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Annual Report 2012

Annual Report, 2012 [1]

Summary

The world economy in 2012 combined the problems of the euro area sovereign debt crisis and fiscal problems of the U.S., which led to an increased vulnerability of major currencies and a reduction in international trade. Additionally, the decreased demand from economies with a significant weight in world consumption led to a reduction in international prices of raw materials, which is unfavorable for emerging economies and especially for those significantly dependent on the volume and price of raw materials exported. The difficulties range was completed with strong uncertainties that prevailed in 2012 on the financial markets, certain events causing severe turbulence throughout the world.

The Moldovan economy recorded a contraction of 0.8 percent in 2012 compared to 2011, primarily due to the negative development of the agricultural sector, attributable to a pronounced drought, and due to a poor domestic demand. At the same time, the external environment was less favorable, with the contracting European economy, which resulted in a moderate external demand, the exports increasing by only 2.3 percent. Household consumption increased only by 1.0 percent in 2012, the increase being much lower than in 2010 and 2011, due to the slower growth in disposable income of the population and reduced consumption of goods and services in kind. General government final consumption recorded an increase of 0.5 percent. Gross capital formation declined by 2.8 percent, driven solely by the evolution of changes in inventories component. Gross fixed capital formation recorded an increase of 0.4 percent, mostly due to augmented expenditures for capital repairs of fixed capital, while the capital investment registered a decline of 3.1 percent. The modest growth rate in domestic consumption and the investment's contraction led to a lower growth rate of imports of goods and services, so it constituted 2.5 percent. Agriculture declined by 23.3 percent, while gross value added in industry grew by only 0.5 percent. In 2012, the unemployment rate was 5.6 percent, decreasing by 1.1 percentage points. However, the reduction in the number of unemployed people has not been accompanied by a positive trend in employment.

In 2012, the National Bank of Moldova created the conditions necessary to keep the inflation rate within the range of 5.0 percent ± 1.5 percentage points, a goal set for 2012 according to the National Bank's monetary policy strategy for 2010-2012. Thus, in February 2012, the annual inflation rate entered the respective corridor, representing 6.1 percent, and for the month of December 2012 - 4.1 percent. At the same time, in December 2012, the annual inflation rate was by 3.7 percentage points lower than the 7.8 percent recorded in December 2011. During 2012, the annual rate of core inflation has registered a downward trend, mainly due to the slowing domestic demand, so it fell from 5.9 percent in January to 3.7 percent in December. The dry weather conditions in the region, which caused increases in food prices, were the main factors that have exerted inflationary pressures during 2012. At the same time, price increases in the CPI were favored by side effects caused by rises in tariffs in the fall of 2011 and tariff increases in electricity in May 2012. The main factor that weakened the price increase during 2012 was a lower aggregate demand than in the previous years due to the slowdown in the growth of household disposable income. The nominal exchange rate of the national currency against the currencies of major trading partners exercised broadly disinflationary pressures in the reporting period.

Quantifying the macroeconomic situation, the trends and projections of macroeconomic indicators in the medium term, the inflation outlook in the short and medium term on the background of potential risks and uncertainties in the reference

period, as well as to anchor inflationary pressures, the National Bank has promoted during 2012 an adaptive monetary policy under a low inflation, monitoring and anticipating developments in the domestic and international economic environments, so that through the flexibility of the operational framework specific to the inflation targeting strategy, it ensured price stability in the medium term.

Thus, in 2012, the National Bank of Moldova has decided on two consecutive reductions of the monetary policy interest rate by 2.0 percentage points. Within the meeting of the Council of Administration of the NBM on January 26, 2012, after the assessment of the balance of risks associated with the inflation outlook in the medium term, it was decided to reduce the monetary policy rate from 8.5 to 6.5 percent annually. On February 23, 2012, due to the persistence of deflationary risks determined by a potential decrease in the economic activity and domestic demand, and the continued deterioration of expectations on developments in global economic activity, it has been decided to further reduce the monetary policy rate by 2.0 percentage points, from 6.5 percent to 4.5 percent. Until the end of 2012, the aforementioned rate was not changed, being maintained at the level of 4.5 percent.

That decision was aimed at anchoring inflation expectations in terms of strengthening the prospects of keeping inflation within the range of variation of ± 1.5 percentage points from the target of 5.0 percent.

The set of monetary policy instruments used by the National Bank of Moldova, corresponding to the existent operational framework, has proved to be still appropriate for monetary policy implementation requirements.

