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Financial situation of the banking sector in the first quarter of 2019

During the first quarter of 2019, the National Bank of Moldova continued to implement the reforms in the banking sector. It focuses mainly on the process of transparency of the banking ownership aiming to protect depositors' and bank's customers interests. The National Bank continues to make vigorous efforts aiming to strengthen the banking sector, establish strong corporate governance in order to maintain financial stability and support the economic growth.

As of 31 March 2019, 11 banks licensed by the National Bank of Moldova were operating in the Republic of Moldova. During 2018 key changes were made in the shareholders structure of certain banks (at B.C. „VICTORIABANK” S.A., at B.C. „EXIMBANK” S.A, at BC „MOLDOVA-AGROINDBANK” S.A.), which also continue in the first quarter of 2019. Thus, on 22 January 2019, the NBM granted a preliminary permission to the European investor Doverie United Holding AD to purchase 63.89% of shares of BC “MOLDINDCONBANK” SA, the second bank in the banking sector considering the size of the package of assets.

OTP Bank Group - the largest banking institution of Hungary and the third largest of Central and Eastern Europe - intends to become a shareholder of a bank in the Republic of Moldova. In this respect, OTP Bank Group and Groupe Societe Generale signed an agreement on acquisition of the majority stake of BC “MOBIASBANCA – Groupe Societe Generale” S.A. The transaction will be possible only after OTP Bank Group receives the National Bank of Moldova prior written permission, as the Law on banks' activity of the Republic of Moldova stipulates it.

It is worth mentioning that on 4 April 2019 the Regulation on Banking Activity Management Framework entered into force. It will improve the banking regulation and supervision framework. According to the above-mentioned Regulation, banks shall submit, by 30 April 2019, the first reports on internal capital adequacy assessment process (ICAAP) for the situation of 31 December 2018.

The National Bank of Moldova has also approved the Supervisory Review and Evaluation Process Methodology (SREP) (hereinafter – methodology), which transposes international standards and best practices in the field of banking sector supervision. The approval of the methodology is part of the reforming process of the domestic banking supervision framework and represents a fundamental step in implementing a future-oriented risk-based supervision process using professional reasoning. This approach will provide an overall approach by early detection of bank risks and deficiencies, which will contribute to streamlining supervision, ensuring the viability and stability of the banking sector.

At the same time, during the first quarter of 2019, the consolidation of own funds and growth of the loan portfolio in the banking sector continued. It is worth mentioning that the share of non-performing loans in loan portfolios has decreased insignificantly during the reference period, but it remains high. The banking sector has a high level of liquidity. The profit obtained in the first quarter of 2019 increased compared to the same period of the previous year. At the same time, assets and deposits, especially deposits of legal entities have decreased.

The activities of the National Bank of Moldova with regard to two largest banks (BC “MOLDOVA-AGROINDBANK” S.A. and BC “MOLDINDCONBANK” S.A.)

BC “MOLDOVA-AGROINDBANK” S.A.

On 4 April 2019, the Executive Board of the National Bank of Moldova (NBM) lifted the intensive supervision regime for the

BC "MOLDOVA-AGROINDBANK" S.A. and revoked the measures prescribed for the special supervision period.

The decision was adopted after it was found that the bank is able to ensure the transparency of its shareholders, following the acquisition of 41.09% of the bank's share capital by the HEIM PARTNERS LIMITED, a company representing an international consortium of investors: EBRD, Invalda INVL, Horizon Capital. At the same time, the new Board of the BC „MOLDOVA-AGROINDBANK" S.A., established on 22 November 2018 by the decision of the annual general meetings of the bank's shareholders, started to exercise its mandate since 21 March 2019.

BC "MOLDINDCONBANK" S.A.

BC "MOLDINDCONBANK" S.A. continues to be set under early intervention regime.

In order to avoid excessive risks, the National Bank of Moldova monitors on a daily basis the activity of the BC "MOLDINDCONBANK" S.A. under early intervention regime. Consequently, the financial statements of the bank, its transactions, and agenda of the meetings of the management bodies are being examined.

In October 2016, BC „MOLDINDCONBANK" S.A. was set under early intervention regime, after NBM found the concerted activity of a group of persons who acquired and held a qualifying holding of 63.89% in the share capital of the bank, without any prior written permission of the NBM. The early intervention regime still applies to BC „MOLDINDCONBANK" S.A.

