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Financial situation of the banking sector in 2016

During 2016, the National Bank of Moldova carried out quality assessments of the banks' shareholding and applied some remedial measures on large banks to ensure a transparent ownership structure. Thus, the assets recorded an increase and the banks became more resistant, being capitalised with a high liquidity level, which provides for the possibility to finance more actively the country's economy. At the same time, the banking sector has faced certain issues related to the high level of non-performing loans, maintaining the downward trend of the lending activity. In this regard, the banks continued to enhance their corporate governance and risk management framework to which they are subject.

As of 31 December 2016, the banking sector of the Republic of Moldova included 11 banks licensed by the National Bank of Moldova (NBM), of which 4 are subsidiaries of foreign banks and financial groups.

The National Bank of Moldova actions against banks placed under intensive (special) supervision

Following the detection of issues related to non-transparent shareholder structure, engaging in high risk lending operations, the National Bank of Moldova, in accordance with the Law on Financial Institutions, has established special supervision over three banks on 11 June 2015 (BC „MOLDOVA - AGROINDBANK" S.A., BC „Moldindconbank" S.A. and B.C. „VICTORIABANK" S.A. holding 64.2 percent of total banking sector assets). In connection with amendments in legislation, the special supervision has been substituted with intensive supervision until the existing issues in these banks are resolved. The National Bank has created monitoring groups for each bank that examine the financial situation, transactions, management bodies' agenda, participate in the meetings of banks and where appropriate, the National Bank issues recommendations relating to the activity of these banks.

The National Bank of Moldova has prescribed a diagnostic study to these banks, which shall be conducted by an audit company specialized in this field. Based on the results of diagnostic studies, the National Bank of Moldova has adopted decisions on preparing remedial action plans for BC „MOLDOVA-AGROINDBANK" S.A. and B.C. „VICTORIABANK" S.A., requesting the removal of all deficiencies identified in these studies.

In August 2016, the two aforementioned banks have submitted remedial action plans to the National Bank, which have been examined and endorsed positively by the NBM. For this purpose, the banks have taken a number of measures to improve their basic fields of activity, such as: the monitoring of the shareholders and bank's related parties, corporate governance, lending activity, risk management, prevention of money laundering, IT and others. The banks shall report monthly to the NBM on the implementation of the remedial action plans. In turn, National Bank shall intensively monitor these plans and notify the licensed banks periodically of the recommendations issued for their improvement.

At the same time, National Bank shall permanently monitor the shareholders' compliance with the quality requirements provided for by the legislation of the Republic of Moldova.

Thus, in March 2016, National Bank of Moldova has found that a group of shareholders of BC „MOLDOVA-AGROINDBANK" S.A are acting in concert and acquired a qualifying holding in the bank's share capital in the amount of 39.58 percent, without prior written permission from the National Bank. Consequently, pursuant to Article 15, paragraph (2) of Law on Financial Institutions, National Bank has suspended the rights linked to the shares held by these shareholders and informed them about the provisions of this law, as well about the obligation to dispose of the shares acquired in violation of the law in force within three months from the date of the detection thereof. As a result, the three month-period has expired and the shareholders have not disposed of their shares. Pursuant to the provisions of that law, the executive body of BC „MOLDOVA-AGROINDBANK" S.A. annulled these shares and issued new ones, single shareholding, which are exposed for sale to the stock exchange of the Republic of Moldova. In view of the need to restore the corporate governance and to attract a quality investor, the National Commission for Financial Market extended by the decision of 16 December 2016 the maximum period within which the bank may expose for sale the new shares issued by BC „MOLDOVA-AGROINDBANK" S.A. until June 2017.

The NBM found by the decision of 20 October 2016 that a group of persons act in concert in relation with BC „Moldindconbank" S.A by acquiring a qualifying holding in the amount of 63.89 percent, without prior written permission from the National Bank, thereby violating the Law on financial institutions. Hereinafter, the exercise of certain rights of these shareholders has been suspended since 20 October 2016. According to the Law on financial institutions, the shareholders shall dispose of the shares related to the qualifying holding acquired without prior permission from the National Bank of Moldova within the period provided for by the legislation.

