

## THE ANALYSIS OF BANKING SECTOR IN MOLDOVA IN 2014 THROUGH FINANCIAL STABILITY INDICATORS

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*The objective of this article is to analyze the banking sector in the Republic of Moldova in terms of financial stability indicators. Thereby the authors elucidated the main developments of banking institutions in 2014, as reflected by the deterioration of the prudential indicators of this sector. The problems in the banking sector were caused by dubious transactions of some commercial banks, as well as their plight. Despite the establishment of special administration at 3 financial institutions (B.C. „Unibank” S. A., B.C. „Banca Social ” S.A. and B.C. „Banca de Economii” S.A.), the banking sector failed to maintain a reliable activity, causing problems with bank loans.*

**Key words:** banking sector, financial stability, indicators of concentration, uncertainty, assets, deposits, loans, profitability and solvency.

*Obiectivul acestui articol este analiza sectorului bancar din Republica Moldova, prin prisma indicatorilor de stabilitate financiar . Astfel, autorii au elucidat principalele evolu ii ale institu iilor bancare în anul 2014, fiind reflectate prin deteriorarea indicatorilor pruden iali ai sectorului. Problemele din sectorul bancar au fost încorporate de tranzac iile dubioase ale unor b nci comerciale, cât i de situa ia precar a acestora. În pofida faptului instituirii administr rii speciale la 3 institu ii financiare (B.C. „Unibank” S.A., B.C. „Banca Social ” S.A. i B.C. „Banca de Economii” S.A.), sectorul bancar nu a reu it s men in o activitate de încredere, generând probleme la capitolul acordarea creditelor bancare.*

**Cuvinte cheie:** sectorul bancar, stabilitate financiar , indicatori de concentrare, incertitudine, active, depozite, credite, profitabilitate, solvabilitate.

2014

( „Unibank” S.A.,

„ ” S.A. „ ” S.A.),

**JEL Classification: G21; G29; E51; E59; D81.**

**Introduction.** The roles of banking institutions are an important fern in the financial sector of any state. For a stable and efficient financial system, the Moldavian banking sector should be encouraged to obtain high and long lasting performance. One of the main objectives of banking institutions is optimizing profits, the bank performance is an indication of stability and depositor confidence.

In 2014, the financial system of the Republic of Moldova faced a series of risks interconnected at sartorial level. Thus, banking sector stability was disturbed by some negative effects that triggered the deterioration of prudential indicators. The problems in the banking sector were caused by dubious transactions of some commercial banks as well by their precarious financial situation. In this context, uncertainty about the quality of loans and that of bank capital will continue to persist in 2015. The

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indicators for assessing the bank performance have a great expressiveness, reflecting many aspects such as the generating profit level and the operational and managerial efficiency.

#### Degree of financial intermediation

The degree of financial intermediation of the banking sector in the Republic of Moldova (determined as weight of assets, loans and deposits in the GDP) improved significantly over the period 2010-2014, though posting a slight deviation in the 2014 in terms of loans granted in relation to GDP. The weight of bank assets in the GDP increased from 58.8% in 2010 up to 87.5% in 2014. Similar developments were recorded in the case of deposits in relation to GDP. Thus, the weight of deposits in relation to the GDP increased from 40% in 2010 to 58.7% in 2014.

The year 2014 was characterized by a significant increase of 6.7 p.p. in this indicator by the end of 2013, the rise of this indicator was primarily due to the increase (by 26.2%) in balance of deposits at the end of 2014 on account of increase in deposits of individuals by 53%, and in deposits of legal entities by 47.2% (see Figure 1). The growth rate of the intermediation degree pertaining to assets and deposits was more pronounced in 2014 than in the previous year.

