

**2015 SUMMING-UP OF BANKING  
FINANCIAL SECTOR OF THE REPUBLIC OF MOLDOVA**

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*Economic and political uncertainty in recent years has adversely affected the activity of Moldovan banks unfavorably the dynamics of the national economy. The 2015 year can be considered a "rigid" year for the Republic of Moldova, built by the liquidation of three financial institutions at the NBM decision (CB "Unibank" SA, CB "Banca Sociala" SA and BC "Banca de Economii" SA), and the tightening of the monetary policy. That has led to mistrust of the population in this sector, creating problems with bank loans and deteriorating of bank asset. However, commercial banks during 2015 remained sufficiently liquid and capitalized (exception is CB "Unibank" SA, CB "Banca Sociala" SA and BC "Banca de Economii" SA). This article aims to research the financial and banking sector from the Republic of Moldova in 2015 in terms of uncertainty. Therefore, the novelty of the article lies in the analysis of the banking sector from the Republic of Moldova under the main financial prudential indicators. The main research methods were: systemic analysis, synthesis, monographic, logic, etc. The main scientific results obtained in the article, as a conclusion of the research are the identification, analysis of the main activity of the banking sector and the proposed set of recommendations on strengthening the financial stability framework in the Republic of Moldova.*

**Key words:** banking sector, financial stability, loans portfolio, assets, deposits, loans, profitability and solvency.

*Incertitudinea economică și politică din ultimii ani a afectat negativ activitatea băncilor din Republica Moldova, defavorizând dinamica economiei naționale. Anul 2015 poate fi considerat un an „rigid” pentru Republica Moldova, încorporat cu lichidarea celor 3 instituții financiare la decizia BNM (BC „Unibank” SA, BC „Banca Sociala” SA și BC „Banca de Economii” SA) și înăsprirea politicii monetare. Astfel, această situație a condus la neîncrederea populației în sector, generând probleme la capitoul acordarea creditelor bancare și deteriorarea activului bancar. Totuși, băncile comerciale, pe parcursul anului 2015, au rămas lichide și suficient de capitalizate (excepție constituie BC „BANCA SOCIALĂ” SA, Banca de Economii SA și BC „UNIBANK” SA). Acest articolul are ca scop central cercetarea sectorului financiar bancar din Republica Moldova în anul 2015 sub aspectul incertitudinii. Prin urmare, actualitatea prezentului articol constă în analiza sectorului bancar din Republica Moldova prin prisma principalilor indicatori prudențiali financiari. Metodele principale de cercetare au fost: analiza sistemică, sinteza, monografică, logică etc. Principalele rezultate științifice, obținute în articol în urma cercetării, sunt identificarea, analiza principalilor indicatori de activitate a sectorului bancar și propunerea setului de recomandări privind consolidarea cadrului de stabilitate financiară din Republica Moldova.*

**Cuvinte-cheie:** sector bancar, stabilitate financiară, portofoliu de credite, active, depozite, credite, profitabilitate, solvabilitate.

*Экономическая и политическая неопределенность в последние годы негативно отразились на деятельности молдавских банков, выступающих за динамику национальной экономики. Для Республики Молдова 2015 год можно считать «жестким» годом, из-за ликвидации трех финансовых учреждений по решению НБМ (КБ "Unibank" SA, КБ "Banca Socială" SA и КБ "Banca de Economii" SA), а также ужесточения денежно-кредитной политики. Это привело к росту недоверия населения к этому сектору, одновременно создавая проблемы, связанные с*

