Academic Journal of Economic Studies
Vol. 1, No.2, June 2015, pp. 151–159
ISSN 2393-4913, ISSN On-line 2457-5836

The Ratio Evolution Analysis of the Non-Performing Loans Obtained by the Credit Institutions in Romania during the Period 2007-2015

Mirela Cătălina Türkeș

Faculty of Finance, Banking and Accountancy
Dimitrie Cantemir Christian University, E-mail: mirela.turkes@ucdc.ro

Abstract *This article analyses the ratio evolution of the non-performing loans obtained by the privately, Romanian and foreign-owned credit institutions, in Romania, during the period December 2007 - June 2015, depending on the change of the legislation regarding the reporting methodology for the purpose of the institutions surveillance according to the prudential regulations of BNR (National Bank of Romania) and EU Regulation. The results of this analysis highlighted the fact that the non-performing loans ratio went through a spectacular increase during the period 2007-2013, reaching 21.87% following the promotion of a strategic plan based on the recovery of the debts by restructuring actions, rescheduling or enforcement. In 2014, the non-performing loans ratio decreases to 15.33% following the modification of the debt recovery strategic plan by taking them out from the balance sheet and by their integral provisioning.*

Key words Total net assets, past due and doubtful loans in total loans, past due and doubtful claims in total assets, past due and doubtful claims, non-performing loans ratio

JEL Codes: M31, M37

1. Introduction

On January 1st, 2007, Romania joined the European Union after a seven year period during which major efforts were made in the economic reform area.
The Romanian banking sector was among the first sectors to be subject to this ample reform process. Amongst the main actions taken for the purpose of the banking sector reform we can name: the change of the legislation regarding the operation of the credit institutions, regarding the crediting activity (Burduş, 2005), the harmonization of the internal banking regulations with the European regulations.
The year 2007 has been marked by strong transformations which had a positive impact, but also a negative one on the international banking sector. During the first half of 2007 a significant excess of liquidity could be sensed on the financial markets. During the second half of the same year, the international banking crisis was triggered in the USA, the oil price increased in an exaggerate manner, a fact which determined the price increase of all food products (Day, 2009).

The loan granted to the private sector in Romania kept its alert increasing rhythm during the period 2008-2010 although the first effects of the subprime loans crisis in the USA could be felt and namely the reduction of the liquidities on the international financial markets.

In Romania, just like in most of the European countries, the baking sector was financing their crediting activity by using external sources because most of the credit institutions were foreign and they owned foreign and private capital.

At the beginning of 2010, the first effects of the financial crisis start being felt in the Romanian banking sector, such as: volume reduction of the loans granted to the private sector, reduction of profitability, increase of the expenses with provisions, prudent reassessment of the recoverable value from the guarantees of the non-performing loans, reduction of operational expenses, gross value increase of the non-performing loans etc. In Romania, the most significant increase of the non-performing loans stock in the balance sheet of the credit institutions is registered in 2013. At the end of this year, the non-performing loans ratio[1] has reached 21.87%.

1.1. Purposes and objectives

In this paper, we proposed to analyse the evolution of the non-performing loans ratio, during the period December 2007 – June 2015, at the level of the Romanian banking sector, in the light of the reporting and calculation methodology for the purpose of the institutions surveillance by obeying BNR regulations and the norms included in the Regulation (EU) no. 575/2013 of the European Parliament and of the Council.

The trend of the non-performing loans ratios is studied with regard to the change of the strategic plans of the credit institutions concerning the improvement of the loans portfolio as well as of the calculation method of the indicators needed for reporting according to the national and European legislation.

The main objectives of this study are:

- Trend analysis of the total net assets of the institutions in the system which exercise a direct influence over the modification of the loans portfolios volume;
- Evolution analysis of the past due and doubtful loans calculated during the period December 2007 – December 2011, based on the reporting performed according to IFRS;
- Ratio evolution analysis of the non-performing loans, during the period September 2011 – March 2014, calculated based on the reporting performed according to IFRS;

---

[1] The indicator is defined as a share in total loans of the past due loans of more than 90 days and/or the ones where juridical procedures were initiated. Starting with March 2014, it is calculated at the level of all the portfolios – both the ones for which the capital demand for the credit risk is determined according to the standard approach, as well as the ones based on internal rating models.

- Ratio evolution analysis of the non-performing loans, during the period May 2014 – June 2015 calculated based on the indicators sent by the institutions according to the provisions of the Commission Implementing Regulation (EU) No. 680/2014 laying down implementing technical standards with regard to supervisory reporting of institutions according to Regulation (EU) No. 575/2013 of the European Parliament and of the Council.