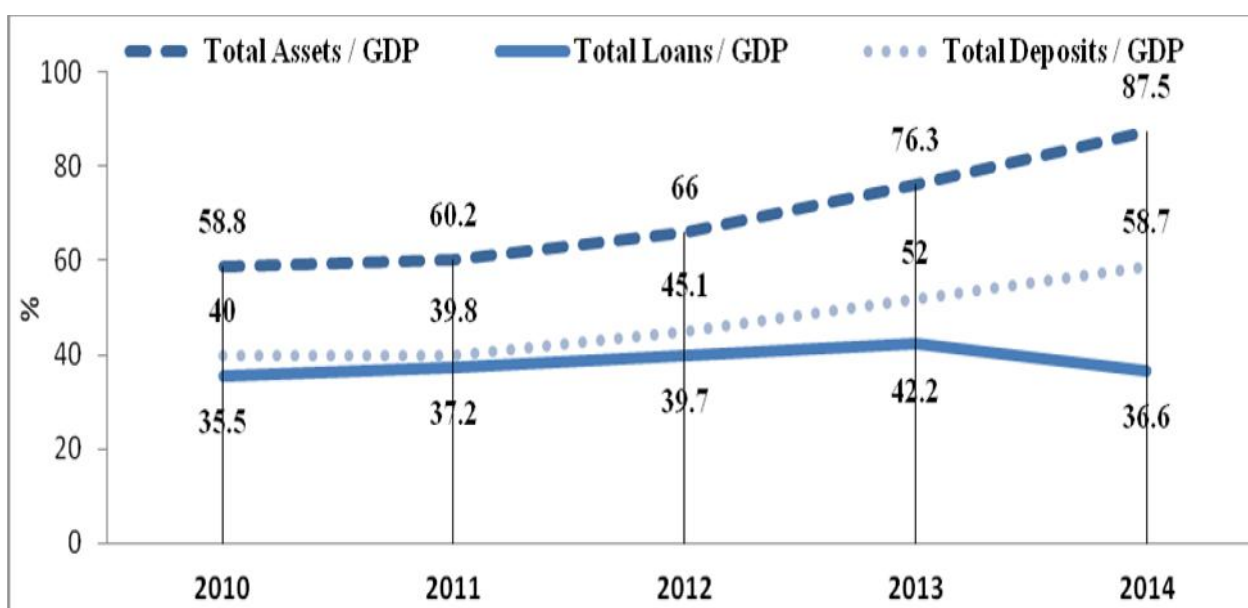


Fig. 1. Degree of financial intermediation, %

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

Deterioration in the quality of banks' loan portfolio (B.C. „Banca Social ” S.A., B.C. „Banca de Economii” S.A. and BCR Chi u S.A.), and additionally the institution of special administration upon 3 financial institutions (B.C. „Unibank” S.A., B.C. „Banca Social ” S.A. and B.C. „Banca de Economii” S.A.), continued to affect negatively the degree of financial intermediation, calculated as a percentage of loans provided by banks to the GDP, and at the end of 2014 its value equaled 36.6%, posting a decrease of 5.6 p. p. compared to the end of 2013. The decrease in this indicator will continue to record negative dynamics also in 2015, against the background of problems in the banking sector, which may gradually disturb the stability of the sector.

#### Analysis of market concentration indices in the banking sector

Having analyzed the market concentration index (Herfindahl-Hirschman Index), as of December 31, 2014, we found that the market concentration ratio in the banking sector is moderate in terms of value of deposits (1,361.6 points) and value of loans (1,560.9 points) (see Table 1).

As of the end of 2014, in terms of bank assets value the market was concentrated. Four commercial banks held 64.2% of total assets. Referring to the assets value, as of December 31, 2014, the market leader was BC Banca Social S.A. with total assets of 20,115.9 million MDL, i. e. an increase by 4.5 times compared to 31.12.2013, recording a share of 20.6% of the total assets in the sector. It was followed by BC Moldova-Agroindbank S.A. whose volume of assets totaled 15,341.4 million MDL, posting an increase of 14.4 million MDL, compared to 31.12.2013, bank's market share was 15.7%.

Table 1

## Concentration index in the banking sector, %

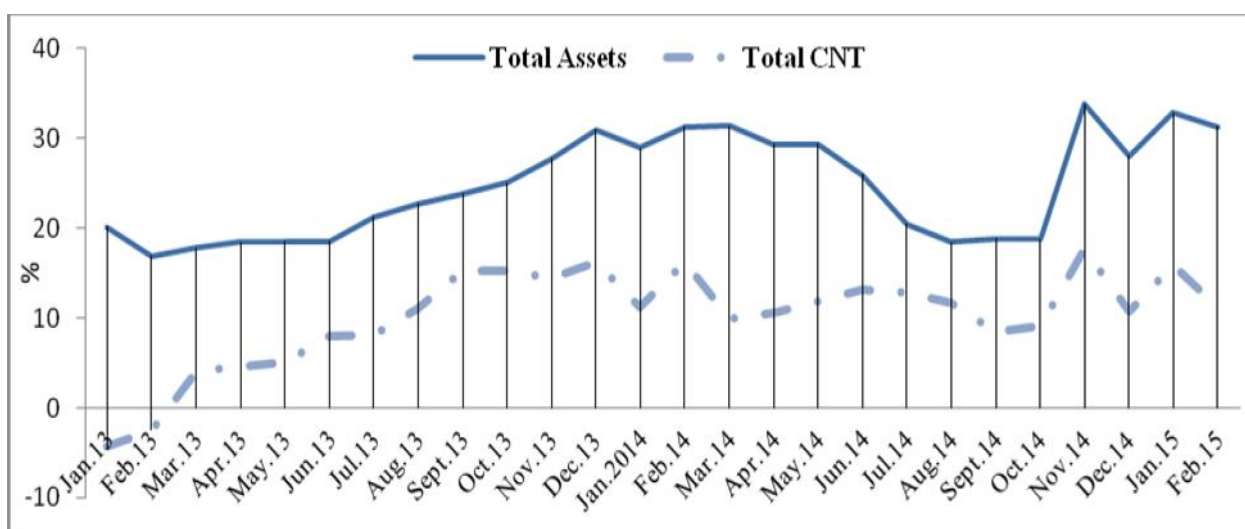
Nr.	Name of the Bank	Market share by value of assets (%)		Market share by value of loans (%)		Market share by value of deposits (%)	
		31.12. 2013	31.12. 2014	31.12. 2013	31.12. 2014	31.12. 2013	31.12. 2014
1	BC „MOLDOVA - AGROINDBANK” S.A.	17.6	15.7	22.8	26.5	18.3	17.5
2	B.C. „VICTORIABANK” S.A.	15.3	12.5	16.6	14.1	18.2	14.7
3	BC „Moldindconbank” S.A.	16.8	13.6	18.8	21.8	18.0	13.7
4	B.C. „Banca de Economii” S.A.	11.2	14.3	3.7	3.3	11.3	10.8
5	B.C. „EXIMBANK - Gruppo Veneto Banca” S.A.	6.0	4.0	2.5	5.6	3.9	3.1
6	BC „BANCA SOCIALA” S.A.	5.8	20.6	7.2	4.8	5.8	21.2
7	BC „MOBIASBANCA – GroupeSocieteGenerale” S.A.	5.9	5.9	6.9	8.4	5.7	6.2
8	B.C. „UNIBANK” S.A.	9.5	3.6	8.3	2.3	8.7	4.0
9	B.C. „ProCredit Bank” S.A.	3.9	3.2	5.5	5.6	3.1	2.7
10	B.C. „ENERGBANK” S.A.	2.6	2.1	2.5	2.6	2,6	2.1
11	B.C. „FinComBank” S.A.	2,6	2,1	2,6	2,6	2,2	2,1
12	BCR Chi inau S.A.	1.3	1.1	1.2	1.1	0.9	0.8
13	B.C. „COMERTBANK” S.A.	1.1	0.9	1.0	1.0	1.1	0.9
14	BC „EuroCreditBank” S.A.	0.4	0.4	0.4	0.4	0.2	0.2
<i>HHI index (points)</i>		1178.2	1303.1	1385.3	1562.9	1298.6	1361.64
<i>CR-4index (%)</i>		60.9	64.2	66.5	70.8	65.8	67.1

