	100%
Guaman Poma	39	48	100%
Adesa	30	45	100%
FONCODES Cusco	780	1,600	14%
Total potential to provide to INFOCORP ^c	10,000	23,157	17.4%
TOTAL GENERAL	39,800	50,993	8.9%

Source: Velasco (2003)

^a In Thousands USD.

^b At March 2003.

Table A.7. Products of summary information consulted in Cusco, Nov. 1st, 2001 – Sep. 30th, 2002

Product	Consultations	Positive encounter	%
SICOM	865	196	22.70
Order of payments	865	106	12.27
Consolidated SBS by borrower	864	425	49.14
Rectifications	815	-	-
SBS' Consolidated credit report	608	272	44.74
Debts SBS	393	20	5.15
Debts Pension Funds	288	2	0.66
Debts SUNAT	247	12	4.71
Debtors	178	19	10.63
Legal representatives (for organizations)	169	38	22.43
Orders of payment, by drawer	165	9	5.33
Number of consultations of an individual or organization	156	48	30.41
Interdictions to open a bank account	156	7	4.59
Cancelled credit cards	156	3	1.74
International commerce activities (from the Customs administration)	82	3	3.67
Addresses	40	31	77.55
Directories of basic information	40	16	39.00
Deta cons	9	5	59.00
Directory of businesses (from the Tax administration)	0	0	100.00
TOTAL	6,097	1,211	19.87

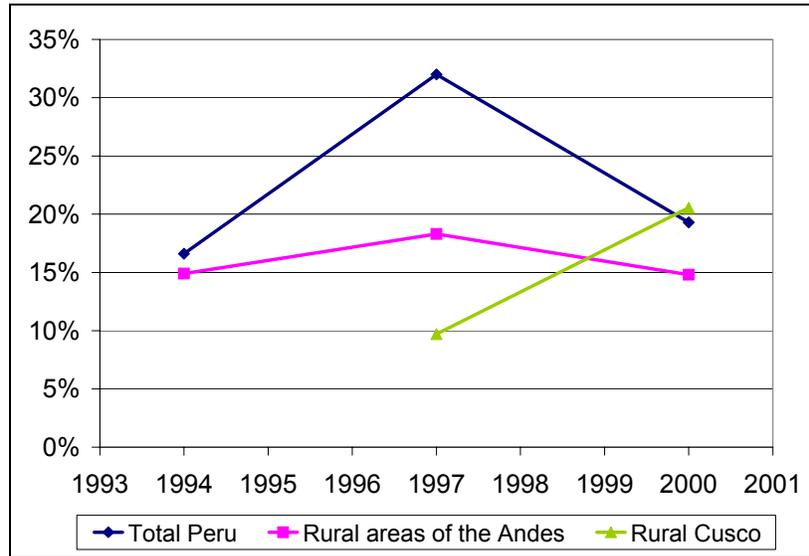
Source: Velasco (2003)

Table A.8: National use of INFOCORP, Sept 1st, 2001 – Aug 30th, 2003

Department	Number of unregulated MFIs	Number of consultations	Hit rate
Lima	20	250,150	83.8%
Cusco	6	27,240	86.0%
Ayacucho	3	18,129	87.9%
Puno	3	17,156	71.9%
La Libertad	3	16,149	90.8%
Junín	5	15,854	86.0%
Arequipa	2	11,904	86.0%
Lambayeque	2	10,017	88.2%
Huanuco	2	9,764	78.2%
Ucayali	1	8,999	75.3%
Piura	0	7,022	91.5%
San Martín	n/d	6,777	79.6%
Cajamarca	2	6,244	78.9%
Ancash	3	5,250	74.0%
Apurímac	2	5,151	75.0%
Ica	2	2,267	87.5%
Huancavelica	1	1,516	55.5%
Amazonas	1	1,136	68.0%
Moquegua	2	1,093	88.6%
Tacna	n/d	881	87.3%
Tumbes	1	122	80.3%
Loreto	1	96	96.27%
Pasco	0	0	0.0%
Madre de Dios	0	0	0.0%
TOTAL and AVERAGE		422,917	82.57%

Source: Statistics administration of the COPEME-INFOCORP agreement.

Figure A.1: Evolution of the share of households with access to credit



Source: Trivelli (2002), ENNIV 2000.

APPENDIX B

Table B.1: Date of creation, size, and default rate of lending institutions in Peru

Institution	Year of creation	Patrimony ^a	Loan portfolio ^a	Def. rate ^b
Multiple banks				
Banco de Crédito del Perú	1889	584,278	2,682,815	4.46
Banco Internacional del Perú - Interbank	1897	113,911	747,881	6.42
Banco Wiese-Sudameris	1943	377,746	1,473,688	12.17
BBVA Banco Continental	1951	308,124	1,622,021	4.70
Banco de Comercio	1967	19,782	82,604	19.80
Banco Financiero del Perú	1986	64,423	247,901	9.93
Banco Interamericano de Finanzas	1991	32,781	310,168	1.70
Banco Sudamericano	1993	46,473	426,076	5.00
Banco del Trabajo	1994	26,058	157,594	3.37
Suc. en el Perú de Citibank N.A.	1920	113,968	483,352	1.48
BankBoston, N.A. Sucursal del Perú	1996	31,039	280,160	0.48
Banco Standard Chartered	1998	25,311	32,801	19.68
Banque BNP Paribas-Andes S.A.	1999	9,640	6,074	0.00
Mibanco	1998	25,343	92,383	1.37
TOTAL MULTIPLE BANKS		1,778,877	8,645,517	6.26
Financial entities				
Solución - Financiera de Crédito	1996	20,341	79,617	0.00
Financiera CMR	1997	32,081	88,590	1.16
Volvo Finance Perú	1997	11,825	19,514	20.83
Financiera Cordillera	2000	19,897	65,137	0.04
TOTAL FINANCIAL ENTITIES		84,144	252,858	2.03
CMACs				
CMCP Lima	1947	7,678	13,437	0.95
CMAC Piura	1982	14,762	71,503	3.84
CMAC Trujillo	1984	9,354	49,290	1.97
CMAC Arequipa	1986	16,433	68,737	2.97
CMAC del Santa	1986	1,775	10,259	2.29
CMAC Sullana	1986	6,364	26,129	3.51
CMAC Maynas	1987	2,763	12,841	2.66
CMAC Cuzco	1988	6,153	28,556	1.64
CMAC Huancayo	1988	5,482	24,767	3.10

CMAC Ica	1989	3,463	10,079	6.03
CMAC Paita	1989	2,069	7,631	3.93
CMAC Pisco	1992	652	2,664	4.47
CMAC Tacna	1992	4,339	17,148	2.17
CMAC Chincha	1997	439	2,638	2.22
TOTAL CMACs		81,726	345,680	2.91
EDPYMEs				
EDPYME Confianza	1998	1,133	4,808	2.73
EDPYME Edyficar	1998	5,851	21,912	6.06
EDPYME Nueva Visión	1998	1,056	2,127	2.37
EDPYME Crear Arequipa	1998	1,082	4,048	3.70
EDPYME Crear Tacna	1998	1,022	3,367	8.20
EDPYME Proempresa	1998	1,666	5,793	2.40
EDPYME Raíz	1999	17,278	15,828	6.75
EDPYME Credivisión	2000	1,272	1,152	6.96
EDPYME Alternativa	2001	545	788	3.22
EDPYME Camco Piura	2001	397	297	8.10
EDPYME Crear Trujillo	2001	342	1,445	2.15
EDPYME Crear Cusco	2000	376	1,078	2.87
EDPYME Pronegocios	2002	849	982	0.00
EDPYME Solidaridad	2000	448	1,113	8.73
TOTAL EDPYMEs		33,315	64,737	2.99
CRACs				
CRAC Cajasur	1993	2,760	10,814	4.73
CRAC Chavín	1994	876	1,640	18.21
CRAC Libertadores de Ayacucho	1994	500.79	3,659	14.95
CRAC Quillabamba-Credinka	1994	903	3,829	9.24
CRAC San Martín	1994	2,870	16,107	5.22
CRAC Señor de Luren	1994	2,361	9,671	3.78
CRAC Cajamarca	1995	729	2,445	4.41
CRAC Cruz de Chalpón	1995	824	5,197	5.70
CRAC Nor Perú	1995	2,482	12,568	6.60
CRAC Profinanzas	1995	490	3,179	11.44
CRAC Los Andes	1997	596	1,154	19.52
CRAC Prymera	1998	1,603	2,604	2.74
TOTAL CRACs		16,995	72,867	6.60

COPEME-affiliated MFIs^c			
Adra Ofasa	388	459	0.00
Asociación Mujeres en Acción (AMA)	183	235	19.90
Caritas del Perú	697	1,615	8.70
GCOD	186	266	13.10
Edaprospo – ALCOM	91	302	4.20
Edaprospo – PAF	178	569	6.10
FINCA	1,223	773	0.80
Fondesurco	146	1,085	17.80
Fovida	398	392	2.30
Idesi La Libertad	148	337	5.20
Idesi Lambayeque	45	198	15.40
Idespa	179	178	15.40
Instituto de Promoción Regional (IPR)	143	251	3.80
Manuela Ramos	1,833	1,562	3.15
MIDE	4	340	6.70
AB Prisma	5,220	5,244	41.20
Promujer	942	1,317	0.00
TOTAL COPEME MFIs	12,005	15,122	18.49
TOTAL GENERAL	2,007,062	9,396,782	13.59

Sources: SBS, COPEME (2003)

El presente informe es una publicación de la SBS. Los datos corresponden al primer trimestre del 2003.

Table B.2: Date of creation, size, and default rate of lending institutions in Cusco

Institution	Start of operation in Cusco	Provinces of operation	Loan portfolio ^a	Clients	Default rate
Banco de Crédito	May 2000	Cusco, Canchis, La Convención	12,326	790	5.0%
Interbank	n/a	Cusco	12,050	10,356	3.5%
Banco Wiese Sudameris	Jul 1994	Cusco	5,794	683	38.1%
Banco Continental	Jun 1998	Cusco, La Convención, Espinar	18,705	2,089	6.4%
Banco del Trabajo	Apr 1996	Cusco	4,217	n/a	n/a
TOTAL MULTIPLE BANKS			53,092	13,918	8.4%
CMAC Cusco	Mar 1988	Cusco, Canchis, Calca, La Convención, Espinar	24,000	20,000	4.2% ^b
CRAC Quillabamba	Nov 1994	Cusco, Canchis, La Convención	3,900	5,200	11.4% ^b
EDPYME Crear Cusco	Dec 1999	Cusco	1,130	1,000	4.6% ^b
EDPYME Credivisión	Apr 2000	Cusco	770	1,636	11.0% ^b
Financiera Solución	Feb 1998	Cusco	2,511	n/a	n/a
TOTAL REGULATED MFIs			29,800	27,836	5.0%
CAC Santo Domingo de Guzman	n/a	Anta	3,800	4,900	13.5%
CAC Quillabamba	n/a	Anta	1,800	2,316	30.0%
Asociación Arariwa	n/a		1,220	4,600	3.0%
ONG IFOCC	n/a		348	850	13.0%
PEJ PA Sicuani	n/a		348	930	4.0%
MIDE	n/a		260	3,051	5.0%
Carit�s del Per�	n/a		230	1,050	15.0%
Carit�s del Per�, Promesa Sicuani	n/a		230	800	4.0%
PAC Hormiga Sicuani	n/a	Anta, Chincheros, Calca, Ollantaytambo, Cusco,	145	800	5.0%
CIUR INTI	n/a	Urubamba, Oropesa, Pisac,	140	320	2.0%
Imagen	n/a	Taray, San Salvador, Quispicanchi, Yucay,	80	60	4.0%
Runamaki	n/a	Canas, Canchis, Espinar	73	160	13.5%
Caritas Sicuani	n/a		69	322	1.6%
IPID Sur Sicuani	n/a		53	163	29.0%
Adra Ofasa	n/a		39	442	0.1%
Centro Desarrollo Rural Yanapay	n/a		290	700	100.0%
Guaman Poma	n/a		39	48	100.0%
Adesa	n/a		30	45	100.0%

FONCODES Cusco	n/a	Valle Sagrado, Anta, and Paucartambo	780	1,600	14.0%
TOTAL UNREGULATED MFIs			10,000	23,157	17.4%
TOTAL GENERAL			92,892	64,911	8.3%

Sources: SBS, Velasco (2003), Ministry of Agriculture

^a *At March 2003.*

^b *At December 2002.*

GUATEMALA

Analysis of the lending and credit reporting systems in the formal and agricultural sectors

by

Carlos Enrique Herrera Castillo

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EXECUTIVE SUMMARY

Farmers and small business owners in Guatemala have access to three types of banking institutions: formal sector banks, such as the Industrial Bank or the Coffee Bank (Bancafé); agricultural sector banks, such as the Agromercantil Bank and the Bank of Rural Development (Banrural) which loan exclusively to those involved in agricultural production; and microfinance institutions such as the Association of Technical Cooperation (ACT) and Fe y Alegría. This consultancy involved interviewing representatives of the formal and agricultural banking sectors as well as forming and interviewing focus groups of client individuals and organizations.