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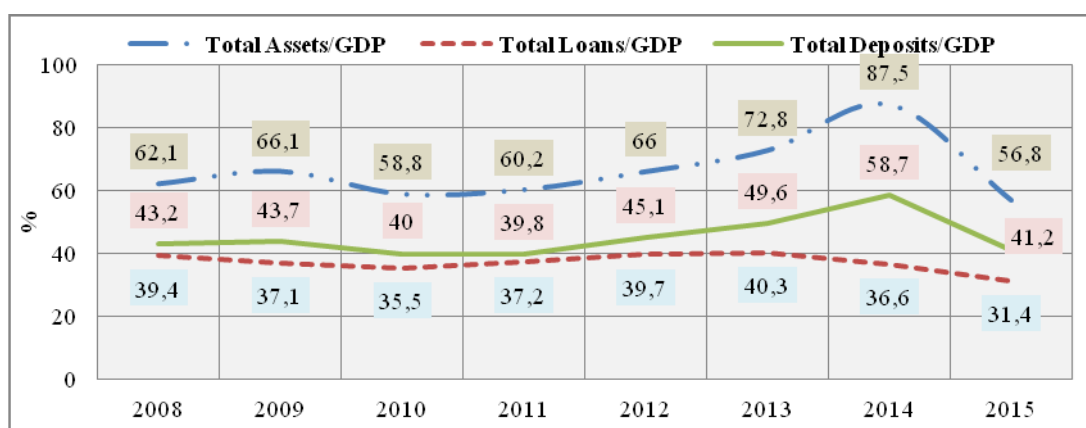
предоставлением банковских кредитов и ухудшением банковского актива. Тем не менее, коммерческие банки в течение 2015 года оставались ликвидными и достаточно капитализированными (исключение составляют: КБ "Unibank" SA, КБ "Banca Sociala" SA и КБ "Banca de Economii" SA). Данная статья призвана исследовать финансовый и банковский сектора Республики Молдова в 2015 году в условиях неопределенности. Актуальность статьи заключается в анализе банковского сектора Республики Молдова через призму основных финансовых пруденциальных показателей. Основные методы исследования: системный анализ, синтез, монографический, логический и т. д. Основные научные результаты, полученные в результате исследования, являются: идентификация, анализ основных показателей деятельности банковского сектора и разработка рекомендаций по укреплению финансовой стабильности в Республике Молдова.

**Ключевые слова:** банковский сектор, финансовая стабильность, кредитный портфель, активы, депозиты, кредиты, рентабельность, платежеспособность.

**JEL Classification:** E51, E59, G21, G28.

**Introduction.** During the last years the biggest threat for the stability of the financial system of the Republic of Moldova is represented by the disruptions in the banking sector. These were generated by the shady transactions of some commercial banks (B.C. „Unibank” S.A., B.C. „Banca Sociala” S.A. and B.C. „Banca de Economii” S.A.), being in liquidation procedure and able to destabilise the financial and budgetary system causing a high level of inflation and demonetization of economy.

Financial destabilisation of the banks from the Republic of Moldova remains to be immediate because on June 11, 2015, NBM established special supervision on the biggest banks from the Republic of Moldova, and namely: B.C. Moldova Agroindbank, B.C. Victoriabank and B.C. Moldindconbank. The decrease in this indicator will continue to record negative dynamics also in 2016, against the background of problems in the banking sector, which may gradually disturb the stability of the sector. Though, during 2015, the prudential indicators of the banking sector on solvability, liquidation and coverage degree of provisions recorded adequate levels. These were maintained under regulatory limits even in the precarious economic conditions.



**Fig. 1. Degree of financial intermediation, %**

*Source: Authors' calculations based on the data of the National Bank of Moldova.*

**Situation from the banking sector is as following:**

**At the end of 2015 deterioration trends of bank assets quality, affecting the entire banking sector are registered.** Throughout 2015, the annual growth rate of bank assets has been on the rise (since March 2015 – 24,80% up to September 2015 – 27,27% as compared to the last year), totaling 104504,1 million MDL in bank assets on September 30, 2015. This increase is due to profit generating assets (with a weight of 57,8% in total assets). *But from September 2015, decreasing trends regarding the bank assets have been observed.* These signs of concern are reflected since October 2015 (-16,91%) and continue at the beginning of 2016 (in January 2016 (-26,72%)) compared to the last year, totaling 70351,8 million MDL in bank assets on January 31, 2016.

The deterioration of the bank assets quality can influence in future on reducing the level of the bank capitalization and could disturb the financial stability of the sector.