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

As of December 31, 2014, B.C. „Moldova Agroindbank” S.A. maintained its market leader position in terms of lending. Thus, the bank's share in all loans provided accounted for 26.5%, a position which would not be lost in a short time (total balance of 10,826.1 million MDL, which increased by 18.0% compared to December 31, 2013). The second market leader was B.C. „Moldindconbank” with a market share of bank loans amounting to 21.8%, followed by B.C. „Victoriabank” S.A. (14.1%). With regard to the structure of deposits, at the end of December 2014, the market leader position in terms of balance of attracted deposits was held by B.C. „BancaSocial ” S.A. with a total balance of 13,903.1 million MDL, recording an increase by 5 times compared to December 2013. The bank's market share was 21.2%. It is followed by BC „Moldova Agroindbank” S.A. (17.5%), as of December 31, 2014, it posted balance of attracted deposits totaling 11,487.7 million MDL, or by 20.7% less compared to December 31, 2013.

#### Dynamics of bank assets

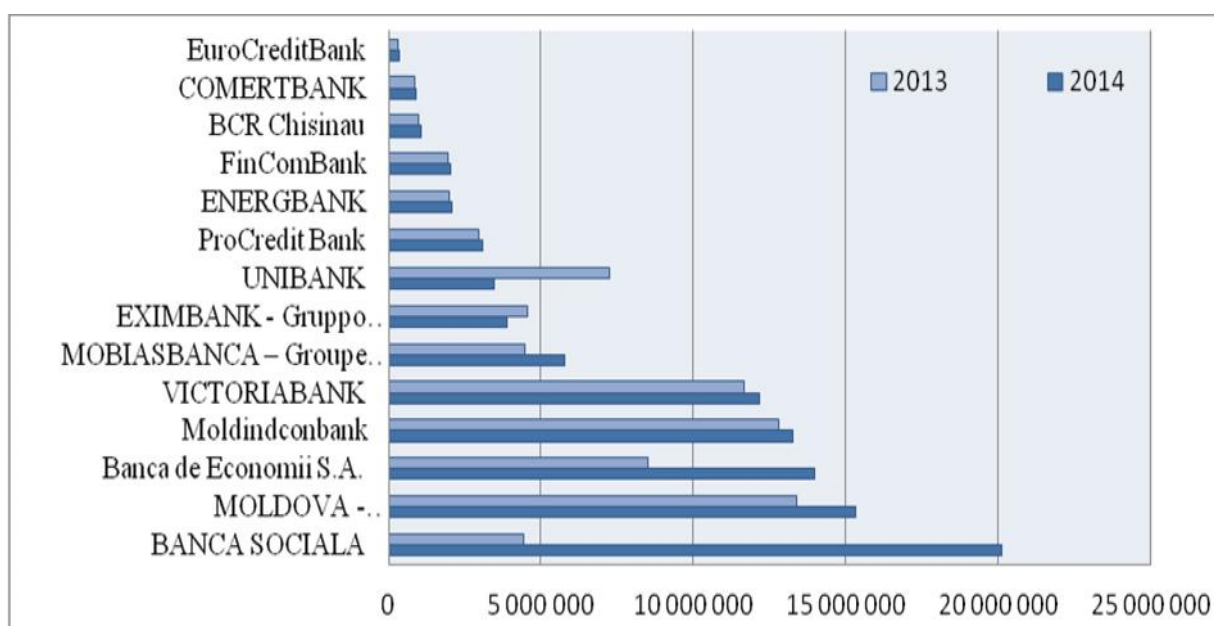
Similar to the situation posted in 2013, total bank assets showed positive dynamics in 2014 following an increase of 28% totaled 97,584.4 million MDL. Profit-generating assets accounting for 44% of total assets, however compared to December 31, 2013 there was a decrease of 13.4%. By the end of 2014, the annual growth rate of bank assets was on the rise. This increase was clearly reflected from October 2014 (18.76%) until December 2014 (28.09%).