2. Literature review

According to the IMF Guide (Financial Soundness Indicators: Compilation Guide) in the category of non-performing assets, there are included loans and other assets whose instalments, representing principal and interest, are registering delays of 90 days or more. According to the national legislation, the non-performing loans will include in addition those loans with a service of debt less than 90 days which offer clear indications of non-reimbursement, such as the case of bankruptcy.
In the international practice, the criterion of the 90 days remains the most important element for determining the non-performing loans.
In his banking terms dictionary, the author Thomas Fitch defines the non-performing loan as being the loan for which the payment of the principal and of the interest is overdue for more than 90 days and the debtor is in insolvency (Fitch, 2000).
Moody's[2] is an important provider of loan ratings, risk analysis and research of the loans. This company considers that the loan becomes non-performing in the following situations: for the loans granted to the population if they register delays for the principal and for the interest of at least 60 days, for the commercial and leasing loans if they register delays for the principal and for the interest of at least 90 days, any loan for which there are clear indications of non-performance[3].
According to the IMF Guide and international practice, the gross value of the past due and doubtful loans is given by the value of the loans and interests classified in "loss 2" – delays of more than 90 days and/or for which juridical procedures were initiated, registered within the total loans portfolio.

3. Methodology of research

This study proposes to analyse the ratio evolution of the non-performing loans regarding credit institutions (banks, foreign banks branches and Creditcoop) based on the three differentiated calculation methodologies (DiVanna, 2010), agreed by BNR during the period December 2007 – June 2015, using the financial reporting FINREP and COREP, the reporting prepared according to IFRS and the reporting prepared

[2] www.moodys.com/Pages/car001.aspx
[3] www.bnr.ro/r20100705RP.pdf

according to the provisions of the Commission Implementing Regulation (EU) No. 680/2014 laying down implementing technical standards with regard to supervisory reporting of institutions according to Regulation (EU) No. 575/2013 of the European Parliament and of the Council.

4. Data analysis

In Romania the number of the credit institutions decreased from 43 in 2008 to 40 in 2015. The total net assets within the system have registered a constant evolution during the last four years reaching values between 362 – 365 bill RON (see table 1).

Table 1. The evolution of the total net assets of credit institutions in the period 2007-2015

Date	Number of credit institutions	Foreign banks' branches	Total net assets
	(No.)	*(No.)*	*(RON bill.)*
Jun. 2015	40.00	9.00	363,274.30
Dec. 2014	40.00	9.00	364,143.30
Dec. 2013	40.00	9.00	362,259.20
Dec. 2012	40.00	8.00	365,618.10
Dec. 2011	41.00	8.00	353,910.90
Dec. 2010	42.00	9.00	341,946.34
Dec. 2009	42.00	10.00	330,183.50
Dec. 2008	43.00	10.00	314,441.50
Dec. 2007	42.00	10.00	251,425.80

During the period 2007-2015, the assets of the privately-owned institutions decreased in average with 3.37% and the assets of the foreign-owned institutions increased with 8.67% (see figure 1).

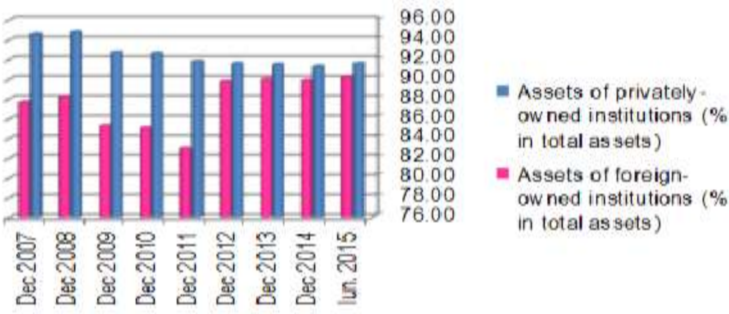

Figure 1. The trend to the assets of privately-owned institutions and to assets of foreign-owned institutions in the period 2007-2015

According to the data provided by the balance sheets of the credit institutions, the gross value of the past due and doubtful loans granted to the clientele had a strongly ascending trajectory from 42.7 bill. RON in 2007 to 530.8 bill. RON. This increase of more than 12 times the value of the past due and doubtful loans reflects the non-performance degree of the loans portfolio (see figure 2).

