

Macroeconomic situation, bank lending and SME finance in Moldova

2. German-Moldovan Forum on SME Finance

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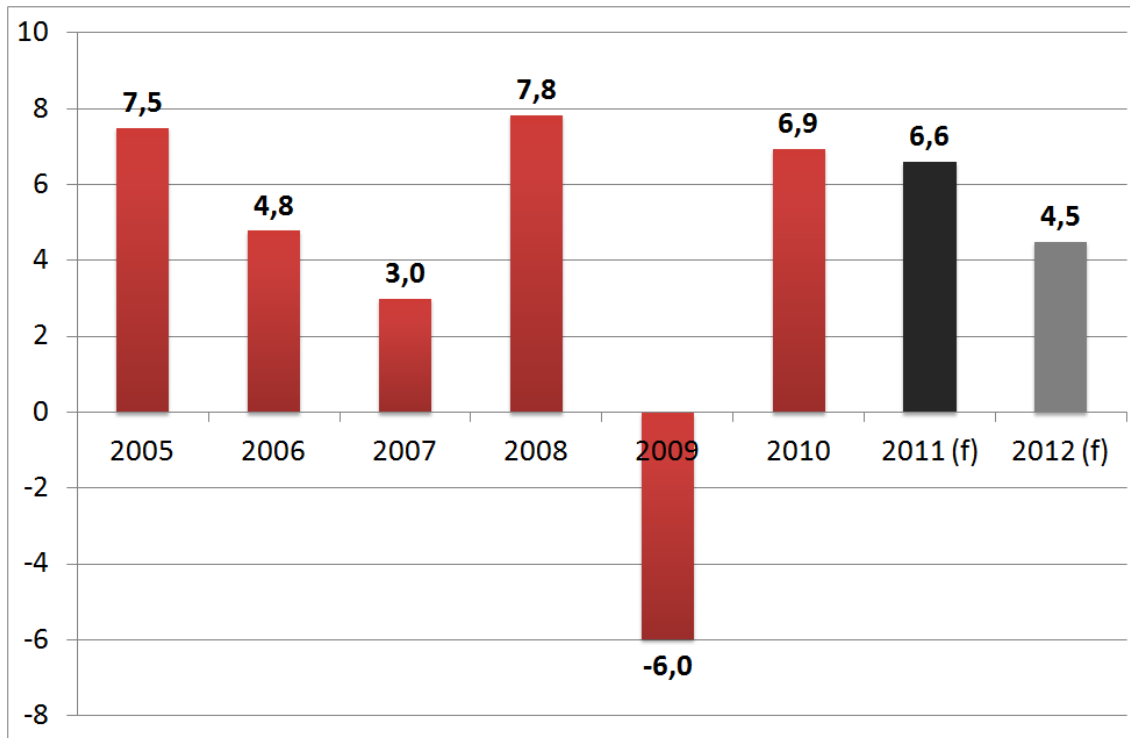
Chişinău, 25 October 2011

1. Macroeconomic situation: Selected issues
2. Bank lending
 - 2.1 Monetary policy and bank lending
 - 2.2 Structural issues concerning bank lending
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1. Macroeconomic situation: Selected issues