**Fig. 2. Annual growth rate of assets and of TRC, %**

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

In 2014, in terms of competition of banking assets held by the top 5 banks in total assets, there was a negative trend. Correspondingly, as of December 31, 2014 the weight of assets held by the top five banks in the aggregate assets accounted for 76.75% posting an increase of 6.32 p.p. in comparison with December 31, 2013. Assets are the one generating the greatest risks for commercial banks therefore there is need for cautious management thereof.

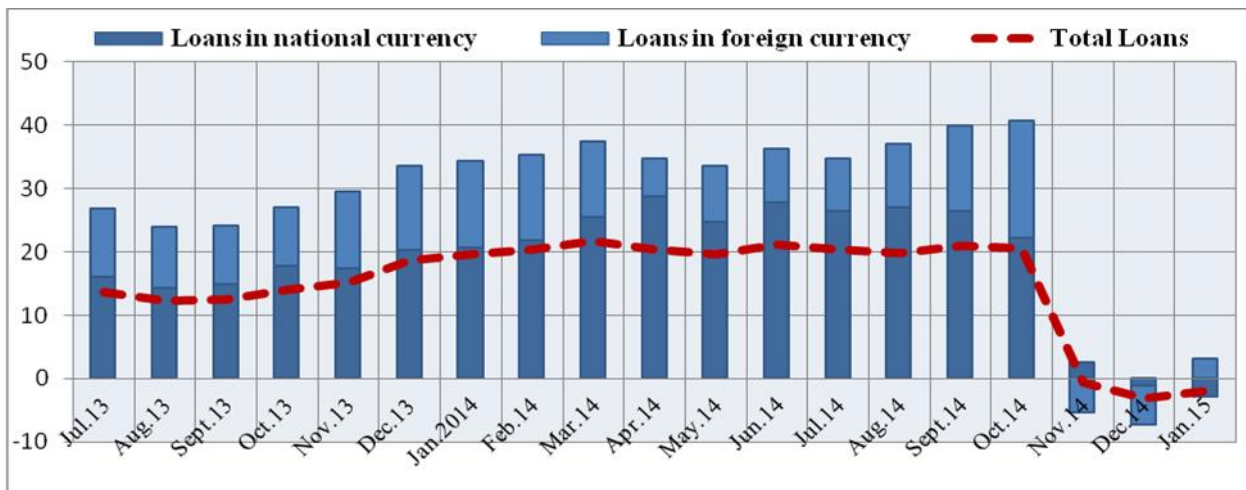


**Fig. 3. Development of commercial banks assets, million MDL**

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

#### Development of bank loans

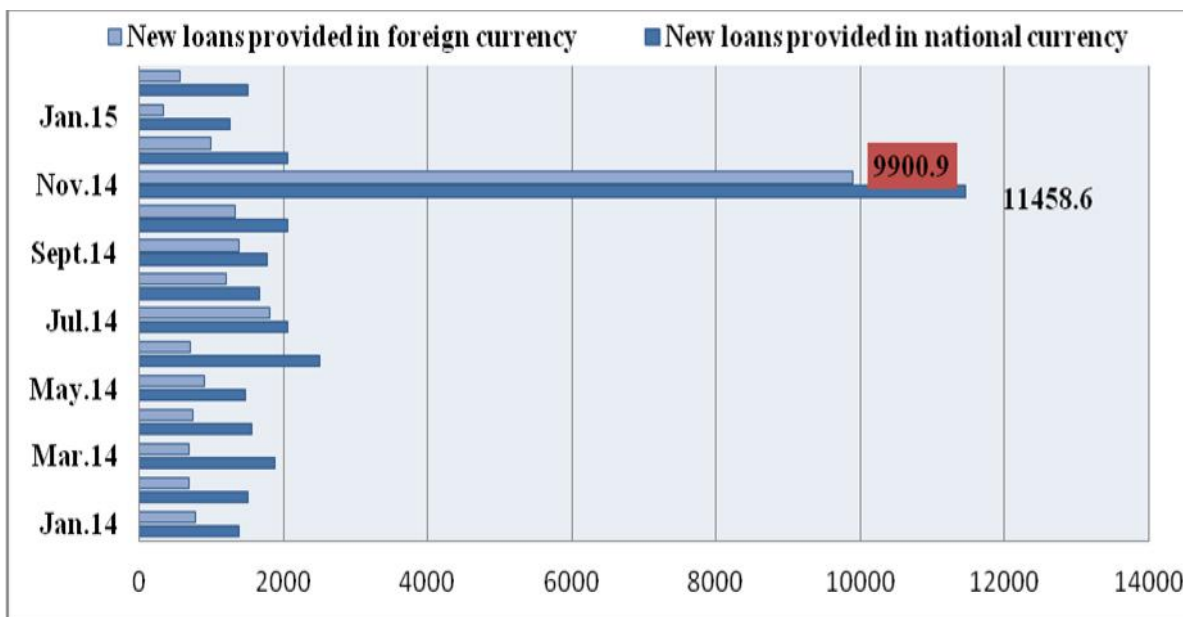
In 2014, the lending activity in the Republic of Moldova posted contradictory developments. As of December 31, 2014 the *balance of bank loans* amounted to 40,841.98 million MDL, i.e. decreasing by 3.2% compared to December 31, 2013. After a period when the lending activity was on the rise, which lasted almost 10 months (from December 2013 to October 2014), in November 2014 the loan portfolio decreased considerably. Thus, the annual growth rate of loans provided by banks in November 2014 decreased by 0.67% compared to the same period of the last year and in December 2014 by 3.17% splay. The largest contribution to the decrease posted in November 2014 pertained to loans in foreign currency reduced by 17.4% and loans in national currency by 13.6% compared to October 2014.