Thereafter, National Bank has suspended on 20 October 2016 the mandates of members of the management bodies of BC „Moldindconbank" S.A. and appointed temporary administrators with the powers of the Council and of the Chairman of the bank's Administrative Committee. As of 19 January 2017, the NBM extended for a period of three months the mandates of the temporary administrators of BC „Moldindconbank" S.A (except for the mandate of Mr. Nicolae Dorin, Chairman of Moldovan Banks Association, whose mandate expired and may not be extended).

At the same time, the NBM has approved the audit company which will carry out the assessments of shares, debts and equity of BC „Moldindconbank" S.A.. The aforementioned report shall be submitted to the National Bank of Moldova in the second half of February 2017.
It should be mentioned that after the application of the early intervention regime, the liquidity situation of BC „Moldindconbank" S.A. remained stable, without significant withdrawals of deposits as anticipated.

In order to restore the corporate governance and to complete the Council of Administration of B.C. „VICTORIABANK" S.A., the NBM requested the organisation of an extraordinary general meeting of shareholders and the urgent submission of the candidates' files. Thus, National Bank has confirmed two persons to exercise the functions of member of the Council of Administration and the Council of Administration in its new composition became operational as from 14 October 2016. It should be also mentioned that the NBM gives increasing attention within intensive supervision to the shares' classification and shareholders' transparency. In this regard, the NBM initiated the procedures for assessing the shareholders holding qualifying holdings in the capital of B.C. „VICTORIABANK" S.A..

Financial situation of the banking sector and the compliance with prudential regulations

As of 31 December 2016, the situation of the banking sector, reflected based on the reports submitted by the

licensed banks in accordance with the legislation in force, recorded the following trends:

The total assets of the sector were MDL 73.0 billion, increasing by 6.0 percent (MDL 4.2 billion) compared with the end of the previous year.

As of 31 December 2016, gross loan portfolio amounted to 47.7 percent in total assets or MDL 34.8 billion, decreasing by 9.0 percent during 2016. Total volume of new loans decreased also by 12.8 percent than the similar period of last year. The decrease was determined mainly by the lack of loan demand and a more prudential approach applied by banks against potential debtors. Thus, the banks increased the investments in securities (certificates of the National Bank of Moldova and state securities) by 2.2 time, amounting to 15.3 percent of total assets.

The remaining assets, which amount to 37 percent, are held by banks in accounts opened with the National Bank, in other banks, in cash etc.

During 2016, the share of non-performing loans (substandard, doubtful and compromised) in total loans increased by 6.4 percentage points compared to the end of last year, accounting for 16.3 percent per sector as of 31 December 2016. This indicator varies from a bank to another, reaching the highest level of 33.8 percent.

The banks placed under intensive (special) supervision recorded the highest upward trend of non-performing loans, also due to the requirements issued by the National Bank of Moldova for loan reclassification on the basis of the prudential approach applied by the NBM, these loans being granted prior to the establishment of the intensive (special) supervision by the NBM.

With reference to the prudential limits on maximum exposure of 15 percent, it should be mentioned that following the efforts made by the National Bank of Moldova, BC „Moldindconbank" S.A has taken a number of remedial measures and as of 31 December 2016, the bank has complied with the provisions of Regulation on large exposure. At the same time, according to the measures plan submitted by BC „Victoriabank" S.A., the bank will take the necessary measures to comply with large exposure limits until the end of February 2017.

The high level of the risk-weighted capital adequacy allowed the banks to absorb losses from worsened loan quality. In order to avoid the risk capital inadequacy for covering the potential losses in the case of further deterioration of the assets' quality, the National Bank of Moldova as the supervisory authority has requested the banks to review the policies and strategies for the efficient monitoring and management of the non-performing loans level and for strengthening the capital. The policies/strategies submitted to the NBM are in process of examination.

The average risk-weighted capital adequacy was 30.3 percent, increasing by 4.0 percentage points compared to the end of last year, this indicator has been complied with by all banks (limit for each bank ≥ 16.0 percent), varying between 22.6 percent and 121.3 percent.

