THE STANDARD CREDIT REFERENCE BUREAU AND THE PERFORMANCE OF MULTINATIONAL BANKS OPERATING IN THE EAST AFRICAN COMMUNITY

BY

JOSEPH MACHERU NGUNJIRI

A RESEARCH PROJECT SUBMITTED IN PARTIAL FULFILLMENT OF THE REQUIREMENTS OF THE DEGREE OF MASTER OF BUSINESS ADMINISTRATION

SCHOOL OF BUSINESS

UNIVERSITY OF NAIROBI

JUNE 2012

DECLARATION

This research project is my original work and has not been submitted for examination in any other university.

Signature: ………………………….. **Date: ………………………**

JOSEPH MACHERU NGUNJIRI

This research project has been submitted for examination with my approval as a University supervisor.

Signature: ………………………….. **Date: ………………………**

DR. JOHN YABS

DEPARTMENT OF BUSINESS ADMINISTRATION

UNIVERSITY OF NAIROBI

SCHOOL OF BUSINESS

ACKNOWLEDGEMENTS

It would not have been possible to write this project without the help and support of the kind people around me, to only some of whom it is possible to give particular mention here. First, I owe special thanks to God Almighty for granting me good health and success in this project. Above all, I would like to thank my Fiancée Mutanu for her personal support and great patience at all times. My parents, brothers and sisters have given me their unequivocal support throughout, as always, for which my mere expression of thanks likewise does not suffice.

This Project would not have been possible without the help, support and patience of my principal supervisor, Dr John Yabs, not to mention his advice and unsurpassed knowledge in International business. The good advice and support of my second supervisor, Prof Martin Ogutu, has been invaluable, for which I am extremely grateful. I would also like to thank my colleagues and friends for their great support.

DEDICATION

This research project is dedicated to my father, who taught me that the best kind of knowledge to have is that which is learned for its own sake. It is also dedicated to my mother, who taught me that even the largest task can be accomplished if it is done one step at a time and to my Fiancée Mutanu whose advice, insightful criticisms, and patient encouragement aided the writing of this project in innumerable ways.

ABSTRACT

The management of credit risks has become an important concern to policy makers, as they seek drive good performance of multinational banks. This research project examines the need for a standard Credit Reference Bureau to overcome the challenges of the EAC states integration and ensure a progressive performance of the multinational banks. This work aims to show that integration of the EAC has necessitated the need to re evaluate potential risks such as bad debts and high impairment levels, which continually threaten the performance of multinational banks, and propose necessary measures to overcome the identified challenges.

This study used a descriptive survey. The population of this study consisted of 5 Multinational Banks in the EAC and used both primary and secondary data sources in gathering data for analysis. The primary data was collected using semi-structured questionnaires. Data presentation was done by use of bar charts and graphs, percentages and frequency tables. The inferential statistic regression and correlation was done to establish the extent to which CRB ratings affects the performance of multinational banks.

The study concluded that the achievement of this goal calls for composition of a professional body, with an international network and reputable global affiliates to provide regional and international subscribers with both proactive and reactive solutions to credit risk management through a comprehensive range of services. The study concluded that prudential regulation and effective management of the standard credit reference bureau would lead to more robust credit policy enforcement, thus positively impact to the performance of multinational banks. Credit risk would be lower, recovery costs and impairment rates would significantly reduce.

TABLE OF CONTENTS

LIST OF TABLES

LIST OF FIGURES

ABBREVIATIONS

CRB	Credit Reference Bureau
EAC	East African Community
NPLs.	Non Performing Loans
MFI’s	Micro Finance Institutions
MNB’s	Multinational Banks
GNP	Gross Net Products
GDP	Gross Domestic Products

CHAPTER ONE

INTRODUCTION

1.1 Background of the Study

Multinational banks in the East African market are plagued by credit information problems which lead to increased transactions costs, increasing bad debt rates and high impairment rates, often to such an extent that potential borrowers are denied access to credit in the formal sector. (Tumusiime-Mutebile, 2011). A key challenge for policy makers concerned with financial market development is how to design policy interventions which can mitigate informational imperfections and thus reduce their negative externalities. The kernel of the challenge is how to ensure that accurate and reliable information about those which wish to raise finance can be acquired in a cost effective manner by those who provide finance and bear the risk of doing so.

Credit Reference Bureau provides an institutional solution to the problem.

A Credit Reference Bureau (CRB) is a potential source of information for market participants who are trying to ascertain the creditworthiness of borrowers. Essentially, reference bureaus offer judgments (they prefer the word "opinions"[1]) about the quality of loans and bonds issued by corporations, governments, as well as "sovereign" issuers abroad, and mortgage securitizers (Lawrence J. White, 2009). A well functioning Credit Reference Bureau mitigates information related market failures because it is compulsory for all participants in the credit markets to provide and share information, even in circumstances where they may have private incentives not to do so. This was the motivation to the introduction of a Credit Reference Bureau (Tumusiime-Mutebile, 2011).

The real effects towards the introduction of CRB's may end up being further progress towards the development of EAC rather than easier access to credit (Sarah Collier, 2011). And there have been calls to introduce a standard CRB for the whole of the EAC as part of the process of streamlining economies and regulations.

1.1.1 The Credit Reference Bureaus

Credit reference bureaus play a major role in offering judgments or opinions about the quality of credit extended by financial institutions. These Bureaus not only provide information on the creditworthiness of individuals but can also act as a reference point for the credit rating agencies, in order to achieve its full benefits. (Christopher Cox ,2007) noted that it is useful to review the history of credit rating agencies and their role in the financial markets. Credit ratings have been used to distinguish among grades of debt creditworthiness since early last century. (Gautam & Randall, 2003) observed that one of the fundamental economic problems faced by developing countries is the difficulty in mobilizing funds to increase investment. The level of income is often too low to generate sufficient savings, and the domestic financial system often does a poor job of directing those funds back into domestic capital formation. This makes access to international capital markets an important resource for obtaining funds to raise the level and accelerate the pace of investment and growth.

In order to gain access, developing countries must first obtain a favorable rating of their creditworthiness by one or more credit rating agencies. A strong credit rating will play a major role in determining the cost and availability of credit flows, and the failure to maintain a strong rating will possibly lead to a reversal of capital flows, a disruption of the financial system and an overall economic downturn. It has been not just the likelihood, but the fact, of such financial crises in many parts of the developing world that has focused so much attention on the role played by credit rating agencies in international capital markets and the world economy. This paper will look at the credit rating agencies and their methodologies, analyze the current policy concerns regarding their role in capital flows, and offer a few recommendations on how to make improvements.

1.1.2 Performance of Multinational Banks

This paper investigates whether foreign subsidiaries outperform their parent banks in terms of profitability and what determines this outcome (Oskar Kowalewski, 2010). Using a sample of multinational banks and their subsidiaries in a large number of countries, this study shows that, on average, foreign subsidiaries are less profitable than their parent banks. However, the results show that foreign subsidiaries tend to perform better than their parent banks if they are well capitalized, have low overhead costs and loss low provision. I find also show that foreign subsidiaries tend to perform better than their parent banks if the latter are underperforming in the home market. While, the legal distance between host country and host country is an important determinant of the profitability of the subsidiary in relation to its parent bank, to a lesser extent, are the host market's characteristics. Finally, foreign banks are more likely to outperform parent banks in developing markets than in developed countries. However, different bank and host country determinants influence the profitability of the subsidiaries in these countries. Further, the foreign banks in the region have higher liquidity ratio in their portfolio compared to the local banks (Felix Lazaro, 2012). Liquidity ratio is the ability of banks to pay off their short term debts obligations. In Kenya, foreign banks' liquidity ratio accounted to m0.34 while that of the local banks accounted for 0.33. In Tanzania foreign banks accounted for 0.50 while local banks accounted for 0.33 liquidity ratio. Foreign banks in Rwanda recorded 0.39 liquidity ratios and local banks recorded 0.33. However, it was only in Uganda where the local banks recorded a higher liquidity ratio of 0.41, leaving behind foreign banks those 0.40 liquidity ratios.

1.1.3 Multinational Banks in the EAC

Some of the well known MNB's in the EAC includes Barclays Bank, Standard Chartered Bank, Kenya Commercial Bank, CFC Stanbic, Citi Bank, Diamond Trust Bank, etc. The good performance of Multinational banks has led to the development of a global market that has spurred economic growth across nations. These banks have taken advantage of the investment opportunities that comes with the integration and has thus spread rapidly. Foreign banks in Uganda constitute about 79 per cent of the market share, 54 per cent in Rwanda, 50 per cent in Tanzania and 45 and 41 in Kenya and Burundi respectively. The impact of this on market segmentation is obvious. The dominant position makes it difficult for local banks to compete with foreign banks that typically gave access to lower cost financing and more superior technology from parent banks in home countries (Felix

Lazaro, 2012). Despite the fact that MNB's are performing well in East Africa, they are plagued by credit information problems which lead to increased transactions costs, often to such an extent that potential borrowers are denied access to credit in the formal sector. (Tumusiime-Mutebile, 2011).

1.1.4 Emergence of Credit Reference Bureaus in Africa

The African financial market has emerged globally as having the highest growth opportunity. As most of the African countries did not have the right laws in place to accommodate credit reference bureaus, it posed a serious risk of default by the MNB's customers. To eliminate this risk, firms have had to offer the finance facilities at very high interest rates to caution themselves from this risky operating environment. Impairment costs grew higher thus decreasing the companies' profit, a situation that necessitated the introduction of credit rating agencies.

Credit Reference Bureau (CRB) Africa (Commonly known as CRB Africa) set foot in Africa to address the high rates of defaults that threatened Multinational Banks operating in the African states, by offering credit rating services and information sharing (CRB Africa website). CRB Africa specializes in the establishment and operations of "Closed User Group" Credit Information Sharing Mechanisms for the Financial Sectors in Africa, carefully designed to comply with the relevant confidentiality regulations (Tumusiime-Mutebile, 2011). CRB Africa has been able to build strong relationships across Africa with numerous local and international banks, credit card companies, and financial institutions by converting their non-performing loans, levering the recover of bad debts and reducing future credit risks, through the provision of verifiable, proactive credit report information.