Small borrowers, particularly in rural areas, are most likely to get credit through microfinance institutions or cooperatives (hereafter “MFI’s”) which charge high interest rates (as high as 36%) and initially allow borrowers access to relatively small amounts, sometimes also requiring borrowers to form groups in which members are mutually responsible for borrowed funds. In spite of these restrictions MFI’s are popular because applications are easy, funds are provided quickly, no collateral is required, and some provide technical assistance. MFI’s actively work with borrowers on developing their enterprises, and in case of trouble have occasionally forgiven part of borrowers’ debts. Because of this, MFI’s are popular not only as the avenue of last resort for “high credit risk” clientele but for more established borrowers, who often develop feelings of loyalty for these supportive institutions. One small problem is that some MFI’s need to be educated about checking the references of potential borrowers to prevent clients from borrowing simultaneously from many institutions beyond their ability to repay.

As the size of a business increases, borrowers come to need more credit than MFI’s are willing to provide, and they turn to either agricultural sector or formal sector banks. Formal sector banks are generally unwilling to support crop cultivation activities unless borrowers are of considerable size, while agricultural lenders will lend to more agricultural producers. Both formal and agricultural banks require collateral, and in some cases have been forced to foreclose on mortgaged land. Both types of bank require all applicants to fill out some rather complex paperwork, which is a significant barrier for some potential

clients. In case of default, these banks often are willing to renegotiate the terms of repayment, but will not forgive outstanding balances. (For example, in the case of crop failure, agricultural lenders encourage farmers to continue to make payments by raising livestock.) Interest rates tend to be lower than at MFI's, varying with the type of loan, and unlike the MFI group lending, these banks never hold borrowers responsible for the debts of others. Formal sector lenders provide resources which help well developed industries, but because of the paperwork and collateral requirements some groups prefer to remain with MFI's as long as possible, in spite of the higher interest rates.

The linkages between MFI's and more formal banks are not well developed. Formal sector banks generally do not consider clients' MFI credit histories in their lending decisions, consulting agencies such as Digidata, Bancared, and Transuni3n, none of which include MFI credit histories. MFI's have developed an infrastructure for credit references, including the West Central Credit Risk Station, which supports more than 100 of the 2000 MFI's operating in Guatemala. More recently formal, agricultural, and microfinance institutions have come together to form a universal database called Crediref. As of January 2003, the database included information on over 58,000 loans, involving upwards of 120,000 people. Crediref personnel are working to include information from more MFI's, which means introducing new software and training lending institutions on how to use it to track loans and share credit information with the central database. Many MFI's are joining, but many more are nervous about sharing their credit information, so there are political as well as technical barriers to implementation.

All types of bank utilize the same means of identification, the "C3dula de Vecindad," so the development of a central authority for all credit information seems eminently feasible. If the information of the Bank Association of Guatemala and that of the West Central Credit Risk Station were incorporated into Crediref, formal sector institutions would be more able to make use of credit histories developed by MFI clients as part of their background checks. The development of a central database should help MFI's keep better track of their clients and should help borrowers demonstrate ability to repay, helping them get access to credit via other sectors as needed.

INTRODUCTION

The FAO's Terms of Reference creating this consultancy called for an investigation of moneylending institutions of two types: those in the formal sector, issuing large numbers of loans to individuals for business purposes, and institutions in the agricultural sector, accepting land as collateral for small farm loans seeking funds to cover planting and harvesting costs. The TOR also required analysis of the various institutions' use of Credit Bureau information to improve lending strategies and thereby minimize delays in repayment, misuse of lent funds, so-called "double dipping," and over-indebtedness among borrowers. Credit bureau information enables the institutions to lend more appropriately, strengthening their overall financial standing and making it more likely that they will continue to be able to offer services.

In Guatemala today, few lenders participate in agricultural financing, due to the higher level of risk associated with such investments. However, this outcome is likely to be far from the social optimum, since such loans generate employment and deepen economic development. Without some type of protection against this risk, though, lenders are unlikely to be able to lend to agricultural producers, so one potential avenue by which both lenders and society might benefit is if crop insurance were made available.

This report is based on personal interviews with those involved in the area, including both lenders and their clients.

RESULT OF FORMAL SECTOR INTERVIEWS

The Terms of Reference calls for making contact with four of the most important banking entities assisting big investors in the formal sector in Guatemala. These include the Coffee Bank, S. A.; BANCASOL; the Industrial Bank, S. A., and the International Bank.

Interviewing representatives of these banks, we determined that members of the formal sector use similar criteria to identify clients and to grant credit. The banks do not use credit agencies, preferring to send their own executives and Credit Advisory departments to directly evaluate claims and to verify the information potential borrowers submit with their applications for credit.

For this sector, it is not so important that a client has “graduated,” so to speak, from a microfinance entity in order to gain credit at this other level. It is more important that they fulfill the requirements that the bank establishes, which are mainly that they have the capacity to meet their payment obligations. The key points formal sector banks evaluate in decisions to extend credit are:

- Credit history,
- Credit standing,
- Financial situation,
- Capacity for repayment,
- Level of indebtedness, and
- Viability of the proposed project.

Credit bureaus are used both to corroborate the commercial references and to check credit. The most used bureaus are the Bank Association of Guatemala, Public Information (DIGIDATA, CORP.), TRANSUNIÓN, and each bank’s own credit division. The Coffee Bank is the only one among the four that consults the CREDIT REFERENCES CORPORATION -CREDIREF -.

The Formal Sector does not have a specific mechanism for loan supervision and pursuit of claims. Instead they field their own collection administration, which is part of the responsibility of the Department of Collections.

Both formal and agricultural lending institutions use the personal identification card (Cédula de Vecindad) as the only document to establish the client's identity, cross-checking the information on the card and the client's name.

There seem to be no absolute limits on either mortgage or fiduciary loan amounts; rather, banks decide whether to lend any given amount based on their evaluation of the borrower's repayment history and capacity for repayment.

If a loan goes into arrears, banks often employ a two-part strategy. First they try to reach an agreement with the client by altering interest rates or payment schedules to achieve repayment over a longer period. If this is ineffective, the bank is forced to turn the account over to their collection division, which may pursue legal action.

The formal sector does provide some loans to agricultural producers, but generally only to large scale producers of traditional products such as sugar, cardamom, or coffee. Since the prices of some commodities have dropped over the past few years, banks have decreased their agricultural lending.

Market interest rates vary by borrower. Mortgage rates can range from 15-19%, while fiduciary loans are usually about 20 to 25%.

In interviews, banks indicated that there are no legal restrictions on the establishment of new bank agencies or the closing of existing firms or branches. Decisions about opening or closing branches are made by bank executives based on their assessment of the profitability of such policies.

In an interview with the Director of the Bank of Guatemala's Department of Studies, it was confirmed that there is no law dictating the opening or closing of branches of the National Bank System. Such decisions are up to each bank, except when financial problems force a closure.

Specific Experience of the Coffee Bank, S.A.

As to risk assessment, this institution has access to the Bureau of the Bank Association of Guatemala, TRANSUNIÓN and Public Information (DIGIDATA, S.A.), and, since 2002, CREDIREF reports, which investigate references. Besides that, the Bank has an internal “Do not loan” list of bad credit risks. Potential borrowers’ references are investigated in each of these databases, and based on these an assessment is made as to whether the applicant qualifies or not. If the prospective borrower does not qualify, an attempt is made to identify the reason for disqualification, and based on this additional information the application is re-evaluated. Rejection generally occurs only if the client has credit with another institution, was previously more than 30 days late in making a payment, or has other bad references reported by one of the services referenced above.

As far as micro- and small enterprise, the Bank generally does not make loans in the agricultural sector but they will support farmers raising cattle, pigs, and birds. This is because crops are too risky; to support raising crops would require some type of insurance to cover crop failures.

As a formal sector bank they work with some borrowers who have “graduated” from microfinance or agricultural sector institutions, based on a database constructed from the bank’s experience operating as a communal bank, during which it worked with clients unable to obtain formal sector loans. These clients did well enough with their loans that they were transferred to the formal sector individual loans. There is also a group of clients who came from NGOs and established savings accounts with BANCAFE. (Until 1999, BANCAFE assisted some MFI’s, providing savings accounts for their clients, and some of these clients continue to be serviced by the bank.)

Jointly with the Rotary Club, BANCAFE helps finance microcredit programs for communal banks, which are only offered to women. Twenty five communal banks have been created, serving approximately 6,500 clients. These banks can only lend up to Q 800.00, and if a group requires more the parent bank (i.e. BANCAFE) can provide assistance by opening them a credit line and eventually graduating them to individual direct loans.

Additionally, agricultural sector lenders are in the process of identifying other microfinance organizations willing to carry out alliances similar to that of the Rotary Club.

RESULTS OF AGRICULTURAL SECTOR INTERVIEWS

Although the terms of Reference require of the identification of three entities dedicated to making loans to the agricultural sector, in Guatemala there are only two institutions that focus their lending in this sector. These are the Bank of Rural Development, S. A. -BANRURAL - and Agromercantil Bank, S. A.

For this sector, just as in the formal sector, it is important to evaluate the commercial references of clients applying for credit. These banks consult the following credit bureaus: the Bank Association, Public Information (DIGIDATA, CORP.) and TRANSUNIÓN. The only credit bureau BANRURAL consults is CREDIREF, though CREDIREF does not have nationwide coverage. BANRURAL is also a member of and makes use of the West Central Credit Risk Station. It should be noted that BANRURAL's West Regional Director is a member of the Executive board of this Central Credit Risk station.

These lenders are not legally required to, and have not historically, forgiven debts in case of natural disaster or crop failure, but they have been willing to adjust loan conditions to allow clients to pay the debt under improved conditions. They don't have a policy of granting credit to clients working for wages but support "productive activities" (i.e. agriculture), such that the pending crop guarantees the payment of the debt.

This sector recruits clients by traditional means, either waiting to be approached by prospective borrowers or employing advisors or bank executives to more actively recruit borrowers. Client identity is established through use of personal identification, or in some cases simply via the complete name of the user or the Number of Tributary Identification -NIT -.

If a borrower falls behind in his/her payments, the administrative collection contacts the borrower to discuss conditions for repayment. If no agreement can be made, the bank will

resort to legal action. There have been cases in which the banks have been forced to foreclose on mortgaged lands due to the borrowers' failure to pay their loans, usually in the cases of the cultivation of coffee.

Supported agricultural production includes cash crops like sugar, cardamom, coffee but only with specific clients. Recently, products like banana, melon, and some vegetables are also receiving financing. Non traditional products as Chinese peas, string beans, raspberries, zucchini, and brocolli have also been granted loans in cases where borrowers can offer a guarantee or refund of the loan, commonly through farmers' associations that market their products abroad.

Representatives of the agricultural sector indicated that they ignore laws restricting them from opening or closing branches.

RESULTS OF FORMAL SECTOR FOCUS GROUPS

INTERVIEWS WITH SMALL BUSINESS OWNERS

Small business owners in a variety of industries were interviewed, including mechanics, a maker of garment labels, a uniform supplier, a manufacturer of embroidery for small ready-made clothiers, a printer, and a leather goods importer. Some said that they began their company with their own resources; others relied upon loans from family and friends. Later, the businesses obtained loans from microfinance institutions, including Genesis Empresarial, FUNDEMIX, Fe y Alegrias and ACT.

These loans were granted quickly and without many requirements. These businesses were expanding and needed machinery and raw material to support their growth. Eventually their needs were larger than could be met by MFIs, so they moved on to banks, who provided not only loans in larger amounts but also at lower rates and over longer terms. Banks made many requirements, however, including the filing of complicated paperwork, for which the

entrepreneurs were forced to turn to third parties. Banks providing loans to these businesses include: BANRURAL, Agromercantil Bank, Industrial Bank and FIGSA. One interviewee noted that the bank he started out with increased its interest rates repeatedly, moving from 16 up to 25%, at which point he transferred the debt to another bank that at the moment charges him 16%. All loans were on an individual basis, so the interviewees were unable to make any comparisons with solidarity group loans.

All the interviewees indicated that they had come to the banks asking for the loans rather than being solicited for them by bank officials.