Tier I capital was MDL 9.4 billion, increasing by 4.8 percent (MDL 0.4 billion) during 2016. The increase of Tier I capital was driven mainly by the profit in the amount of MDL 1.5 billion obtained during 2016. At the same time, the capital increase was influenced negatively by the loan reclassification (increase in provisions by 41.7 percent or MDL 723.0 billion).

Considering that the capital is the main source of covering losses incurred in case of risks materialisation, National Bank has previously requested the banks to adopt a more prudent and conservative policy relating to the distribution of dividends.

Thus, in order to strengthen the banks' capital, the NBM initiated some amendments to Regulation on risk-weighted capital adequacy, which refer to the redirection of the profit registered during the previous years, exclusively for the capital increase.

It should be mentioned that only the well capitalised banks are able to absorb all risks that could arise/materialise and participate actively in financing the entire economy.

As of 30 December 2016, the profit of the banking sector accounted for MDL 1.5 billion. Compared to the same period of the previous year, the profit increased by 28.2 percent due mainly to the increase in interest related income by 130.7 percent. At the same time, the non-interest related income decreased by 9.5 percent.

Return on assets and return on equity represented 2.0 percent and 11.9 percent as on 30 December 2016 (increasing by 0.3 percentage points and 1.8 percentage points, respectively).

Banks have maintained the liquidity indicators at a high level. Thus, the long-term liquidity ratio (liquidity principle I) accounted for 0.6, reaching practically the same level as at the end of previous year. Current liquidity on the system (liquidity principle II) accounted for 49.2 percent, increasing by 7.5 percentage points. It should be mentioned that the liquid securities recorded during 2016 the highest increase of 129.8 percent in the structure of liquid assets.

According to prudential reports of 31 December 2016, the balance of deposits increased by 9.2 percent during the reporting period, accounting for MDL 54.8 billion (deposits from individuals amounted to 68.8 percent of total deposits, deposits from legal entities - 31.0 percent and deposits from banks - 0.4 percent). The deposits from individuals had the highest impact over the deposits' increase, which increased by MDL 2.7 billion (7.6 percent), maintaining the credibility of the domestic banking sector. The balance of deposits from legal entities has also increased by MDL 2.0 billion (13.2 percent).

Development of the legislative framework and its alignment to the EU framework

A number of Laws on amending and supplementing some legislative acts, including the amendments and supplements to the Law on financial institutions no.550-XIII of 21.07.1995 has been approved during 2016. These amendments and supplements aim at strengthening the national legislative framework in order to increase the level of transparency and quality of the banking shareholding, establishing the banks' activity management framework, including risk management depending on the nature and complexity of each bank, determining the functioning regime of the foreign banks' branches on the domestic market, as well the provisions related to the transactions with the bank's employees and their related parties, etc.

The process for the development and amendment of the normative acts has been initiated pursuant to Activity Plan in order to be in line with the last amendments to the Law on financial institutions.

In this regard, the draft decision of the Executive Board of the National Bank on approving the Regulation on banks' activity management framework is ongoing, being at the public consultation stage. Therefore, this draft includes the provisions related to the development of a management framework in banks, which could create premises for carrying out efficiently and effectively the bank's activity without excessive risk-taking by banks.

At the same time, Law on banks' recovery and resolution and Law on single central Securities Depositary were approved during 2016. These legislative acts have been developed with the IMF support and are based on the international standards in the field.

In 2017, the activity on developing a new legislative framework in the financial and banking field will be concluded along with the conclusion of Twinning project on strengthening the NBM's capacity in the field of banking regulation and supervision financed by the EU in the context of the EU Directive 2013/36/EU and Regulation 575/2013 (CRD IV), whose beneficiary is the National Bank of Moldova.

The entry into force of the Law on the activity of banks and investment companies projected by the end of 2017 and, subsequently, the entry into force of the secondary normative framework for the implementation of its provisions, will represent the transition from the application of international standards Basel I to the last standards in the field - Basel III. At the same time, the terms and conditions imposed by the EU - Moldova Association Agreement will be complied with fully along with the promotion and entry into force of the new legislative framework.

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