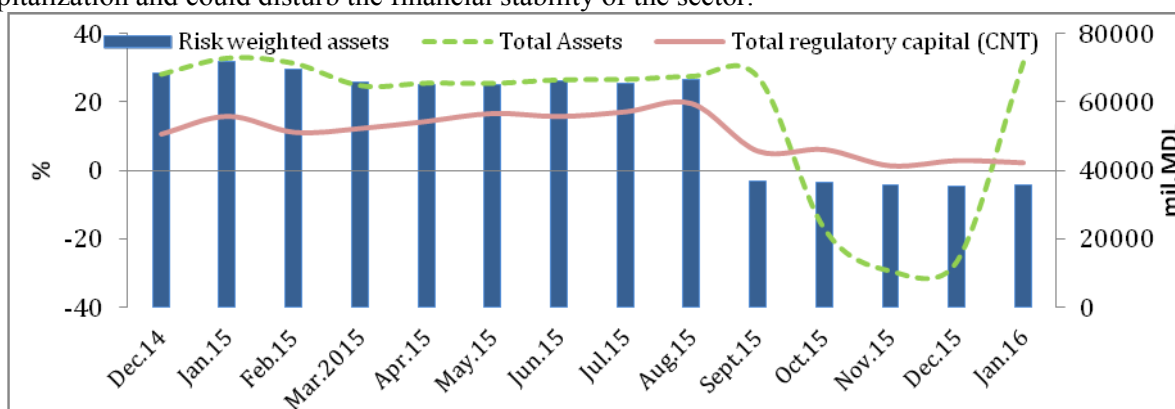


Fig. 2. Development of the bank capital quality

Source: Author’s calculations based on the data of the National Bank of Moldova.

The raise in the base rate in 2015 has generated more expensive bank loans affecting the real sector and the entire national economy. At the end of 2014 there has began the slowing growth of new loans provided by banks which in 2015 have been transformed in a moderate decrease of lending. In December 2015, the gross loans portfolio provided by the commercial banks has had a negative development (-6,5% in comparison with the same time last year), and the volume of new loans provided by banks was mentained in a negative trend (-19% in comparison with the same time last year). In a great measure this decrease was influenced by the precarious situation of those three problematic financial institutions (B.C. „Unibank” S.A., B.C. „Banca Socială” S.A. and B.C. „Banca de Economii” S.A.), and the low level of confidence of the population. In September, 2015, the biggest contribution to the decrease have had the loans in national currency decreasing by 32% in comparison with the same time last year, while the loans in foreign currency increased by 9% in comparison with the same time last year.

