

**PROBLEMS OF FINANCIAL STABILITY OF COMMERCIAL BANKS
IN THE REPUBLIC OF MOLDOVA**

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Banks are an integral part of the overall financial activity of the country, business activity indicator in the Republic of Moldova. Therefore, making an analysis of the activities of these institutions, as a system, it will be possible to make correct conclusion about the state of the national economy at the present stage of development of our state. This explains the relevance of the topic. The purpose of this article is to identify the features of the functioning of the financial institutions system, in particular the banking system of the Republic of Moldova. When writing this article we used printed periodicals, book publications, Internet resources. We used scientific methods of research, such as synthesis, grouping, comparing and others.

Keywords: *commercial bank, financial stability, financial condition, profitability, liquidity*

Bancile sunt o parte component a activit ii financiare a întregului stat, indicator al activit ii de afaceri din Republica Moldova. De aceea, efectuând analiza activit ii institu iilor date ca sistem, putem face concluzia corect despre starea economiei na ionale la etapa actual de dezvoltare a statului nostru. Cu aceasta i se explic actualitatea articolului dat. Scopul articolului dat este detectarea particularit ilor func ion rii sistemului financiar, i îndeosebi a sistemului bancar în Republica Moldova. Pentru perfectarea articolului dat au fost folosite edi ii periodice, sursele internetului. În articol au fost folosite a a metode ca cercetarea, sinteza, gruparea, compararea i altele.

Cuvinte-cheie: *banca comercial , stabilitatea financiar , pozi ia financiar , profitabilitatea, lichiditatea*

JEL Classification: E58, E59, E63, E62, E69, H69.

Introduction. The activity of commercial banks is so diverse that their real essence is uncertain. In modern society, the commercial banks, which are private and public institutions, engage in a wide variety of types of operations and provide their clients with a wide range of financial services. They not only organize the turnover of money and credit relations, through them are carried out cash, currency

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transactions, sale and issuance of securities, in some cases, brokerage and asset management, as well as the financing of the national economy as a whole. Commercial banks have a number of non-traditional banking transactions such as leasing, factoring, operations with precious metals, forfeiting, trust operations, guarantees and sureties and other types of services.

Today, the group of commercial banks in different countries includes a number of institutions with different structures and different ownership relations. This topic is very relevant nowadays. Commercial banks system develops very rapidly. Commercial banks have their place in the economy and play a special role in the functioning of economic entities.

Results and discussions. The effectiveness of the credit and banking system of the country is largely determined by the financial stability of each commercial bank individually. Stability refers to the ability of the bank in a dynamic market environment conditions to withstand negative external and internal factors, to ensure the reliability of deposits of legal entities and individuals, to protect the interests of shareholders and to fulfill their service obligations regarding customers that generally determines the stability and the rhythm of profit growth.

To ensure the stability of the bank and effective management of the commercial bank in the current environment, it is necessary to assess its real financial condition.

The assessment of the financial condition of credit institutions together with the mandatory standards can be carried out by analyzing the system of financial indicators that provide the criterion for evaluating specific aspects of banking activities, focusing on the profitability of a commercial bank.

With the commercialization of the banking activity profitability is the main aim of credit institutions. The income, generated by the assets, becomes a source of growth. High profitability of banking business allows to pay dividends to the shareholders of the bank, it is a necessary condition for increasing its capital.

The profitability of the bank is an important characteristic of its stability. It is necessary to create adequate reserve funds, incentives for staff and management to expand and improve operations, to improve the quality of provided services and, finally, to carry out successful emissions and, consequently, to obtain capital growth, allowing to increase the volume and improve the quality of provided services.

When analyzing the stability of a business bank in terms of its profitability the following items are determined:

- The level of return on assets;
- Interest margin;
- Interest rate spread;
- The level of coverage of non-interest expenses by non-interest income;
- Profitability of the prevailing assets;
- Profitability of borrowed funds;
- Profitability of credit operations, etc.