UNION OF SMALL READY-MADE CLOTHIERS

The group began acquiring credit as a solidarity group in Genesis Empresarial and began with a credit of Q.5,000.00 for each member. Over time they have increased their credit limits, which in some cases are up to Q.150,000.00 as individual credit. They have recently opened a credit line through the Credit Card BI-CLUB of the Industrial Bank, with the help of the Chamber of Industry of Guatemala with which they are affiliated. This credit line is used to purchase raw material when there are emergencies and they try to always pay off the loan as quickly as possible in order to maintain availability of the balance in case of need. The maximum credit that they can borrow on the card is Q. 75,000.00. Also they have open credit with the warehouses that sell them raw materials, and the company that sells them machinery provides them with financing. They believe that these opportunities for financing have allowed them to expand their business and improve their operations.

As to individual versus group loans, they prefer the individual. Individual credit makes them individually responsible for the payment of their debt and since they know they are personally responsible, they become more careful administrators of their commitment. When loans are made on a group basis, a late payment by any member harms the credit record of the entire group.

They agree that it is easier to obtain financing through an NGO than it is through the bank system, though the interest rates are more advantageous in the formal sector than in the NGOs. This has motivated some to seek funding in the formal sector. They mentioned also that a benefit of the MFI's is the ability to apply directly without registering with a credit agency.

- **ENTREPRENEURS THAT PERSISTED IN AN MFI RATHER THAN MOVING TO THE FORMAL FINANCIAL SECTOR**

These entrepreneurs enjoyed the flexibility and opportunity for access to increasing levels of funding offered by the MFI's. They preferred the opportunity to develop good credit without having to put up collateral. Loan amounts have increased from Q3,000 to Q.200,000 over time, with interest rates of 18% to 20%. The managers are faithful to the institution for the support that it has provided them over the years.

Another reason for remaining with the MFI is that they have developed an affinity for the institution, having been provided with training and technical assistance. Further, the quickest solution to financial difficulties is to go to the MFI's.

RESULTS OF AGRICULTURAL SECTOR FOCUS GROUPS

- **CEMUSDA ASSOCIATION / SUMPANGO**

The members of this Association have obtained credit from different entities including the Cooperative ECOSABA, through NGOs such as ACT, and from larger banks like BANRURAL which require collateral. They indicated that at first they were nervous about putting their land up as collateral, but were eventually able to pay off their loans. They indicated that ECOSABA requires repayment of capital and monthly interest. ACT requires repayment within one year but also offers technical consultation and training.

In case of natural disaster or crop failure the borrowers cannot cancel the loan, as lenders don't forgive them their debts but they are forced to continue paying back the credit. The cooperative

ECOSABA, though, has credit insurance such that the client must pay a monthly portion of the balance owed; in other words, they have less an insurance policy than an opportunity for flexible accounting.

ACT offers a type of credit insurance such that if the main debtor dies, the insurance covers the balance of the owed capital.

Some members of the Association have had to borrow from other revenue streams to pay agricultural debts, in some cases selling part of their land to make payments.

When asked what improvements they would like to see in terms of credit, participants in the focus group indicated that they would prefer more flexibility in the timing of payments, lower interest rates, and loan insurance. They like the fact that being punctual in making payments has allowed them to create a good credit record that gives them access to obtain more financing in the same institution.

CEMUSDA itself grants credit at a monthly interest rate of 2.5%, but they set a lower rate for community development projects. The association also supports its partners with agricultural and social technical consultation.

Members of the focus group said that the agricultural sector peaked in the 1980's, in which non-traditional exports displaced traditional products such as the tomato and chili pepper, leading to price increases in the latter goods.

Guatemalan products cannot compete with Mexican products in prices, since the Mexicans use chemical inputs and produce tomatos more cheaply. The Mexicans can send trucks of their tomatos to the market driving out the Guatemalan product, which has led the Guatemalans to export their tomatos to El Salvador.

About 70% of the produce in El Salvador is imported from Guatemala, although regrettably the Salvadoran Government established a tariff on the Guatemalan produce, which hurt the Guatemalan farmers.

In the 1980s farmers made a lot of money and acquired more land, goods, houses, and vehicles, but today they are being forced to sell off some of these assets. As a response they began to group in associations and look for ways to assure themselves a minimum level of income to keep their businesses operating.

To this end CEMUSDA created the Fund of Socioeconomic Integration, whereby the farmer acquires the habit of saving. This Fund has several advantages, including the saving but also crop insurance in the event of natural disasters and protection from price volatility. They pay 10 cents per pound of the exported product, which is returned to them 6 months later. This is a pilot program that was implemented for 2003 and they are confident that it will work. The Program of Alimentary Security works production costs against sale prices, seeking ways to guarantee farmers a positive return and hence a secure income through crop insurance, yearly prices, or surpluses, depending on annual production and total savings.

- **ACT's ENTREPREUNERS**

The Association of Technical Cooperation -ACT - grants credit for business, agriculture, housing and communal goods through the provision of large grants with a low interest rate. The mission of this Association is to support the improvement of the small farmer's socioeconomic situation, as well as that of the micro and small entrepreneurs in Guatemala, through providing high quality financial services adapted to the necessities of the sector.

To check on ACT's progress, clients were interviewed who indicated that ACT grants are preferable to mortgaging their land or the use of other institutions like BANRURAL.

In case of crop failure or failed experimentation, contracted debts have not been entirely forgiven but terms of repayment have been modified such that they could always fulfill the required commitment after renegotiation. Since farmers have other revenue streams such as income from raising animals, they will have other means for repayment.

Several of the members of ACT indicated that they have obtained more than one loan with this institution due to the relative ease of application and speed of processing. They said that the

amounts of their loans have been up to Q.10,000.00. Apparently it is possible to obtain up to Q.100,000.00 by starting with two loans of less than Q.10,000.00 and working to establish credit through timely payments. Some clients have obtained even larger amounts by developing a longer credit history and staying with the institution for five years or more. (Such loan amounts require the posting of land as collateral.) ACT offers several types of loan durations, including two months, six months and one year. When ACT began the maximum loans were for Q.25,000.00 but over time they have increased the maximum for established borrowers to Q.200,000.00.

Large borrowers approaching ACT's maximum amount are also eligible for loans through the formal sector, but sometimes choose ACT because of ACT's service or for the access to training and consultation provided by ACT. ACT prefers not to lend such high amounts, but feels an obligation to support its long term clients in spite of the fact that its primary mission is to assist micro and small enterprises. ACT encourages such large borrowers to seek formal sector loans, and offers support services so clients can get through the process of borrowing from such institutions. Some clients have requested that ACT notify the formal sector lending institutions that the required amounts cannot be provided by ACT.

In the agricultural area the largest amounts that have been granted for mortgages are Q.80,000.00 to Q.100,000.00. Different terms have been granted for different types of production. This institution at the moment doesn't grant separate loans to two members of the same family because of the risk that both might fall behind in payments. ACT also doesn't grant credit to people over 60, since their insurance doesn't cover that age range. The insurance in question covers borrowers who die while in the process of repayment, and the fee for it is 2%. If a client dies, the family brings the death certificate to ACT, and the remaining balance is taken care of. If a borrower has an established history with ACT and reaches the age of 60, credit is granted to a relative.

ACT does not provide crop insurance, and in case of crop failure they generally will not forgive loans but will renegotiate the terms. In a few cases they have forgiven part of the debt when the impossibility of repayment is demonstrated.

The monthly interest rate is 2.5% on smaller balances and it diminishes in the case of housing loans to 2.2%. In addition ACT charges an administrative handling fee of Q.75.00. ACT is affiliated with CREDIREF, which allows them to verify the references of its users. In the case of collateral loans they also carry out field supervisions before granting credit for agricultural, industrial, or trade activity.

INTERVIEWS WITH MICROFINANCE INSTITUTIONS

INTERVIEWS WITH MICROFINANCE INSTITUTIONS			
MICROFINANCIAL INSTITUTION	MAXIMUM AMOUNT LENT	RATE OF INTEREST	ALLIANCE WITH BANK SYSTEM
GENESIS EMPRESARIAL	Microenterprise Q.25,000 Small Enterprise Q.150,000	30% flat rate up to Q.15,000 Over Q.15.001, 30% on balances	Not allied with any formal financial institution, but if a client goes through the Genesis system of increasing loan amounts and establishes a good credit history but needs more than Genesis can offer, the MFI will assist the client to obtain a larger loan from a formal banking institution
ACT	Up to Q.200,000. 25% of the credits are agricultural.	25% on balances for productive activities and 24% for housing	They advise entrepreneurs to take out loans from some bank, but if for some reason the entrepreneur doesn't want to leave ACT they are sometimes able to increase the amount they offer. They don't have an alliance with any bank.
FUNDESPE	Q. 100,000	26% on balances	They don't have any type of alliance with the formal financial system.
CDRO	Q. 15,000	36% on balances	They don't have any type of alliance with the formal financial system, only with BANRURAL for clients' savings accounts.
FE Y ALEGÍA	Q. 60,000	18% for mortgages, 30% on fiduciary and solidarity group loans	FEY ALEGIA has no alliance with a formal sector institution. If entrepreneurs require amounts over Q.60,000, they are encouraged to seek funding elsewhere, but if they don't want to leave the program, they will allow repeat loans at Q 60,000, and in the case of clients with particularly lengthy credit histories with FEY ALEGIA, sometimes credit ceilings are expanded to Q.75,000.

INTERVIEWS WITH MICROFINANCE INSTITUTIONS			
MICROFINANCIAL INSTITUTION	MAXIMUM AMOUNT LENT	RATE OF INTEREST	ALLIANCE WITH BANK SYSTEM
MENTORESEMPRESARIALES	Q. 200,000	Mortgages: 19%	MENTORES EMPRESARIALES made alliances in the past with Genesis Empresarial and Banrural, but they discontinued these alliances due to some bad experience, and decided instead to raise credit ceilings for their “graduates.”
AYNLA	Communal Banks’ partner loans: Q.3,000, Solidarity Groups Q.75,000 per member, Mortgages: Q.250,000	32% for Communal Banks 26% for Solidarity Groups and mortgages	AYNLA is not interested in such alliances. They believe that trying to help their clients get formal sector loans helps neither them nor their clients, as the formal sector does not acknowledge input from MFI’s
ASIDE	Q.150,000	22%	They have no interest in such alliances. Clients interested in pursuing higher amounts are encouraged to leave the institution and apply with a bank.
AGUDEZA	Communal banks: Q.4,000 per member, Solidarity groups: Q.15,000 per member, Individual Q.40,000. (26% of borrowers are agricultural.)	30%	AGUDEZA has no alliance with any particular formal sector institution, but clients seeking higher amounts will be given recommendations about which bank to proceed with. The final decision about whether to move on and if so, where to go, is up to the client.
ASDESARROLLO	Individual loans, starting at Q.7,000, reach a maximum at Q.100,000, but clients may be allowed to borrow Q.150,000	Loans for trade businesses: 30% Other productive activities: 26%	They neither have nor desire such an alliance. They support clients who have come up through their program, supporting them with larger amounts if necessary. They don't give loans to small entrepreneurs that have not begun with ASDESARROLLO.

INTERVIEWS WITH MICROFINANCE INSTITUTIONS			
MICROFINANCIAL INSTITUTION	MAXIMUM AMOUNT LENT	RATE OF INTEREST	ALLIANCE WITH BANK SYSTEM
FUNDAMUJER	Solidarity groups Q.10,000 per member; Individuals Q.30,000	30% on fiduciary loans and 28% on mortgages/ collateral-based loans.	They are allied with BANCAFE, although this alliance has not been very productive since FUNDA MUJER only gives financing, and the clients require training, accompaniment and technical attendance to develop investment plans and fill out forms.
ASPECAGUA	Only working at the moment with 20 groups of coffee producers, they don't have a set maximum grant, but adapt to the client's needs.	24% on balances	ASPECAGUA is not interested in such an alliance. The clients don't want to deal with the formal financial sector's many requirements, and are very happy borrowing with the association.
PAFMAYA/IDEMAYA	Q.50,000	31 % on balances.	They have formed a Fideicommissum with Banrural such that PARMAYA approves the credit and the bank provides the loan. However, there is no mechanism through which PARMAYA assists clients with applying for larger loans

NATURAL EXPERIMENTS

CREDIT REFERENCES CORPORATION - CREDIREF

The Guatemalan ministry of the economy, the AGIL program of USAID (the United States Agency for International Development) and the German cooperative PROMOCAP/GTZ laid the foundations for CREDIREF, and the founding institutions, the Coffee Bank, S. A., Bank of Rural Development, S. A., and the Net of Microfinance Institutions of Guatemala, REDIMIF, signed the founding documents on February 21, 2002. In June of the 2002 the Confederation of Cooperative of Guatemala -CONFECOOP – joined the partnership. CREDIREF has grown from the four founding institutions to 397 MFI's, two banks, twenty associations and foundations of the REDIMIF and 375 cooperatives of the 9 federations of the CONFECOOP.

