THE NON-PERFORMING CREDITS AND THEIR IMPACT ON THE FINANCIAL STABILITY

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Abstract

Financial stability means a situation where the financial system market-and intermediaries, market infrastructures-may face major disruptions jolting, without being able to draw and to place monetary funds effectively and to withstand shocks without hurting the real economy. Loans affect financial stability, in that it does not bring more revenue, but not necessarily represent losses or outstanding.

Further evolution of the present annual average effective interest, cost of capital determination technique, principles and general rules concerning lending, credit portfolio management.

Key words: non-performing credits, cost, equity, credit activity, credit portfolio, financial stability.

1. Preliminary data

The non-performing credits are representing the dominant risk to the financial stability. They kept on increasing both as volume and rate, from 14.3% for the last month of the year 2011 to the level of 16.8%, but with a lower volume as against the previous years, in the year 2011 the increase counted for 2.5%, comparatively with 4% in 2010 and 5% for 2009.

The rate of the non-performing loans of the crediting institutions increased by 2.2.% between the months December 2011 and June 2013 from the level of 8.2% to the level of 10.4% while the volume of non-performing increased by 28% over the same interval of time.

The sustained evolution during the first month of the year 2012 is reflecting, partially, the adjustments assigned by IFRS, the acknowledgement in the balance sheet of the non-preforming liabilities previously recorded in accounts outside the balance sheet, as well as the re-evaluation of the quality for certain credits restructured during the previous years.

The conditions for financing companies and population developed in an ordered way in the years 2011 and 2012. The crediting flows tend to be directed to a larger extent towards the sectors more efficient and those supporting the durable economic growth of Romania.

Up to date, the plans of restructuring issued by the bug banking groups being present in Romania as well, did not influence negatively the general situation of their subsidiaries and branches from our country; the dynamics of the financing of companies and population became positive again while the net sales of assets, placed on a downwarding tendency, are made with the purpose to improve the quality of the credits portfolio.
2. The evolution of the effective yearly average interest

One of the key factors of the banking activity is the interest, which is the main characteristic of the banking credit.

Currently, the interest rate is expressed without referring to the time period, since this one is implicitly considered as being 1 year.

The level of the interest rate is given by the demand and offer for financial funds.

The offer for financing is formed by: individuals with high income; legal persons holding availabilities in excess.

The financing demand is formed by:
- Individuals needing to acquire goods of long-term utilisation, dwellings, cars etc.;
- Legal persons searching financing for their own stock;
- The Government of the state borrowing in accordance with the state investment policy;

The demand of capital is varying in an inverse ratio with the interest rate. As much as the interest rate is lower, the volume of credits contracted by the population of economic agents is bigger.

From a theoretical point of view, any positive interest rate implies a process of erosion of the interest or even of the advanced capital; from the bank point of view we can make the difference between two categories of interest: the discounted interest and the collected interest.

"The evolution of the effective yearly average interest"

Source: processed data out of the NBR, INSSE reports

The discounted interest (paid) is representing the crediting of the current account of the Client with the interest due as communicated to him, calculated according to the following formula: \( \text{Interest} = \text{Daily sold} \times \text{Interest percentage} / 365 \times 100 \).

The collected interest is representing the interest applied for covering debts of the Clients towards the Bank, representing interests, commissions, fees, penalties.

The delay penalty is established on the basis of a rate of fix interest being calculated according to the formula: \( \text{Interest} = \text{Daily sold} \times \text{Percentage of Interest} / 360 \times \).
100 being applied without prior notification over the entire duration of the debtor account until the day the debit is covered.

An issue particularly significant in the frame of the banking activity consists of achieving an optimum relation between the collected interests and the paid ones, taking into consideration that this difference will eventually represent the profit of the bank.

The credit being nowadays the most important product of the commercial banks from our country, establishes the interest as a part of its cost. The credit cost stands along with the risk as a basic component of the price for the banking product called credit.

From the point of view of the crediting or debiting bank for the calculation of the interest it is extremely important whether the interest is fixed or variable. Sometime, a margin is added to the interest applied by the bank, depending on the risk coefficient.

The clients want to know how much the loan will cost and therefore, they are paying a great attention to the interest calculation which they want to be specified in the loan contract.

The commercial banks are interested to draw deposits from the economic agents and individuals who tend to become the main resource for the crediting activity.

