

# Transparency comes into spotlight

New legislations take years to develop, but once approved, they can alter the entire way an industry functions. In the UAE, the banking sector is undergoing major transformations as the government takes transparency to the next level



UAE Banks Federation's CEOs Advisory Council met earlier this year, where they discussed preparations for Al Etihad Credit Bureau

Until recently, UAE banks had no way of checking on a potential customer's borrowing history with other lenders. There was no system in place to allow that nor to stop a consumer from submitting various copies of a salary statement and obtaining multiple loans from different banks.

This came at a high price following the global economic recession: loan losses in UAE banks shot up from

AED 25 billion at the end of 2008 to nearly AED 47 billion in 2010, leading to a tightening of lending and forcing banks to set aside billions of dirhams as a safeguard against nonperforming loans.

A report by EFG-Hermes released in May this year highlighted Abu Dhabi Islamic Bank (ADIB) as one of the most vulnerable, having held the most exposure to the retail sector. The bank has already taken steps to shield itself by establishing provisions

of 1.62 percent of total customer risk-weighted assets, which is above the Central Bank's minimum requirement of 1.5 percent.

The government also endured tough times in dealing with citizens' borrowing habits. In late 2011, the Ministry of Presidential Affairs had to launch a debt settlement fund with an initial budget of AED 10 billion to help bail out indebted Emiratis, most of whom had multiple credit cards and loans.

## Credit bureau comes to the rescue

Al Etihad Credit Bureau is set to change all this. By maintaining financial track records for all individual bank customers in the UAE, the bureau will be able to provide reliable data, including historical information on those who have defaulted on their loans in the past. By next year, the bureau will also provide the same information about companies.

‘Al Etihad Credit Bureau will be a major step for banks because it will provide more clarity on customer exposures and customer behaviour patterns outside the bank, which will allow for more informed decision making based on a customer’s financial capability,’ Suvo Sarkar, General Manager of Retail Banking and Wealth Management at Emirates NBD, told Insight Magazine.

What the bureau will not cover is the value of mortgaged assets, a person’s investments with a bank, credit rating for individuals or consultations, or any other information not requested by the applicant.

Speaking of applicants, those who will be eligible to request and obtain credit information are federal and local entities, commercial banks, investment and leasing companies, financial institutions, commercial and professional establishments,

cooperative associations and locally registered branches of foreign companies.

## Phased rollout

Established as a Public Joint Stock Company by the UAE Federal Government in 2012, and with a paid-up capital of AED 200 million, Al Etihad Credit Bureau was rolled out in four phases.

In the first phase, consumer credit data was collected from a group of UAE financial institutions. In the second phase, a similar database was created for the commercial sector, including small and medium enterprises (SMEs), utility companies, Etisalat and du, and insurance providers.

The third phase saw value added services introduced to the lenders, and as a final step, all historical data on consumers were compiled.

As of April 2014, 25 lending institutions, controlling approximately 96 percent of the retail credit market, had provided information on loans and credit cards to Al Etihad Credit Bureau. However, the new entity aims to coordinate all banks in the UAE, which are at least 52, in addition to other credit providers, telecommunication companies and government authorities.



Marwan Ahmad Lutfi,  
CEO of Al Etihad Credit Bureau

‘Al Etihad Credit Bureau will help strengthen the UAE’s financial infrastructure and add demonstrable value to the banking sector. To do this, we are forming solid partnerships with banks and other financial institutions in the country to ensure the efficient and accurate transfer of information between both sides,’ says Marwan Lutfi, CEO of Al Etihad Credit Bureau.

## A welcome change

Mashreq Bank, Standard Chartered, and Emirates NBD have already joined the bureau in the soft launch along with other financial institutions.

‘Emirates NBD is a significant contributor and partner to Al Etihad Credit Bureau and will play an active role in its launch. We have been providing inputs and doing data checks with the Credit Bureau for a



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**Suvo Sarkar**, General Manager,  
Retail Banking and Wealth  
Management at Emirates NBD

few months now. We've also worked closely with the bureau to train our frontline and back office staff on all aspects of its launch," highlights Sarkar.

It's easy to see why banks have embraced these new regulations. Although they are obliged to join the bureau, it is through this system that they will be able to gain insight into consumer credit history before extending new debt. And by doing so, they can determine the credit worthiness of prospective credit card and loan applicants.