On May 5, 2002, CREDIREF was formally added to the General Mercantile Registration of the Republic of Guatemala, and in September of the same year CREDIREF began operations, officially being launched in October, 2002.

CREDIREF is a shareholder owned corporation with its own capital. It supports all three microfinance sectors with a modern and efficient system that offers nationwide coverage and is accessible over the internet.

The main objectives of this Corporation are the following:

- To provide information on borrowers to the institution partners of the Corporation so as to reduce risks and uncertainty faced by lenders, and to speed up MFIs' lending operations.
- To carry out and document more complete credit analysis, including information on borrowers' late payments as well as their overall financial situations

- To contribute to the stability of the microcredit industry by means of the delivery of excellent information, reducing the bad debt burden of MFIs

By January of 2003, this Corporation had added six affiliated institutions including BANRURAL, BANCAFE, GENESIS EMPRESARIAL, MENTORES EMPRESARIALES, FUNDEMIX and FAFIDESS. Altogether CREDIREF's institutions had made 58,578 loans, had 105,818 direct debtors, and another 53,405 contingent debtors for a total affected population of 123,510. In addition, 9,761 consultations have been held.

BANCARED oversees administration of the database, which classifies clients into three types of credit-worthiness: doubtful, effective, and retired. Information is only given regarding clients directly referred.

The information is updated weekly, and records are kept for 12 months. Consultations are carried out via Internet from the point of service. Entry to the database requires a series of access keys, restricting access to authorized users: indications are that system security is rigorous and totally reliable.

CREDIREF determined that it should support both national and international MFIs by providing an information database for consultation on credit risks and timely repayment. The institutions affiliated with REDIMIF share their credit information and make consultations through the network. In addition, five other institutions consult the CREDIREF database but are unable to add their client information to the database due to a lack of the appropriate software. By date of entry to network, they are:

- FE Y ALEGRIA
- ACT
- CRISOL

(all three of which entered in the March of 2003)

- FAPE
- FUNDESPE

(which entered in the April, 2003)

SHARE DE GUATEMALA is also expected to join soon.

CREDIREF has sent them tools to incorporate the software, and is in the process of hiring a systems engineer to support the MFIs in becoming full members of the network.

On examining several MFI's, CREDIREF found that most still track clients using the program EXCEL, while only five use the System 100 that is compatible with CREDIREF's system. On October 2, 2003 a meeting is scheduled for the REDIMIF-affiliated MFI's that are not full members of CREDIREF to encourage them to update their systems and thereby share their credit information, which will benefit all network users.

CREDIREF has also met with the Coordinator of the West Central Credit Risk Station, to discuss sharing information. The latter will make an evaluation of the operative and administrative costs of integrating systems, and based on this evaluation CREDIREF will present a proposal for combining databases, which will be to mutual advantage.

However, since 50% of the Coordinator's information belongs to BANRURAL and another 6 thousand clients or so are ACT's, CREDIREF is not certain that this information sharing will be helpful.

CREDIREF, financed by PROMOCAP/GTZ and the Program BID/MINECO, is in the process of creating a consultancy to develop a business plan.

- **INTERVIEW WITH THE CHAIRMAN OF CREDIREF / EDGAR BÚCARO**

According to Mr. Bucaro, the main concern of the Corporation has been the creation of one central unified database containing information from all partners of CREDIREF, specifically REDIMIF and CONFECOOP. However, integration of REDIMIF's database has been slow, and the main obstacle to integration with the Corporation has been a lack of compatibility between the systems of the institutions comprising REDIMIF. CREDIREF has lent support to

the institutions to help with the process of systematizing, as has REDIMIF itself. Also, to encourage rapid integration, contracts with member institutions include a clause through which the member institutions are forced to submit their information for inclusion in the CREDIREF database. All members of REDIMIF are expected to be completely incorporated in CREDIREF in the next two months.

There are also political problems with the integration, as some institutions are wary that giving up sovereignty over their own information opens up the possibility that the information might be misused. To assuage these fears, CREDIREF is sending representatives to meet personally with Managers and the Executive boards of the MFIs to build confidence in CREDIREF.

CREDIREF also plans to meet with West and North Central Credit Risk Stations as well as the Ministry of Economy to try to increase awareness of their mission and reassure them that they share information with the only objective of reducing risk in their own credit portfolios.

- **INTERVIEW WITH THE REPRESENTATIVE OF CONFECOOP AT BOARD OF ADMINISTRATION OF CREDIREF / LIC. JULIO CONTRERAS.**

Mr. Contreras commented that cooperatives affiliated with CONFECOOP have given the following reasons for not transferring their information to the central database and for not consulting CREDIREF.

1. The cooperatives distrust CREDIREF and are simply uncomfortable with sharing their databases.
2. The cooperatives are afraid that the information they provide will be misused. (They need to be convinced to trust CREDIREF and share their information.)
3. There are some technical barriers to sharing their information.
4. They have had difficulties finding computer science professional to support them.

5. CREDIREF should help motivate the institutions to share their information.

He maintains that CONFECOOP will be ready to enter CREDIREF by January 2, 2004.

WEST CENTRAL CREDIT RISK STATION

The West Central Credit Risk Station is an institutional coordination program in Guatemala in charge of processing information on MFI users' credit records, including the status of current loans. When a borrower's profile is checked it declares her either "solvent" or worthy of credit, or "insolvent."

The station was created in 1996 after many attempts to share information by exchanging users' listings and credit information among the biggest organizations. After a few less successful attempts to share information, the MFI's decided to create a central station in charge of compiling borrower information.

In 1999 overcoming some mutual mistrust between the institutions and gathering donations for furniture, equipment, and software to set up an office, the station was founded. Its objectives are:

GENERAL OBJECTIVES

- a) To reduce defaults in the affiliated institutions to the Program
- b) To increase financial security and improve lending outcomes

SPECIFIC OBJECTIVES

- a) To enhance financial stability and coordination between MFIs, to insure the continuity of funds to make loans

- b) To avoid “double dipping,” borrowers taking loans from multiple institutions beyond their ability to repay
- c) To select credit-worthy potential borrowers from the pool of applicants
- d) To make available information on borrowers’ credit records with all organizations.

As of March 2002 the station had been asked for 2,840 reports on clients of which 24% had credit records. Of these 82% were dependable borrowers and 19% doubtful users in other organizations.

There are offices in Solola that cover the departments of Chimaltenango and the Capital City, an office in Quiché, in San Cristobal (in the department of Totonicapan) covering Totonicapan and Quetzaltenango; and they are opening three additional offices in the north and west of the Republic in the departments of Alta Verapaz (Cobán), Huehuetenango and in the Municipality of Nebaj of the Department of Quiché. A map is attached.

Overall information about the portfolio is given to the Executive Board but specific client Information remains confidential. In cases where it is necessary to access specific listings, the only group with access are Central Station employees.

Currently they have a database of 60,000 users, 10% of which are doubtful clients, and this is updated at least every other day. Updates made to the database are sent to the different offices of the Central station by fax. Affiliated institutions have the obligation to update the database within 30 days. Updates are submitted in electronic form (diskette).

The statement of solvency granted by the central station is not a direct grant of credit but rather one prerequisite of a client’s obtaining funding at some institutions. The central station hopes to integrate many small commercial lenders currently handling a lot of microcredit independently of the station, since including information from such small firms would greatly enhance their database. The manager of the Central Station says that affiliated institutions have reduced their default rate by 50%, from 13% to 6%, which is an encouraging sign.

The Manager of the Central Risk Station has compared notes with the CREDIREF, but as the latter is a for-profit organization many smaller groups will not be able to participate. The Station is a non-profit organization, designed to support all the institutions regardless of their portfolio volume.

They are working on improving client institutions' access to their information by creating a web page. The Central station is consulted approximately 100 times each day, and they hope to be available for nearly 100% of inquiries.

Today they serve at least a hundred affiliated MFIs, including AYNLA, ACT, FAFIDESS, AGUDESA, FUNDESPE, ADEPH, cooperatives like COOPERATIVE COOLHUA, CHUIMEQUENÁ AND ARGUETA and the formal bank BANRURAL. The manager of the West region is a member of the Executive board, and a future goal is to make contact with Fenacoac and the credit agencies of the other banks in the region to try to integrate them into this Central station. Utilizing one such service is not mutually exclusive with others. The affiliated organizations have divided their portfolios into 4 areas: microentrepreneurial, agricultural, housing, and communal banks, including group savings and credit plans.

The resources that this station generates will be used to strengthen the organization, to open more offices, to train the members of the affiliated entities, for needed programs to strengthen affiliated institutions, advertising, computer software, creation of the web page, and for station representatives. These representatives work with lending institutions to improve lending strategies and build lender- Station rapport.

There are about 2,000 MFI's, as many formal as informal, mostly concentrated in the west of Guatemala (due in part to Guatemala's history of armed conflict).

The manager emphasizes that the purpose of this organization is not to benefit some specific people or institutions but to strengthen the MFI's and promote their advancement. It also strives to promote collegiality between lending institutions.

The Executive Board is chosen through a General Assembly. Elections occur in local assemblies, naming officers to committees and to the General Assembly, from which

members of the Executive Board are chosen. The Executive board meets monthly and the Regional Committees every two months.

OTHER CREDIT BUREAUS

- **BANCARED**

Ten formal sector banks came together to create the ATM Cost Center and again joined forces to form BANCARED. BANCARED soon came to administer the database of all members' credit portfolios. Eventually it became a credit bureau, consulted by these banks to verify clients' payments. BANCARED was created in 1996 and in 1998 the Bank Association of Guatemala (ABG) automated the information. Since then BANCARED has functioned as a partner of the ABG, in order to automate the banking system. BANCARED's business is not to sell information but rather to provide technical support in portfolio management. It has a contractual obligation not to transfer information to non-affiliated clients.

BANCARED continues to provide technical support. It is contracted with CREDIREF AND ABG, but does not have a database open to the public.

- **TRANS UNIÓN**

TRANS UNIÓN belongs to the Marmon Group with headquarters in Chicago, and began operations in 1968. It is a world leading corporation in:

- Administration of credit information
- Risk Analysis
- Acquisition of new clients
- Limiting losses
- Maximizing Profitability, and

- Fraud Control

It is active in the USA, Canada, Mexico, Costa Rica, Peru, Chile, Puerto Rico, Spain, India, South America, Kenya, Hong Kong, El Salvador, Honduras and Guatemala. It has strategic alliances with Dun & Bradstreet in Dominican Republic, Colombia, Korea, Israel, Australia and Italy.

It began operations two years ago in Guatemala. TRANS UNION is in the process of establishing the first Central America-wide Central Risk station, partnering with the World Bank through the IFC. They are currently active in all Central American countries but Nicaragua.

In Guatemala they have focused on:

1. Defining strategic partners. Currently these partners are the Bank Association of Guatemala -ABG - and The Chismógrafo. The Chismógrafo was founded in 1989 and it is a repository of court records dating back to 1991. They have developed a strong relationship with the Bank Association of Guatemala.
2. To get familiar with the systems of personal identification in the different municipalities of the departments of Guatemala.
3. To improve attitudes toward a Central Risk station

TRANS UNION builds databases on a private contractual level. Its credibility is enhanced by the fact that it is a multinational corporation.

Its main objective is to incorporate all banking sectors in a national system, including the Bank Association of Guatemala, CREDIREF, and other central stations of risk.

- **DIGIDATA, S.A.**

DIGIDATA is a credit bureau using the database and personnel of the old INFORNET. It is also known as “Public Information.”

DIGIDATA, S.A. is a credit agency with a database composed from the submissions of mercantile societies and individual merchants and also including court records. They charge a US\$40 monthly fee to allow banks, credit-granting institutions, and individuals to consult DIGIDATA up to 30 times per month, or more for an additional service fee.

- **THE BANK ASSOCIATION OF GUATEMALA**

Currently the ABG has a contract with BANCARED who offers them technical support and administers their database. They are negotiating an agreement with TRANS UNIÓN to include more services, and 96% of the Bank System has already transferred its database there. (Only two of the smallest banks have not yet transferred their information.)

- **THE SUPERINTENDENT OF BANKS**

The SIB is the internal Central station of Risk that manages credit information for the Bank System. Under some new regulations promulgated by the SIB's Department of Risk Evaluation, microcredit will be included in an information-sharing regime. The new regulations are expected to be approved in September and to go into effect in January of the year 2004.