The analysis of banking activity in terms of its profitability allows the managers to formulate the credit and interest rate policy, to identify less profitable operations and to develop recommendations in order to gain more revenues. The solution of these tasks aims at reaching the objectives that the bank's shareholders settle for the management: to improve the quality of assets, to reduce the cost of liabilities and, on this basis, to provide capital growth and income, sufficient for the reproduction of banking activity and payment of dividends.

The level of profitability depends on several key factors:

- the use of financial leverage;
- the use of fixed costs share, which the bank bears by increasing its operating profit;
- control over operating costs in order to transform the biggest part of the costs into net income;
- control over the degree of risk of banking operations, so that the losses would not reduce to zero the bank's profit and equity.

The qualitative analysis of profitability is based on the analysis of the structure of incomes and expenses of the bank, trends in the structure change, as well as quantitative measurement of banking operations profitability. The reserves of profitability growth are usually found in more efficient use of assets by increasing the proportion of "working" or interest-earning assets and by reducing the assets that don't bring income (cash, correspondent and reserve accounts, investments in fixed assets, etc.). Thus

profit depends on the quality of assets, the level of their profitability, volume and structure of attracted resources and their costs.

Since the ultimate goal of the banking activity is to make a profit, the bank's task is not only to find the resources for active operations and to ensure the return of borrowed funds at the request of the owner, but also to attract the resources at optimal terms and price, and to place them so as to cover acquisition costs, receiving income. The nature of banking activities implies the possibility of obtaining high income and at the same time implies the presence of high risk. Taking into account the bank's liabilities to depositors and the bank's role in the economy, it is necessary to find such a combination of active and passive operations, which would offset the costs, provide the required level of profitability and liquidity, offset risks and the bank's activities would fit the parameters of regulatory requirements.

Having analyzed the data of the commercial banks from the Republic of Moldova on profits and / or losses for the years 2014-2015, the size of the total profit of the banking sector exceeded 1.4 billion lei.

Compared to 2014 when this indicator was 713 million lei, the total profit in the sector has doubled.

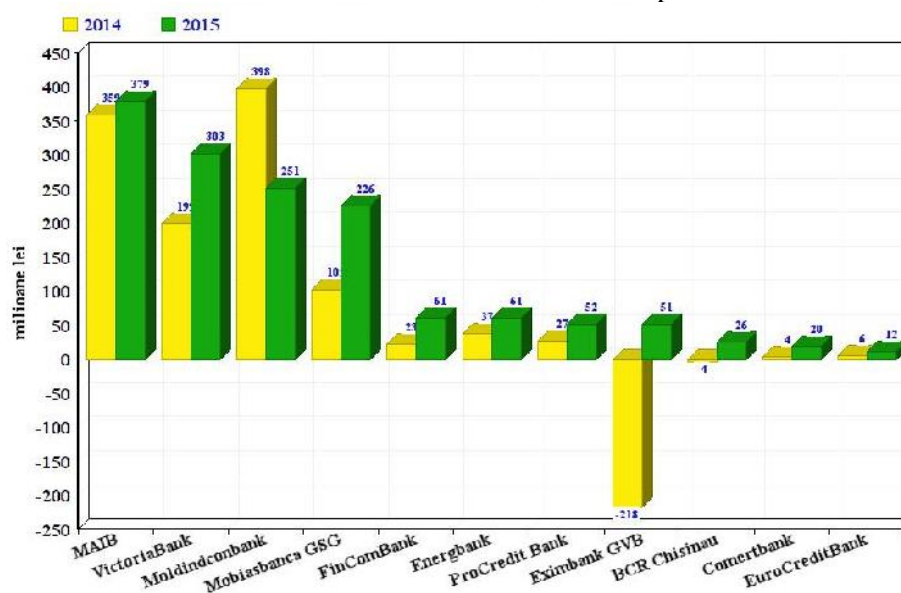


Fig. 1. Profits / losses reported by the banks from Moldova in 2014-2015, mil. lei
Source: Elaborated by the author based on the data provided by the NBM.