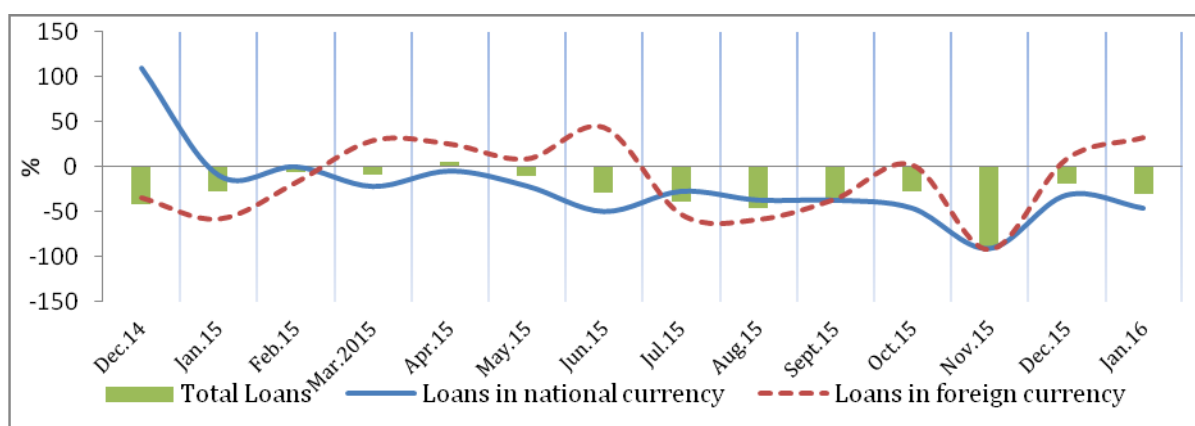


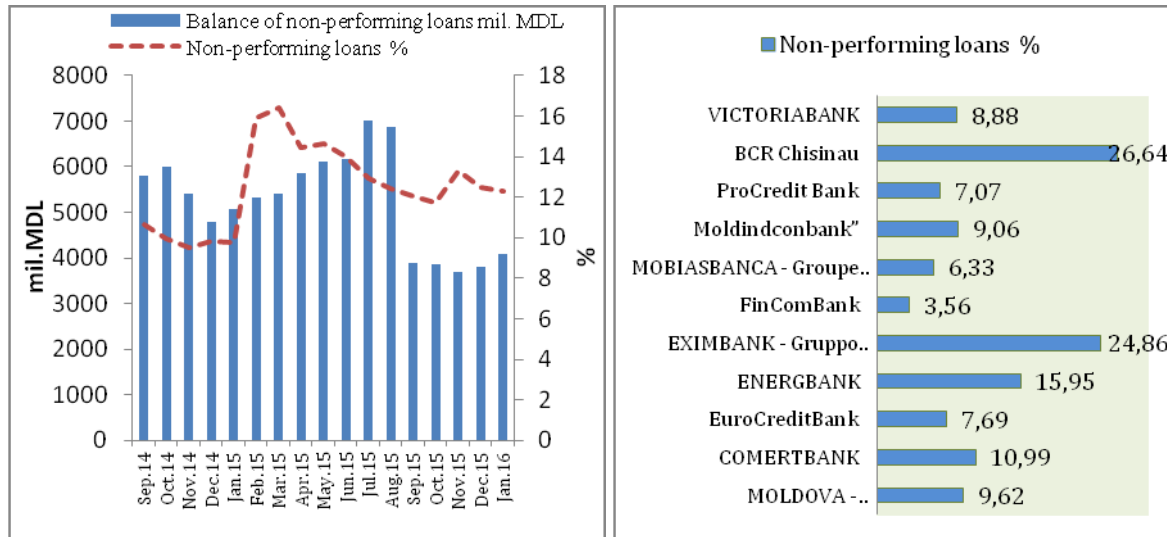
Fig. 3. Annual growth rate of loans in foreign and national currency, %

Source: According to the data of the National Bank of Moldova.

The upward trend of loans provided by banks in national currency became a major concern being reflected by the slowdown in economic activity, high level of incertitude and exchange rate risk. However, a cause which generated the reduction of loans in national currency in 2015 was also the tightening of monetary policy promoted by NBM (increase in the base rate from 17,5% in July to 19,5% in September 2015<sup>4</sup>, and mandatory reserves).

<sup>4</sup> During the meeting of August 26, 2015 the Administration Council of the National Bank of Moldova (NBM) decided to raise the base rate applied on the main short-term monetary policy operations by 2,0 p.p., from 17,5 to

In 2015, the amount of non-performing loans accounted for 3798,58 million MDL decreasing by 21% compared to December 31, 2014. On December 31, 2015 the weight of non-performing loans in total loans decreased by 1,78 p.p., compared to December 31, 2014, representing 9,95%. *The decline in indicators of the loan portfolio quality in September, October and December 2015 was due to the exclusion of the three problematic commercial banks from the calculation. Obviously, this decrease in the ratio of non-performing loans is favorable for the entire banking sector. However, lending activity is still influenced by the currency and inflationary risks, the bank's management capacity and economic crisis in the country.*



**Fig. 4. Weight of non-performing loans in banking sector, %**

Source: According to the data of the National Bank of Moldova.