Under the influence of increased liquidity excess, the liquidity injection activity of the NBM in 2012 can be characterized as a secondary one, as the liquidity sterilization operations from the market, like in 2011, continued to play the main role.

The standing facilities regime (overnight deposits and credits) in 2012 allowed banks to manage their liquidity efficiently and provided National Bank of Moldova with more flexibility to conduct the monetary policy.

In 2012, the required reserves mechanism continued to exercise the monetary control function, which is closely correlated with that of liquidity management by the NBM.

Maintaining the required reserves ratio at the level of 14.0 percent of the base was explained by the passivity of interbank money market, aiming at improving its quantitative and qualitative indicators and at improving the transmission mechanism.

The firm management of liquidity in the banking system aimed at ensuring the proper functioning of the money market, maintaining the balance between price stability and national economic recovery.

The NBM intervened in the foreign exchange market during 2012 as a buyer of foreign currency in order to ensure that the annual inflation rate would fall within the range of variation of ± 1.5 percentage points from the target of 5.0 percent, and in order to strengthen the foreign exchange reserves. Amid a relatively low demand of foreign currency from economic agents, the foreign currency excess was generated by a net supply of foreign currency from individuals and a massive net inflow of foreign loans and investments. At the same time, the increase of the balance of current accounts and deposits in foreign currency of individuals and legal entities contributed to increased liquidity in foreign currency on the domestic foreign exchange market. In light of these developments, and within the limits of the promoted monetary policy, the NBM has absorbed in 2012 the foreign currency excess by purchasing foreign currency from the interbank foreign exchange market in the amount of USD 310.1 million.

At the end of 2012, the official reserve assets amounted to USD 2515.0 million, increasing by 28.0 percent from the end of 2011, covering about 4.7 months of imports (in 2011 – 3.6 months of imports) and 110.6 to percent of the total external debt of the Republic of Moldova in the short term.

On December 31, 2012, in the Republic of Moldova were 14 banks licensed by the National Bank of Moldova, including four branches of foreign banks and financial groups. On February 15, 2012, the NBM has withdrawn the license to conduct financial activity of BC "Universalbank" S.A.

It should be mentioned that, from January 1, 2012, banks have started using the International Financial Reporting Standards (IFRS).

Tier I capital in the banking sector amounted to MDL 6924.0 million, decreasing by MDL 473.5 million (6.4 percent) as compared to the beginning of 2012. As of December 31, 2012, Tier I capital of banks corresponded to the established minimum standard (≥ MDL 200.0 million), with the exception of two banks.

The Tier I capital decrease was due to the increase of calculated amount, but unreserved, of the allowances for impairment losses on assets and conditional commitments by MDL 977.2 million or by 61.1 percent, which is excluded from the calculation of Tier I. Allowances for impairment losses on assets and conditional commitments increased due to the worsening of the loan portfolio quality at some banks.

It should be mentioned that, in accordance with the Regulation on Risk Weighted Capital Adequacy, on December 31, 2012, the amount of minimum capital was set at MDL 200.0 million.

The average risk-weighted capital adequacy on December 31, 2012 has still maintained at a high level - 24.4 percent, indicating a high degree of safety of banks, determined by the existence of a potential for conducting operations without affecting the capital. However, a bank does not comply with this indicator.

During 2012, the Moldovan banking sector has recorded the following trends. The assets under IFRS amounted to MDL 58304.4 million, increasing by MDL 9.0224 million (18.3 percent) from the beginning of the year. The asset growth was determined both by increasing debt to MDL 8414.1 million (21.2 percent) and by increasing capital (IFRS) by MDL 608.3 million (6.3 percent).

The share of non-performing loans (substandard, doubtful and compromised) in total loans has increased by 1.6 percentage points from the beginning of the year, representing 14.5 percent on December 31, 2012.

For 2012, the return on assets and return on equity of licensed banks have recorded the value of 1.1 percent, and 5.6 percent, respectively, decreasing compared to the end of 2011 by 0.7 percentage points and 5.0 percentage points, respectively.

The net interest margin was 5.1 percent on December 31, 2012, decreasing by 1.3 percentage points compared to the end of 2011.

Long-term liquidity in the banking sector was 0.7 (maximum 1.0) as on December 31, 2012. Current liquidity in the banking sector was 32.9 percent (minimum 20.0 percent) at the end of 2012. Both indicators are respected by all banks.

See also

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