According to the legislation, the aforementioned shares had to be disposed within three months. Due to the fact that they were not sold, and consequently canceled in January 2018, the bank issued new shares, amounting to 63.89% of the bank's share capital, which have been exposed to sale for a period of three months, as a single package, at a price set after the evaluation made by an international audit company. The deadline for sale was extended several times while the last decision for another three months extension, was taken by the NBM Executive Board on 18 January 2019.

In January 2019, NBM Executive Board adopted the decision on the preliminary approval to acquire more than 50% of the share capital of BC "MOLDINDCONBANK" S.A. by the potential Bulgarian investor "Doverie-Invest" S.A.

In February 2019, the sale-purchase transaction of the new-issued single share package by BC "MOLDINDCONBANK" S.A. was performed, following which, on 21 February 2019 the Agency for Public Property purchased and registered the ownership rights on the package of 3,173,751 shares, which accounts for 63.89% of the share capital of BC "MOLDINDCONBANK" S.A. Subsequently, on 18 March 2019, during the auction conducted on the regulated market of the Stock Exchange, the Bulgarian company "Doverie-Invest" S.A. acquired 3,173,751 shares of B.C. "MOLDINDCONBANK" S.A., as a single package, at the total value of MDL 764,048,815.74, displayed for sale by the Public Property Agency. The registration of ownership rights on the above-mentioned shares took place on 22 March 2019, thus, "Doverie-Invest" S.A. becoming the majority shareholder with a qualified holding of 63.89% in the bank's capital.

Subsequently, the Executive Body of the National Bank of Moldova decided to extend the mandate of the temporary administrators of BC "MOLDINDCONBANK" S.A. for a period of six months starting with 20 April 2019. The mandate was extended considering the necessity of ensuring the continuous, uninterrupted and prudent administration of the bank during the designation and approval period, according to its Bylaws and legislation, of its statutory management bodies.

BC "MOLDINDCONBANK" S.A. operates in normal regime and provides all services, including those related to deposits, lending and settlement operations.

The activities of the National Bank of Moldova with regard to other banks

Following the process of making the banking ownership transparent, the NBM Executive Board adopted, on 11 January 2019, two decisions on „Banca de Finanțe și Comerț" S.A. and BC „ENERGBANK" S.A.

Therefore, with regard to the „Banca de Finanțe și Comerț" S.A., the National Bank found that a group of shareholders

acted in concert. They purchased and held a qualifying holding of 36.15% in the share capital of the bank, without a prior written permission of the National Bank, violating the provisions of the Law on banks' activity. As a result, the National Bank suspended the exercise of certain rights for these shareholders (the right to vote, to convoke and organize the general shareholders meeting, to propose topics in the agenda, to nominate candidates for the banks Supervisory board, the executive board and to receive dividends). The respective shareholders had to dispose their shares within the time limits provided by the law.

With regard to the BC "ENERGBANK" S.A., the National Bank established that a group of shareholders acted in concert and held 52.55% in the share capital of the bank, without a prior written permission of the NBM. Following these findings, the decision on the suspension of certain rights of these shareholders was adopted. Moreover, according to the law, these shareholders had to dispose their shares held in the share capital of BC „ENERGBANK” S.A.

On 11 January 2019, following the NBM assessment, the Executive Board of the National Bank of Moldova decided to suspend some rights of a shareholder that held 3.98% of the share capital of BC „ENERGBANK” S.A. The shareholder's rights were suspended because of failing to comply with the requirements on the financial adequacy and solidity, provided in Article 48 of the Law on banks' activity no 202 of 06.10.2017. The respective shareholder was supposed to dispose the shares held in the share capital of BC "ENERGBANK" SA within the terms provided by the Law.

Thus, considering that the size of the package of suspended shares exceeded 50% of the bank's capital, the NBM has also decided to apply measures of early intervention on BC "ENERGBANK" S.A., in accordance with the Law on banks' recovery and resolution. Some of the Managing body of the bank, remained functional, were supplemented with temporary administrators, appointed by the NBM, to assure a prudent governance of the bank during the period of solving the deficiencies identified in the bank's ownership structure.