3. The technique to set up the cost of the capital
In order to set up the cost of the borrowed capital there are several factors to consider, among which: the credits being ranted; the cost of resources for the bank granting the credits; services for payments made by the banks; deposits and savings; the discount tax; the interest applied on the financial market; the commissions; the wages of the banking personnel; the salary of the trustee of the goods deposit or the commission for this one; the emoluments, expertise, travelling etc.

While some of these factors play a concrete role and can be quantified, others are purely factors of general economic policy. Generally speaking, the cost of the capital materialized in the credits granted to the economic agents is established depending on the interest applied to these credits which, at its turn, is based on the resources cost and the inter-banking interest. The cost of the capital is representing first and foremost, the financing cost.

The economic agent takes into consideration not only the cost of the loan but also the total costs of capital, including the costs for functioning and investment. The decrease of the interest rate and, hence, of the cost of the capital, is a way to encourage the production and investment and contributes to the increase of the production of goods and services as well as to the increase of the circulating speed of the money.

4. General principles and rules concerning the crediting activity
By its crediting activity, the bank should strictly observe the provisions of the Banking Law no. 58/1998, Law no.101/1998 concerning the statute of the NBR, the norms, instructions and regulations issued by NBR, bearing regulating prerogatives in the monetary, crediting, foreign exchange and market domains, as well as their own norms and working instructions.

The crediting operations are considered, basically, as being a low risk but they must take into account all the elements included in the process of approving, granting, utilizing credits and, consequently, in order to get a correct classification, there is a detailed documentation to be submitted as regards the identity of the client, his historical with the Bank and/or other banking/non-banking financial institutions, its credibility, the
nature of the activity run by the respective client, the purpose and destination of the required funds as utilisations from the credit, the risk profile of the client, the credit being sent for approval only after a perusal analysis and approved on the basis of the approvals set up by the internal norms of credit granting.

The credit facilities – the clients of the bank would take advantage of the credit granting facilities of the bank if complying with the conditions of eligibility, as provided by the specific crediting norms, the provisions of a specific norm and the risk profile of the client.

As a general rule, the crediting facilities are not granted to:
- The clients with a degree of critical risk and the clients against who restrictive steps have been taken by national/international authorities, through final and irrevocable decisions issued in the case of money laundering or other economic infringements;
- The non-resident legal persons originating in countries with relaxed fiscal legislation, without a profound analysis;
- Other clients not complying with the eligibility conditions established by the bank.

The banks must secure the definition and issue of the policies and guiding lines in the frame of credits granting, guaranteeing the qualitative standards set up by the Bank for the solvency analysis, securing the observance of the normative dispositions in force in Romania, guaranteeing also the setting up and the evolution of the evaluation criteria in time.

The crediting activity takes into consideration also the optimum management of the financed positions by analysing their dynamics and utilization under various technical forms, by sectors/branches of economic activity.

The banks have the obligation to secure a correct formalization as well as the administrative and accounting management of the warranties for the granted credits, by the corrects checking and accounting improvement of the warranties, both real and personal, set up in the bank’s favour, guaranteeing their formal and substantiated correctness.

5. The management of the credits portfolio

Presently, the credits are by far the most important banking product in our country. This is why, their monitoring since the moment of approval and granting makes part of the management of the credits granted by the commercial banks.

The credit applications are registered separately from other documents in the „Register for the evidence of the credits applications and”. In this register the following items are inscribed: date, credits applicants, the type of the requested credit, its purpose, type of the approved credits and the date of the termination of the credit contract. All the other documents connected with the credits are inscribed in the ordinary register of inputs-outputs.

A particular position in the management of the credited by the commercial banks is held by the identification of the credits actually granted. This identification is achieved firstly through the order number of the credit contract, the code of the analytic account opened to the credits beneficiary.

The management of the credits granted by the commercial banks implies, mainly, the permanent monitoring of the way in which the funds put at the disposal of the economic agents are utilized.

This monitoring is made by the bank management but mainly by the credit officers. On the basis of the received documents, the organs in charge of the bank are proceeding to the scriptural verification of the credits guarantee, the accomplishment
of the cashing up as scheduled by the incomes and expenses budget and the forecasted parameters for the investment objectives put in function.

Meantime, the mode in which the economic agent constitutes its resources is also verified.