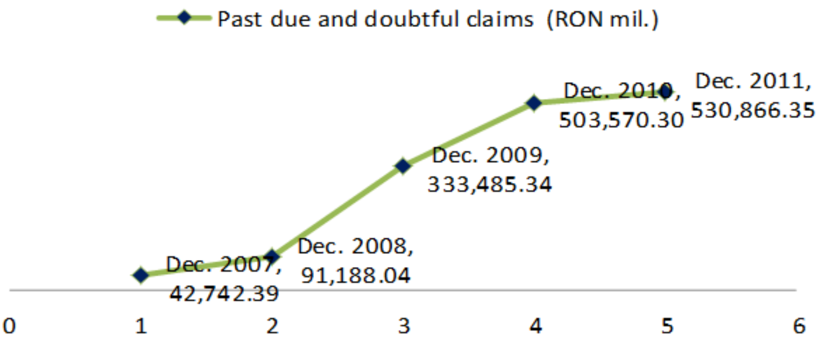

Figure 2. Ascending trend of past due and doubtful claims in the period 2007-2011

The share of the past due and doubtful loans granted to the clientele in total loans portfolio, at net value, has increased constantly from 0.22% in December 2007 to 1.45% in December 2009 and it reached 2.32% in December 2011 (see figure 3).

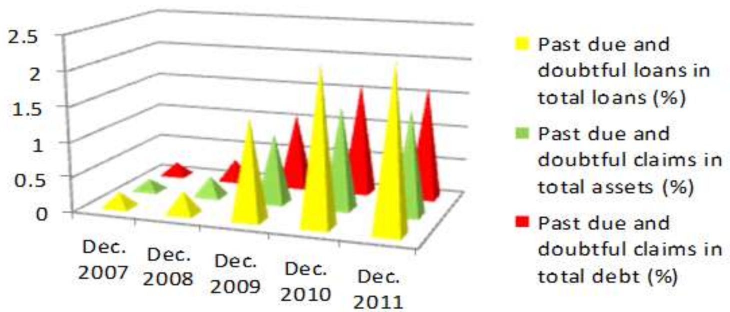

*Figure 3.*Trend share of past due and doubtful loans in total loans, of past due and doubtful claims in total assets and in total debt, in the period 2007-2011

Practically, during the period December 2007 – December 2011, the constant increase of the share of the loans and interests classified in the category "loss 2" in total loans granted to the clientele has determined the quality depreciation of the loans portfolio.
Under these conditions, the covering degree with provisions of these exposures was high, being between 95.7% and 97.8% during the period 2007 - 2011.
During the period September 2009 – March 2011, in light of the increase of the foreign currency indebtedness, both of the population as well as of the non-financial institutions, in a much faster rhythm compared to the national currency, it took place a deepening of the gap between the assets and liabilities in the foreign currency. The rapid extension of the loans portfolio in foreign currency has led to the increase of the credit risk and implicitly to the volume increase of the non-performing loans in foreign currency in a much more accelerated extent compared to the one in RON.
The ratio of the non-performing loans has increased almost 4 times, from 6.46% in 2009 it reached 22.26% in March 2014. (see figure 4)

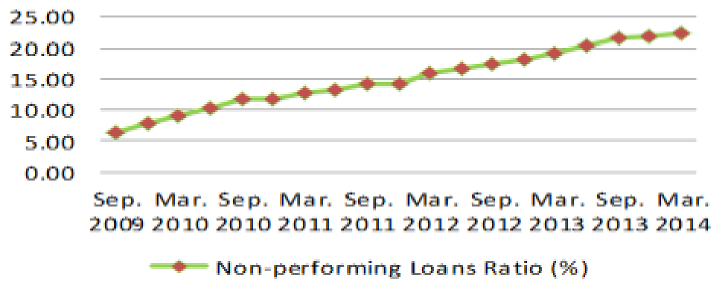

Figure 5. The evolution of non-performing loans ratio during the period Sep. 2014 to Mar. 2015

This strong quality deterioration of the loans portfolio during the last 6 years was mainly due to the worsening of the clients financial situation in light of the international crisis – felt in the case of the non-financial companies, as well as of the population, but also due to the implementing of the new accounting treatments imposed by IFRS. These treatments presume the acknowledgement in the balance sheet of the past due claims previously registered in off-balance accounts, for which expected future flows of cash were calculated.
Starting with May 2014, in order to improve the quality of the loans portfolio, BNR recommended to all the institutions within the system to modify their strategic plans, in line with the market conditions.
Up to this date, the most used methods adopted by the institutions for the reduction of the non-performing loans ratio were: restructuring, rescheduling and enforcement.