On 21 February 2019, the Executive Board of the National Bank of Moldova decided to suspend some rights of a shareholder that held 9.6% of the share capital of BC „ENERGBANK” S.A., for failing to comply with the requirements on the financial adequacy and solidity, provided in Article 48 of the Law on banks' activity no 202 of 06.10.2017. The respective shareholder shall dispose the shares within a three months period.

Subsequently, in April 2019, the Executive Board of the National Bank of Moldova decided to extend the shareholders' disposal term of the shares of B.C. "ENERGBANK" S.A. and of the "Banca de Finanțe si Comerț" S.A. respectively.

Over the first quarter of 2019, a warning was issued against certain banks (B.C."EuroCreditBank" S.A., B.C."EXIMBANK" S.A, BC "ProCredit Bank" S.A.) following the targeted and full scope inspections performed by the NBM. Thus, warnings were applied to B.C. "EuroCreditBank" S.A. following the targeted inspection aimed to assess the suitability of the information systems and the continuity of activity, whilst towards B.C. "EXIMBANK" S.A. and BC "ProCredit Bank" S.A. – because of failure to comply with certain requirements of the legislation, as well as of the deficiencies found within the administration framework, etc.

Therefore, the banks shall eliminate all the deficiencies that were found during the on-site inspections.

The financial situation of the banking sector and compliance with prudential regulations

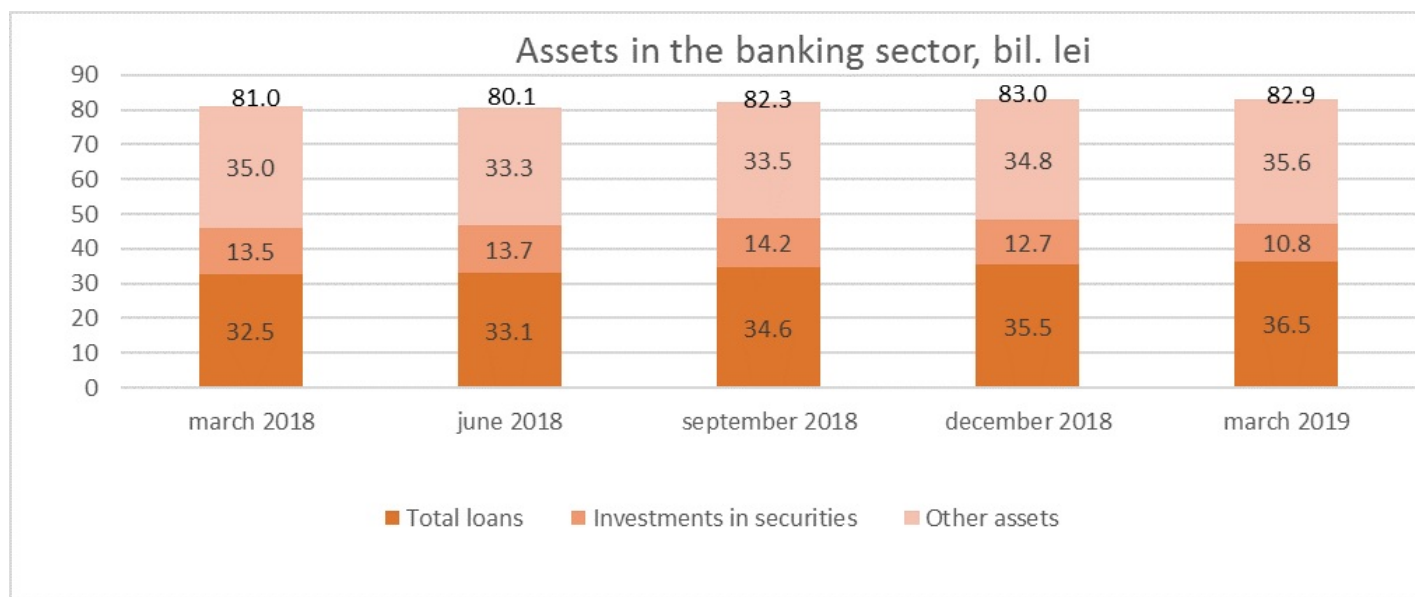
As of 31 March 2019, the situation in the banking sector, as it is described in the reports submitted by the licensed banks, showed the following trends:

Assets and liabilities

The total assets amounted to MDL 82.9 billion, decreasing during the first quarter of 2019 by 0.2% (MDL 152.9 million). In the structure of assets, the most significant decrease was recorded in the balance sheet for debt securities at amortized cost of 16.7% (MDL 1.8 billion). At the same time, the biggest growth was recorded for other on-sight deposits – of 23.0% (MDL 1.6 billion).