It is unlikely that the SIB will make an alliance or share information with CREDIREF in the near future, since the law specifies that they can only share information between banks. The legal standing of CREDIREF is expected to change, however, by article 58 of the Bank and Financial Laws which says:

“ARTICLE 58. System of Credit Risk Information: The Superintendent of Banks will implement a system of credit risk information, to which the participating entities shall be obliged to provide relevant information. Banks, financial groups, and other entities of financial intermediation approved by the Monetary Board of the SIB will have access exclusively for credit analysis.

The Bank Association of Guatemala tried to form an alliance with the Superintendent of Banks, both since the ABG wanted the legal support of the SIB and because the SIB seems to be more efficient, but the alliance was not formed.

MONEYLENDING INSTITUTIONS	NATIONAL INSTITUTIONS	URBAN AREA INSTITUTIONS	RURAL AREA INSTITUTIONS
INTERNATIONAL BANKS	International Bank	International Bank	
GOVERNMENT BANKS			
AGRICULTURAL MONEYLENDERS	Banrural S. A.	Agromercantil Bank S. A. / Banrural S. A.	Banrural S. A.
FORMAL COMMERCIAL MONEYLENDERS	The Coffee Bank S. A. Industrial bank	The Coffee Bank S. A. Industrial Bank Bancasol	The Coffee Bank S. A.
MICROFINANCE FORMAL INSTITUTIONS		Génesis Empresarial ACT FUNDESPE	Génesis Empresarial ACT FUNDESPE
NGO/ SMALL MFI		FE Y ALEGRIA MENTORES EMPRESARIALES AYNLA ASDESARROLLO	CDRO FE Y ALEGRIA MENTORES EMPRESARIALES AYNLA ASDESARROLLO

CREDIT AGENCIES			
GOVERNMENTAL CREDIT AGENCIES	Ministry of agriculture FIS		Ministry of agriculture FIS President's Program Wife's
INTERNATIONAL CREDIT AGENCIES	World Bank AID BID BCIE AECI	World Bank AID BID BCIE ASDI AECI	World Bank AID BID BCIE ASDI AECI INTERVIDA
FORMAL SECTOR CA'S			
MFI/NGO CA'S			

CONCLUSIONS

Formal sector lenders

- Formal lenders do not recruit clients of the Microfinance Institutions. Formal lenders have their own policies and requirements.
- Formal lenders do not use credit agencies, offering loans through their own business promoters who visit the managers to solicit business.
- The lenders choose whether or not to grant credit based on: credit record, credit standing, financial situation, payment capacity and level of indebtedness. They don't consider whether potential borrowers had a good credit record with an MFI.

- Client identity is established through personal ID and corroborated by the Number of Tributary Identification (NIT).
- The size of the requested credit is what moves borrowers from MFIs to the formal sector.
- Formal lenders require guarantees or collateral.

Agricultural Lenders

- Like formal sector lenders, agricultural lenders take into account commercial references as well as the credit of clients requesting financing.
- Agricultural lenders do not use credit agencies, but offer loans through their own credit promoters or to borrowers approaching them.
- When payments are in arrears, the bank verifies the cause. They will not forgive the loans but will renegotiate terms of payment if the client's credit record is good.
- Banks do not make lending decisions based solely on whether clients are earning wages as opposed to being in a microenterprise, but base lending decisions on clients' ability to repay.
- Agricultural lenders require personal identification, and in particular the "Cédula de Vecindad."
- In case of default, agricultural lenders seek to renegotiate terms of payment, but if this does not work, they take legal action. In some cases the bank is forced to repossess the client's property.

Formal Sector Focus Groups

- The advantages of taking out individual loans as opposed to group borrowing from MFI's are that being personally accountable makes people be better administrators of their commitments.
- Borrowers were forced to go to the formal sector lenders for the amount of credit that they required, as the MFI that assisted them previously could not give them very high loans.
- The industrial businesses grew with access to large formal sector loans, which they used to buy large volumes of raw materials.
- Members have only worked with small lenders, they have not borrowed from different institutions.
- Members have not had contact with any Credit Agency, but rather have had direct contact with lenders.

Agricultural Lenders' Focus Groups

- Borrowers have had to put up their land as collateral.
- Borrowers were initially nervous about putting up their land, but they didn't have a choice if they wanted to get loans.
- In the case of natural disaster if borrowers are unable to pay their debts the lender doesn't forgive the debt, and some have had to sell part of their land to pay the loan.
- In the case of crop failure, clients have to search for alternate means of repayment, and they usually don't carry out any extra business, but instead raise more animals for sale to cover the debt.
- The most useful reformation in the loan contract is the provision of insurance to cover cases of crop failure or death of the borrower.

Central Risk Stations or Credit Bureaus

- The Bureaus of Credit that lend information to the public are: TRANS UNIÓN DIGIDATA, S. A., CREDIREF and the COORDINADORA DE OCCIDENTE (West Central Risk Station).
- Lack of integration of institutions such as banks, cooperatives, and commercial lenders into the Credit References Corporation (CREDIREF) is a concern
- CREDIREF does not educate institutions about the importance of consulting a client's references before authorizing a loan.
- A short term goal is to facilitate an alliance between the Credit References Corporation - CREDIREF - and the West Central Risk Station, which would create a database of approximately 150,000 clients.
- It would be useful to include the information of the West Central Credit Risk Station in the database of CREDIREF and then to make an alliance with the Bank Association of Guatemala, or with TRANS UNIÓN, which will administer ABG's information. Also, TRANS UNIÓN has contracts with other commercial companies, so an even larger database could be created.

BOLIVIA

Credit Information Reporting in Bolivia

by

Rémy N. Kormos

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Executive Summary

This country case study provides an overview of the context, regulatory framework and key issues for credit information reporting in Bolivia, with a focus on formal and informal microfinance institutions.

After describing the formal financial industry and the NGO microfinance sectors (Sections 2 and 3) and the applicable regulatory frameworks, Section 4 of the case study focuses on the major developments in microfinance in Bolivia over the last ten years, including the commercialization of microfinance institutions (MFIs), the entry of new commercial lenders (including consumer credit) into the traditional microfinance field, and the saturation of the market and over-indebtedness crisis which hit the microfinance sector during 1998-2001, after a decade of spectacular growth.

Section 5 provides a detailed analysis of the legal and regulatory framework for credit reporting in Bolivia, including the state-run central credit registry, the new regulations for private credit bureaus introduced during 2000-2003, and existing informal credit bureaus, black lists and information vendors. A new credit bureau (FINRURAL) established to exchange information between the central credit registry and informal MFIs is examined.

The research undertaken for this study indicates that during the years leading up to the microfinance over-indebtedness crisis of 1998-2001, the central credit registry had incomplete coverage, and a large percentage (as high as 56% in 1998-1999, depending on how the microfinance sector is defined) of microfinance clients did not appear in the registry. Indeed, the central registry (which was only accessible to the formal sector) did not cover the clients of informal microfinance NGOs. As a result, when commercial lenders started targeting the microfinance market in the late 1990s, large numbers of individuals and small firms were able to obtain more than one loan, in part because their names did not appear in the central credit registry. Other factors contributed to the crisis, including the inappropriate use of consumer credit lending technologies and philosophies by some of the new commercial entrants to the microfinance sector, as well as an economic recession which hit Bolivia in 1999.

The regulatory responses to the crisis included new rules allowing private credit bureaus to operate (and share credit information with the central registry), and new regulations distinguishing consumer lending from microcredit.

This country case study concludes that Bolivia would be a good choice for further research on credit information reporting, and that there is a great deal of published material and data on the microfinance sector in Bolivia.

More specifically, there are several areas of credit information reporting in Bolivia identified in this study which lend themselves to further analysis and research. These include:

- (a) the microfinance crisis of 1998-2001 and the impact that incomplete credit bureau coverage had on this crisis of over-indebtedness;
- (b) the development and impact of the new private credit bureau regulations on credit information asymmetry in Bolivian microfinance;
- (c) possible contributions from the Bolivian experience on the debate on specialized vs. general credit bureaus, and private vs. central credit registries; and
- (d) an examination of use of credit reporting systems by urban vs. rural MFIs.

1. Introduction

This country case study was prepared pursuant to collaboration between the Department of Agricultural and Resource Economics of the University of California at Berkeley and the Food and Agriculture Organization of the United Nations, Office for Latin America.

With a view toward identifying future research opportunities in the area of credit information reporting in Bolivia, this paper provides (i) an overview of the formal financial sector and of the NGO sector, with a focus on microfinance institutions (MFIs) which are users or potential users of credit bureaus, (ii) an outline of the applicable regulatory and supervisory framework, institutions and recent developments, and (iii) a summary of the current state of credit information reporting in Bolivia, including both the central public credit bureaus and private credit bureaus. A detailed bibliography is also included.

This case study concludes that for a number of reasons, including recent developments in the regulatory framework, past events in the microfinance sector, and an extensive body of scholarly literature and case studies on microfinance, Bolivia would be an excellent subject for more in-depth research initiatives in the area of credit information reporting. Possible areas for further investigation are discussed in the final section.

1.1 Overview of the Formal and Informal Financial Sectors

Like most countries in the region, the Bolivian financial sector as a whole can be divided into formal and informal sectors. The term “formal” or “regulated” financial sector denotes domestic and foreign-based banks, private financial funds, and credit unions, all of which are required to be licensed and are regulated by the state. The formal sector includes commercial banks and non-bank financial service providers that offer a variety of microfinance products.

The “informal” or “unregulated” sector is comprised of non-profit organizations and NGOs providing microfinance products, typically to impoverished and rural clients. The informal sector is primarily donor-funded and non-commercial, and is not licensed or regulated by the state. The informal sector also includes a number of credit unions that have not applied for or not received their licenses but are operating. Table 1 below provides an overview of the formal and informal sectors, with a focus on microfinance institutions.

The distinction between the formal and informal sectors, in particular in microfinance, is very significant in Bolivia, since regulated microfinance institutions (MFIs) are required (from the moment they are licensed) to report information on their customers to the central credit bureau operated by the state (and to consult the credit bureau when evaluating a loan applicant)—while the informal MFIs are not required to do so.

1.2 Overview of Credit Information Reporting in Bolivia

Until recently, Bolivia only had one formal credit bureau, the State-run “Sistema de Central de Información de Riesgo Crediticio” (CIRC) at the Superintendence of Banks and Financial Entities. The CIRC only covers the formal sector (including some banks and private financial funds that offer microcredit loans) and their clients. Until very recently NGOs and other informal microfinance institutions have not shared their clients’ credit information with or had access to the CIRC database (Campion, 2001). Recent legislative changes have permitted the establishment of private credit bureaus and the sharing of information between these credit bureaus and the CIRC for microfinance and consumer credit, but credit information from unregulated lenders’ clients remains limited. In the past NGOs have instituted informal credit information sharing systems, including “black lists”, but these have been limited both geographically and in terms of the data collected. Foreign credit bureaus are yet to establish operations or invest in Bolivia, unlike the markets in other Latin American countries such as Peru and El Salvador (Luoto, 2003; Miller, M., 2003).

**Table 1: Overview of Formal and Informal Financial Sectors
in Bolivia, by Total Portfolio (*Cartera Vigente*)**

Type of Entity	Total Portfolio as of Dec. 1998 (USD)	Total Portfolio as of June 2001 (USD)
Commercial Banks	4,023,610,554	2,769,455,643
Total Formal MFIs (BancoSol + MFI FFPs)	132,252,099	159,187,900
BancoSol	70,720,936	60,057,926
Microfinance FFPs ²¹	61,531,163	99,129,975
Consumer Credit FFPs	109,088,924	19,619,894
Microfinance NGOs	37,663,787	53,206,523
Credit Unions (<i>Cooperativas</i>)	186,246,537	178,933,446

Source: González-Vega & Rodríguez-Meza (2002); SBEF, Finrural.

2. Formal Financial Sector

This section provides an overview of the formal financial industry, including both banking and non-banking sectors. Note that a number of regulated banking and non-banking entities provide microfinance type lending.

²¹ The microfinance Private Financial Funds included here are Caja Los Andes, FIE, EcoFuturo and PRODEM.

2.1 Banking Sector

The commercial banking sector in Bolivia as of June 2003 was made up of nine domestic banks²² and four foreign banks²³, operating more than 350 branches. (Superintendencia de Bancos y Entidades Financieras Bolivia, “SBEF”, 2003).

A bank is defined under the Banking Law as “an authorized financial entity, of national or foreign origin, habitually devoted to operations of intermediation and the provision of financial services to the public within the framework of the present law, in the national territory as well as internationally”²⁴

As of May 31, 2000, the consolidated assets of the commercial banking system amounted to USD \$5,294 Million, representing 86% of the total assets in the financial system as a whole. Total deposits amounted to USD \$3,572 Million in 1,007,000 accounts.