In order to support them in their portfolio cleaning process, BNR proposed/ recommended to the credit institutions a plan of measures built on 4 stages[4]:

1. Taking out of the balance sheets the integrally provisioned non-performing loans (the banks keeping their right to recover the debt);
2. Integral provisioning and taking out of the balance sheets of the loans with a debt service of more than 360 days;
3. Integral provisioning and taking out of the balance sheets of the loans granted to companies in insolvency;
4. Performing an external audit of the provisions established according to IFRS and of the guarantees.

The results and the effects of implementing these measures were beneficial for all the participants of this market and they materialized into a reduction of the non-performing loans ratio, from 20.39% in March to 12.80% in December 2014 (see figure 5).

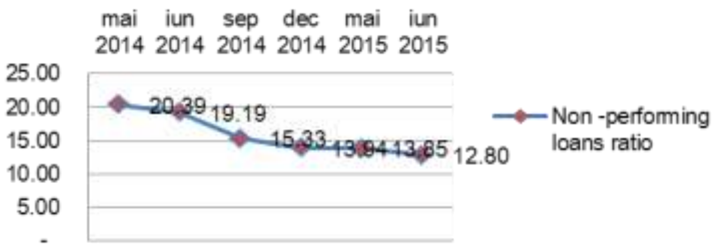

Figure 5. The trend of non-performing loans ratio during the period May 2014 to June 2015

This favourable effect of the assets quality improvement and of the balance sheets cleaning of the institutions was followed by an unfavourable effect (less desired) of reduction of the system profitability following the expenses increase with the provisions.

5. Results

Within the Romanian banking sector, the accelerated increase of the non-performing loans ratio, during the period 2009-2014, is the result of the cumulated action of some factors, such as:

– The increase in a more accelerated rhythm of the granted loans portfolio, in foreign currency, to the clients in the private sector, following the use by all credit institutions of some external financing sources;
– The worsening of the clients financial situation in light of the occurrence of the financial crisis effects within all the Romanian economy;

4 Op. cit. www.bnr.ro/RA2014pdf, p. 26

– The harmonization of the Romanian banking legislation with the European legislation, the application of new accounting treatments and the modification of the reporting according to the provisions of the Commission Implementing Regulation (EU) No. 680/2014 laying down implementing technical standards with regard to supervisory reporting of institutions according to Regulation (EU) No. 575/2013 of the European Parliament and of the Council.

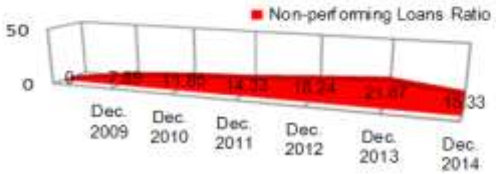

Figure 6. The trend of non-performing loans ratio during the period 2009-2014

The reduction of the non-performing loans ratio with approximately 30% was possible due to the modification of the strategic plans of the credit institutions, at BNR recommendation. Thus the credit institutions moved on from actions such as: restructuring, rescheduling or enforcement to other new actions such as: taking out of the balance sheets the integrally provisioned non-performing loans; integral provisioning and taking out of the balance sheets of the loans granted to companies in insolvency or of the loans with a debt service of more than 360 days and performing an external audit of the provisions established according to IFRS and of the guarantees.

5. Conclusions

In conclusion, for the cleaning of the loans portfolio, the institutions have formed specialized collecting companies to which they transferred the biggest portion of the non-performing loans taken out of the balance sheet and provisioned integrally (consumer loans, loans for purchase of goods, credit cards and mortgage loans). These companies' object of activity is the debt recovery of the institutions which became their majority shareholders. Currently, the most of the transactions especially targeted by these companies are related to the non-performing loans with mortgage guarantees.

Refrences

Burduș, E. (2005). *Tratat de management –.Strategia organizației și managementul strategic*, Ed. Economică, p. 45.
Day, G. (2009). *Strategic Marketing Analysis Top-down and Bottom–up approaches*, Marketing Science Institute, Cambridge, May, p. 67.

DiVanna, J.A. (2010). *The future of retail banking*, Publisher Palgrave, London, p. 123.
Engler, H., Essinger, J. (2000). *The future of banking*, Publisher Pearson Education, London, p. 35
Fitch T. (2000). *Dictionary of Banking Terms*, Third Edition, Editions McGraw Hill, New York, p. 13.
Saunders, A. (2003). *Financial Institution Management - A modern perspective*, McGraw Hill, Irwin, p. 92.
www.bnr.ro
www.moodys.com/Pages/car001.aspx