As of 31 March 2019, the balance of the gross loan portfolio accounted for 44.0% of the total assets or MDL 36.5 billion, increasing by 2.9% (MDL 1.0 billion) during the reporting period. At the same time, the volume of new loans granted during the first quarter of 2019 increased by 32.4% compared to the same period of the previous year.

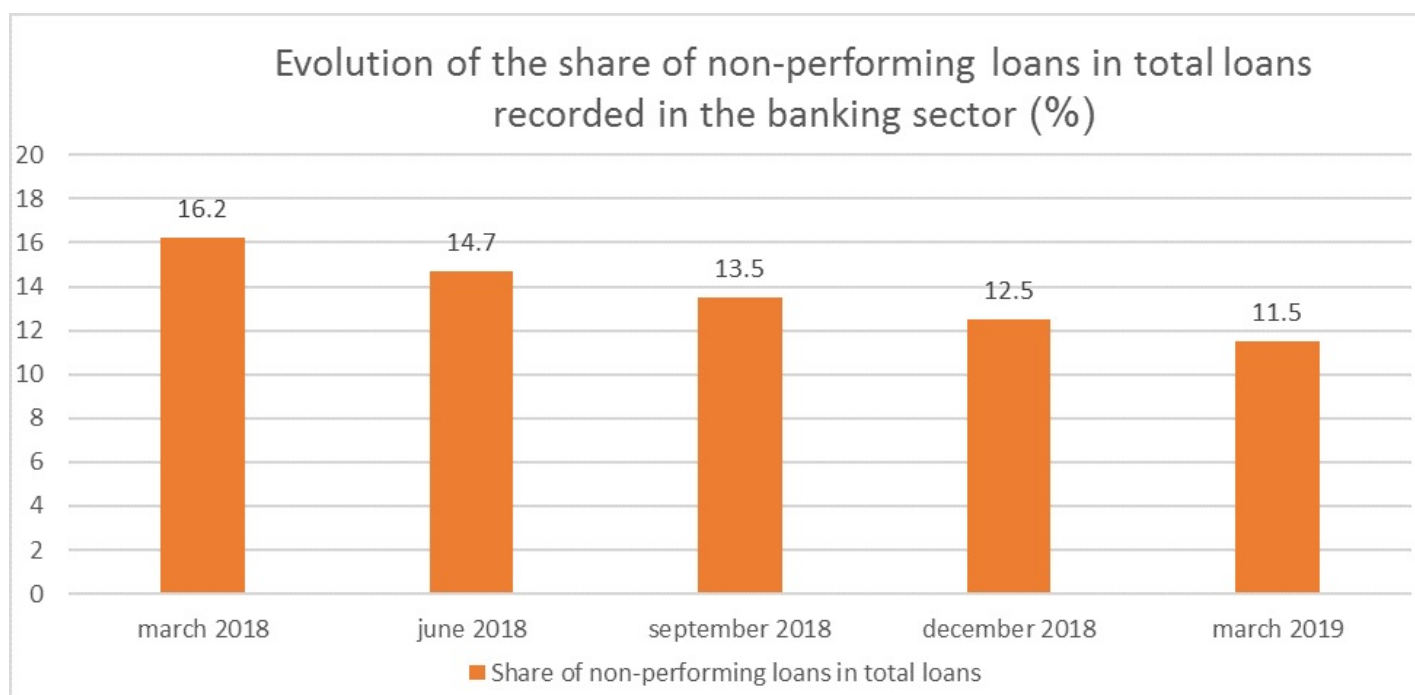
The largest increases in the loan portfolio were recorded for loans granted for the purchase / construction of the real estate and consumer loans, due to the decrease in the interest rate during the analysed period. At the same time, the National Bank of Moldova encourages banks to focus their efforts more on financing the real economy.



The investments in securities (certificates of the National Bank and state securities) recorded a share of 13.0% (MDL 10.8 billion) of the total of assets, which represents 2.3 percentage points less compared to the end of 2018.

The rest of assets, which amount to 42.9% are held by banks in the accounts opened at the National Bank, in other banks, in cash etc.