Currently, this is the leading rating Agency in Africa, with a wide base for its services in South Africa, Mauritius, Nigeria and Cameroon. Recently, the Agency was able to penetrate to Tanzania, Uganda and subsequently to Kenya in 2009 (CRB Africa website). To achieve real benefits of the credit reference bureau in Africa, there is need for the composition of a professional body, with an international network and reputable Global affiliates, to provide hundreds of subscribers both regionally and internationally, with both proactive and reactive solutions to credit risk management through a comprehensive range of services.

1.1.5 Credit Reference Bureaus in the East African Community

The East African community member counties include Kenya, Uganda, Tanzania, Burundi and Rwanda. Uganda was the first country in the EAC to have a private credit bureau, which began operation in May 2008 under the Compuscan Company. In his speech, (Tumusiime-Mutebile, 2011) the Central Bank of Uganda Governor pointed that all supervised financial institutions i.e. commercial banks, credit institutions and deposit taking microfinance institutions are participating. The Credit Information Sharing mechanism was launched in Kenya following the gazetting of the Banking (Credit Bureau) Regulations, 2008 on 11th July 2007. The Regulations were issued pursuant to an amendment to the Banking Act passed in 2006 that made it mandatory for the Deposit Protection Fund and institutions licensed under the Banking Act to share information on Non Performing Loans through credit reference bureaus licensed by the Central Bank of Kenya. In addition, the amendment to the law also provides for sharing of information on Performing Loans (Jared Getenga, 2011).

The Bank of Tanzania has announced plans to establish a Credit Reference Bureau which should be operational by the end of year 2012. It is hoped that more information for lenders will reduce loan defaults, lower interest rates and increase access to credit (Sarah Collier, 2011). The first credit reference bureau Rwanda was officially launched in 2010. Credit Reference Bureau (CRB) Africa, which was cleared by the National Bank (BNR) in February 2010 to start its operations, works together with banks to gather information on loans and borrowers, in order to allow financial institutions to be better informed about persons or organizations that request credit (Francois Kanimba, 2010). The BNR governor for his part expressed his satisfaction with this new evolution in financial mechanisms, and said that the establishment of such a financial information center will constitute a significant support to business. The bureau would help tackle one of the big challenges of the Rwandan banking sector, which are non-performing loans. CRB will not only greatly reduce the risk of giving out such loans, but will also save banks time and money which in the past was spent on loan recovery. Burundi remains the only country in the EAC without a Credit reference Bureau.

1.2 Research Problem

Credit bureaus cannot function without a reliable identifier for each person in a database. It is estimated that up to 20 percent of Kenyan national identification cards are forged, whilst in Uganda and Tanzania there are no national identity cards. This accounts for substantial losses for banks. To promote the availability of credit information at both the national and regional level, it would be useful if an EAC model law on credit information and credit bureaus were to be prepared and made part of the protocols covering the implementation of the EAC common market, allowing licensed financial institutions in all EAC member states the same rights to access credit bureau databases in all members of the EAC (*Mark Tomlinson,2007).* One of the problems critical to the economists is to identify the influence of credit information sharing and credit rating agencies in determining the key economic indicators i.e. lending rates, inflation rates and employment levels.

MNB's, being the Credit Providers in EAC have over the last two years, expressed great interest in the future of Credit Information Sharing. Enhanced financial access arises whenever information collateral is built into credit decisions. The outcome is: fewer mistakes by lenders; less default by borrowers and appropriate pricing of credit. Today, with the collaboration of the Central Banks of the EAC, there is functional credit reporting systems that enables all commercial banks share default information through licensed credit reference bureaus per country. The macro-economic benefits of this mechanism can only be achieved when the entire credit market participates (Sarah Collier, 2011). Prior studies that have been done show that the lending rates affect the performance of financial institutions. Mwindi (2002) in his study on the relationship between interest rates charged by MFIS and performance of micro and small enterprises in Nairobi found out that high interest rates hinders financial performance of the Microfinance institutions. Kithinji (2010) in her research on credit risk management and profitability of commercial banks in Kenya observed that the credit information gathered will guide the bank in assessing the probability of borrower default and price the loan accordingly. She did not look at the effects of Credit information to the overall bank performance.

In her study, Gatwiri (2011) on the determinants of lending rate of commercial banks in Kenya observed that the interest of economists is to know the determinants of lending interest rates, and that there is a gap in literature on the various factors that determine the interest rates among commercial banks. Looking at the emphasis that is laid on the determinants of the Lending rates for the commercial Banks, there is a research gap on the level of contribution of Credit Reference Bureaus to the determination of lending rates, and its impact to the performance of MNB's after the full establishment of the EAC. Further, ability to pay utility bills and credit cards on time should contribute to the determination of customer's creditworthiness. The time is ripe to introduce sharing of performing and non performing loan data so that good borrowers can use their profiles to negotiate lower interest rates with lenders and bad borrowers to pay high interest rates to compensate for the good borrowers.

1.3 Research Objectives

To identify the influence of a standard credit reference bureau (CRB) on the performance of multi-national banks in the East African Community (EAC).

1.4 Value of the Study

This analysis will help the multinational financial firms in the EAC market understand the implications of market integration and take appropriate measures that will guard their organizations from collapse, credit crunch and management of bad debts. As credit reference bureaus collect, manage and disseminate customer information to lenders within a provided regulatory framework, MNB’s managers will understand the positive and negative impacts of credit ratings on their decisions. Potential international investors who may want to channel their funds for investment in the EAC will benefit from a greater variety of risk-return profiles for making investment decisions.

The Government and financial policy makers will benefit from this study as they will gain insight on the impact of credit ratings on the key economic indicators such as lending rates, inflation rates etc, thus will be able to formulate policies that will enable financial institutions determine effective lending rates and manage inflations. Fund managers who act as custodian and managers of the funds will benefit from knowing the high risk areas of investments for their firms thus determine their credit appetite and establish future market forecasts. Researchers will benefit from documented information into the overall impact of credit reference bureaus in the development and growth of the EAC with the understanding of the international operating environment. Academicians will benefit from the findings of this study as it will add to the body of existing knowledge in Multinational Banks and credit reference Bureaus. The results will demonstrate the need for a standard credit reference bureau and its influence to the growth and development of the multinational firms operating in the EAC.

CHAPTER TWO

LITERATURE REVIEW

2.1 Introduction

Multinational banks in the EAC are plagued by credit information problems which lead to increased transactions costs, often to such an extent that potential borrowers are denied access to credit in the formal sector. The adverse consequences of information imperfections for financial markets were analysed in the 1970s by Joseph Stiglitz and George Akerlof; work for which they received the Nobel Prize (Tumusiime-Mutebile, 2011). The etymology of the word “credit” is the Latin verb “credere”; to trust or believe. Unfortunately trust alone is rarely sufficient to ensure that a creditor will ever get her money back; hence credit decisions must be made on the basis of accurate and reliable data. Without such data creditors will be reluctant to risk their money. A key challenge for policy makers concerned with financial market development is how to design policy interventions which can mitigate informational imperfections and thus reduce their negative externalities.

The lack of credit information results in high lending and default rates for loans, as lenders cannot establish which borrowers are creditworthy and which are likely to default on loans. This puts small and start-up businesses at an immediate disadvantage as large business may find their creditworthiness easier to prove (Sarah Collier, 2011). For instance, some banks provide loans only to businesses that have been established for a number of years. High lending rates also mean credit is out of reach for much of the economies population. The kernel of the challenge is how to ensure that accurate and reliable information about those which wish to raise finance can be acquired in a cost effective manner by those who provide finance and bear the risk of doing so. Credit Reference Bureau provides an institutional solution to the problem.

A well functioning Credit Reference Bureau mitigates information related market failures because it is compulsory for all participants in the credit markets to provide and share information, in circumstances where they may have private incentives not to do so. Furthermore, the pooling of information in a CRB reduces the social costs of acquiring information. This was the motivation for the Bank of Uganda, and with the support of development partners such as KfW, GTZ and the World Bank, to introduce a Credit Reference Bureau in their country. (Tumusiime-Mutebile, 2011).

In the recent past, Multinational banks have identified enormous investment opportunities in the African economies, due to the increased credit appetite by the large number of foreign investors. To meet this growing demand, Multinational banks have tremendously grown their loan book to a great extent. Their operating decisions such as borrowing are decentralized within the firm to subsidiary operations in each country thus creating challenges on lending. Multinational banks have classified lending as a potential risk, as they are often challenged by increasing bad debt rates. To counter this lending risk, multinational banks have welcomed the idea of credit information sharing and rating, as the absolute mechanism to reduce the bad debt and impairment rates that often decrease their operating profits. Credit information sharing and rating is done by authorized rating agencies usually called Credit Reference Bureaus (CRB).

2.2 Credit Reference Bureaus

Credit bureaus, also known as credit reference agencies, are institutions that collect details on a commercial or individual borrower's obligations from a variety of sources, including - for individuals - banks, credit card companies, and retail lenders, or - for businesses - public sources, direct investigation, and suppliers. Once collected, the data is then cross-checked and merged to produce a comprehensive credit report which can be used by potential creditors. A credit history report can contain negative information, that is information on defaults, or both negative and positive information, containing details on all open and closed credit accounts, credit amounts, and repayment behavior (Mark Tomlinson,2007). Credit reference bureaus is an institution that offers judgments or opinions about the quality of credit extended by financial institutions. These Bureaus not only provide information on the creditworthiness of individuals but can also act as a reference point for the credit rating agencies, in order to achieve its full benefits. (Christopher Cox ,2007) noted that it is useful to review the history of credit rating agencies and their role in the financial markets. These credit ratings have always been used to distinguish among grades of debt creditworthiness since early last century. (Gautam & Randall, 2003) observed that one of the fundamental economic problems faced by developing countries is the difficulty in mobilizing funds to increase investment.