Economic growth

GDP growth, y-o-y, %

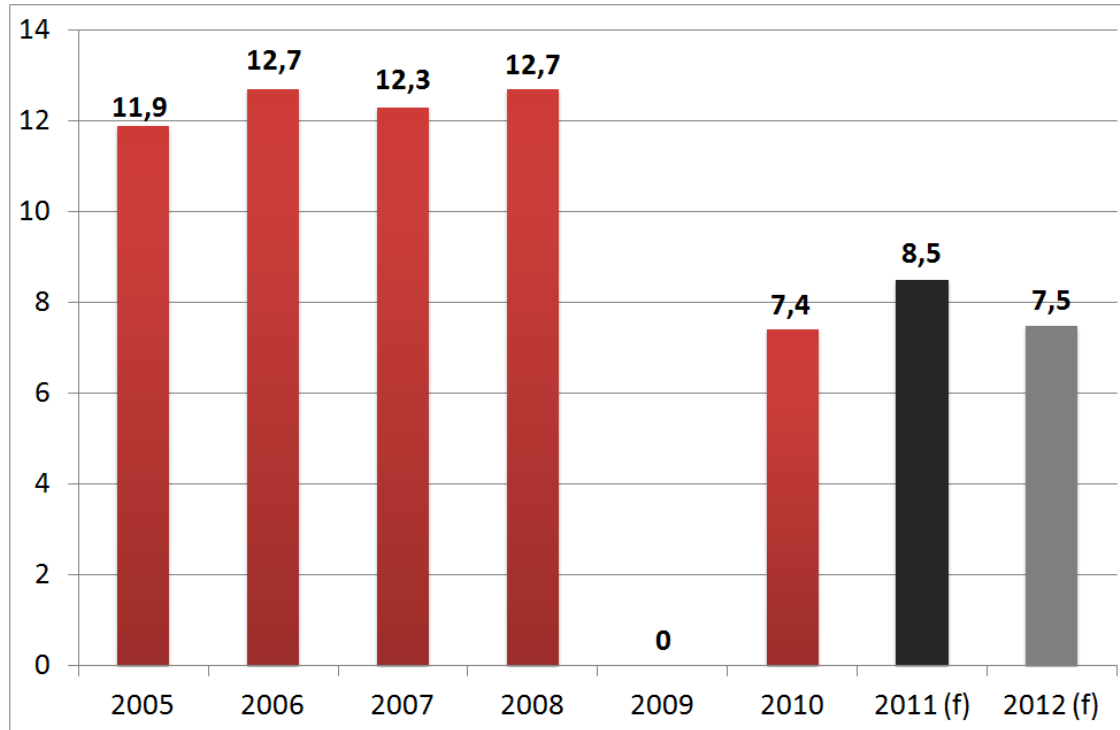


- 2010: Strong and quick recovery after crisis
- 2011: Strong growth continues
- 2012: Slow-down forecast; need for structural reforms

Source: NBS

Inflation

CPI, average, y-o-y, %



Source: NBS

- Until 2008: Relatively high inflation (two-digit)
- 2009: Very low inflation due to crisis
- Since 2010: Stabilisation of inflation rates in single digit realm, despite higher energy/food prices

Reason:

- Change in monetary & exchange rate policy
- Inflation targeting instead of exchange rate targeting

Exchange rate

Exchange rate MDL/USD, 2005-2012f



Source: NBS

Since adoption of inflation targeting:

- Lower interventions of NBM on foreign exchange market
- Higher fluctuation of nominal exchange rate (MDL/USD)
- But: Interventions from time to time to restrain volatility

Macroeconomic situation and SME lending

Economic growth

- Good for SME and SME lending
- But: Lack of structural reforms a problem for long-term growth perspective

Inflation

- Relatively low and stable inflation good for SME lending

Exchange rate policy

- Flexibility crucial to avoid an exchange rate misalignment
- Fixed systems: Risk of overvaluation/deterioration of int. competitiveness → Risk for SME & SME lending

Thus: Macroeconomic situation/policy matters for SME lending

2.1 Monetary policy and bank lending

Transition economies in Eastern Europe:

- Strong fluctuations of lending activity in recent years
 - Very high lending growth before the crisis
 - Abrupt decline during crisis
 - Very low lending after crisis
- “Boom and bust cycle”

Implication for SME finance:

- Bust period/credit crunch: Very difficult to obtain a loan
 - Boom period: Inappropriate checking of creditworthiness of borrower; many companies struggle later to pay back debt
- Both periods of cycle not really good for SME

What is to be done?