Here we talk about the money resources meant to reimburse the long and medium term credits and to the payment of the related interests. The information arising from the analysis of the documents is centralized at the agencies, branches and finally the headquarters of the commercial banks. These references are called reference model of the situation of the long, medium and short term credits.

The efficient management of the credits implies the analysis of the credits portfolio of the commercial bank, the setting up of the financial performances of the loan and classifications concerning the credits utilization.

By the end of December 2012, Veneto Banca – București Branch, recorded about 30,000 clients, out of which over 21,000 individuals and about 9,000 legal persons.

This shows a decrease as comparatively the previous exercise, due to the massif closing of current long time inactive accounts, mostly of individuals, occurring within the first days of the year 2013 but with effect starting with 31.12.2012.

If analysing the clients depending on the commercial criterion "sales channel" at group level, the largest segment is by far that of the clients Retail - "Affluent and Universal", representing almost 74% of the total, followed by the segment IMM - "Small Business", which represented about 16.1%. According to the distribution of the clients by the criterion "sales channel", the outcome is that, out of the clients' basis, the attention goes to the Retail.

The end of the year 2007, brings a turn-over figure to the Group exceeding 39 billion euro, so that the increase recorded counts for over 15.6 billion euro in 2006.

The ex Intra Group, had a key contribution since an infusion of capital took place, which brought changes in relative terms, amounting about 10.5 billion euro, representing 26.8% of the consolidated turn-over figure.

By the end of the year 2009, the business volume of the Group exceeded the threshold of 45.6 billion euro, representing an increase of almost 3.6 billion euro, so that there is an increase of more than 8% to be recorded comparatively with the situation by the end of the year 2008.

The business volume of the Group closed the year 2010 with positive results in a un-favourable economic context, recording 74.1 billion euro, so that an increase of almost 28.5 billion euro is recorded comparatively with the situation by the end of the year 2009.

The tough economic conjuncture had a significant impact on the banking activity, correspondingly reflected by the balance sheets at the end of the years.

Veneto Banca Group - București Branch managed to maintain a positive result due to its capability to line up with the needs of the clients as well as through adopting a prudential management.

In the year 2011 the turn-over figure of the Group is set at 77.2 billion euro, representing an increase of 3.1 billion euro in absolute terms on the sold recorded by the end of December 2010.

By the end of the year 2012, the business volume of the Group exceeded the threshold of 80.1 billion euro, representing a increase of almost 2.9 billion euro, comparatively with the situation by the end of the year 2011.
The evolution of the business volume

Evoluția volumului de afaceri (în miliarde €)

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<tr>
<td>Volumul de afaceri (CA)</td>
<td>80.092</td>
<td>77.213</td>
<td>74.087</td>
<td>45.652</td>
<td>42.889</td>
<td>39.034</td>
<td>23.413</td>
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Source: processed data out of the financial reports published by Veneto Banca - București Branch, integrant part of Veneto Banca Group

The value of the credits granted kept on increasing in 2007, the year being closed with an increase of about 10 percentage points. The volume of credits for Veneto Banca Group amounted 14.2 billion euro, out of which over 3.3 billion euro resulted out of the merge with the ex Banca Populara di Intra Group. As we can notice from the graphic, the banks from inside Veneto Banca Group contributed with 2.3 billion euro for the increase in this segment +26.8%, from about 8.6 billion euro to over 10.8 billion euro.

The performances of the other institutions of credit from Veneto Banca Group have been also positive, with a bench mark for Banca di Bergamo with an increase of 32.9%, Banca Meridiana also with a positive trend reaching 41.5% and Veneto Banca – București Branch, which recorded an increase of over 76.7%.

The loans segment increased from 2.8 billion euro la 4.6 billion euro during the year 2007 which is a positive performance. The loans to the retail clients represented approximately a third of the granted loans by the Group Veneto Banca. By the end of the financial exercise of the year 2008, Veneto Banca Group achieved a volume of credits counting for 16.4 billion euro.

In a context characterized, at a first glance, by a progressive slowing down of the economic cycle, followed by a crisis on the financial markets, Veneto Banca Group recorded a significant increase of the crediting segment.

The credits to individuals and companies confirm the fact that the economy has been affected, mainly in the sector of the small and medium companies, which was the most affected by the most acute phase of the crisis, when the banking system faced a situation of shortage in liquidities and, consequently, the slowing down of the crediting process.