The level of income is often too low to generate sufficient savings, and the domestic financial system often does a poor job of directing those funds back into domestic capital formation. This makes access to international capital markets an important resource for obtaining funds to raise the level and accelerate the pace of investment and growth. Access to information on credit histories and on registered assets used as collateral helps lenders assess the creditworthiness of potential clients. Although a credit history is not a substitute for risk analysis, when banks share credit information, loan officers can assess borrowers' creditworthiness using objective measures. And if lenders are also reassured by strong creditors' rights, they can take greater, well-informed risks. This in turn can facilitate access to financing, particularly for small and medium-size businesses.

Where collateral laws are effective and credit registries are present, banks are more generous in extending loans. Doing Business measures the legal rights of borrowers and lenders and the scope and quality of credit information systems (John Burton & Janamitra Devan, 2010). Many small and medium-size companies do not have access to formal credit and have to rely on personal funds and operating profits. This is particularly true in developing economies. Many of these smaller firms were hit hard by the financial and economic crisis as demand for their products fell. In this environment, improving access to credit by strengthening the regulatory environment is even more important.

Encouraging the sharing of information through credit registries or bureaus and strengthening the legal framework related to collateral are two ways to make it easier to get credit. Economies that rank high on the ease of getting credit typically have credit bureaus that share information on individuals and firms and include both positive and negative credit information obtained from banks, credit unions, microfinance institutions, retailers and utility providers (John Burton & Janamitra Devan, 2010). They tend to have bureaus that do not limit coverage to large loans and that provide historical information on borrowers, and generally guarantee the right of borrowers to inspect their data.

In addition, these economies have a legal framework that encourages lending by financial institutions to the private sector. Their laws ensure secured creditors' rights through a registration mechanism for secured interests allow out-of-court enforcement of security rights and protect secured creditors during insolvency processes.

2.3 Performance of Multinational Banks

This chapter examines the factors that determining the performance of the MNB's such as geographic distance between subsidiaries of multinational banks and their headquarters, availability of market information, availability of loanable fund and the presence of foreign investors in the home countries. Using various performance indicators of 340 subsidiaries in 54 emerging and developing economies from 69 global banks during the years 1994–2008, we find evidence that first, the distance constraint adversely affects loan growth, profitability, and performance of foreign bank subsidiaries, and second, the unfavorable information asymmetry faced by foreign banks, due to the distance constraint in financing foreign clients cannot be fully overcome by establishing their presence abroad. (Ji Wu, Bang & Alina, 2010). We further examine if the effect of distance is symmetric across different banks and countries and find the following various economic, financial, and institutional factors to affect the strength of distance constraints in the multinational banking activities.

The entry mode of foreign banks, the history of presence in local markets, the existence of credit information institutions, the cultural similarity between the home and host markets, financial depth, financial crisis periods, the stock market development, the banking market structure in host markets, and the hierarchy of the subsidiary in the multinational banking conglomerate largely affect the performance of MNB's. Generally, foreign subsidiaries outperform their parent banks in terms of profitability. Using a sample of multinational banks and their subsidiaries in a large number of countries, this study shows that, on average, foreign subsidiaries are less profitable than their parent banks. However, the results show that foreign subsidiaries tend to perform better than their parent banks if they are well capitalized, have low overhead costs and loss low provision (Oskar Kowalewski, 2010). I find also show that foreign subsidiaries tend to perform better than their parent banks if the latter are underperforming in the home market. While, the legal distance between host country and host country is an important determinant of the profitability of the subsidiary in relation to its parent bank, to a lesser extent, are the host market's characteristics. Finally, foreign banks are more likely to outperform parent banks in developing markets than in developed countries. However, different bank and host country determinants influence the profitability of the subsidiaries in these countries.

Further, the foreign banks have higher liquidity ratio in their portfolio compared to the local banks (Felix Lazaro, 2012). Liquidity ratio is the ability of banks to pay off their short term debts obligations. In Kenya, foreign banks' liquidity ratio accounted to 0.34 while that of the local banks accounted for 0.33. In Tanzania foreign banks accounted for

0.50 while local banks accounted for 0.33 liquidity ratio. Foreign banks in Rwanda recorded 0.39 liquidity ratios and local banks recorded 0.33. It was only in Uganda where the local banks recorded a higher liquidity ratio of 0.41, leaving behind foreign banks those 0.40 liquidity ratios.

2.4 Multinational Banks in the East African Community

While Africa has taken some steps toward regional financial integration, many of the benefits seem to be elusive. Several concerns engulf the factors that lead to the success of the MNB's in the EAC, such as; what aspects of financial sector integrations have the regions attained, and what should be prioritized among that which remains? What financial reforms should be undertaken? , What financial regulations, infrastructure and instruments should be tapped to deepen the financial sector and drive shared economic growth? Regional economic communities in Africa frequently focus upon the long term goal of a monetary union and prioritize convergence criteria, marginalizing discussions on banking supervision, payment systems, credit information and other pieces in the backbone of financial system (Mark Tomlinson,2007). Yet the regionalization of these elements can offer significant gains either in conjunction with or in absence of a monetary union.

For the MNB's, setting up the credit bureau is only the first step in a successful reform. In many economies credit bureaus have the capacity to collect more information but lack the legal backing to do so. Reformers need to create the regulatory framework that will allow the sharing of data and foster trust in the system by both banks and borrowers. This often requires adopting a new credit bureau law or amendments to existing banking and data protection laws. Most of the EAC economies took this step in 2008/09. Including credit information from retailers and utility companies such as electricity providers and mobile phone companies is an effective way to increase coverage. But this is among the harder aspects to reform because these companies often are regulated by different institutions than financial companies are. Only 40% of bureaus include information from non-banking sources (John Burton & Janamitra Devan, 2010). Yet positive information on payment of electricity and phone bills can help establish a good credit history for those who need it the most—women and youth, many of whom have had no contact with the banking sector before requesting a business loan.The EAC banking sector has already achieved a high degree of integration within the region, and this trend is continuing (Mark Tomlinson,2007). Multinational banks in the EAC generally view moves towards further integration in a positive light, and expect regulatory harmonization to offer additional opportunities to reduce costs by eliminating the duplication of legal entities and the costs of having three sets of regulators. MNB’s in the EAC includes Barclays Bank, Standard Chartered Bank, Kenya Commercial Bank, CFC Stanbic, Citi Bank, Diamond Trust Bank etc.

Most of these banks have taken advantage of the investment opportunities that comes with the integration and has thus spread rapidly. Foreign banks in Uganda constitute about 79 per cent of the market share, 54 per cent in Rwanda, 50 per cent in Tanzania and 45 and 41 in Kenya and Burundi respectively. The impact of this on market segmentation is obvious. The dominant position makes it difficult for local banks to compete with foreign banks that typically gave access to lower cost financing and more superior technology from parent banks in home countries (Felix Lazaro, 2012). Despite the fact that MNB's are performing well in East Africa, they are plagued by credit information problems which lead to increased transactions costs, often to such an extent that potential borrowers are denied access to credit in the formal sector (Tumusiime-Mutebile, 2011). This has led to the need for standard credit reference bureaus to solve the current and future related challenges of full integration of the EAC. When a government agency imposes cost-based taxes/ regulations on a MNB with private cost information, it may initiate countervailing regulations by another of the governments with which the MNB's interacts. In this study, we will analyze the problem of optimal regulation of MNB's under incomplete cost information (via trade taxes) by multiple governments as a problem of common rating agency with adverse selection (Eric W. Bond & Thomas A. Gresik, 1999). By focusing on the game played by the competing governments and its effects on credit ratings, we characterize the equilibrium trade taxes and show that the non-cooperative behavior of the governments not only reduces aggregate national welfare but also reduces firm profits.

2.5 Emergence of Credit Reference Bureaus in Africa

Middle East and North African countries have seen a growing interest in credit reporting, and Tunisia, Egypt and Morocco successfully reformed their credit information system in 2006. As for Sub-Saharan Africa, with the exception of South Africa, only eight countries have any public or private bureau coverage (Mark Tomlinson,2007). However, between 2002 and 2007, important legal changes were made to enable private credit bureau operations in Ghana, Uganda, Tanzania and Zambia, and at least three private credit bureaus were established in Nigeria. Several countries, including Mozambique, Angola, Madagascar, and Mauritius have initiatives to develop credit reporting. A major challenge in developing credit reporting in Africa is the small size of the credit markets, as credit bureaus rely on economies of scale to cover their large up-front investment through the sale of credit reports.

Another important challenge is often the lack of national IDs, the absence of physical addresses, or variations in names. It is estimated that up to 20 percent of Kenyan national identification cards are forged, whilst in Uganda and Tanzania there are no national identity cards. The use of biometric identification, such as has been recently implemented in Uganda, promises to provide a valuable solution to borrower identification problems. Credit bureaus are critical to the expansion of credit in any economy, as they overcome some of the information asymmetries that prevent lenders from assessing risk profiles (Sarah Collier, 2011). On the one hand, credit histories ease adverse selection problems as they allow good creditors to establish reputational collateral (where complete information is recorded). On the other hand, they reduce moral hazard by recording negative financial behavior, thereby improving repayment and default rates (Mark Tomlinson, 2007). The consequent expansion of lending volume is particularly beneficial to generally underserved economic actors, such as micro, small and medium enterprises

Economies that rank high on the ease of getting credit typically have credit bureaus that share information on individuals and firms and include both positive and negative credit information. They tend to have bureaus that do not limit coverage to large loans and that provide historical information on borrowers (John Burton & Janamitra Devan, 2010). CRB Africa is a professional body currently providing hundreds of subscribers with both proactive and reactive solutions to credit risk management through a comprehensive range of services (Sarah Collier, 2011). It has a presence in over 12 countries in Africa and covers East, West, North and Southern Africa through its respective country offices. Through its global network of credit information organizations and affiliates, CRB Africa ensures best possible service delivery for its clients, whether regional or abroad through its wide network and reputable global affiliates, thus able to meet serve its in over 104 countries worldwide.