Goal: Reduction in lending volatility

Instrument for monitoring situation:

- Comparison between current and “equilibrium” lending
- If ratio too high/upper threshold surpassed: Credit boom
- If ratio too low/lower threshold not reached: Credit crunch

Main monetary policy instruments to reduce fluctuations:

- Central banks’ interest rates
- Reserve requirements

But also: Fiscal policy important → Policy coordination

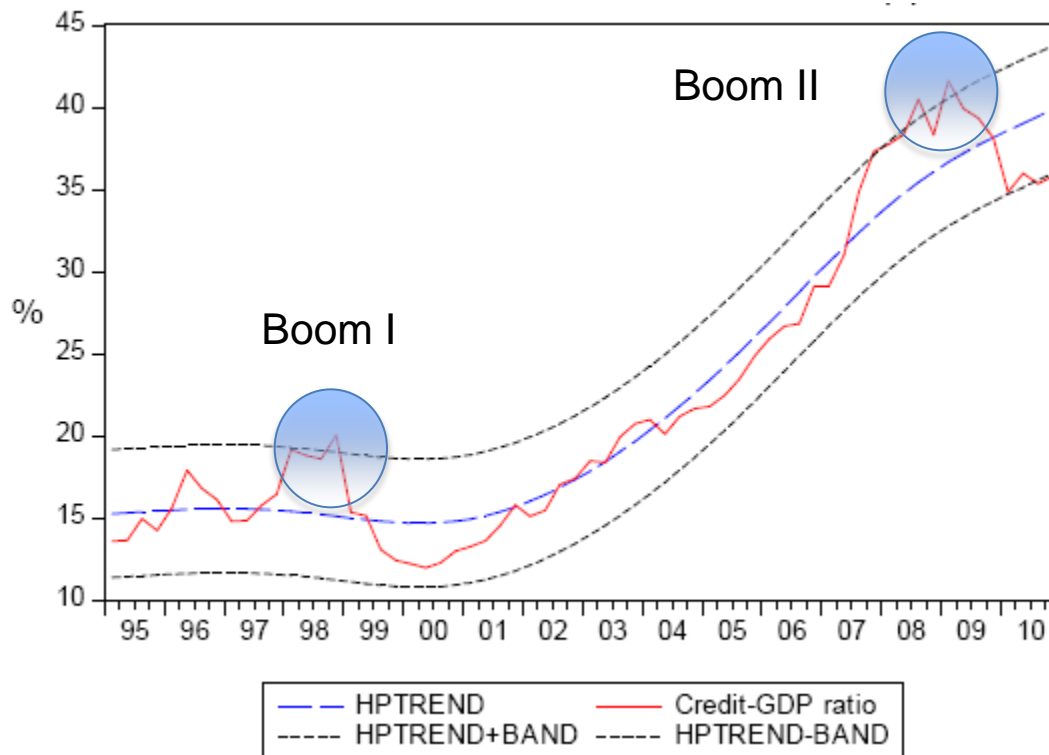
NBM policy in this respect

- Analysis of boom and bust cycle in the past
- Research conducted on request of NBM by GET Moldova; see policy paper PP/03/2011
- Result: Two events of credit booms since independence
- Thus: Important initial steps already conducted

Further steps:

- Establishment of forward-looking monitoring system
- Training of NBM experts for using the monitoring system
- Implementation of policy measures if danger arises
- Here: Need for technical cooperation