Moldova Agroindbank registered the highest profits in 2015 - 378.5 million lei. VictoriaBank ranks second with a result of 303.3 million lei of financial profit. The 3rd position belongs to Moldindconbank, which finished 2015 with a profit worth 251.3 million lei.

Mobiasbanca Groupe Societe Generale ranks the fourth, at a short distance from the "podium", it reported profit for the year amounted to 225.5 million lei.

Next in the rankings are FinComBank (61 million), Energbank (60.7 million lei), ProCredit Bank (52.2 million lei) and Eximbank GVB (51.4 million).

The profitability ranking for 2015 is completed by BCR Chisinau (26.4 million lei), Comertbank (20 million lei) and EuroCreditBank (12.2 million lei).

We note that none of the 11 licensed banks have reported losses at the end of 2015, while at the end of 2014 four banks reported losses. The exact data on profits or losses reported by banks in 2014 and 2015 are presented below in a table.

Also you can see graphs illustrating the financial results of banks in late 2014 or 2015 as well as the evolution of the first 4 banks during 2015.

Liquidity is also a necessary condition for the stability of the financial condition of the commercial bank. Liquidity is characterized by the ability to quickly convert assets into means of payment for early repayment of debts. Providing liquidity is an essential condition of the stability. Liquidity refers to the ability of credit institutions to fulfill their obligations and meet customers' needs through the sale of assets or their borrowing at prices no higher than competitors'. Any difficulty in the bank's activities relating to liquidity is only a symptom that points to the existence of other more fundamental problems.

Liquidity management is one of the key tasks of bank management and the mistakes and miscalculations in this area could lead to significant negative consequences, both for the individual bank and the entire banking system as a whole.

Liquidity analysis reveals the potential and actual trends, indicating a deterioration in the liquidity of the bank's balance, to analyze the factors that caused the development of negative trends and to take necessary measures to improve the situation. The key factors affecting the liquidity, are:

- the quality of management of the bank's activities
- the sufficiency of the bank's equity capital;
- the quality and stability of the bank's resource base;
- the degree of dependence on external sources of borrowing;
- balance of assets and liabilities by amounts and terms;
- the risk level of the bank's assets;
- the profitability of the bank's assets;
- assets' structure and diversity.

Liquidity is of great importance not only for the bank itself, but also for its customers. High liquidity is an indicator that the client can return the invested funds or can obtain a bank loan at any time. It protects the shareholders of the bank against the forced sale of assets in case of force majeure.

Experience has shown that current liquidity is the most important in terms of the bank's stability, which means that the bank has short term assets with maturities for paying liabilities to the depositors.

In most cases the banks, that have difficulties with current liquidity, are not able to survive, even if they possess long-term quality assets. Delays in paying liabilities to the clients cause chain reactions among bank customers. The news spreads on the market, panic starts among customers and the bank is forced to interrupt payments.