**Fig. 4. Annual growth rate of loans in the banking sector, loans in foreign currency and in national currency, %**

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

At the same time, in November 2014 there was an excess of new loans made in amount of 21,359.5 million MDL (accounting for 52.5% of total loans in the whole banking sector), respectively, loans provided in national currency accounted for 53.6% of total new loans and in foreign currency - 46.4%. According to the reports published by the NBM, we observe that the excess new loans, granted in November 2014, were made to legal persons in national currency with maturity of 2 to 5 years in the amount of 10,235,072 thousand MDL at an average interest rate of 9.68% and to legal entities in foreign currency (in amount of 9,317,864 thousand MDL) at an average interest rate of 8.20%.



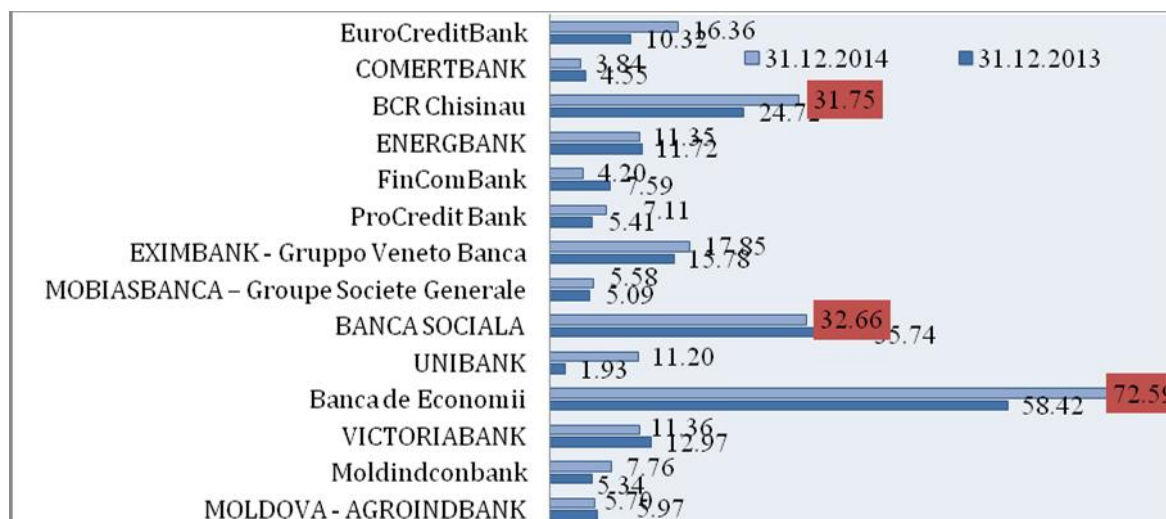
**Fig. 5. Volume of new loans provided in MDL in foreign currency, million MDL**

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

In this context, the analysis of the loan structure by maturity date in 2014 showed that the loans with maturity from 2 years to 5 years remained the most attractive also in December 2014. Thus, their share in the total volume of loans provided in national currency amounted to 38.4% in December 2014, and average interest rate on these loans was 11.35%. Most of the loans provided in MDL were made to legal entities, i.e. accounting for 79% of total loans in MDL and the average interest rate as of December 2014 was 10.64%.



By the end of 2014, there was an improvement of the loan portfolio quality in the banking sector, as the value of non-performing loans decreased by 2%<sup>1</sup> compared to the beginning of the year. As of December 31, 2014, the weight of non-performing loans in total loans increased by 0.17 p.p., compared to December 31, 2013, equaling 11.73%. Another indicator that showed higher risks for capital loss was the weight of net non-performing loans in the total regulatory capital; as of December 31, 2014, it decreased by 6.6 p.p. down to 53.04% compared to December 31, 2013.



**Fig. 6. Weight of non-performing loans in the banking sector as of 31.12.2013 and 31.12.2014, %**

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

At the end of 2014, the highest weights of nonperforming loans pertained to three commercial banks (B.C. “Banca Social ” S.A. – 32.66%; B.C. „Banca de Economii” S.A. – 72.59% and BCR Chi in u S.A. – 31.75%) out of 14 banks. The upward trend of this indicator reflects deterioration in the quality of the credit portfolio of these banks as well as the low level of stability of the entire banking system. Lending activity remains to be the main loss-generating source in a bank. Thus, to avoid the lending-related risks, financial institutions turn to make loans to profitable industries. In this context, we noted that in 2014 the highest weight in the total loans pertained to loans provided to trade (32.9%), followed by loans made to food industry (9.8%), consumer loans (7.4), loans to processing industry (7.4%), credits to services providers (7%), followed by loans to agriculture (6.4%).

**Dynamics of bank deposits.** The *balance of deposits* in the banking system as December 31, 2014, amounted to 65,462.5 million MDL, increasing by 26.2%, compared to December 31, 2013. This ascending trend was largely due to the increase in the balance of deposits in national currency by 9.3% and that of deposits in foreign currency by 47%, compared to December 31, 2013. Following the depreciation of the national currency over the last period, population gave preference to deposits in foreign currency, which accounted for 52.1% at the end of September 2014, while the deposits in national currency represented 47.9% of total deposits. This is explained by the fact that the average interest rate on deposits in the banking system is more attractive in the case of deposits in foreign currency (in December 2014 – 3.98%, or 0.56 p.p. increase compared to January 2014) than the interest rate on those in national currency (in December 2014 – 6.47%, or 0.62 p.p. decrease January 2014). Reducing investment in national currency population was subject to high fluctuations of the exchange rate in 2014, nominal depreciation of the against the USD and EURO is more than 11% compared to previous year, while deposits in domestic place ments exposed population loss of purchasing power risk.