2.6 Credit Reference Bureaus in the EAC

The East African community member counties include Kenya, Uganda, Tanzania, Burundi and Rwanda. Uganda was the first country in the East Africa to introduce a credit reference bureau. Kenya and Rwanda followed and introduced private credit information bureaus, and Burundi has a government run credit bureau. Tanzania is the only EAC state without a credit bureau but in the process of establishment to streamline financial practices with the rest of the EAC. Uganda was the first country to have a private credit bureau, which began operation in May 2008 under the Compuscan Company. In his speech, (Tumusiime-Mutebile, 2011) the Central Bank of Uganda Governor pointed that all supervised financial institutions i.e. commercial banks, credit institutions and deposit taking microfinance institutions are participating. A total of 640,000 financial cards have been issued to the customers of financial institutions; these are all borrowers or prospective borrowers. Nearly 50,000 credit enquiries are made to the Credit Reference Bureau every month. Great progress has been achieved and strong safeguards have been built into their system, stipulated through regulations issued by the

Central bank of Uganda, to protect the accuracy and confidentiality of information given to the Credit Reference Bureau and to ensure that it is only used for the purposes for which it is intended.

In Kenya, The Credit Information Sharing mechanism was launched following the gazetting of the Banking (Credit Bureau) Regulations, 2008 on 11th July 2007. The Regulations were issued pursuant to an amendment to the Banking Act passed in 2006 that made it mandatory for the Deposit Protection Fund and institutions licensed under the Banking Act to share information on Non Performing Loans through credit reference bureaus licensed by the Central Bank of Kenya. The amendment to the law also provides for sharing of information on Performing Loans (Njuguna Ndung'u, 2012) . To date, two credit bureaus have been licensed by the Central Bank, namely CRBAfrica Limited and Metropol CRB. This was the culmination of many years of deliberations between the Kenya Bankers Association (KBA), the Central Bank of Kenya (CBK), the Ministry of Finance and the office of the Attorney General aimed at finding a solution to various challenges facing the lending environment in Kenya.

Credit Providers in Kenya have expressed great interest in the future of Credit Information Sharing (Jared Getenga, 2011). Enhanced financial access arises whenever information collateral is built into credit decisions. The outcome is fewer mistakes by lenders, less default by borrowers and appropriate pricing of credit. The Banking fraternity has so far been at the forefront of introducing this important reform in the credit market. Today, with the collaboration of the Central Bank of Kenya, there is a functional credit reporting system that enables all commercial banks share default information through licensed credit reference bureaus. The Central Bank of Tanzania is currently adopting plans to establish a Credit Reference Bureau. It is hoped that more information for lenders will reduce loan defaults, lower interest rates and increase access to credit. One of the major problems of doing business in Tanzania is thought to be the difficulty in accessing credit (Sarah Collier, 2011). Tanzania is East Africa's second biggest economy, but the World Bank ranks it fourth in East Africa for ease of doing business. Access to credit remains one of the greatest barriers to Tanzania's economic development. It represents one of the biggest challenges in African countries generally, and only a few people have access to bank accounts or savings. The time has come to make two more important steps in moving CIS forward (Jared Getenga, 2011). The first critical step is to extend the benefits of CIS to good borrowers.

Clearly, the time is ripe to introduce sharing of performing loan data so that good borrowers can use their profiles to negotiate terms with lenders. The other critical step is to extend this mechanism to all other credit providers. The macro-economic benefits of this mechanism can only be achieved when the entire credit market participates. .

The first credit reference bureau Rwanda was officially launched in 2010. Credit Reference Bureau (CRB) Africa, which was cleared by the National Bank (BNR) in February 2010 to start its operations, works together with banks to gather information on loans and borrowers, in order to allow financial institutions to be better informed about persons or organizations that request credit (Francois Kanimba, 2010). The BNR governor for his part expressed his satisfaction with this new evolution in financial mechanisms, and said that the establishment of such a financial information center will constitute a significant support to business. The bureau would help tackle one of the big challenges of the Rwandan banking sector, which constitutes non-performing loans (Fred Ojiwa, 2010).

Burundi has no credit reference Bureau, though the government has set up its regulations to include credit information sharing. The CRB is likely to reinforce these positive trends, but the real effects of the introduction of the CRB may end up being further progress towards the East African Community (EAC) rather than easier access to credit. Thus, there have been calls to introduce a standard CRB for the whole of the EAC as part of the process of streamlining economies and regulations which is yet to commence.

2.7 The impact of Credit reference bureaus MNB's in the EAC

To remain competitive, CRB worldwide must not stand on their laurels; they must introduce innovative services to meet the evolving needs of their clients. For example, Compuscan Credit Reference Bureau in Uganda is currently introducing a Credit Scoring System which is intended to facilitate quicker and better decision making by the participating financial institutions (Tumusiime-Mutebile, 2011). The impact of credit rating or scoring agencies on financial markets has become one of the most important policy concerns facing the international financial architecture. Ratings indicate a relative credit risk and serve as an important metric by which many investors and regulations measure credit risk. The poor performance of these agencies and the sudden collapse of large financial institutions have brought renewed criticism of their methods, regulatory status and role in financial markets.

Prior to this independent source of information, banks played a key role in shaping investor perceptions of corporate borrowers. After all, banks had greater knowledge from the inside information they obtained in their role as direct lenders and as bond underwriters. By lending and underwriting, banks were putting their money and reputations on the line. If the borrower failed to meet its obligations, the reputation of the bank would be damaged and that would make it harder for the bank to retain existing and attract new clients. In essence the bank certified the quality of the bonds to the public with the bank's reputation. Alternatively, the bank as creditor would become more involved in the business of the corporation and become an insider (Ji Wu, Bang & Alina, 2010). There were no disclosure requirements prior to the securities acts of 1933 and 1934. This created an asymmetry in the availability of information in the U.S. capital markets. The impact of rating agencies was to help level the playing field and improve the efficiency of capital markets. The role of CRB would solve other asymmetric information problems between investors and asset managers (Ji Wu, Bang & Alina, 2010). The use of credit ratings help police the conflicts of their interests and of clients whose money, the managers invest. Asset managers may be tempted to invest in higher risk securities even though investors would unknowingly approve them. The use of ratings by investment policies can limit the risk in the asset manager's investments at a low monitoring cost and thus benefit investors. Although agencies officially state that they look at a large array of factors when assigning ratings to sovereign borrowers, studies have shown that most ratings can be determined by a few economic variables. (Cantor and Packer, 1996) found that more than 90% of the cross-sectional variation in country ratings could be attributed to six factors: per capita income, GDP growth, external debt burden, inflation experience, default history and level of economic development.

These results leave out crucial variables i.e. capital flows and foreign exchange which could provide a possible explanation of why rating agencies fail to forecast crises. (Antonio Alfonso,2003) conducting a similar study argues that GDP per capita is virtually the only relevant economic variable for determining developing countries' ratings. Credit ratings and regulation also impacts the creation and sustainability of jobs. The central banks can create rating agencies compliance jobs at the expense of jobs that are more highly valued by the market (Ji Wu, Bang & Alina, 2010), i.e. consumers. Economists refer to this as misallocation of resources, when capital and labor are directed to less productive or unproductive uses and have real consequences on the economy. Bad policies can increase total jobs, and good policies can decrease total jobs.

CHAPTER THREE

RESEARCH METHODOLOGY

3.1 Introduction

This chapter presented the research design, sampling methods, and techniques that were used in data collection and analysis and the methodology that was used to carry out the study. This included the study design, target population, data collection tools and techniques, and data analysis method and presentation.

3.2 Research Design

This study used a descriptive survey which attempted to describe or define a subject, often by creating a profile of a group of problems, people, or events, through the collection of data and tabulation of the frequencies on research variables or their interaction, (Cooper and Schindler, 2006). In this case, the research problem was the impact of a standard credit reference bureau (CRB) on the performance of multinational banks in the East African Community (EAC) market.

Descriptive research was more rigid than an exploratory research and sought to describe the uses of a product, determined the proportion of the population that used a product, or predicted future demand for a product. This descriptive research defined questions, people surveyed, and the method of analysis used prior to beginning data collection.

3.3 Population of Study

In this study, the target population was the specific population about which information was desired. According to Ngechu (2004), a population is a well defined or set of people, services, elements, events, group of things or households that were being investigated. The population of this study consisted of several multinational banks which were in operation in the EAC market, at the time of study.

3.4 Data collection

The study used both primary and secondary data sources in gathering data for analysis. The primary data was collected using semi-structured questionnaires. Questionnaires were considered to collect qualitative data because they were cheap, respondents were given time to fill-in the questionnaires, they did not require as much effort from the questioner as verbal or telephone surveys, and often had standardized answers that made it simple to compile data. The questionnaires were both open and close-ended questions (Munn and Drever, 2004) and were administered through drop and pick to Credit managers, Product managers and financial managers from the sampled multinational banks in Kenya and through electronic mails to those outside Kenya.

Secondary data was collected from journals and reports from World Bank, IMF, Commercial banks and Central Banks of the 5 countries in the EAC, regarding the impact of the CRB on the performance of the multinational banks for the last 3 years from 2009 - 2012.

3.5 Data Analysis

The collected data was thoroughly examined and checked for completeness and comprehensibility. The data was then be summarized, coded and tabulated. Descriptive statistics such as means, standard deviation and frequency distribution were used to analyze the data, which was then coded and entered into the Statistical Package for Social Sciences (SPSS 17) for analysis. SPSS was used to perform the analysis as it aided in organizing and summarizing data by use of descriptive statistics such as tables.

Data presentation was done by the use of bar charts and graphs, percentages and frequency tables. The inferential statistic regression and correlation was performed on the data to establish the extent to which the standard credit reference bureau (CRB) impacted on the performance of multi-national banks in the East African Community (EAC) market.