*During 2015 the commercial banks remained to be liquid and sufficiently capitalized (exceptions are BC „BANCA SOCIALA” S.A., Banca de Economii S.A. and BC ”UNIBANK” SA). In 2015 the liquidity indicators of the banking sector have fallen within the normative established by the National Bank of Moldova. The weight of liquid assets (liquidity principle II) accounts for 41,55%, increasing by 19,07 p.p. compared to December 31, 2014, excepting the group of problematic banks which recorded values inferior to those controlled by the NBM minimum liquidity requirement ( $\geq 20\%$ ). The value of liquidity indicator on long term (liquidity principle I ( $\leq 1$ ))<sup>1</sup> of the entire banking system was 0,72% on December 31, 2015 less by 0,82 p.p. compared to December 31, 2014, this coefficient refers to 11*

*19,5% annually. Thus, the members of the Executive Committee of the NBM, at the meeting of November 26 2015, unanimously decided to maintain the monetary policy interest rate at the level of 19.5 percent annually. This decision of the Executive Committee of the NBM is argued by the fact that the monetary policy measures taken by the NBM since the beginning of the current year so far shall still actuate through different transmission channels in the national economy including by influencing the interest rates on loans and deposits in national currency, thus exerting further effects on future inflation developments. Details on: <http://www.bnm.md/ro/content/26-noiembrie-2015-comunicat-al-bancii-nationale-moldovei>*

<sup>5</sup> *During 2015 the NBM has come up with amendments to the draft Decision of the Council of Administration of the NBM „On amending and supplementing the Regulation on bank liquidity”, approved by the Council of Administration of the NBM, minutes no. 28 of August 8, 1997, the Official Journal of the Republic of Moldova, 1997, no. 64-65, art. 105 of October 2, 1997. In this draft it has been proposed to replace the liquidity principle I which referred to the long term liquidity and foresaw that the amount of bank assets with maturity period of more than 2 years should not exceed the amount of its financial resources with the same term. After the amendments the following maturity bands shall be used: up to a month; 1-3 months; 3-6 months; 6-12 months and over 12 months, expressed as a ratio between the actual liquidity and needed liquidity for each maturity band. Details on: <http://www.bnm.org/ro/content/proiect-hca-al-bnm-cu-privire-la-modificarea-si-completarea-regulamentului-cu-privire-la-0>*

commercial banks. Consequently we observe that the majority of commercial banks recorded a rather high coefficient leading to an excess of bank liquidity. This liquidity increase occurred in the context of tightening of the monetary policy promoted by the NBM. So, the NBM will continue to manage the liquidity excess through sterilization operations in order to support the proper functioning of the interbank money market. However, the development of monetary market from the last period highlights some barriers to storage liquidities by the commercial banks.

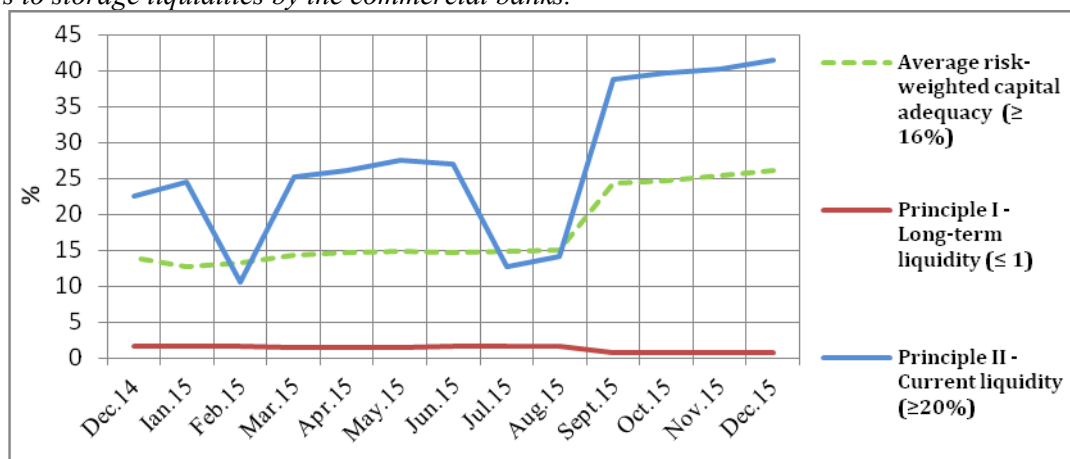


Fig. 5. Average risk weighted capital adequacy in the banking sector, liquidity principles I and II, %

Source: According to the data of the National Bank of Moldova.