<sup>1</sup>As of 31.12.2014, in absolute terms, non-performing loans amounted to 4,790.34 million MDL and as of 31.12.2013 – 4,876.44 million MDL.



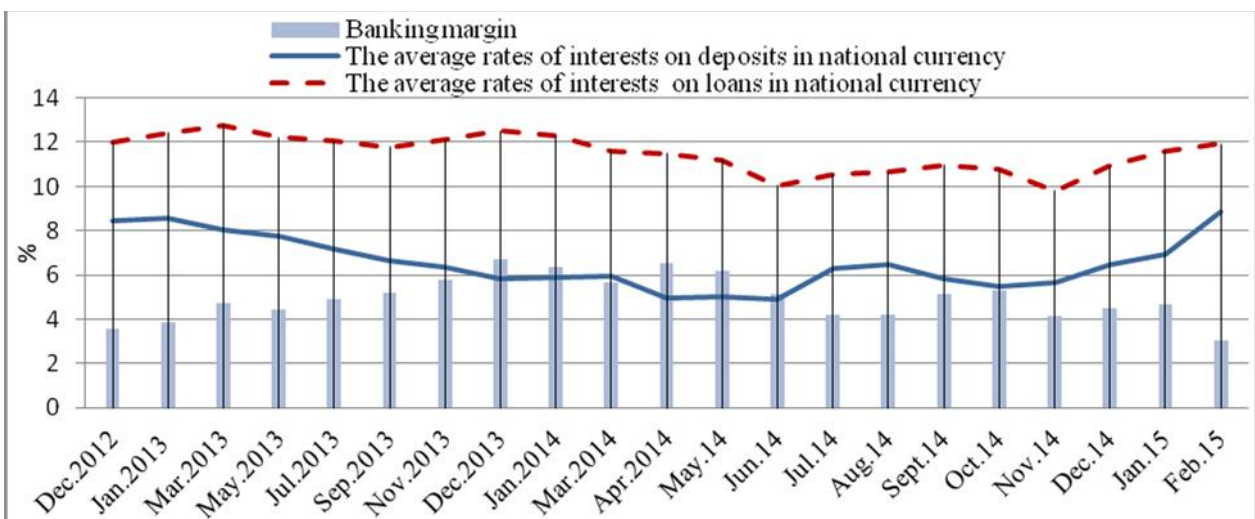
**Fig. 7. Annual growth rate of deposits in the banking sector, deposits in foreign currency and in national currency, %**

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

In terms of maturity of the deposits in national currency, population mostly preferred term deposits for 6 to 12 months. Thus, in December 2014, the highest weight in the total term deposits attracted in national currency still pertained to deposits for terms of 6 to 12 months (41.7%). Correspondingly, the term deposits in foreign currency for terms of 6 to 12 months also had a maximum weight of 44.1% and an average rate of 4.25%.

**Development of the average interest rate in the banking system**

As of December 31, 2014, the bank loans cheapened by 1.34 p.p., the average interest rate on new loans provided in the banking system decreased from 12.29% in January down to 10.95% in December. Correspondingly, the average interest rates on loans in foreign currency also fell by 0.11 p.p., from 7.83% in January 2014, down to 7.72% in December 2014. New deposits in national currency were attracted by commercial banks, in December 2014, at an average rate of 6.47%, i.e. an increase of 0.56% compared to January 2014 (5.91%). At the same time, the average interest rates on deposits in foreign currency declined from 4.60% in January 2014 to 3.98% in December 2014, decreasing by 0.62 p.p.



**Fig. 8. Development of the banking margin\*, average rates of interests on deposits and loans in MDL, %**

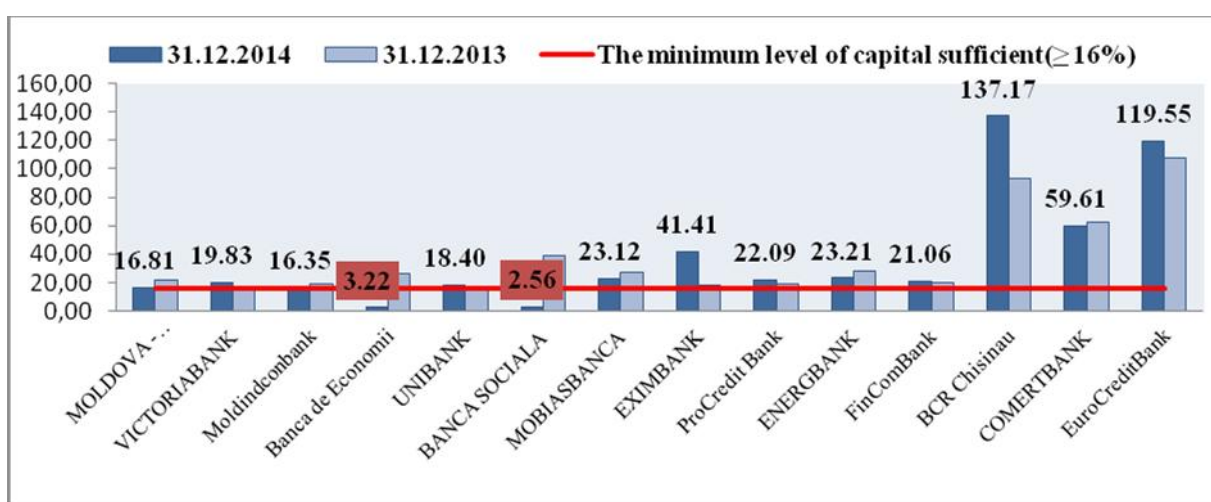
Source: Authors' calculations based on the data of the National Bank of Moldova.