CHAPTER FOUR

DATA ANALYSIS, RESULTS AND DISCUSSION

4.1 Introduction

In this chapter, I discussed the interpretations and presentations of the findings based on the objective of the study which was to establish the influence of a standard credit reference bureau (CRB) on the performance of multi-national banks in the East African Community (EAC) states. This chapter focused on data analysis, interpretation and presentation and presents the discussion and conclusion of the study. The sample frame of my study was 5 multinational banks with the total population study composed of 8 correspondents from each bank i.e. 2 Credit Managers, 2 Management Information analysts popularly known as MI Analysts in Banks, 2 Risk managers and 2 Finance analysts. 28 respondents responded and returned the questionnaires constituting to 85% response rate. Gatwiri (2010) indicated a respondent rate of 50%, 60% or 70% is sufficient for a study and therefore a respondent rate of 85% for this study was impressive.

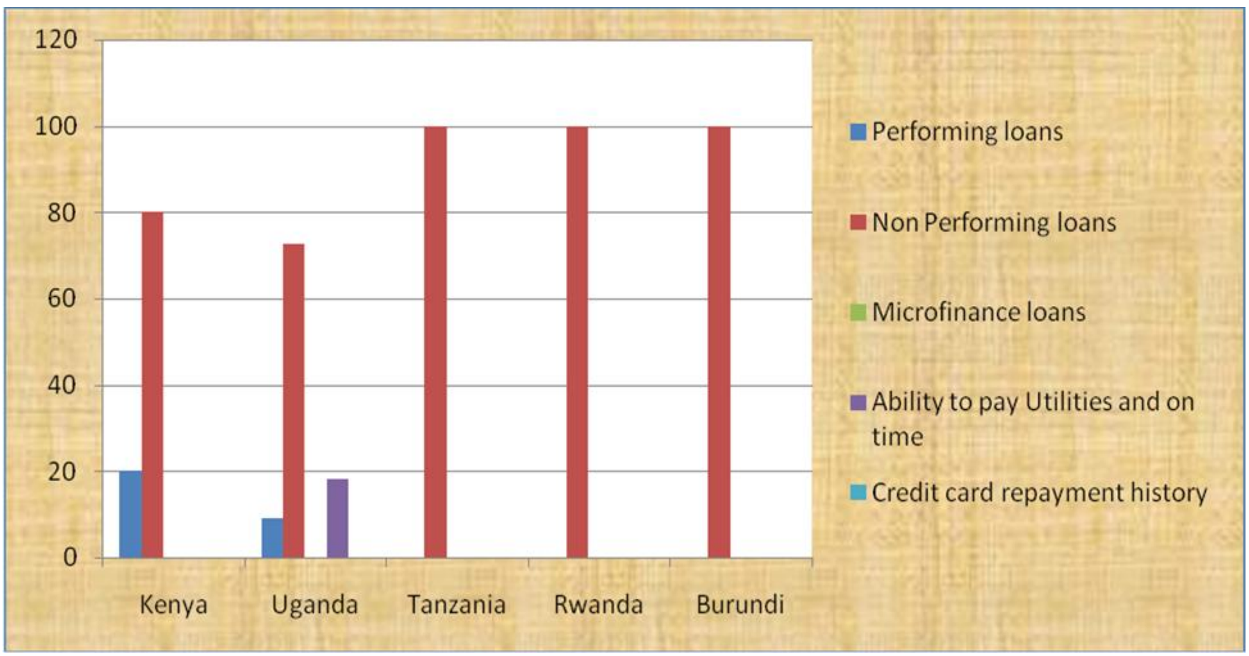
4.1.1 General information

The regulatory authority of the Credit reference bureau in each country is the Central Bank. The respondents from Uganda indicated that there is only one credit reference bureau operating under the registered name, CompuScan Credit Reference Bureau under the supervision of the Central bank of Uganda. In Kenya, the respondents noted that the CRB Africa was the first to be registered and operate, and with time, the Central Bank of

Kenya authorized Metropol CRB to further carry out the business. In Rwanda, the CRB Africa is the only credit reference bureaus authorized by the National Bank of Rwanda (NBR). In Tanzania, the respondents indicated that Information is already streaming in to set up the credit reference bureau, and the banks are already utilizing the facility, though at the very initial stages. Burundi has a government run credit reference bureau which is already in full operation.

4.1.2 The Types of Information collected by different CRB's in EAC.

Figure 4.1 Types of Information collected by different CRB's in EAC.



Source: Analysis from Questionnaires

This study sought the type and extent of information collected by various credit reference bureaus. From the findings most CRB's consider non performing loans as the greatest factor affecting the determination of credit rating in the five East African States.

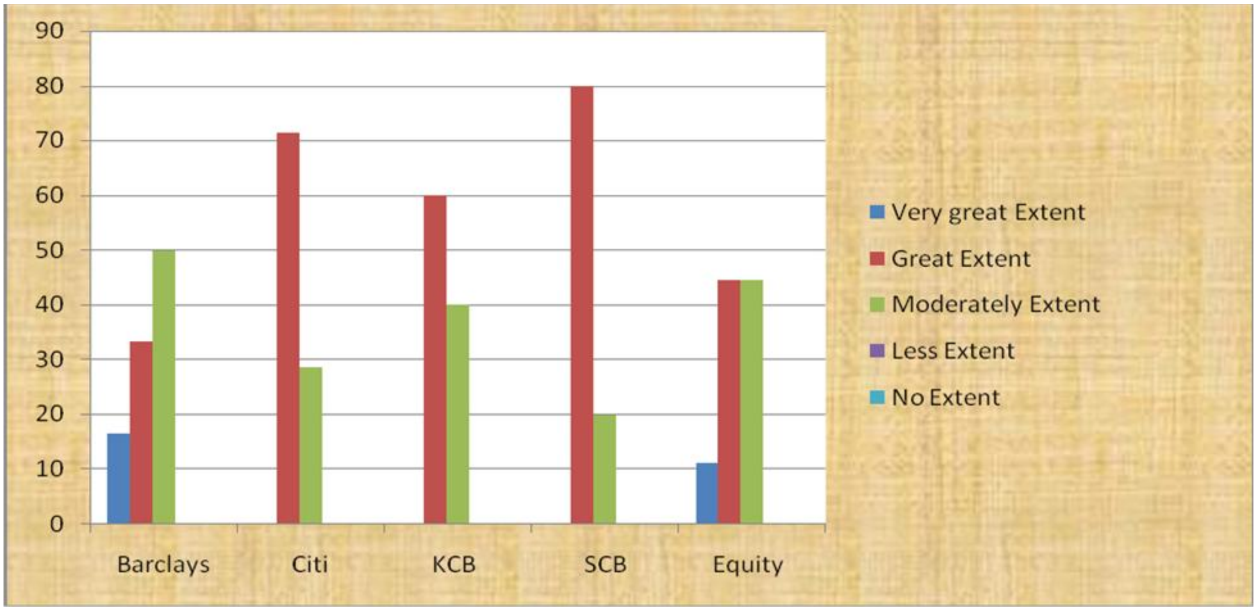
The study further found out that other factors such as performing loans are taken into consideration in Kenya and Uganda only. However, there is no real benefit and value in collecting this information as it does not lead to any benefits to the borrower of funds. In Uganda, there have been constant attempts to include factors such as ability to pay utility bills on time though the benefits are yet to be realized. Other factors critical to lending i.e. ability to repay micro finance loans, SACCO loans and credit card repayment history which would greatly add value to the credit ratings for the borrowers have not taken into consideration. This implied that economic factors in the market such as the credit ratings is largely dependent on one factor, and this leads to decisions aimed only to punish bad borrowers of funds without rewarding the good borrowers of funds.

4.1.3 The value of information collected by CRB to the decision making process.

The respondents were requested to indicate if the information collected by the credit reference bureaus adds value to the banks decision making process. From the finding majority of the respondents indicated that indeed CRB adds value to the decision making process by aiding in credit scoring and loan approval processes, thus reducing the lending risk. The customer’s behavior in lending can easily be determined by checking his/her borrowing history from various institutions. This assists to institute efficient controls where the lending risk is reduced as the CRB accords comfort in lending to honest or credit worth customers. This information further ensures that defaulters do not shift from one lender to another after default. The study further found that banks can be able to identify if the customer has loan facilities with other banks that he or she has failed to disclose to the lender, and thus identify the probability of repayment. Further, by gathering and providing information on borrowers' debt profiles and repayment history, CRB aids the lenders enough information to reduce defaulting rates and thus reduce bad debts. This also gives good borrowers a chance to negotiate good deals with financial institutions. The respondents further indicated that the report has also been used to verify information about the client, such as the client name, date of birth, telephone numbers etc. This has a positive impact as decision makers are certain that the client's documents are authentic to those in the CRB, thus avoid instances of wrong listing of innocent customers or to the worst scenarios, control fraud and corruption.

4.1.4 The rate with which CRB information has influenced banks lending rate.

Figure 4.2 How the CRB information has influenced banks lending rate



Source: Analysis from Questionnaires

The study sought to identify the extent to which the type of information collected affects the determination of the lending rates, ultimately affecting the profitability of the banks. The respondents indicated that Barclays bank is affected to a moderate effect, with Citi bank, Kenya commercial bank, Standard chartered bank and Equity Bank affected to a great extent. The respondents indicated that the effect was dependent on the market segment or target clientele for each bank. In overall, more than 50% of the respondents indicated that the information affected the profitability of the bank to a great extent as this information is critical to reducing the impairment rates, a factor that is critical in the profitability line of the bank accounts. The respondents further explained that this information helps reduce bad debts and costs related to recovery, thus decreases losses. The respondents noted that this information helps to encourages good borrowers negotiate for lower interest rates.