In 2015 the level of capitalization<sup>1</sup> for 11 commercial banks from the sector recorded superior values of 26,16% (increasing by 12,24 p.p. compared to December 2014) which indicates fair functioning conditions and a specific competitiveness climate for national banks.

NBM shall to monitor attentively and incessantly the evolution of the banking capital considering that its volume and quality determine the absorption capacity of losses generated by the risks arising from the banking activity.

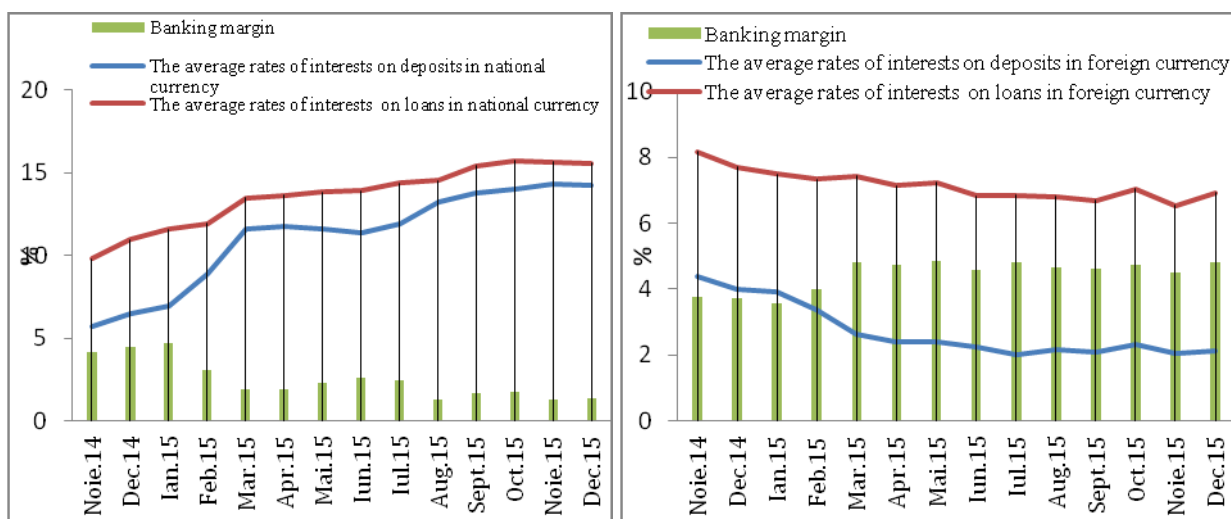


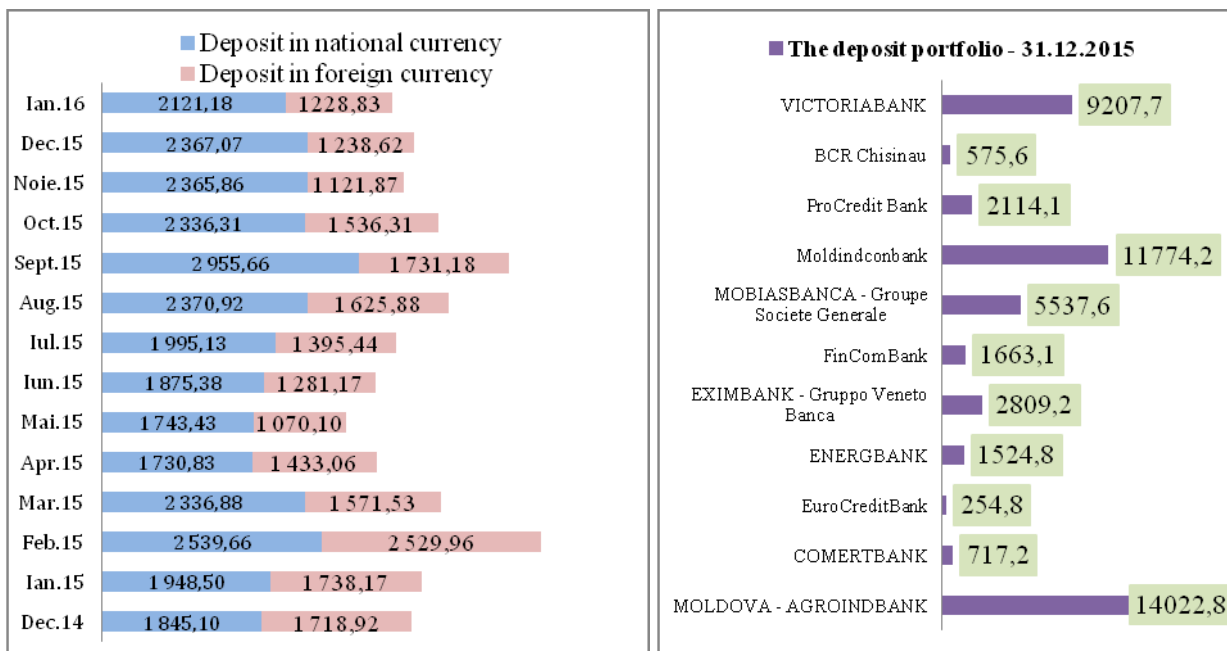
Fig. 6. Development of the banking margin\*, average interest rates on deposits and loans in MDL and foreign currency, %

Source: Author's calculations according to the data of the National Bank of Moldova.

\*Note: Banking margin index was calculated as the difference between the average rate on loans in MDL/foreign currency and average rate on deposits in MDL/foreign currency.

<sup>6</sup> Below the minimum requirement set by NBM ( $\geq 16\%$ )

**The increase of interest rates in the national currency was caused largely by the containment of the monetary policy generating the population unconfidence to deposits in MDL.** On December 31, 2015 the balance of deposits in the banking system amounted to 50201,5 million MDL, decreasing by 23,3%, compared to December 31, 2014. This decreasing trend resulted largely from the decreasing balance of deposits in foreign currency by 22,7% and deposits balance in national currency by 24% compared to December 31, 2014. In 2015, the new term deposits registered a constant increase from 3561,02 million MDL in December 2014 to 3605,69 million MDL in December 2015. Given the depreciation of national currency from the last period, population prefers foreign currency deposits whose weight was 