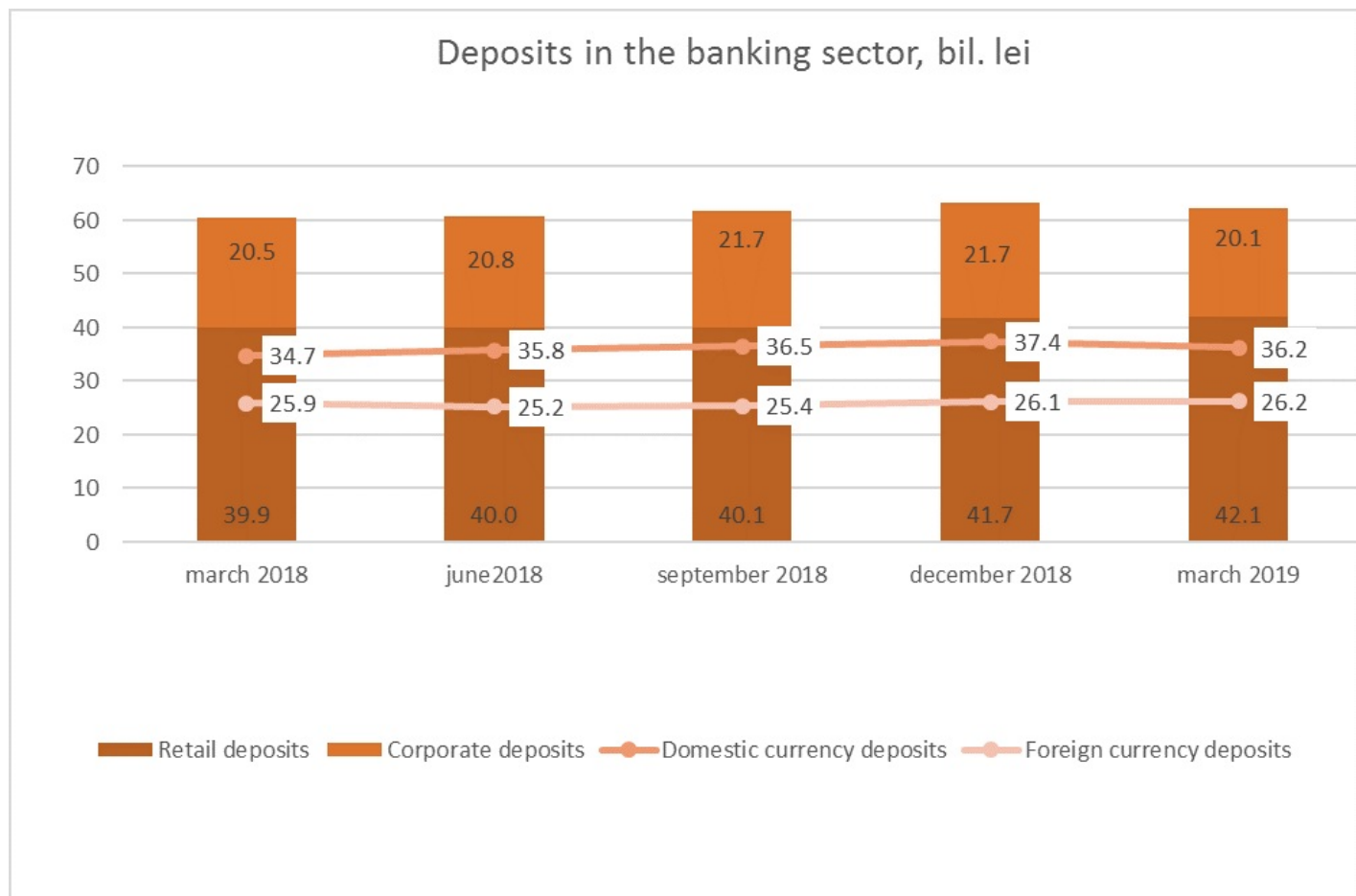
During the referred period, the share of non-performing loans (substandard, doubtful and compromised) in the total loan portfolio has decreased by 1.0 percentage point compared to the end of 2018, and represented 11.5% as of 31 March 2019. This share diminished at almost all banks, the aforementioned indicator varying from 5.3% to 28.7% from bank to bank. Banks tend to reduce the share of non-performing loans in the total loans.