Despite the context characterizing the year 2009, respectively the profound economic crisis and a generalized restriction of the crediting offer, Veneto Banca Group kept on supporting the funds requirements as the attention was directed towards the retail segment and small and medium companies.

By the closing of the financial year 2009, the volume of the credits at consolidated level, counted for 17.8 billion euro, showing the evolution of approximately 1.4 billion
euro, with an upward tendency by 8.5 percentage points as against the year 2008.

The portfolio of credits at consolidated level of the year 2010 increased up to 25.7 billion euro, showing an increase of 7.9 de billion euro as from the beginning of the year, equal to 44.6 percentage points.

The development of the portfolio has been generated by the loans granted on medium and long term, mainly through mortgage credits which, during that period recorded an increase amounting 4.6 billion euro, representing thus +56.8 percentage points.

During the same period, the credits for current needs recorded an increase of 1.2 billion euro, +30.7 percentage points, while the sector of other transactions, including basically credits for payments in advance, recorded an increase of 479 million euro, +16.4 percentage points.

In 2011 Veneto Banca Group kept on supporting the funds requirements for the retail segment and small and medium companies. By the end of December 2011, the portfolio of credits at consolidated level exceeded the threshold of 27 billion de euro, an increase of 1.3 billion euro from the beginning of the year. The evolution of the portfolio was satisfactory if considering the economic context and the progressive deterioration of the prospects of growth for the real economy.

During the year 2012, the crediting activity at the level of Romania recorded a progressive slowing down. Although the demand keeps on persisting, the economic and financial conditions in Romania imply a prudent process of crediting based on drastic criteria. Under the circumstances, Veneto Banca Group kept on securing to the largest extent the support for financing the requirements of both individuals and companies.

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<tr>
<td>Credită de nevoi curente</td>
<td>2,396</td>
<td>3,992</td>
<td>4,301</td>
<td>4,696</td>
<td>5,556</td>
<td>5,701</td>
<td>5,418</td>
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<td>Anumite credită cu răscoale active</td>
<td>2</td>
<td>62</td>
<td>7</td>
<td>62</td>
<td>46</td>
<td>456</td>
<td>797</td>
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<tr>
<td>Credită cu ipotecă</td>
<td>2,781</td>
<td>4,622</td>
<td>5,586</td>
<td>8,153</td>
<td>12,770</td>
<td>13,245</td>
<td>13,048</td>
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<td>Carduri de credit, Duscopere de cont</td>
<td>55</td>
<td>98</td>
<td>113</td>
<td>136</td>
<td>893</td>
<td>674</td>
<td>539</td>
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<td>Contracte de leasing financiar</td>
<td>580</td>
<td>734</td>
<td>761</td>
<td>739</td>
<td>776</td>
<td>803</td>
<td>785</td>
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<td>Factoring</td>
<td>112</td>
<td>121</td>
<td>152</td>
<td>102</td>
<td>63</td>
<td>73</td>
<td>142</td>
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<tr>
<td>Alte tranzacții</td>
<td>1,627</td>
<td>2,889</td>
<td>3,154</td>
<td>2,925</td>
<td>3,731</td>
<td>3,404</td>
<td>3,209</td>
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<tr>
<td>(credite pentru avansuri)</td>
<td></td>
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<tr>
<td>Titluri de creanță</td>
<td>117</td>
<td>1</td>
<td>0</td>
<td>325</td>
<td>458</td>
<td>409</td>
<td>354</td>
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<tr>
<td>Active neperformante</td>
<td>213</td>
<td>588</td>
<td>773</td>
<td>1,260</td>
<td>1,960</td>
<td>1,963</td>
<td>2,566</td>
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<tr>
<td>Activele transferate din amonistate</td>
<td>684</td>
<td>1,997</td>
<td>1,653</td>
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<tr>
<td>Total credită accedite elențelor</td>
<td>8,568</td>
<td>14,265</td>
<td>16,399</td>
<td>17,799</td>
<td>25,736</td>
<td>27,846</td>
<td>26,858</td>
</tr>
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Source: processed data based on financial reports published by Veneto Banca Group

Conclusions

The rate of the non-performing loans of the crediting institutions increased by 2.2% between the months December 2011 and June 2013 from the level of 8.2% to the level of 10.4% while the volume of non-performing increased by 28% over the same interval of time.

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References