52,5% at the end of December 2015 while the deposits in national currency representing 45,5% of total deposits. This is explained by the fact that the average interest rate in the banking system of the deposits in foreign currency is more attractive (being – 2,12% in December 2015, decreasing by 1,81 p.p. compared to December 2014) compared to the rate in national currency (December 2015 – 14,22% increasing by 7,75 p.p. compared to December 2014).



**Fig. 7. Development of new deposits attracted by banks in national and foreign currency, million MDL**

*Source: Author's calculations according to the data of the National Bank of Moldova.*

**Respecting the made analysis we come with the following recommendations.**

**Recommendations on strengthening the financial stability framework:**

1. *Redefining the role of the National Bank of Moldova (NBM)* and including in its power the objective of financial stability safeguarding by accomplishing the necessary amendments to the law on NBM (art. 5), which could increase the NBM responsibility with this objective. Enhancing the capacity to implement supervisory and regulatory actions in time.

2. *Drafting the Financial Stability Reports* (taking into account the experience of the EU member states) to identify and disclose the risks associated with the financial and banking system. Drawing up regulatory document of financial and prudence indicators which predict crisis situations and setting their threshold values.

3. *Strengthening the crisis management framework.* Enhancement the functionality of the National Committee for Financial Stability (NCFS) by intensifying the coordination between member agencies. Developing the perspective vision and comprehensive intervention plan to solve the financial crisis by NCFS by identifying the necessary changes in legislation.