Note that of these commercial banks, only Banco Solidario S.A. (BancoSol) is engaged primarily in microfinancing activities, and because of this BancoSol is often treated separately in government statistics. As of 2000, the total assets and deposits of BancoSol represented less than 2% of the banking system (Gomez, Tabares & Vogel, 2000).

2.2 Non-Banking Sector

The regulated, non-banking financial sector in Bolivia as of June 2003 was made up of seven Private Financial Funds (*Fondos Financieros Privados*) (FFPs)²⁵, 29 credit

²² Banco Santa Cruz S.A., Banco Nacional de Bolivia S.A., Banco de la Unión S.A., Banco Mercantil S.A., Banco BISA S.A., Banco Económico S.A., Banco Solidario S.A., Banco Ganadero S.A.

²³ Banco de la Nación Argentina S.A., Citibank N.A., Banco do Brasil S.A..

²⁴ Law No. 1488 Law on Banks and Financial Institutions (April 1993, as amended), Section 1.

unions (Cooperativas de Ahorro y Crédito), 13 mutual societies (Sistema Mutual de Ahorro y Préstamo para la Vivienda), two general deposit warehouses (Almacenes Generales de Depósito) and one financial services company. All of these entities are required to obtain licenses from the SBEF (SBEF, 2003). The non-banking formal financial sector primarily serves the microfinance and consumer credit sectors.

2.2.1 Private Financial Funds (FFPs). FFPs were created in 1995, as “non-banking financial entities, whose principal objective is channeling resources to micro and small scale borrowers whose activities are located in urban as well as rural areas.”²⁶ The driving force behind the creation of this type of entity was the desire of certain NGO MFIs to become licensed and regulated in order to take savings deposits from the general public; the first FFP to become licensed was Caja Los Andes-FFP, and offspring of Pro-Crédito NGO, an NGO supported by GTZ (Gomez, Tabares & Vogel, 2000).

FFPs are required to obtain a license from the Superintendence of Banks and Financial Entities, and their operations can be limited by the SBEF to specific activities; for example, FFPs, in addition to being restricted from offering checking accounts, may not offer savings accounts and time deposits unless specifically licensed to do so (Gomez, Tabares & Vogel, 2000). The licensing requirements are set out in SBEF regulations, and the broad operational rules are in the Law on Banks and Financial Entities. The licensing requirements are less stringent than those for the banking sector.²⁷ FFPs can be functionally classified into two categories: microcredit FFPs (such as Caja Los Andes (established in 1995), FIE (1998), EcoFuturo (1999) and PRODEM (1987)) and consumer credit FFPs (such as Acceso (1996), Fassil (1996) and Fondo de la Comunidad (1996)).

²⁵ Financiera Acceso S.A., Caja de Ahorro y Préstamo Los Andes, Fondo Financiero Privado Fassil, Fondo de la Comunidad, Fondo para el Fomento a Iniciativas Eco., Fondo Financiero Privado Eco Futuro, Fondo Financiero Privado Prodem.

²⁶ Supreme Decree No. 24000 of May 1995. Translation is from Gomez, Tabares & Vogel (2000).

²⁷ Circular SB/288/99 (Titulo I, Cap. I, Sec. 3); Law No. 1488 of April 3, 1993, Law on Banks and Financial Entities, Arts. 76-81.

As of May 31, 2000, total assets for FFPs amounted to USD \$145 Million, representing approximately 2% of the total financial system. Consolidated deposits totaled USD \$73 Million. Total number of deposit accounts was 24,199, representing 1.5% of the system.

2.2.2 Credit Unions. Savings and credit cooperatives have historically offered micro-credit type services to their members, but in the mid-1990s credit unions started adopting lending technologies developed by self-identified MFIs (Rhyne, 2002). The 1993 Banking Law required credit unions that mobilize public deposits (“Open Cooperatives”) to comply with all formal sector licensing and regulatory requirements, including the requirements to report to and consult the central credit bureau (CIRC).

As of May 2000, a total of 207 credit unions were operating in Bolivia. Of these 140 were open cooperatives, 60 had solicited licenses, and only 19 had obtained licenses. As of the same date, the consolidated assets of credit unions represented 4% of the total financial system, but in terms of number of deposit accounts, credit unions represented 20% of total accounts—reflecting a disproportionate share of small depositors (Gomez, Tabares & Vogel, 2000).

2.2.3 Others. The remaining categories of regulated financial entities are mutual associations (which provide housing-related credit) and the catchall “financial services entities” for non-deposit taking organizations. An example of such type of entity would be a private credit bureau. Another example is La Nacional Financiera Boliviana (NAFIBO), a mixed public-private company that coordinates state and international assistance to the formal microfinance sector.

2.3 Supervision of Formal Financial Industry

The financial industry in Bolivia is supervised by the Superintendence of Banks and Financial Entities (SBEF), which enforces the laws and regulations (including policies set by the Central Bank of Bolivia), and also has regulatory powers. The SBEF is divided into three departments: the Intendancy of Banking Entities, the Intendancy of Non-Banking Entities, and the Intendancy of Norms and Procedures. As discussed in more detail below, Bolivia's public credit bureau, the Central de Información de Riesgo Crediticio (CIRC), is located within the SBEF. The SBEF, together with the Superintendence of Securities, Pensions, Insurance and Reinsurance, constitute Bolivia's Financial Regulatory System.²⁸

The SBEF has been an autonomous regulatory and supervisory body since 1987, when it was made independent from the Central Bank. This change was made at the same time that several state-owned banks were closed and the Government instituted a liberalization of the regulatory regime. As a result, the SBEF is generally considered to be an effective and independent body that has been able to take a technical rather than political approach to its regulatory and supervisory duties (Fondesif/GTZ, 2002; Gomez, Tabares & Vogel, 2000).

3. The Informal Sector: NGOs

Bolivia has a relatively well-developed NGO sector, with numerous non-profit and donor-supported organizations providing microcredit type loans. As a result of their status, they are not regulated by the SBEF, are not required to obtain a license from the SBEF and cannot take savings from the public (Rhyne, 2001).

Many of these NGOs, through NGO associations or guilds such as Asociación de Entidades Financieras Especializadas en Microfinanzas (ASOFIN), Corporación de Instituciones Privadas de Apoyo al Microempresa (CIPAME), or La Asociación de Instituciones Financieras para el Desarrollo Rural (FINRURAL)²⁹, have lobbied to be

²⁸ Law No. 1732 of November 29, 1996; SBEF Website at www.sbef.gov.bo.

regulated by the SBEF. Because the SBEF reportedly does not consider the safeguarding of donor funds to be within its ambit, it has consistently taken the position that it is not responsible for supervising NGO activities (Gomez, Tabares & Vogel, 2000).

Although the NGO sector has gradually reduced its dependence on foreign donor funding, such funding continues to play a significant role. In 1995 the government established the Fondo de Desarrollo del Sistema Financiero y de Apoyo al Sector Productivo (FONDESIF), aimed at supporting both regulated and non-regulated MFIs and coordinating state and international support to the sector (FONDESIF, 2003, González-Vega, 2002c).

As is described in more detail below, many NGOs have chosen to establish for-profit, licensed entities; examples include the formation of commercial bank BancoSol in 1987 by the PRODEM NGO, and the creation of FFP Caja Los Andes by NGO Procredito in 1992 (Navajas, Conning & Gonzalez-Vega, 2003). Traditional NGOs continue to offer a variety of microcredit services, and as shown in Table 1 above, the NGO sector has actually fared better than the formal microcredit sector, showing growth between 1998 and 2001, a period during which most MFIs suffered significant losses of clientele. As of 2002, NGOs made up only 17% of the total microcredit loan portfolio, but together NGOs accounted for 38% of active microfinance clients in Bolivia (Rhyne, 2002).

Microfinance NGOs can be classified on the basis of their clientele as being principally urban or rural in focus. The main urban microfinance NGOs include Cidre (established in 1991), Diaconía-FRIF (1991), Funbodem (1987), Idepro (1988), and ProMujer (1991). The main rural microfinance NGOs include Agrocapital (1995), Aned (1978), Crecer (1986), Fades (1988), Fondeco (1990) and Sartawi (1990).

4. Bolivian Microfinance (Formal and Informal Sectors): Recent Developments and Crisis

²⁹ FINRURAL is discussed in more detail below, as it operates a private credit bureau (Central de

In part because several microfinance NGOs successfully transformed themselves during the 1990s into commercial microfinance providers—BancoSol in particular—the development of the Bolivian Microfinance sector has been closely documented by Bolivian and foreign observers.³⁰ Although it is beyond the scope of this paper to provide a detailed history, an overview of the major trends and of the crisis that hit the microfinance sector in 1998-2001 is essential to understanding the current credit reporting system and the challenges faced by public and private credit bureaus in Bolivia.

The major developments in the Bolivian microfinance sector over the last decade can be schematically broken down as follows: (i) the transformation of traditional microfinance NGOs into commercial MFIs, including BancoSol and some of the Private Financial Funds (FFPs), (ii) the dramatic rise and fall of consumer credit lenders, (iii) the entry of other commercial lenders into the microfinance sector, (iv) the crisis of 1998-2001 and resulting contraction of the microfinance sector, and (v) regulatory responses to the crisis.

4.1. Emergence of Commercial Microfinance Institutions

In addition to the NGO microfinance institutions active in the country in the 1980s and 1990s, formal sector MFIs started appearing in the early 1990s, with BancoSol, the first formal-sector MFI, starting operations in 1992.

As noted above, BancoSol's predecessor, the PRODEM NGO, started operating in 1987 and had already developed a substantial clientele. Utilizing group lending, where borrowers do not need collateral but are required to belong to a joint-liability group, BancoSol soon established itself as a dominant player. Throughout the 1990s BancoSol had the highest return on assets (5.2% in 1998), asset quality (0% arrears) and capital adequacy (16.3%) (Rhyne, 2002).

In 1995 other NGOs chose to set up regulated MFIs, and subsequently other private financial funds (FFPs) and credit unions joined the fray. One major competitor of

Riesgos de Entidades no Fiscalizadas) catering to MFIs.

BancoSol, Caja Los Andes (an offspring of the NGO Procredito), chose lending technologies quite distinct from BancoSol's group lending approach, focusing instead on individual liability loans and closer screening of applicants. (Navajas, Conning & Gonzalez-Vega, 2003).

The growth through 1998 was spectacular, with the total number of microfinance borrowers growing from 120,000 in 1990 to 415,6000 in 1998. (Navajas, Conning & Gonzalez-Vega, 2003). Factors explaining this growth include the stable economic environment during the period, the historical absence of commercial bank involvement in microfinance (traditionally Bolivian banks had served larger business and the elites), innovative lending technologies, economies of scale, adequate regulatory supervision by the SBEF, and international support and technical assistance. (FONDESIF / GTZ 2003). The "formalization" or "commercialization" of MFIs—in particular BancoSol and the four specialized private financial funds—contributed significantly to this growth.

4.2 Consumer Credit Lenders

In 1998, competition in the microcredit sector increased as commercial institutions started targeting traditional microcredit customers. Of particular note was the entry of several Private Financial Funds using consumer credit methodologies imported from more developed countries (for example, Fassil, a FFP opened in 1996, used a consumer credit model imported from Chile). The consumer credit model is based on the ability to tap into the borrower's salary for loan repayment, and works best in countries with a significant number of prime employers. The consumer credit model has a fundamentally different credit administration philosophy: late payments are tolerated and loan officers are not held directly responsible for loans (which tend to be processed assembly-line style) (Rhyne, 2002).

Table 2 (below), from Elisabeth Rhyne's excellent analysis of the commercialization of microfinance in Bolivia, sets out the fundamental differences between microcredit and consumer credit lending.

³⁰ See, e.g. Rhyne (2001) and (2002); FONDESIF / GTZ (2002); González-Vega and Rodríguez-

Meza (2002); Navajas, Conning and González-Vega (2003).

Table 2: Comparison of Microcredit and Consumer Lending in Bolivia

Parameter	Microenterprise Credit	Consumer Lending
Loan Terms	Average near USD 1,000, fast turnaround, competitive interest rates	Average near USD 1,000, short term, fast turnaround, competitive interest rates
Basis for Loan Approval	Enterprise and household cash flow, credit history, group guarantees	Salary, credit score
Basis for Repayment	Motivation for continued access to credit, peer pressure	Steady salary and ability to garnish wages, employer cooperation
Tolerance for delinquency	Zero tolerance; expected delinquency less than 3-5%	Not worried until after 30 days late; expected delinquency 15-20%
Method of Follow up	Immediate personal visit	Letter by mail
Staff Organization	Loan officer responsible for own client	Assembly line loan processing
Basic Philosophy	Trust and responsibility	Information management

Source: Rhyne, 2002.