Further, customer confidence increases leading to increased deposits thus giving the bank a golden opportunity to grow their asset book and thereby increase their lending levels. The respondents further noted that borrowers will be very efficient to repay to avoid being listed as defaulters. The respondents in Uganda noted that CRB reports are a source of information about client borrowing status, but influence the general performance of the bank. If the banks in Uganda fails to submit the monthly number of loans issued report on time(with 10 days of month end) then, the bank is fined Ugx 30,000,000/= thus directly affecting the profitability of the bank. Further, if the CRB system i.e. the Compuscan system is off, as a bank the processes are affected because the final decision cannot be made without having the financial report printed to assessment. This may be negative publicity to the banks and thus loss of loans to other banks.

4.1.5 The response rate of CRB to the Banks requests.

Table 4.1 CRB's response rate to the Banks requests

% Responsiveness	Kenya	Uganda	Tanzania	Rwanda	Burundi
Excellent	0%	0%	0%	0%	0%
Good	60%	80%	40%	50%	20%
Satisfactory	30%	10%	30%	40%	80%
Poor	10%	10%	30%	10%	0%
Total	**100**	**100**	**100**	**100**	**100**

Source: Analysis from Questionnaires

The study sought the response rate of the credit reference bureaus towards the multinational banks requests for customer information and reports. From the findings, none of the respondents in all the three countries rated the response rate as Excellent. However, 60% of the respondents agreed that there was good response in Kenya and Uganda. Some of the respondents in both countries rated the responses satisfactory and having not met their standards or needs. In Tanzania, respondents seemed to lack confidence with their reference bureau as they are not in sync with the full realization of the operations of a credit reference bureau.

This may have been occasioned by the newness of the concept in Tanzania, given that the Credit reference Bureau was launched recently. 40% rated it good, with similar rating of 30% as satisfactory and poor. In Rwanda, 50% of respondents rated their credit bureau as good and 40% satisfactory, with 10% rating it as poor. In Burundi, only 20% rated their credit reference bureau as good, with 80% rating it satisfactory.

4.1.6 The professionalism of CRB in dealing with credit information.

Table 4.2 Professionalism of CRB in dealing with credit information

Professionalism	Kenya	Uganda	Tanzania	Rwanda	Burundi
Excellent	10%	20%	0%	0%	0%
Good	60%	70%	60%	60%	55%
Satisfactory	30%	10%	30%	40%	35%
Poor	0%	0%	10%	0%	10%
Total	**100**	**100**	**100**	**100**	**100**

Source: Analysis from Questionnaires

The study sought to identify the professionalism attached to obtaining credit information by the credit reference bureaus in their states. From the findings, majority of the respondents strongly agreed that there is a good rate of professionalism attached in obtaining credit information. Corruption reports were not reported by any of the respondents indicating a good platform to the integration and establishment of a standard credit reference bureau in the EAC. Further, respondent's reported that the credit reference bureaus recruited their staff on a merit basis, and a large number recruited from the banks across the states. Uganda rated the best in professionalism with a score of 20% as Excellent and 70 % as good. The respondents were happy with the standards maintained by the credit reference bureau.

Kenya ranked second with 10% of the respondents rating it Excellent and 60 % as good. However, 30% rated the bureau as satisfactory. 60% of the respondents in Tanzania and Rwanda rated their credit reference bureau as good and a further 30% and 40%

respectively, rating satisfactory. In Burundi, 55% of the respondents rated their credit reference bureau as good, with 35% and 10% rating satisfactory and poor respectively. This clearly implied that the professionalism applied across the EAC was on average good, thus a positive report that upon integration of the EAC, there would be a good environment for setting a professional standard credit reference bureau which would positively influences lending operations and in effect affect the financial performance of the Multinational Banks.

4.1.7 The ratings of CRB's Products and services.

This study sought to provide an overview of the banks perception towards the credit reference bureaus products and services as this directly impacts to their view and operations procedures on the decision making processes.

Table 4.3 CRB's Products and services ratings

Products & Services ratings	**Kenya**	**Uganda**	**Tanzania**	**Rwanda**	**Burundi**
Excellent	0%	0%	0%	0%	0%
Good	70%	90%	80%	70%	40%
Satisfactory	30%	10%	20%	20%	50%
Poor	0%	0%	0%	10%	10%
Total	**100**	**100**	**100**	**100**	**100**

Source: Analysis from Questionnaires

The respondents rated the products and services of their credit reference bureaus in Kenya as 70% good and 30% satisfactory, with none rating the products poor or excellent. This provides a platform for various positive improvements. In Uganda, there was the best rating with 90% of the respondents indicating good products and services especially due to the wholesome nature of the information fed to the bureau, which includes ability to pay utilities and performing loans that, are currently being introduced. 10% of the respondents indicated satisfactory products and services.

In Tanzania, 80% of the respondents indicated good products and 20% satisfactory with none rating them poor or excellent. In Rwanda, 70% of the respondents rated the products and services good, with 20% and 10% rating them satisfactory and poor respectively. In Burundi only 40% of the respondents rated the products and services good, with 50% and 10% rating them satisfactory and poor respectively. The overview shows that the products and services are key in supporting the decision making process and thus can be well deemed to boost the performance of the Multinational banks.

4.1.8 Quality Measure of CRB's Products and services on the banks performance.

The study sought the extent to which the quality of CRB products and services affect financial performance of the banks. Majority of the respondents indicated that the CRB's had good quality products which met their needs and expectations regarding quality and performance.

Table 4.4 Quality Measure of CRB's Products and services

Do Products & Services quality meet banks expectations	Kenya	Uganda	Tanzania	Rwanda	Burundi
Yes	90%	90%	80%	90%	60%
No	10%	10%	20%	10%	40%
Total	**100**	**100**	**100**	**100**	**100**

Source: Analysis from Questionnaires

The respondents pointed out that this approach to quality management of products and services went way ahead to satisfy the banks needs and also the customer needs. This study indicated that on average, 90% of the entire respondents from all countries praised the appellate process. In this process, customers appeal on their credit ratings directly with the Credit Reference bureaus or the legal systems and upon proper investigations; they are awarded the rightful ratings. Further, the legal mechanisms surrounding the appellate processes are designed in a manner that no customers would be punished entirely due to their non performing loans, and that failure to make some repayments could not make them entirely miss out on credit advancements in future. Most respondents commented that those customers with bad history can also access credit, though at punitive rates thus enhancing better performance of banks.

4.1.9 Factors that affect on time delivery of credit reports and ratings.

Table 4.5 Factors that affect on time delivery of credit reports and ratings

Time delivery of reports by CRB	**Kenya**	**Uganda**	**Tanzania**	**Rwanda**	**Burundi**
Excellent	0%	0%	0%	0%	0%
Good	70%	80%	60%	70%	60%
Satisfactory	20%	10%	20%	20%	20%
Poor	10%	10%	20%	10%	20%
Total	**100**	**100**	**100**	**100**	**100**

Source: Analysis from Questionnaires

This study sought the extent to which time delivery of reports affect the decision making process and the turn around times within which the bank must make a decision to lend or not to lend. In Kenya, 70 % of the respondents were happy of the service level agreements to receive the reports. Of the respondents, 20% and 10% rated the time delivery as satisfactory and poor noting that it takes on average 3 hours to get the report from the CRB and if the payment is not done in advance i.e. the payment per application is kes 30.00 generally known as credits, this delays the turn around time, thus an inconvenience to the customer and damages the banks operational reputation too. System failures were considered a great challenge by most of the respondents as they are the major challenge in time delivery. Majority of the respondents noted that Banks are supposed to get this information on credit to avoid such eventualities.

In Uganda, 80% of the respondents were happy of the time delivery with 10% rating satisfactory and poor. In Tanzania, it takes on average 24 hours to get the credit reports 60% of the respondents rated the process as good, with 20% satisfactory and poor and noting that the automation of the process would yield better results. In Rwanda, time delivery was good as per the 70% of the respondents and that the automation of the process was doing them good. In Burundi, the laws surrounding the response modes needs to be reviewed to allow timely delivery of information to the bureau and banks.

4.2 Factors that will affect the CRB's Operations after Integration.

Table 4.6 Effect of CRB after the EAC full Integration

Will integration of EAC affect CRB's operations?	**Kenya**	**Uganda**	**Tanzania**	**Rwanda**	**Burundi**
Yes	90%	100%	80%	100%	70%
No	10%	0%	20%	0%	30%
Total	**100**	**100**	**100**	**100**	**100**

Source: Analysis from Questionnaires

The study sought to identify what the market felt and their expectations regarding the operations of the credit reference bureaus after the full integration of the EAC. In Kenya, 90% of the respondents agreed that the integration will directly affect the operations of the CRB's in each state while 10% did not agree that there would be any effect in operations. In Uganda and Rwanda, all the respondents indicated that the integration will affect the CRB's operations across the EAC. 80% and 70% of the respondents in

Tanzania and Burundi agreed that there would be effects on operations while 20% and 30% refuting the fact respectively. On average, the respondents indicated that numerous changes were bound to take effect after the integration of the EAC market. Commercial bank lending rate would now be affected by economic factors not only affecting the individual states but the entire EAC.

The respondents indicated that CRB will have a tough time to collate information from across the other credit bureaus as investors seek to obtain credit on favorable rates in different banks across the states. Inter bank competitions will advance and thus make lending rates of commercial banks rigid due to market concentration. The respondents also indicted that competition may constrain effective monetary policies and influence market pricing in determining loan and deposits rates. Most respondents indicated a need to set up a standard credit reference bureau and at least form an Umbrella credit reference bureau where all the individually accredited institutions will be feeding their data to, in order to address the credit risks.

4.3 The expected challenges of a standard CRB

The study sought to identify the expected challenges of a standard credit reference bureau to the performance of Multinational Banks in the EAC. Majority of the respondents indicated that the different legal systems in the EAC would pose the greatest challenge to the efficient running of the standard credit reference bureau. They noted that the legal systems needed to be regularized to avoid major challenges in dispute resolutions on matters of credit. Most respondents suggested on a dispute resolution committee to specifically address the issues of Credit ratings. Respondents in Uganda raised issues on the Identification of individuals as most of the population in Uganda does not have proper identification documents. Information fraud is more likely as there is an opportunity for fraudsters to duplicate identity in different geographical locations. The challenge of the National Identity cards to be used since customers may use passports or their national ids depending on the policy employed by various bank/member nations. A good example is where customers have used both old and new generation identity card or passport or military identity card to secure loans from financial institutions. It becomes difficult to trace the unique identifier since all Identity cards are in operation.