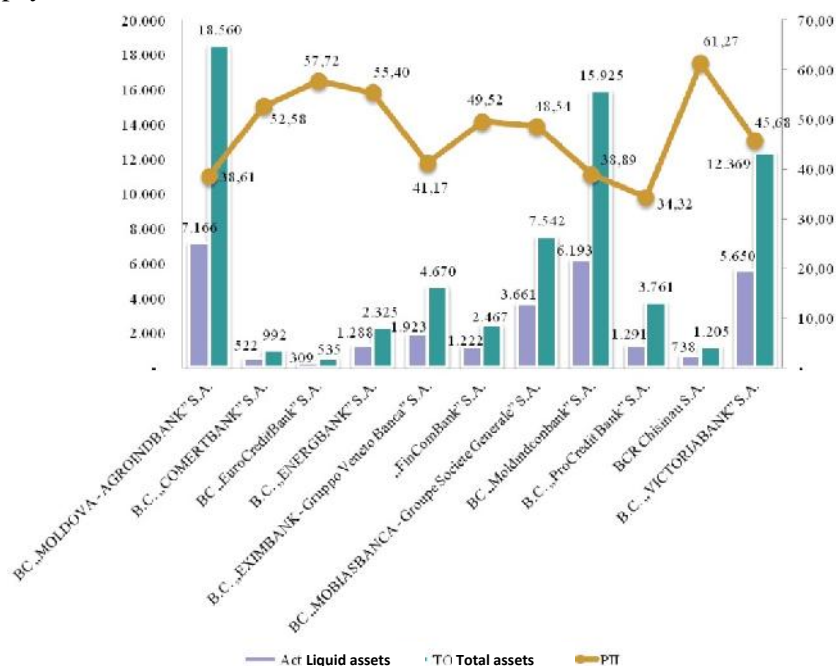


Fig. 2. Principle II in the banking sector of the Republic of Moldova on 01.31.2016, mil. lei
Source: Elaborated by the author based on the data provided by the NBM.

From Figure 2 we can see that on 31/01/2016 all licensed banks had the liquidity indicator (P II) higher than the norm set by the National Bank of Moldova (at least 20%). The biggest indicator of Principle II system belongs to BCR Chisinau (61.27%) and the lowest to B.C. "ProCredit Bank" S.A. (34.32%), the average in the sector being 42.59%.

Figure 2 shows that there is excess of liquidity in the banking sector. At first glance this phenomenon is not too positive because it shows that the bank doesn't invest its resources rationally.

According to the Regulation on bank liquidity, long-term liquidity (PI) is the ratio of assets with maturity over 2 years and bank liabilities, this ratio should not be higher than 1 (one).

From Figure 3 we can see that there are banks that have long-term liquidity ratio close to the limit, which means that the bank in question has placed money at about the same term when it withdrawn its resources. This does not mean that the bank will encounter some difficulties in honoring its obligations.

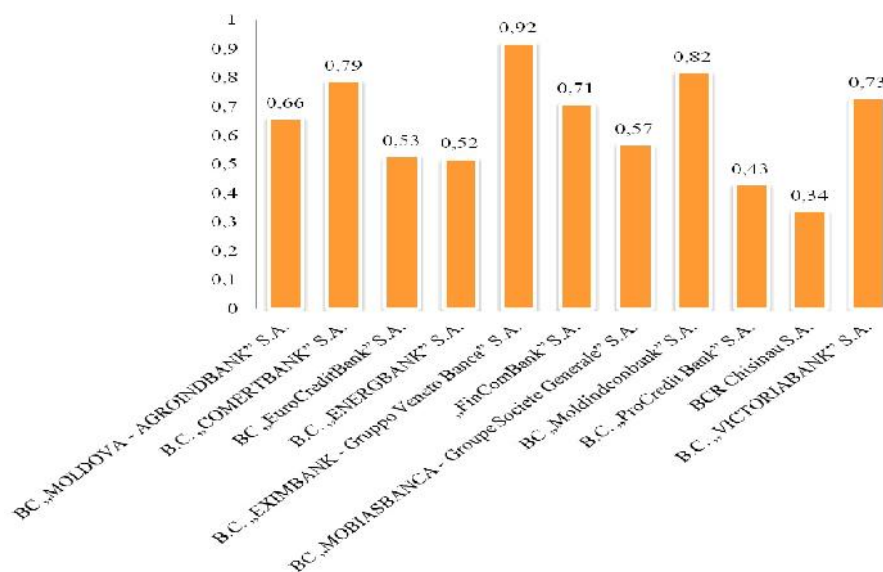


Fig. 3. Principle I in the banking sector in the Republic of Moldova on 31.01.2016, mil. lei
 Source: Elaborated by the author based on the data provided by the NBM.

Banks always have access to REPO's operations conducted by the National Bank of Moldova, some banks have access to credit lines from parent banks or from the group to which they belong. Total regulatory capital is included in the calculation of Principle I of liquidity. All licensed banks have sufficient capital and reserves from retained earnings to meet any challenges that may arise in their work. Thus, there is no reason for any concern.