\*Note: The banking margin index was calculated as the difference between the average rate on loans in MDL and average rate on deposits in MDL.

The banking margin for transactions in foreign currency had a smaller variation margin compared to that for transactions in national currency. In December 2014, the banking margin for transactions in national currency was at the level of 4.48%, decreasing by 2.21 p.p. compared to December 2013, while the low (4.14%) of 2014 was posted in November 2014. Correspondingly, in December 2014, the margin related to foreign currency transactions recorded a stable development, reaching the level of 3.74%, though posting a slight decrease of 0.66 p.p. compared to December 2013.

#### Development of bank capital

At the end of 2014 the *solvency ratio* in the banking system recorded a value inferior to the minimum requirement set by law (16%), amounting to 13.21% (a decrease of 9.81 p.p. compared to 31.12.2013), due to worsened financial situation in B.C. „Banca de Economii” S.A. (3.22%) and B.C. „Banca Social ” S.A. (2.56%). Despite the under level of the risk-weighted capital adequacy throughout the banking system, at the end of 2014 there was a positive dynamic in the TRC, which posted an increase of 10.6% as of December 31, 2014, compared to December 31, 2013. Correspondingly, as of December 31, 2014, Tier I capital increased by 9.8% up to 8,707.29 million MDL compared to December 31, 2013. The risk-weighted assets recorded in 2014 an increase of 92.6% compared to 2013.



**Fig. 9. Average of the risk-weighted capital adequacy in the banking sector, %**  
Source: Authors' calculations based on the data of the National Bank of Moldova.

The share of foreign investments in the banks' capital increased from 72.24%, as of December 31, 2013 to 76.75% as of December 31, 2014. However, this contributed to lowering of the market concentration degree: by December 31, 2014 the weight of the 5 largest banks' assets in total assets declined to 67.48%. Four licensed banks have fully foreign owned capitals (B.C. „EXIMBANK-Gruppo Veneto Banca” S.A.; B.C. ”ProCredit Bank” S.A.; BCR Chi in u S.A.; B.C. „COMER BANK” S.A.), followed by B.C. „Mobiasbanc – Groupe Société Générale” S.A. with 96,69% foreign capital and B.C. „Euro Credit Bank” S.A. – 98,82%.

#### Development of bank profitability and liquidity

The indicator *return on equity* (ROE) throughout the banking sector recorded a lower level than that of the previous year (6.39% in 2014 compared to 9.42% in 2013). ROE analysis based on determinants, revealed a slight deterioration in remuneration pertaining to bank capital as a result of the diminished capacity of assets to generate profit (from 1.56 in 2013 to 0.92% in 2014). The return on assets (ROA) in the banking system measures the effect of managerial capacity to use financial and real resources of the banking society with the view to generate profit. In December 2014, overall banks' profit amounted to 778.2 million, which is 23.7% less compared to the same period of 2013.

Therefore, three commercial banks recorded negative financial results at the end of December 2014: B.C. „Eximbank Gruppo Veneto Banca” S.A. – 217.8 million MDL, followed by Banca de Economii S.A. – 202.5 million MDL and BCR Chi in u S.A. – 3.7 million MDL. In terms of profit, it has to be mentioned that at the end of December 2014, B.C. „Moldova Agroindbank” S.A. was leading with the profit equaling 397.5 million MDL, followed by B.C. „Moldova Agroindbank” S.A., that obtained profit in amount of 357.5 million MDL and B.C. „Victoriabank” S.A. with 205.4million MDL.



At the end of 2014, *liquidity indicators* of the banking sector registered values above the regulated level, liquid assets ratio (liquidity principle II) accounted for 21.63%, or 12.13 p.p. less compared to December 31, 2013. Long-term liquidity throughout the banking system recorded 1.54%, as of December 31, 2014, or by 0.83 p.p. more compared to December 31, 2013. However, on December 31, 2014 there were three commercial banks (B.C. “Banca Social ” S.A., B.C. „Banca de Economii” S.A. and B.C. „Unibank” S.A.) posting values lower than those regulated by the BNM – minimum level of liquidity ( 20%). Thus, ensuring adequate liquidity is one of the most important objectives of the management of any banking institution. In order to avoid difficulties in procuring the necessary resources with the view to meet own commitments at any given time, banks have to tackle the liquidity risk.