Such a transparent process should protect them against high-debt burdens or over-leveraged situations, leading to fewer defaults at a time when personal borrowing is on the rise. UAE Central Bank data shows that total lending in the country rose by 9 percent in 2013 to reach AED 1.29 trillion – its faster growth since 2008, when it soared by 41 percent.

Seeing how Singapore benefitted from the launch of its credit bureau in 2002, with average default rates for credit cards falling from 2.4 percent in 2002 to 2.07 percent in 2012, Al Etihad Bureau is bound to have a similar impact.

## What it means for SMEs

SMEs are likely to gain the most out of such a system. 'SMEs that already have a performance track record and good credit history captured through a credit bureau mechanism, will always have a greater ability to negotiate financing from banks,' explains Ehsaan Uddin Ahmad, head of Global Transaction Services and SME at Noor Islamic Bank.

The International Finance Corporation recently reported that the chances of obtaining a bank loan for a small business increases from 28 percent in countries without a credit bureau, to 40 percent in countries that do have a credit bureau. A credit reporting system can also reduce loan pricing for SMEs and boost bank appetite for extending finance to this segment.

But according to Younis Al Khoori, Undersecretary of the Ministry of Finance, SMEs who want to apply for loans after the credit bureau comes into effect will have to put in an effort to create a personal credit history, because banks are very likely to look at the people behind start-ups.

As individuals running businesses, they should have clean records of payments to telecom companies and utilities, and of credit cards and personal loans, if any.

## Defaults expected

Over the long term, having access to consumers' financial records upon request should speed up financing decisions and bring down the price of credit as risk factors decrease and lender confidence rises.

'For customers, it could mean that based on their overall exposure and good financial behaviour, they could get faster access to credit and potentially better terms from

the financial institution. In the long run, it would also encourage more responsible financial behaviour among customers," explains Sarkar.

Initially however, adapting to the process is expected to be a challenging journey, especially for retailers, whose loans make up 49 percent of ADIB's total loans, 44 percent of Dubai



**AbdulAziz Al Ghurair**, Chairman,  
UAE Banks Federation and  
CEO Mashreq Bank

Islamic Bank's, 41 percent of First Gulf Bank's and 22 percent of Abu Dhabi Commercial Bank's (ADCB) loans.

'The credit bureau is nearly ready. But there will be some pain...The banks will discover how much they have overlent to retail customers and there will be clarity,' AbdulAziz Al Ghurair, chairman of the UAE Banks' Federation, was cited as saying by The National. 'Retail customers will also discover they have overborrowed and cannot borrow any more,' he said.

Al Ghurair, who is also the chief executive of Mashreq Bank, estimates that the level of defaults would be between 5 and 7 percent. 'We expect there will be an increase in the level of personal defaults, but this merry-go-round will [eventually] stop'.



## GCC derivatives exchange

Meanwhile, as the country seeks to develop its capital markets, discussions of establishing a Gulf Derivatives Exchange have resurfaced.

The GCC-wide exchange was first proposed more than a decade ago but shelved in the wake of the financial crisis, partly because derivatives trades were seen as one of the main causes of the economic collapse. In the region, firms including ADCB, Dubai's Mashreq Bank and Kuwait's National Industries Group all lost hundreds of millions of dollars on derivative bets.

But analysts argue that many banks in the region already engage in over-the-counter derivative trading, which is difficult to regulate and can also be risky. Whether exchange trading would solve the issue though is yet to be determined.

Now that the UAE has been upgraded to an "emerging market" status by global index provider MSCI, an announcement made in May 2014,

officials have been planning the next course of growth, investigating the prospects of derivatives trading albeit with greater caution.

Nine companies are included in the MSCI UAE Index, namely Abu Dhabi Commercial Bank, Aldar Properties, Arabtec, DP World, Dubai Financial Market, Dubai Islamic Bank, Emaar Properties, First Gulf Bank and National Bank of Abu Dhabi.

The MSCI's reclassification of the UAE is expected to open a wide pool of investor capital, and increased use of derivatives could reinforce the position of GCC financial firms

among international markets. But to introduce a Gulf Derivatives Exchange would require many laws, rules and regulations, and even systems, according to Rashed Al Baloushi, Chief Executive of the Abu Dhabi Securities Exchange.

Times are certainly changing for the UAE's banking sector as the government places greater emphasis on transparency and as regulators tread carefully into new waters. These developments can only benefit the long-term stability of the financial sector.

- Heba Hashem

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