4. *Strengthening the system of deposits insurance.* Strengthening the funding of the Deposit Guarantee Fund (DGF) by developing a methodology of target funds and amendment the legislation on

providing a DGF credit line from the Ministry of Finance. Amending the Law on DGF and Law on NBM regarding the inclusion of NBM as a backup additional funding source for FGD and the increase of deposit guarantee to raise the confidence in the banking system.

**Recommendations on banking supervision:**

1. *Active assessment of the risk profile of banks.* NBM has to assess the risk profile of the banks concerning the risks to which they are exposed, management effectiveness of risks and the risks they pose to the financial system. Making the monthly analysis of the banking system stability based on a set of financial and prudence indicators. Quarterly assessment of the system vulnerabilities to the potential credit, exchange and interest risk based on stress-tests.

2. *Application of macro-prudential aspects to tackle the systemic risks.* NBM has to determine the risk in a more ample context than that limited to the balance sheet of the individual banks. The macroeconomic environment, business trends, accumulation, and concentration of risks in the banking sector have a great impact on the risk exposure of the individual banks. The data of the individual banks, data at the sector level and aggregate trend data gathered by the supervision authorities should be included in the deliberations of the competent authorities responsible to ensure financial stability (no matter if they activate separately from the supervision authority), to contribute to the identification and analysis of the systemic risk.

**Enhancement the quality of corporate governance in banks:**

1. *Developing a consistent conception on corporate governance* in banks from the Republic of Moldova aligned to the recommendations of the principles of the Basel Committee on Banking Supervision BCBS and alignment of banking regulations under this conception by NBM.

2. *Property and control structures disclosure.* NBM has to bring into force firmly and efficiently the legal norms on identification and adequacy requirements of the final and control beneficiaries in banks. These actions should contribute to the improvement of the transactions monitoring with the related parties and global framework of risk management in banks. The decision factors have to be established as a main priority of the regulatory framework- property and control structures disclosure, to develop an action plan, to analyze alternating approaches and ask the property and control position disclosures. The disclosure of the agreements between shareholders is also necessary.

3. *Disposal the concept of nominal property/ holder of law.* The nominal property is allowed by law and this contributes to the lack of transparency of the shareholders. In fact, only the first level of disclosure is present- that of nominal property with off-shore ghost companies frequently used to cover the identity of the real owners.

4. *Lowering the threshold for approval of big transactions by shareholders* (for example from 50% to 25% of the company's assets) especially when the sale is made to a related party. Currently, this decision is taken by the Council of Administration. AGA decides on such transactions only when its value is bigger than 50% of the total value of the company's assets.

5. *Enhancing the quality of banks councils.* The Western banking experience suggests the necessity for some regular rigorous assessment of bank council and its members' activities, the assessment report being available to the interested public. This is important to ensure that the council and its individual members discharge their duties properly and the members of the council are professional people meeting also other specific requirements submitted by the banking supervision department. The Councils of the banks should improve their skill level and competencies. The Councils have to strengthen their position by developing specific knowledge in the banking field especially insisting on the presence in the Council of experts from the field of the banking risks.

6. *Establishing the Audit Committee in banks.* The Boards of Statutory Auditors cannot be replaced by the Audit Board, constitution of which is now recommended internationally. Respecting the global trend in which the role and responsibility of Council are more and more highlighted and enhanced, the

disposal of Board of Statutory Auditors by transferring their functions to the Audit Board shall be considered as one of the policy options.

7. *Implementation of corporate governance principles.* NBM should more emphasize the promotion of good corporate governance in banks and control if banks adopted truly and implemented efficiently healthy policies of corporate governance. We recommend in this regard the drafting of a Corporate Governance Code for banks by NBM in trine to CNPF in the form of templates under which banks could develop their own code. In developing this code, should be taken into account the principles of the Basel Committee on Banking Supervision (BCBS) related to the corporate governance.

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