Further, respondents pointed the different modes of payments as a challenge especially due to the exchange rate differentials. Respondents indicated case scenarios where a Kenyan business man would send loan repayment amount to a Ugandan bank and fall short of the payment amount by a few coins due to change of foreign exchange rates. The study also found out that the risks in various countries might not cut across the East African Countries. Every country has their unique risks addressed by the registered credit bureaus. Respondents indicated that lack of accurate information from financial institutions on the history of borrowers and lack of co-operations between countries might be a more serious challenge. The respondents in Uganda pointed out that some banking institutions still fail to cooperate 100% and put on hold the client's financial card to hold him/her from going to transact with other banks. Some respondents revealed that lack of political will may hold back the benefits of the EAC integration and thus make the credit reference bureaus operate independently, thereby complicating the whole process.

The study further indicated that different cultures across the EAC states would cause a more serious challenge. In Kenya only, there are 42 tribes all with different cultures and equally Uganda, Tanzania, Rwanda and Burundi. Further, each country has its own unique business culture and business policies. Harmonizing all these cultures to include them in determination of credit rating would be a challenge. Respondents indicated that Standardization works on assumption of similar causes of potential risks across EAC countries hence a misleading way to tackle the risk of impairment. There is need to gather further data specific to each country depending of behavioral ways of how subjects deals with credit. Further, this study revealed that a standard CRB means almost a perfect regional management information system yet this has always proved a challenge in terms of resources and design perfection.

4.4 Key considerations to overcome the above challenges in MNB's

This study sought to propose solutions to the challenges expected to arise from the integration of the EAC. Various respondents proposed the provision of analytical information on trends in impairment. This is aimed at availing credit projections based on data extracted from a full market view, involving all banks. Respondents noted that as a central database, the Standard credit reference bureau will be the most appropriate tool to fight against non performing loans by alerting banks with statistical analysis necessary to determine whether individuals are credit worthy or not. The respondents also proposed a central system with the entire customer base with the credit ratings on boarded. This would provide an immediate identification of customers and save a lot of time and efforts that are currently there in credit decision making.

The respondents proposed numerous measures put to ensure accurate information is availed to the CRB's. Minimum errors should be recorded in reporting NPL's and penalties proposed for banks with such erroneous reports. The respondents suggested a robust way to ensure defaulters listed are properly informed, with reasons thereof, to avoid penalizing people wrongfully. Respondents suggested a robust way to regularize foreign exchange differentials on foreign borrowers. A proposal by respondents indicated that there is need to establish a common currency within the EAC to solve the foreign exchange risk scenarios.

Further, the respondents suggested the provision of trend performance of various banking institutions in EAC to aid multinational banks review their performance against the local banking institutions for improved performance. This would assist to bring better ideas in management of credit reference bureaus and further build better capacity by Seconding key individuals from the CRB abroad to the standard CRB in the EAC. This would go a long way in providing market status reports for EAC on the potential zones for doing business and also give accurate analysis basing on customer details provided whether he/she is a potential client or likely to be a defaulter. Some respondents indicated a need for cultural training to avoid the risk of intercultural business challenges. This would assist to reduce default rates as the lenders will select their market segments wisely, and design respective products depending on the cultural backgrounds of the market segments.

4.5 Regression Analysis

A multivariate regression model was applied to determine the factors influencing the adoptability of credit ratings by Multinational banks in the EAC states. The Linear regression used in this model was: Y (Credit Ratings Rates) = $\alpha + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 +$ ẹ, where

Y= Credit Ratings Rates α = Constant Term β_1= Beta coefficients

X_1= Lending rates X_2= Cost of funds $X_{3=}$ Inflation

ẹ = Error Term

Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Change Statistics				
					R Square Change	F Change	df1	df2	Sig. F Change
1	.083(a)	.698	.718	0.34	1.741	6	.207	8.191	.001(a)

Source: António A. & Raquel Ferreira, 2003

a Predictors: (Constant) Market structure**,** Cost of funds, Inflation

Dependent: Credit Ratings

Adjusted R^2 is called the coefficient of determination which indicates how credit ratings varies with variation in factors determining lending rates for Multinational banks which includes market factors**,** cost of fund and inflation. From table above, the value of adjusted R^2 is 0. 718. This implies that, there was a variation of 71.8% of lending rates with variation in factors determining lending rates of commercial banks which was statistically significance with P-Value of 0.01 which was less than 0.05 at a confidence level of 95%.

ANOVA (b)

ANOVA (b)

Model		Sum of Squares	Df	Mean Square	F	Sig.
1	Regression	3.841	5	.307	5.191	0.01(a)
	Residual	7.714	76	.059		
	Total	11.556	81			

Source: António A. & Raquel Ferreira, 2003

a Predictors: (Constant) market factors, cost of fund and Inflations

Dependent: Credit Ratings

Regression, Residual, and Total- The Total variance was the difference into the variance which can be explained by the independent variables (Model) and the variance which was not explained by the independent variables (Error). The strength of variation of the predictor values influence the determination of lending rates dependence variable at 0.01 significant levels.

Coefficients (a)

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	7.000	.375		3.640	0.01
	Market Factor	0.981	.495	.857	2.931	0.03
	Cost of fund	0.917	.646	.792	2..803	0.04
	Inflation	0.768	.428	.691	1.906	0.02

Source: António A. & Raquel Ferreira, 2003

a Predictors: (Constant) Market factor**,** Cost of fund, and Inflation

Dependent: Credit Ratings

$Y = 7.000 + 0.981\ X_1 + 0.917X_2 + 0.768X_3$-

From the above regression model, it was found that Credit Ratings of Multinational banks would be at 7.000 holding market factors, cost of funds and inflation constant at Zero. Increase in markets factors such as credit risks, competitions change in industrial trends and increase inter bank rate would lead to an increase in lending rate by a factor of 0.981 with P value of 0.003. An increase in cost of fund (loan) such as increase in management fees, taxes, salaries of staff would lead to an increase in lending rate by 0.917 while a unit increase in inflation would lead to a increase in lending factors for commercial banks by a factor of 0.768 with P value of 0.004. This would automatically translate into decreased performance. This shows that there existed a positive relationship between Credit Ratings and lending rate.

CHAPTER FIVE

SUMMARY, CONCLUSIONS AND RECOMMENDATIONS

5.1 Summary

The study revealed that majority of the Multinational banks derives significant benefits from the operations of the credit reference bureaus. The study further established that prudential regulation, effective CRB supervision and better credit policy enforcement are the most influential factors influencing the performance of multinational banks.

From the findings, the study revealed that there is need for the establishment of an effective standard credit reference bureau with well stipulated guidelines to offer credit ratings and references for the multinational banks, a well laid out legal framework, a dedicated spirit from the multinational banks and a well informed customer on the benefits of credit rating in order to gain the benefits of a EAC integration. Further, a dedicated regulatory authority would play a great role to positively settle the question of bad debt management, reduce impairment and recovery costs thus lead to a better performing multinational bank.

The study found that other than the factor of credit ratings affecting performance of multinational banks, Staff costs, inflation levels, foreign exchange rates as well as Treasury bills and bond rates, average deposit rate, reserve and liquidity requirements and mandatory investment levels required by the Central banks of the EAC states also influence the performance of multinational banks and thus should be integrated to add more value to the credit reports. The study also revealed that increased cost of loans leads to increased non performing loans as loans become more expensive to repay.

5.2 Conclusion

The study concluded that prudential regulation and effective management of the standard credit reference bureau would lead to more robust credit policy enforcement. This would have a positive impact to the performance of multinational banks as the credit risk would be much lower, recovery costs would significantly reduce, and impairment rates would significantly reduce and thus lead to better control in the operations of the organization. The overall impact would be a strong growth of the banks asset book and profitability.

The study concluded that other factors critical to boosting the standards and quality of credit ratings include addition of customer information such as the level of performing loans, the repayment history of micro finance loans, SACCO loans, Hire purchase installments, credit card repayments and the ability to pay utilities on time, would influence the banks lending rates, thus directly influence the performance of the bank. The study concluded that there existed a positive relationship between credit ratings, lending rate, and the performance of multinational banks.

5.3 Policy Recommendation

Given the findings from this study, there are a number of policy recommendations that can be adopted by the multinational banks. A policy recommendation is simply a written policy advice prepared for some group that has the authority to make decisions. The Multinational banks policy recommendations are the key indicators through which

Multinational banks policy decisions will be made in most levels of banks across the EAC states.

From the findings and conclusion, the study recommend that credit reference bureaus should consider generation of accurate reports that would feed in the determination of the lending rates by taking into consideration factors such as; customers performing loans, the repayment history of micro finance loans and SACCO loans, Hire purchase installments, credit card repayments and the ability to pay utilities on time, to directly influence the banks lending rates, thus influence the performance of the multinational bank. In this policy, good borrowers would automatically enjoy lower lending rates and bad borrowers would access credit, though at higher rates. Overall impact would be increased lending and credit appetite for banks as good borrowers strive to take economic advantage of low interest rates and the economy at large would be re-engineered.

Lending is the core business operation for the banks and therefore the study recommend that Multinational banks management should determine lending rates with great consideration on the Credit reports and ratings as a key factor, and jointly consider inflation rates, demand for loans, macroeconomic environment and economic status in their decision making processes. The study recommended that management of Multinational banks and credit reference bureaus should be actively involved in the determination of the lending rate based on credit ratings and reports so as to create a less risky and better macroeconomic business operating environment. A clear EAC policy inter linked with other economic factors such as competitions, risks, cost of fund such as salary of the staff and management fees and inflation due to economic changes in the country when determining lending rates would create a positive relationship between credit ratings and the performance of multinational banks, as this would further get into details of customer behaviors on some products such as salary advances etc.