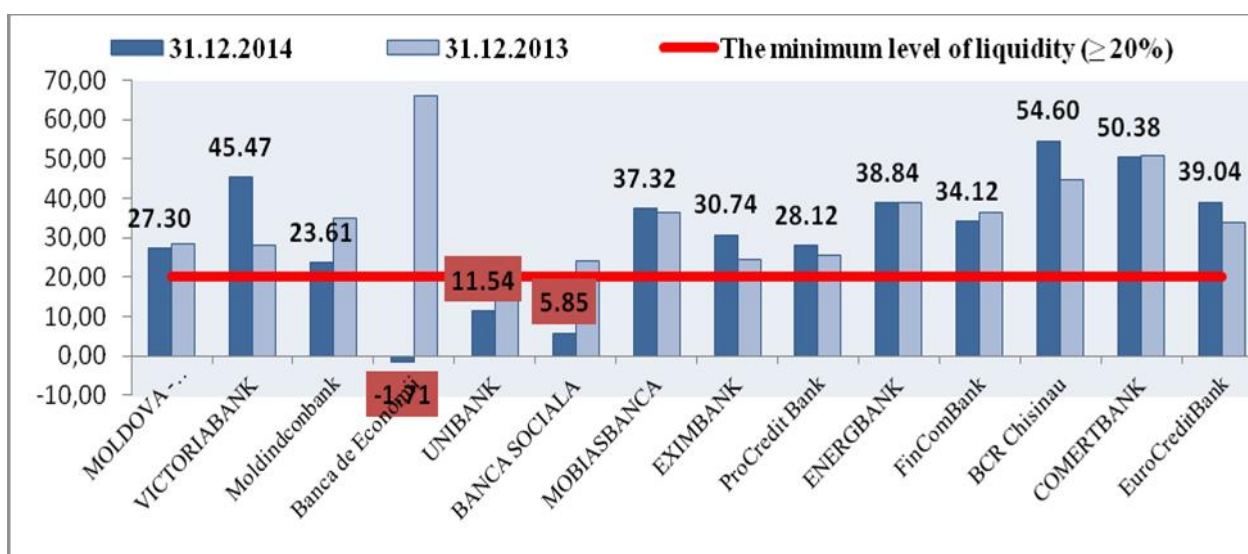


Fig. 10. Liquidity indicators of the banking sector, %

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

### Conclusions

The main indicators of the banking sector activity had a contradictory evolution in 2014. Thus, at the end of December 2014 in comparison with the end of December 2013, the main indicators of banking sector activity **posted following deteriorations:**

- ✓ Decline in bank profit by 23.7%, totaling 778.2 million MDL, due to the negative financial results recorded by three commercial banks: B.C. „Eximbank Gruppo Veneto Banca” S.A. – 217.8 million MDL, B.C. „Banca de Economii” S.A. – 202.5 million MD and BCR Chi in u S.A. – 3.7 million MDL;
- ✓ Increase in the volume of non-performing loans from 1.56% to 11.73%;
- ✓ Decrease in the balance of bank loans by 3,2%, down to 40,847.98 million MDL;
- ✓ Capital adequacy recorded a value inferior to the minimum requirement set by law ( 16%), amounting to 13.21% (a decrease of 9.81 p.p. compared to 31.12.2013), due the worsened financial situation in B.C. „Banca de Economii” S.A. (3.22%) and B.C. „Banca Social ” S.A. (2.56%);
- ✓ Increase in the risk-weighted assets by 92.6%;
- ✓ Decrease in ROE from 9.42% in 2013 down to 6.39% in 2014;
- ✓ Reduction in ROA from 1.56% in 2013 to 0.92% in 2014;
- ✓ Deterioration in the quality of credit portfolio of the banks: B.C. „Banca Sociala” S.A. – 32,66%; B.C. „Banca de Economii” S.A. – 72,59% and BCR Chi in u S.A. – 31,75%;
- ✓ Decrease of liquid assets ratio (liquidity principle II 20%) by 12.13 p.p. compared to 31.12.2013, registering 21.63%. Reduction of this indicator down to the limit set by the NBM was triggered by worsened situation in the case of three commercial banks: B.C. „Banca Social ” S.A., B.C.„Banca de Economii” S.A. and B.C.„Unibank” S.A. and institution of special administration upon these 3 financial institutions.

However, despite the problems emerged in the sector because of these three commercial banks, some indicators posted positive developments, thus at the end of December 2014 compared to the end of December 2013 it was attested:

- ✓ Increase in the bank assets by 28%, up to 97,584.4 million MDL;

- ✓ Reduction, in absolute terms, in the non-performing loans by 2% down to 4,790.34 million MDL;
- ✓ Rise in the balance of bank deposits by 26.2%, up to 65,462.5 million MDL;
- ✓ Increase in the balance of bank deposits in national currency by 9.3% (preponderantly on account of the deposits of banks);
- ✓ Increase in the balance of bank deposits in foreign currency by 47%;
- ✓ Decrease in the average interest rate on loans in national currency from 12.51% in December 2013 down to 10.95% in December 2014;
- ✓ Decrease in the average interest rate on loans in foreign currency, from 8.91% in December 2014, down to 7.72% in December 2014;
- ✓ Decrease in banking margin for transactions in national currency from 6.69% in December 2013, down to 4.48%, or by 2.21 p.p.;
- ✓ Decrease in banking margin for transactions in foreign currency from 4.4% in December 2013, down to 3.7%, i.e. by 0.7 p.p.;
- ✓ Increase of the TRC by 10.6%;
- ✓ Increase in the I Tier capital by 9.8% up to 8,707.29 million MDL.

*The NBM should closely monitor the developments in the economic and financial environment at the country level and possible risks to the financial sector, taking action to maintain an adequate level of prudential indicators by Moldovan banking sector.*

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