As illustrated in Table 2, the terms offered to borrowers by consumer lenders were quite similar to those offered by microcredit lenders, and indeed during the late 1990s the new consumer credit lenders targeted the lower income individuals and microenterprises who traditionally comprised microfinance borrowers. The aggressive marketing employed by the consumer lenders was quite successful, as traditional microfinance borrowers were offered competitive rates and larger loans, as well as a higher delinquency tolerance. The consumer credit lenders initially enjoyed rapid growth, and by some estimates by 1999 the total loans outstanding for consumer credit institutions had reached almost the same level as the microfinance sector. A significant percentage, perhaps as high as 30%, of consumer loans made by consumer credit lenders were made to microenterprises (Rhyne 2002). Likewise, the consumer credit lenders ended up making loans to individuals who already had loans outstanding from formal or

informal microfinance lenders—and significantly in many cases this targeting was deliberate—basically “stealing” customers.

4.3 Other Commercial Entrants into the Microcredit Sector

As the microcredit and consumer credit market enjoyed rapid growth, other commercial lenders joined the fray and offered various types of microfinance or consumer credit products targeted at traditional microfinance borrowers. In particular, three commercial banks, Banco Union, Banco Santa Cruz and Banco Economico, started competing regionally and nationally with traditional microfinance institutions and with the FFPs specializing in consumer credit (Acceso, Fasil and Fondo de la Comunidad). Like the consumer lenders, the new commercial lenders tended to apply inappropriate lending techniques that did not reflect the actual nature of the microcredit market; these techniques first seemed effective at gaining clients, but ultimately resulted in massive levels of delinquency and ultimately in almost complete loss of market share. NGOs and formal MFIs that stayed true to traditional microfinance policies, fared much better, as is illustrated in Table 1 (Fondesif / GTZ, 2002).

4.4. The Crisis of 1998-2001

Faced with aggressive competition from consumer credit and the other recent commercial entries into the microfinance sector described above, traditional MFIs started becoming more flexible in their evaluation of potential and existing clients. The repayment behavior of existing clients was also affected by the new entrants. Ultimately, the zero tolerance policy became less strictly enforced as delinquency rates increased (Fondesif / GTZ, 2002).

At the same time market penetration reached extremely high levels. Rhyne argues that microfinance alone (not including consumer lending) probably exceeded 50% penetration, an unprecedented level for microfinance anywhere in the world. By way of illustration, in 2000 there were approximately 400,000 microenterprise loans outstanding,

for an estimated national market of 600,000 to 1 million microenterprises. (Rhyne 2002) Because clients increasingly took out loans with more than one lender, it is difficult to evaluate the total number of microfinance customers; however the total number of loans outstanding continued to climb during the late 1990s.

Market penetration was followed by saturation and over-indebtedness as customers either borrowed beyond their means (encouraged by the availability of credit and the lending philosophies of new institutions using inappropriate lending techniques), or resorted to “bicycling” loans by taking out new loans to repay existing ones. One author reports that it became a “status symbol” to hold multiple loans (Rhyne 2002). The quality of portfolios held by MFIs deteriorated. The total number of microfinance borrowers had declined to 378,000 by mid 2001.

A major factor in this crisis was the serious economic setback Bolivia suffered in 1999 as shocks from the 1997 Southeast Asian crisis hit Bolivia, with decreased trade and flow of external capital. Prices for the main Bolivian exports dropped, social conflicts erupted and agriculture suffered as well (FONDESIF/GTZ 2002)³¹. The formal banking sector suffered losses at the same time as the microcredit sector did.

Another key factor in the microfinance crisis, which is directly relevant to this country case study, was the absence of a credit reporting system with complete coverage of the microfinance sector, which would have better permitted lenders to identify borrowers with multiple loans. A more detailed discussion of this information asymmetry and its possible impact is provided below in Section 6.

The crisis resulted in higher delinquency rates, drops in outstanding loans, reduced returns on equity and portfolio reductions. For example, between 1997 and 2000, BancoSol’s loans outstanding dropped from 76,000 to 60,976, its return on equity dropped from 24% to 4%, and the percentage of its portfolio at risk (more than 1 day) increased from 2.1% to 12.3%. Table 1 above also illustrates the impact that the crisis had on the formal financial system.

Like many sectors in the Bolivian economy, microfinance and consumer credit faced social upheaval and protests, including the so-called “Debtors Revolt”, during which

³¹ The Fondesif / GTZ (2002) contains an overview of the shocks hitting the Bolivian economy.

debtors associations were formed to lobby for debt forgiveness. Some of these associations were disbanded when their leaders defrauded their members. There was a period in 2001 when violent demonstrations were held, and in July 2001, organizers took hostages at the Superintendence of Banks and Financial Entities in an effort to get the government to forgive their loans. Reportedly, most of the participants in these protests were not traditional microfinance borrowers, but individuals who had taken out consumer loans and were not able to repay them. The legitimate associations ultimately came to an agreement³² with the government and representatives of the financial entities to allow the restructuring of some of the smaller outstanding debts, and the demands for debt forgiveness were abandoned (FONDESIF/GTZ 2002).

4.5 Regulatory Responses

It is important to note that the Bolivian regulatory framework does not have extensive regulations covering microfinance activities per se. Rather, as was outlined above in Section 2, the regulatory framework is organized according to types of financial institutions—banks, private financial funds and credit unions are each subject to the same regulations regardless of the type of lending they undertake. There was no formal definition of “microfinance” in the legal framework, and prior to 1999 all loans below USD \$20,000 were classified as microcredit type loans—even if they were consumer credit loans taken out to acquire goods (Gomez, Tabares & Vogel, 2000).

In response to the microfinance crisis, and in particular the role that consumer credit played in encouraging over-indebtedness, the in 1999 the SBEF issued a regulation to differentiate between microfinance and consumer credit.³³ Thus consumer credit loans were defined as “loans to an individual in terms and interest agreed upon, destined to finance the acquisition of consumer goods or the payment of services, redeemed in successive installments and whose principal source of payment is the salary of the person.” The same regulations also established loan policies more specifically tailored to

³² Framework Agreement of July 2001; the agreement set up a system for mediating disputes involving small debtors.

microcredit loans, and require that MFIs establish adequate financial and credit technologies for microfinance. The SBEF's Intendance for Non-Banking Entities (IENB) has also established supervision and field inspection policies tailored to microfinance, and the IENB supervises BancoSol even though the bank is technically not within the non-banking financial sector (Gomez, Tabares & Vogel, 2000).

Another regulatory response to the crisis were changes in 2000 to the regulatory framework for credit information reporting, discussed in the following section.

5. Framework for Credit Information Reporting in Bolivia

The discussion below of the structure and legal framework for credit information reporting is divided into four parts: (i) CIRC: the state-run central credit bureau at the SBEF; (ii) existing informal credit sharing arrangements, (iii) the new framework for private credit bureaus (Buró de Información Crediticia, or BICs) and (iv) the new FONDESIF credit bureau.

Table 3 below provides an overview of the major formal and informal MFIs and the credit reporting systems they use.

³³ Resolution No. 043 of April 15, 1999, SBEF.

Table 3: MFIs and Credit Reporting

Name of Microfinance Institution	Required Use of CIRC Credit Bureau (reporting and consulting ?)	Access to CIRC Credit Bureau before 2000?	Uses Private Credit Bureau to gain indirect access to CIRC?	Uses Informal Credit Bureaus & Information Collection?
BancoSol (Regulated Bank specializing in microfinance)	Yes. Required by law upon licensing	YES	NO	Must be determined on case by case basis
Private Financial Funds Specializing in Microfinance (Los Andes, FIE, EcoFuturo, PRODEM)	YES. Required by law upon licensing	YES	NO	Same as above
Consumer Credit Private Financial Funds (Fassil, F. de Comunidad, Acceso)	YES. Required by law upon licensing	YES	NO	Same as above
NGOs (Urban Microfinance) (Cidre, Diaconia-FRIF, Funbodem, Idepro, Promujer)	NO	NO	OPTIONALMay use private credit bureaus since 2000; must be determined on case by case basis	Same as above
NGOs (Rural Microfinance) (Agrocapital, Anded, Crecer, Fades, Fondeco, Sartawi)	NO	NO	Same as above	Same as above

5.1 Public Credit Registry: SBEF's Central de Información de Riesgo Crediticio

The Bolivian Public Credit Registry, Central de Información de Riesgo Crediticio (CIRC), is operated by the SBEF and started operations in 1989. The regulations applicable to the CIRC are contained in Circular SB/292/99 as updated.³⁴ The stated objective of the CIRC are to reduce the uncertainty relating the repayment capacities of debtors in order to reduce moral risk, to discipline the market and reduce information asymmetries (SBEF / CIRC, Curso de Inducción, 2001).

5.1.1 Reporting Requirements. All regulated financial entities (including commercial banks, private financial funds (FFPs) and licensed credit unions) are required to report on information on their clients (individuals and legal entities) electronically to CIRC on a monthly basis. The CIRC database covers approximately one million clients. (Campion, 2001). The database covers 142 variables on creditors, including loan transactions during the period, information on the creditors' and guarantors' repayment, and changes to loan terms. Much of the information is used by the SBEF to track economic and financial industry trends, and 40 of those variables of information are shared with institutions consulting the CIRC database when making loan decisions (SBEF / CIRC, 2001).

5.1.2 Consultation Requirements. All regulated financial entities who report to CIRC are required to consult the CIRC when evaluating the creditworthiness of clients for loan decisions.³⁵ As of 2000 the CIRC had an average of more than 5000 daily credit inquiries. The inquiries can be made over the Internet (Bolanos, 2000).

³⁴ Circular SB/292/99 (and amendments thereto) are codified in the Recopilación de Normas Para Bancos y Entidades Financieras, Title VI.

³⁵ Circular SB/292/99, codified in the Recopilación de Normas para Bancos y Entidades Financieras at Tit. VI, Cap. I, Sect. 4.

5.1.3 Limitations of the Public Credit Registry at SBEF / CIRC.

--A great deal of data is collected through the CIRC system, including data not used for credit reporting, which is onerous for the reporting institutions. This is compounded by the fact that debt profiles for all clients must be sent on a monthly basis. CIRC also reports that as result, information processing can be slow (SBEF / CIRC, 2001).

--Credit history reports from the CIRC database are limited to the past 2 months. Although information on overdue loans remains in the database until paid-in-full, borrowers can eliminate negative data by paying off the past-due loan and suffer no long-term impacts due to past bad behavior. This “amnesty” greatly limits the effectiveness of the CIRC data for predicting future payment behavior (Luoto, 2003, World Bank, 2003).

--Privacy protection laws require that financial institutions obtain written permission from individuals prior to accessing the database to check their credit profile.

--CIRC credit reports on individuals do not provide the individual’s address or type of business. This is done in an effort to reduce fears that clients will be “stolen” by competing lenders (Campion & Valenzuela, 2001).

--Individuals themselves are not granted access to their own CIRC files, and cannot change or correct their own files (World Bank, 2002).³⁶

5.1.4 CIRC & Incomplete Coverage of Microcredit Borrowers. The MFIs in Bolivia which are regulated entities (e.g. BancoSol, the FFPs and licensed credit unions) are covered by the CIRC public credit registry. Campion (2001) reports that managers from BancoSol, Caja los Andes and PRODEM indicated in interviews that they would use the CIRC credit bureau even if they were not required to do so.

Informal MFIs, however, are not required to consult the CIRC, and before 2000 could not access the database. As a result, the SBEF estimates that approximately 120,000 loan clients, or 11% of all of Bolivia’s borrowers, remain outside the credit system altogether (Campion, 2001). If you look just at the microfinance sector, then the limited coverage of the CIRC database is even more evident: between 1998 and 1999,

the onset of the crisis, there were a total of more than 351,510 active microfinance clients in Bolivia; of that 56% were served by NGOs, and 44% were served by formal sector MFIs (Gomez, Tabares & Vogel, 2000). Rhyne (2002) indicates that NGOs accounted for approximately 38% of active microfinance clients in 2000.³⁷

The incomplete coverage of the CIRC database with respect to microcredit customers of informal MFIs has been acknowledged to be a serious limitation. Recent legislative changes allowing the sharing of information between the CIRC and private credit bureaus aim to address this limitation. The new regulations relating to private credit bureaus are discussed below in Section 5.3.

5.2 Informal Credit Reporting Systems and Information Vendors

In addition to formal credit bureaus, other means of sharing information about borrowers have been developed by MFIs in Bolivia. Below is a summary of these techniques.

5.2.1 Blacklists. MFIs have established informal credit bureaus to share information, usually negative, regarding microcredit customers. The most basic are simply internal “blacklists” of borrowers who have defaulted or been problematic. Many NGOs in turn have informally shared their blacklists with other NGO MFIs (Campion, 2001).