At the same time, the decreasing trend of deposits continued. According to the prudential reports, they decreased by 1.7%

during the reference period and amounted to MDL 62.4 billion (individuals' deposits constituted 67.5% of the total deposits, legal entities' deposits – 32.3% and the deposits of banks – 0.2%). The decrease in the deposits was largely caused by the decrease in deposits of legal entities by MDL 1.6 billion (7.2%), and the deposits of individuals increased by MDL 452.3 million (1.1%).

Out of the total of deposits, 58.1% represented the deposits in domestic currency, that increased by MDL 1.1 billion (3.1%) amounting to MDL 36.2 billion as of 31 March 2019. The foreign currency deposits accounted for 41.9% of the total deposits, that increased insignificantly by MDL 46.2 million (0.2%) during the reference period, amounting to MDL 26.2 billion. In this way, MDL 98.6 billion foreign currency deposits were attracted, while the exchange rate fluctuation represented MDL (-3.5) million.



Income and rentability

As of 31 March 2019, the profit of the banking system represented MDL 526.7 million, which denotes an increase of 28.0% (MDL 115.1 million), compared to the same period of the previous year.

Total revenues amounted to MDL 1.7 billion, out of which 62.3% (MDL 1.1 billion) represented interest rate revenues, and non-interest revenues - 37.7% (MDL 644 million). At the same time, the total volume of expenditures constituted MDL 1.2 billion, including the expenditures with interest – 28.6% of the total expenditures (MDL 337.8 million), while the non-interest expenditures – 71.4% of the total expenditures (MDL 842.3 billion).

The increase of the profit resulted from the decrease in the non-interest expenditures by 12.7% or by MDL 122.1 million.

Expenditures with interest decreased by 14.9% or by MDL 59.0 million as a result of diminishing average interest rate for deposits. At the same time, the interest rate revenues decreased by 1.6% or by MDL 17.8 million, as a result of the decrease in the interest rate for loans.

As of 31 March 2018, the return on assets and capital constituted 2.4% and 14.4% respectively, increasing by 0.6 percentage

points and 3.6 percentage points, respectively, compared to the end of the previous year.

Compliance with prudential requirements

The banks continue to have high liquidity indicators. Therefore, the value of the long-term liquidity indicator (principle I of liquidity) amounted to 0.7 (limit ≤ 1), being at the same level as at the end of 2018. The current liquidity of the banking sector (principle II of liquidity) diminished insignificantly and constituted 52.3% (limit $\geq 20\%$), more than half of the assets of the banking sector being concentrated in liquid assets. It is worth mentioning that the largest share in the liquid assets belongs to the NBM deposits – 44.5%, which are followed by liquid securities – 24.9% and net interbank money – 20.5%. During the first quarter of 2019, the share of NBM net interbank money increased by 2.9 percentage points, and the share of NBM deposits by 1.2 percentage points. At the same time, the share of liquid securities decreased by 3.1 percentage points and the share of cash – by 1.0 percentage points.

Principle III of liquidity, which represents the ratio between the adjusted effective liquidity and the necessary liquidity on each maturity band, that shall not be less than 1 per each maturity band, was respected by all banks.

According to the reports presented by banks on 31 March 2019, the total own funds rate in the banking sector constituted 26.9%, which was almost at the same level as at the end of the previous year. The regulated limit is respected by each bank and varies between 21.2% and 72.62%.

As of 31 March 2019, the total own funds constituted MDL 11.0 billion and recorded an increase of 1.9% (MDL 208.1 million) during the indicated period. The increase in own funds was determined by the increase in the profit of the previous years by 243.6 million lei. This was mainly due to the adjustment of the general reserve for covering the banking risks at 4 banks, the increase of other items of the global result by MDL 44.4 million to a bank (re-assessment of the participation shares held) and the decrease of adjustments of first level own funds by 127.7 million lei due to prudential filters. At the same time, other reserves decreased by 203.2 million lei due to the adjustment of the general reserve for covering the banking risks.

Concomitantly, the National Bank recommended that the managing bodies of banks should not distribute capital in the form of dividends in order to maintain certain banks stable, able to face challenges relating to capital, imposed on the one hand by existing regulatory requirements and, on the other hand, the conduct of current activities, which expose banks to various risks.