Conclusions. Banking system is a major economic component of any country in the world. No state can exist without this kind of financial institutions like banks. The development of the financial sector contributes to meeting the needs of the economy for quality financial services and financial infrastructure, and to ensuring effective implementation of economic and social policies of the state. In exercising the functions of financial intermediaries, commercial banks were able to mobilize and reinvest considerable financial resources.

Profitability and liquidity indicators of the banks are inversely proportional: the requirements of sufficient profitability of a commercial bank always encounter the limitation of its liquidity. The conflict between liquidity and profitability is a key one, and the stability of the credit institution largely depends on its resolution. The bank is constantly balancing between higher income that can be obtained by granting long-term credits to the borrowers with questionable credit status, by long-term investment, by reducing unused balances and meeting credit demand, on the one hand, and meeting the bank's obligations arising from the withdrawal of deposits, on the other hand. The price for the bank's high profitability is always a loss of liquidity, and the price for the maintenance of a high level of liquidity is the loss of a significant proportion of its earnings. With excessive cash balances at the cash boxes, there is minimal profit on correspondent accounts, and vice versa, profit increases with a decrease in cash balances, an increase in granted loans, increase of investments in other operations.

Thus, when considering the formation of bank's profits and liquidity, their nature and interaction, they seem to be complete opposites in mutual conflict, as in an effort to achieve their maximum profit and liquidity pursue completely opposite goals.

Carrying out an aggressive policy, aimed at maximizing profits, is accompanied by a decrease in the liquidity of the bank balance. At the same time the risk of losses dramatically increases due to the need for the rapid transformation of assets in the means of payment. Liquidity disturbance and lack of available liquid resources to meet current obligations lead to the attempts to compensate it by their additional attraction. Such actions immediately affect negatively the bank's profitability, as these fleeting asset sales usually occur at great discount prices, and attracting liquidity means entails additional costs in the form of interest.

Facing the problem of liquidity, the bank begins to conduct overly cautious policy by placing in cash longer than necessary. Excess liquidity in the bank's balance sheet allows it to feel free in terms of its payment obligations, however, it immediately affects the overall level of profitability. The reasons for reducing the efficiency of the banking sector in the Republic of Moldova are: increasing competition, the massive introduction of new banking products, requiring additional and regular expenses, physical expansion of the network of structural divisions of banks and the growth of related fixed costs, the growth effects of interest rate risk, especially for the banks serving the accounts of the Treasury of the Republic of Moldova, the administrative decision of the National Bank on raising interest rates, and others.

In this connection we can offer the main ways of solving the problems in the banking sector of the Republic of Moldova:

- to increase the share of investments in the fixed assets of the banks in order to increase the competitiveness of financial services on the market,
- to attract a bigger investment volume to be able to give credit not only to enterprises and companies, but also to individuals,
- to lower the interest rate on loans in order to increase the attractiveness of the services provided,
- to increase the network of the companies with which the bank could conclude leasing contracts,
- extensive lending to the population,
- to offer credits to mortgage companies,
- to provide new high quality services,
- the National Bank of Moldova should strengthen control and supervision of commercial banks,
- to change national regulations concerning banking activities in accordance with international regulations and requirements.

In order to harmonize domestic legislation in accordance with BASEL III, Regulation No. 575/2013 of the European Parliament and Council of 26 June 2013 and Directive 2006/48 / EC of the European Parliament and Council of 14 June 2006, the National Bank will introduce Principle III of liquidity (liquidity by maturity bands). Principle III will be calculated as the ratio of effective liquidity and the liquidity needed in each maturity band and shall not be less than 1 per each maturity band. Each component of the asset to be counted will be weighted with a certain coefficient. This is a reserve of funds in order to cope with shocks that may arise or in other words – the actual liquidity. Liabilities are also weighted and the obtained product represents funds that may be required prior period. Principle III of liquidity (liquidity by maturity bands) will enter into force starting with 30/06/2016.

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Recommended for publication: 04.10.2015