5.2.2 Informal MFI Credit Bureaus. Some associations of NGO MFIs have gone beyond blacklists and developed more sophisticated credit information sharing systems. Examples of these credit bureaus include systems targeting urban microfinance customers set up by NGO associations FINRURAL (operational between 1996 and 1998 only) and CIPAME (Campion, 2001). These credit bureaus did not collect or provide extensive

³⁶ These provisions may have changed and the information should be verified.

³⁷ As discussed above, the fact that many borrowers have more than one loan outstanding makes it difficult to evaluate how many clients there are.

information, and even that information was incomplete and in certain cases limited regionally. And since these credit bureaus were not linked to the CIRC database, the number of clients covered was limited (FONDESIF / GTZ, 2002).

5.2.3 Information Vendors. Another means of obtaining information about potential borrowers are information vendors, which collect publicly available information such as penal and civil judgments, newspaper articles and business failures. In Bolivia, Siprotec, within Bolivia's Department of Commerce, has provided such information to lenders since 1995. Its database contains over two million names, including both individuals and corporations. However, it does not collect personal identification numbers, and has suffered criticism for confusing identities based upon similar names of individuals. This service is used by 80% of regulated financial institutions and has over 200 subscribers, mostly from the regulated sector. These organizations primarily use Siprotec's service to gain a fuller picture of an individual or business in addition to the data provided them from the CIRC public credit registry. Another information vendor active in Bolivia is Datos, a regional, private company that provides services similar to Siprotec (Campion & Valenzuela, 2001).

5.3 Private Credit Bureaus: BICs

Prior to 2000, banking regulations prohibited CIRC from sharing credit information with other credit bureaus or with non-licensed microfinance providers. As discussed above, this prohibition limited NGO MFIs access to credit information, and did not allow the sharing of information on MFI customers with regulated financial institutions and banks.

In response to the economic crisis in Bolivia of 1998-2000, in April 2000, Bolivia enacted legislation allowing, among other things, the SBEF to share information with private credit bureaus. The relevant provisions of the legislation expressly permitted the

SBEF/CIRC to share information with private entities exclusively with respect to microfinance and consumer credit, and subject to regulations to be issued by the SBEF.³⁸

The SBEF then proceeded to prepare detailed regulations for private credit bureaus; the final provisions were completed in October 2003.³⁹ A private credit bureau is known as a “Buró de Información Crediticia” or BIC, and is defined as a

“legal entity incorporated as a *sociedad anónima*, whose sole purpose is to process credit information, allowing for the adequate identification of the debtor, the level of indebtedness of the debtor, and the risk level.”⁴⁰

As noted above, BICs themselves are regulated financial entities, and therefore must be licensed by the SBEF. The term “credit information” includes limited data from the CIRC public credit bureau, relating to microfinance and consumer credit, as well as other publicly available information.⁴¹

The BIC regulations also provide that:

- Written permission from the creditor must be obtained before accessing the database for a credit check
- BICs are required to share their data on a cost-free basis with the SBEF/CIRC, and are authorized to share data with other BICs.
- Creditors whose credit data is kept by a BIC may access their own information, and may request the correction of any errors.

As of the date of this paper, no operational private credit bureaus other than the FINRURAL service described below were identified, but it is likely that new private credit bureaus will be established.

³⁸ Law No. 2298 of April 3, 2000, Art. 25 (amending Art. 90 of the Bank and Financial Entities Law).

³⁹ Circular SB/332/00 (11/00) as modified by Circular SB/445/03 (10/03). Codified in the *Recopilación de Normas para Bancos y Entidades Financieras* at Tit. I, Cap. VII, Sec. 1.

⁴⁰ Author’s translation.

⁴¹ Section 2 of Circular SB/332/00 (11/00) as modified by Circular SB/445/03 (10/03). Codified in the *Recopilación de Normas para Bancos y Entidades Financieras* at Tit. I, Cap. VII, Sec. 1.

5.4 The FINRURAL Credit Bureau

The Asociación de Instituciones Financieras para el Desarrollo Rural (FINRURAL) is a private non-profit association of microfinance NGOs founded in 1993. Following the regulatory changes allowing for the creation of private credit bureaus and the sharing of information from the CIRC database for microfinance and consumer credit information, FINRURAL started credit-reporting operations for the non-regulated microfinance sector through the Central de Riesgos de Entidades no Fiscalizadas (CRENF). This credit bureau is separate from the earlier FINRURAL efforts at providing credit information discussed above. The FINRURAL credit bureau is operational and inquiries may be made by Internet.⁴² Capitalizing on the recent legislative changes, the FINRURAL credit will share information with the CIRC, reporting data on the clients of the unregulated MFIs which use the FINRURAL credit bureau, and allowing unregulated MFIs to consult information from the CIRC database indirectly.⁴³

The FINRURAL – CIRC link-up is receiving international technical assistance and funding through the Servicios Financieros Rurales (SEFIR) project implemented by Development Alternatives Inc. (DAI) and funded by the United States Agency for International Development (USAID). One goal of the project is to provide an “integrated service that offers complete credit information at costs based on the different types of markets served” (Website of Development Alternatives Inc., 2003). It is recommended that representatives of the SEFIR project be contacted to obtain further information and updates on the status of the FINRURAL credit bureau. Note also that in 2001-2002 the SEFIR project funded a study of existing credit reporting arrangements for non-regulated

⁴² FINRURAL Website, visited October 2003. Note that access to the credit bureau is password protected. It is not clear how the legal requirement of getting the customer’s permission to submit his or her credit information is met.

⁴³ The author was not able to confirm whether the link-up with the CIRC is currently active.

MFIs. This study is not publicly available, but if possible it should be obtained directly from DAI.

5.5 Overview of Credit-Reporting and Information Sharing Organizations.

Table 3 summarizes the services and coverage of the main credit-reporting and information-sharing organizations in Bolivia. Bolivian credit reporting institutions are allowed to collect and distribute both positive and negative information.

Table 3: Bolivia's Main Information-Sharing Institutions

Name of Credit Reporting/Information-Sharing Institution:	CIRC at SBEF (Public Credit Registry)	FINRURAL Credit Bureau	Siprotec
Founders:	State	Association of NGOs	Bolivian Chamber of Commerce
Public/Private:	Public	Private, non-profit	Private
Year Started:	1989	1993 (but new credit bureau established after 2000)	1995
Membership Type:	Regulated Financial Institutions	Non Regulated Microfinance and other NGOs	200 Subscribers, mostly regulated financial institutions
Free to Members:	No (Annual Fee equal to 1/1000 of Financial Institution's Total Assets)	Informal Credit Bureau	N/A (Subscription Fee)
Supplies Reports to Non-Members:	No	No	N/A
Coverage:	One Million Names	Almost half of MFI Borrowers Represented	2 Million Names
Consultations/Month:	5,000 per day over Internet		80% of Regulated Financial Institutions use
Frequency of Updates:	Monthly	Monthly	
Instant Internet Consultations	Yes		
Main Services Offered:	Banking Supervision; Credit References	Beginning Credit Bureau Services focusing on non-regulated sector; serves as liaison between CIRC and non-regulated financial institutions	Public Information Vendor

Source: Luoto (2003).

6. CONCLUSION & SUGGESTIONS FOR RESEARCH

The research and analysis undertaken for this country case study suggest that Bolivia would be a good choice for further research on credit information reporting and microfinance. From a practical point of view, there exists a substantial body of research and data relating to the financial sector and microfinance in particular, while much further research on the role and impact of credit reporting is needed.

This section provides a brief overview of some of key themes and areas for further research on credit reporting and microfinance in Bolivia.

--Credit Information Sharing and the 1998-2001 Crisis

One possible area for further study would be to examine the impact of the credit information gap (resulting from fragmented credit reporting for microfinance clients in the informal sector) on the overindebtedness crisis of 1998-2001.

As discussed in detail in this case study, the CIRC central credit registry did not cover the clients of informal MFIs during the period leading up to crisis. Informal MFIs account for a large percentage of microfinance borrowers, and the commercial MFIs and consumer credit banks targeted these same borrowers. Although all formal sector MFIs such as BancoSol or the FFPs are required by law to use the CIRC database (both for reporting and for making loan decisions), borrowers who had loans outstanding (or other credit problems) with informal sector MFIs would not appear in that database, thus creating the risk that debtors would take on excessive debt and multiple loans. Rhyne (2002) argues that the information on the CIRC system at the time was so incomplete that it could not prevent overlending.

A number of considerations should be kept in mind when pursuing this approach:

(i) there were exogenous factors that helped precipitate the crisis, such as the recession that hit most sectors of the Bolivian economy in 1999;

(ii) one of the most important causes of the crisis was likely the aggressive tactics and inappropriate use of consumer credit lending technologies by some of the commercial entrants to the microfinance sector⁴⁴;

(iii) many of the participants in the boom in microfinance lending during the 1990s deliberately ignored the credit information they did have. An example would be the tactic of obtaining lists of existing MFI customers and encouraging them to take out additional loans (Rhyne 2001);

(iv) Informal credit reporting systems existed in Bolivia at the time, albeit incomplete, geographically limited, or shared only on a limited basis. There is limited published information available on these informal reporting systems and blacklists.

--The New Private Credit Bureaus

Another area for further research would be to examine the development and impact of the new private credit bureaus (BICs) and how they share data with the CIRC database. It can be argued that the regulatory changes in 2000-2003 allowing private credit bureaus to operate in Bolivia do not solve all the “fragmented information” problems identified in this case study, since informal sector MFIs are still not required by law to use a credit bureau. Indeed, the only change to the system is that now the informal sector has the option of accessing the CIRC database (and sharing data on its customers if it does access it) through the intermediation of private credit bureaus such as the FINRURAL initiative.

Note also that a whole set of challenges remain to convince informal microfinance lenders to use credit bureaus. Typical constraints on credit bureau use in developing countries include (i) cost; (ii) fear of losing clients to other lenders (addressed by limiting identifying client data such as name or business in the credit database being shared); (iii) technological constraints, especially with smaller NGO MFIs; (iv) concerns regarding privacy; and (v) the lack of perceived need, given lending techniques, existing informal or regional credit bureaus and blacklists. It would be useful to obtain further information from MFIs in the field.

⁴⁴ see Section 4 above. The SBEF recognized the need to keep consumer debt separate from microfinance.

Campion (2001) notes that MFIs which rely on the use of group or solidarity microcredit lending typically do not see a need for credit bureaus, and face significantly higher costs if they do use credit bureaus. It would be useful to examine how the availability (or mandatory use of) of credit bureaus would impact these types of MFIs, in particular NGOs. Note that BancoSol does use group lending, and since BancoSol is a regulated entity, its use of the CIRC central credit registry is mandatory.

--Private vs. Public Credit Bureaus; Niche vs. General Credit Bureaus.

As outlined by Campion & Valenzuela (2001), there is an ongoing debate regarding the benefits of niche credit bureaus specializing in microfinance, as opposed to centralized credit bureaus. The assumption had been made that microfinance lending was a unique niche and that niche credit bureaus could best cater to these lenders. The evidence from Bolivia during the 1998-2001 crisis suggests that microfinance clients access a variety of sources (NGO MFIs, consumer credit, commercial MFIs, and the corner store) and that niche credit bureaus don't function well as a result. This limitation is especially evident when formal sector institutions enter the microfinance market. Further study of these issues in Bolivia would be especially useful given the recent overindebtedness crisis.

--Credit Reporting and the Rural / Urban Divide

In recent years the formal, commercial microfinance sector has focused more on urban markets, while NGOs have catered to poorer, rural borrowers. Thus, as of 2000, 75% of NGO clients were rural, and the average size of loans for microfinance NGOs was much lower than for regulated MFIs (Gomez, Tabares & Vogel, 2000). The major MFIs, such as BancoSol, have both rural and urban branches, and representatives from these institutions could presumably provide insight on the differences between these two markets. Any analysis of credit reporting systems in Latin America would need to take into account the rural / urban division, and Bolivia would provide an opportunity to study this area in detail.

LIST OF ACRONYMS USED

BIC	<i>Buró de Información Crediticia</i> (Private credit bureau)
CIRC	Central de Información de Riesgo Crediticio (the central credit registry of Bolivia)
FFP	<i>Fondo Financiero Privado</i> (Private Financial Fund)
FONDESIF	Fondo de Desarrollo del Sistema Financiero y de Apoyo al Sector Productivo
FINRURAL	Asociación de Instituciones Financieras para el Desarrollo Rural
IENB	Intendance for Non-Banking Entities
MFI	Microfinance Institution
NAFIBO	La Nacional Financiera Boliviana
SBEF	Superintendencia de Bancos y Entidades Financieras

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