With respect to the Regulation on large exposures, it is worth mentioning that one bank continues to violate the prudential limit established by the NBM of 15.0% of own funds, however, the bank has a plan aimed to diminish the exposure, within the terms set in the plan.

At the same time, one bank violates the prudential limit of 30.0% of the indicator Share of the sum of ten largest net credit debts in the total loan portfolio and the conditional commitments included in the ten largest debts. The bank has a strategy of gradually diminishing the above-mentioned indicator.

Regarding the compliance with the Regulation on bank's transactions with related parties, two banks violate the prudential limits of exposures related to bank's related parties, following the decision of the National Bank to qualify certain entities as being related, due to legislative modification that took place in 2018. Consequently, the prudential limits relating to bank's related parties have been exceeded. The aforementioned banks submitted to the National Bank the plans on complying with the prudential limits established for exposures to bank's related parties and improving the internal control system for their identification and monitoring, which were examined and accepted by the NBM. Respectively, the banks continue to report quarterly to the National Bank of Moldova about the measures taken.

Development of the national legislative framework and its harmonization with EU legislation

In April 2019, following the entry into force of the Law No 202/2017 on banks' activity, the National Bank of Moldova:

- Approved the Regulation on large exposures (Decision of the Executive Board of the National Bank of Moldova No 109/2019, in force since 19 June 2019). This Regulation establishes requirements to calculate the amount of the exposure, the maximum acceptable limits for the concentration risk of bank's exposure to parties or a group of related parties, portfolio exposures concentrations, and the requirements for monitoring, management and reporting large exposures. The new items of this regulation are:
 - Defining the capital on which the bounds are based;
 - Methods of calculation the amount of the exposure;
 - Establishing exposures that are exempted from applying the limits set by the draft;
 - Credit risk mitigation techniques when calculating the amount of the exposure.

The Regulation establishes that the bank shall have internal regulations, including control and management procedures to identify the groups of related parties, rigorous accounting and administrative procedures as well as adequate internal control mechanisms to enable it to identify, manage, monitor, report and record all the large exposures to parties or group of related parties and their subsequent amendments.

The approval of the Regulation contributes to mitigate the concentration of the credit risk and thus minimizing the maximum losses a bank may incur if the counterparty or the group of related parties may encounter difficulties in honouring the obligations as a debtor.

- Modified the Regulation on bank's transactions with its related parties (approved by the Decision of the Council of Administration No 240/2013). The proposed amendments and adjustments focus in particular on the following:
 - To determine the amount of the exposures to bank's related parties similar to those set out in the Regulation on large exposures;
 - To align the terms in the context of the Regulation on large exposures;
 - To improve the process of presuming certain parties as bank's related parties;
 - To re-assess the features used by the National Bank to identify the parties that have relations or perform transactions with the bank and/or its related parties as a result of supervisory practice;
 - To establish minimum requirements on internal policies and procedures of banks for managing the risks associated with transactions with the related parties.
- On 18 April 2019, the Executive Board of the National Bank of Moldova (NBM) approved the amendments to the Instruction on the submission by banks of COREP reports for supervisory purposes and the Regulation on banks open foreign exchange position.

The decisions were made aiming to adjust the reporting of large exposures and open foreign exchange position, as required by the regulatory framework and the best practices for regulating international financial and banking markets.

This will contribute to the uniform and timely reporting by banks of the information on bank's exposures to a party or a group of related parties, which will improve the supervision of risk concentration of the bank.

Amendments in the open foreign exchange position are in line with International Financial Reporting Standards and impairment provisions for expected loss accounting, as well as those set out in some regulatory acts of the National Bank.

The amendments will result in the more prudent maintenance and management of the open foreign exchange position.

The above mentioned amendments and completions will lead to strengthen the regulatory framework on regulation and supervision of the banks' activity, to minimize the risks to which banks are exposed in the context of large exposures and transactions with banks' related parties and, respectively, to strengthen the financial situation of banks.

The National Bank of Moldova continues to elaborate regulatory acts to implement the provisions of the Law No 202/2017 on banks' activity.

Aligning the banking legislation of the Republic of Moldova to international standards by improving the quantitative and qualitative bank management mechanisms will contribute to the promotion of a secure and stable banking sector,

increase of transparency, trust and attractiveness of the domestic banking sector for potential investors and creditors of banks, as well as for depositors and clients. It will also contribute to the development of new financial products and services.

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