5.4 Limitations of the study

The main limitation of this study was the inability to include local financial institutions and banks which has a direct impact to the credit reference bureau reporting. This study was thus limited to Multinational banks. The study would have covered more financial institutions across banking and micro finance sectors so as to provide a more broad based analysis. However, resource constraints placed this limitation.

The study faced limitation from respondents especially from the Finance and product management departments of the sample population where they felt that they were not the right people to respond to the questionnaires. The researcher explained to the respondents that the information they provided was critical specifically to analyze the profitability levels of the bank, before and after the establishment of the CRB. This comparison was later availed by product analysts from the respective finance and product departments.

The study also faces the challenges of time resources limiting the study from collecting information for the study particularly where the respondent delay in filling in the questionnaire and making numerous follow up calls and electronic mails, to ensure responses to the questionnaire.

Some of the respondents were found to be uncooperative because of the sensitivity of the information required for the study. The researcher explained to the respondents that the information they provided was to be held confidential and was only for academic purpose and in some instances required to commit in writing that there would not be mention of specific banks.

5.5 Recommendations for further study

The study investigated the need for a standard credit reference bureau to the performance of Multinational banks operating in the EAC. This study recommends that a further study should be carried out to determine the influence of culture to the success of a standard credit reference bureau in the East African Community. A further research should be carried to determine the economic impact of credit reference bureaus on lending rates, and its influence to the performance of financial institutions.

The study also recommends that a further study should be carried out to determine the effects of economic factors i.e. market forces, monetary and fiscal policies, costs of loans, inflation, etc to the credit ratings and the performance of commercial banks.

REFERENCES

António A. & Raquel Ferreira & Edmund Freitas & Celso Nóbrega & José Pinheiro, 2003, *Intermediaries, Financial Markets and Growth: Some more International Evidence*, Working Papers 2003/02, Department of Economics at the School of Economics and Management (ISEG), Technical University of Lisbon.

Bond, Eric W. & Gresik, Thomas A. (1999), *Regulation of multinational firms with two active governments: A common agency approach*. Pennsylvania State University, Department of Economics. Retrieved on 26th February, 1999 from http://dx.doi.org/10.1016/0047-2727(94)01493-0.

Burton, John & Devan, Janamitra (2010), *Doing business in the East African Community:* a publication of the World Bank and the International Finance Corporation. Retrieved from http://wwwwds.worldbank.org/external/default/WDSContentServer

Calzolari, G., (2001), *Theory and practice of regulation facing multinational enterprises*. Journal of Regulatory Economics, 20 (2):191-211.

Calzolari, G. & Lóránth, G. (2004), *Regulation of Multinational banks: a Theoretical Inquiry*. CEPR Discussion Papers 4232, C.E.P.R.

Calzolari, G & Lóránth, G. (2005), *Regulation of multinational banks - a theoretical inquiry*, Working Paper Series 431, European Central Bank.

Calzolari, G., 2004, "*Incentive Regulation of Multinational Enterprises*", forthcoming in International Economic Review

Collier, Sarah (2011), *Credit histories may lower risk for lenders and increase access for borrowers*. Retrieved from http://thinkafricapress.com/tanzania/credit-reference-bureau

CRB Africa (2012), Article and publication by economists, Retrieved on 5th June 2012 from http://www.crbafrica.com/bureaux/bureaux.asp

Daniels, J., Radebaugh, L., Sullivan, D. (2007), *International Business: Environment and Operations*, (11th ed). Prentice Hall.

Gatwiri, F. (2011), *Determinants of lending rate of commercial banks in Kenya*, Unpublished MBA project, University of Nairobi.

Getenga, Jared (2011), *Financial Sector Deepening (FSD)*, RCRC Abridged article Retrieved from http://www.kenyacreditinfo.com/

Harr T. and T. Rønde,(2004), *Branch or Subsidiary? Capital Regulation of Multinational Banks*. Mimeo, University of Copenhagen.

Institute of International Bankers, (2001), Global Survey 2001, available at http://www.iib.org/global/2001/GS2001.pdf

International Monetary Fund (2000), *World Economic and Financial Surveys, International Capital Markets: developments, prospects, and key policy issues*, retrieved from http://www.imf.org/external/pubs/ft/icm/2000/01/eng/

Joshi, Rakesh Mohan, (2009), *International Business*, London, Oxford University Press.

Kanimba, Francois (2010), *Credit Reference Bureau starts operations in Rwanda*; Speech by the BRN Governor. Retrieved from http://focus.rw/wp/2010/08/credit-reference-bureau-starts-operations-in-rwanda/

Kibe M.M. (2003), *The Relationship Between Interest Rate Spread And Profitability Of Commercial Banks In Kenya*. Unpublished MBA project, University of Nairobi.

Kowalewski, Oskar (2010), *Multinational Banks and the Performance of Their Subsidiaries Abroad*, Warsaw School of Economics (SGH) - World Economy Research Institute. Retrieved from http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1697852

Lazaro, Felix (2012), *Banks face competition from foreign entities*. International Monetary Fund Article Retrieved from http://allafrica.com/stories/201202270770.html

Ndung'u, Njuguna (2012),*Working towards an East African Monetary Union*. Retrieved from http://www.bis.org/review/r120417a.pdf

Ojiwa, Fred, 2010, The Credit reference Bureau will boost the banking sector in Rwanda, Retrieved from http://allafrica.com/stories/201006250092.html

Setty, Gautam & Dodd, Randall (2003), *Credit Rating Agencies: Their Impact on Capital Flows to Developing Countries,* special policy report 6 retrieved from www.financialpolicy.org

Tomlinson, Mark (2007), *Making Finance Work for Africa: How Creating Scale in Financial Markets Can Support Growth and Development.* Retrieved from http://siteresources.worldbank.org/INTAFRSUMAFTPS/Resources/Working_Paper_on_Regional_Financial_Integration_Jan07.pdf

Tumusiime-Mutebile, E., (2011), *Introducing innovative services to meet credit needs in Uganda*. Retrieved on 29th May, 2012 from http://www.bis.org/review/r081205c.pdf

Wu, J., Jeon, Bang N., Luca, Alina C. (2010), Does distance affect the performance of Foreign banks? Evidence from multinational banking in developing countries, in Suk-Joong Kim, Michael D. Mckenzie (ed.) *International Banking in the New Era: Post-Crisis Challenges and Opportunities (International Finance Review, Volume 11)*, Emerald Group Publishing Limited, pp.431-474. Retrieved on 5th June, 2012 from 10.1108/S1569-3767(2010)0000011018

APPENDICES

APPENDIX 1

QUESTIONNAIRE

i. What is the name of your multinational Bank? ………………………………….

ii. Which country is your bank located in the East African Community? ....

iii. Is there a Credit reference Bureau in your country? (Tick as appropriate)

Yes ☐ No ☐

What is its registered name? …………………………………….....................

iv. Who is the regulatory authority of the Credit reference bureau in your country?

☐ Self regulated

☐ Central Bank / Government

v. Has your Multinational bank adopted the Credit reference guidelines as stipulated by the regulator?

Yes ☐ No ☐

vi. What kind of information does the CRB in your country collect? Please tick the appropriate boxes.

- [ ] Performing loans
- [ ] Non Performing loans
- [ ] Microfinance loans
- [ ] Ability to pay Utilities and on time
- [ ] Credit card repayment history

vii. In your own opinion, do you think the kind of information collected by the CRB add value to your banks credit decision making process? Yes [ ] No [ ]

Briefly explain…………………………………………………………………..…....

…………………………………………………………………………………………

…………………………………………………………………………………………

viii. To what extent has this information influenced your banks lending rate?

Very great Extent [ ] Great Extent [ ] Moderately Extent [ ]

Less Extent [ ] No Extent [ ]

ix. Do CRB's reports influence the performance of your bank?

Yes [ ] No [ ]

Briefly explain

……………………………………..…………………………………....

…………………………………………………………………………………………

x. How do you rate the responsiveness of your credit reference bureau when dealing with your organization?

Excellent ☐ Good ☐ Satisfactory ☐ Poor ☐

xi. How do you rate the professionalism of CRB on dealing with your organization?

Excellent ☐ Good ☐ Satisfactory ☐ Poor ☐

xii. How do you rate the products and services? (Tick as appropriate)

Excellent ☐ Good ☐ Satisfactory ☐ Poor ☐

xiii. Do they meet your needs and expectations regarding quality and performance?

Yes ☐ No ☐

ii. How do you rate their approach to quality management to ensure complete customer satisfaction?

Excellent ☐ Good ☐ Satisfactory ☐ Poor ☐

xiv. How do you rate the delivery on time performance of your CRB in meeting your delivery expectations?

Excellent ☐ Good ☐ Satisfactory ☐ Poor ☐

Approximately, how long does it take to get the responses and why? ……………………………………………………………………………………

xv. In your opinion and based on the current developments of the EAC, will this integration affect the CRB's operations?

Yes ☐ No ☐

If yes, briefly state the nature of effects and their impact to the banks performance.

……………………………………………………………………………………………
……………………………………………………………………………………………

xvi. Is there need for a standard credit reference bureau for the EAC states after full integration?

Yes ☐ No ☐

xvii. Briefly state two expected challenges of a standard credit reference bureau to the performance of Multinational Banks in the EAC.

……………………………………………………………………………………………
……………………………………………………………………………………………

xviii. What other information do you think the CRB should consider in order to positively impacting on the performances of Multinational banks?

……………………………………………………………………………………………
……………………………………………………………………………………………

APPENDIX II

LIST OF KEY MULTINATIONAL BANKS IN THE EAC

1. Barclays Bank
2. CFC Stanbic Bank
3. Citi Bank
4. Diamond Trust Bank
5. Kenya Commercial Bank
6. Standard Chartered Bank
7. Equity Bank
8. Bank of Africa
9. Fina Bank
10. Bank of Baroda
11. Eco Bank
12. I & M Bank
13. Commercial Bank of Africa (CBA)