Credit booms in Moldova: Empirical Evidence

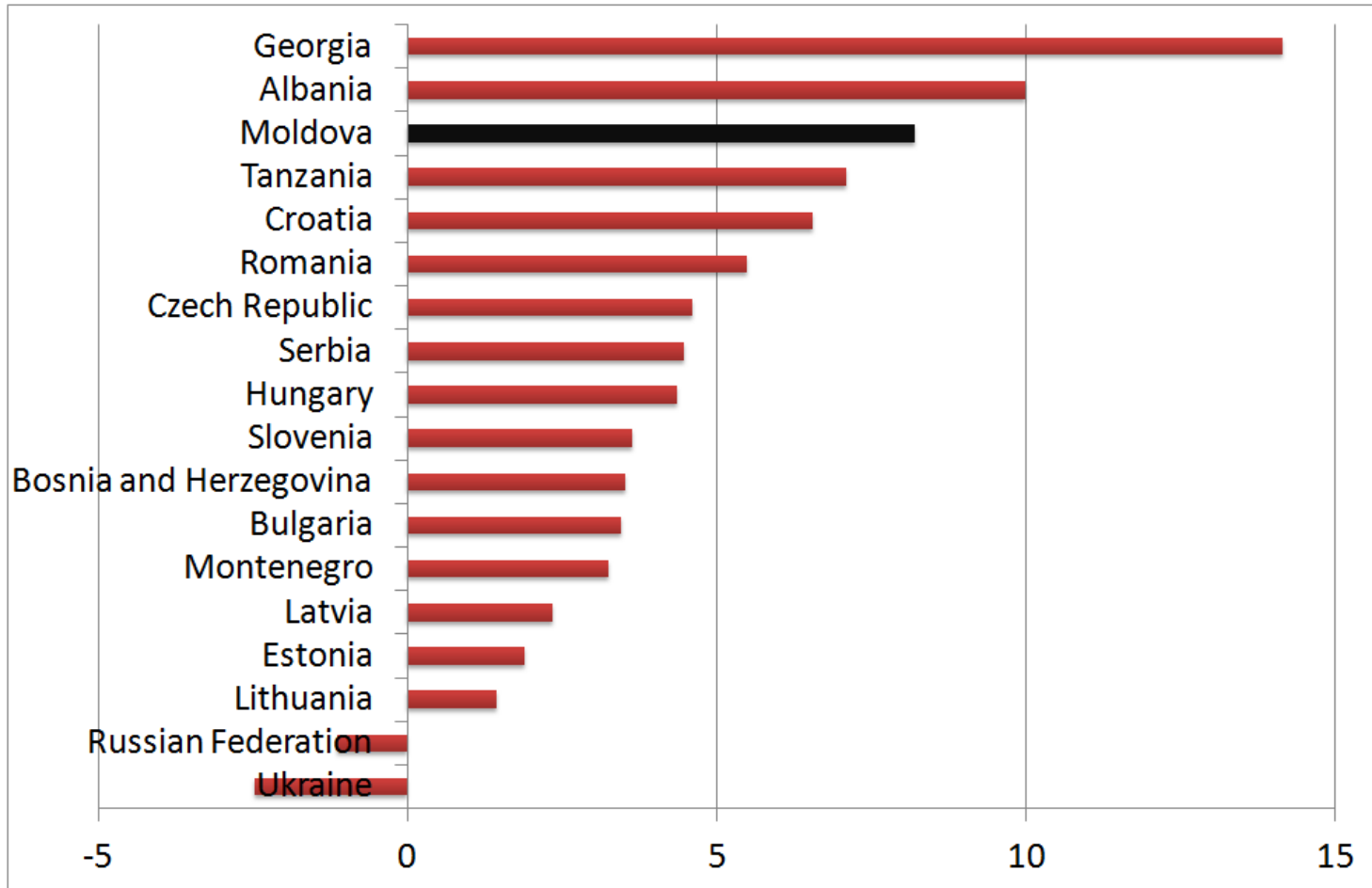


Source: GET Moldova Policy Paper PP/03/2011: "Credit Growth in Moldova: Empirical Analysis and Policy Recommendations"

2.2 Structural issues concerning bank lending

High interest rates constrain access to finance

Real interest rates, average 2005-2010, %



Source: World Bank

Policy measures (overview):

- i. Improvement of creditor's rights → Lower interest rates
- ii. Better working of credit bureaus → Lower interest rates
- iii. Better working of guarantee fund → Better access
- iv. Increase competition and attraction of FDI in banking sector
 - More competition
 - New technologies beyond the traditional collateral based lending
 - Better funding→ Lower interest rates and better access

i. Improvement of creditor's rights

Necessary:

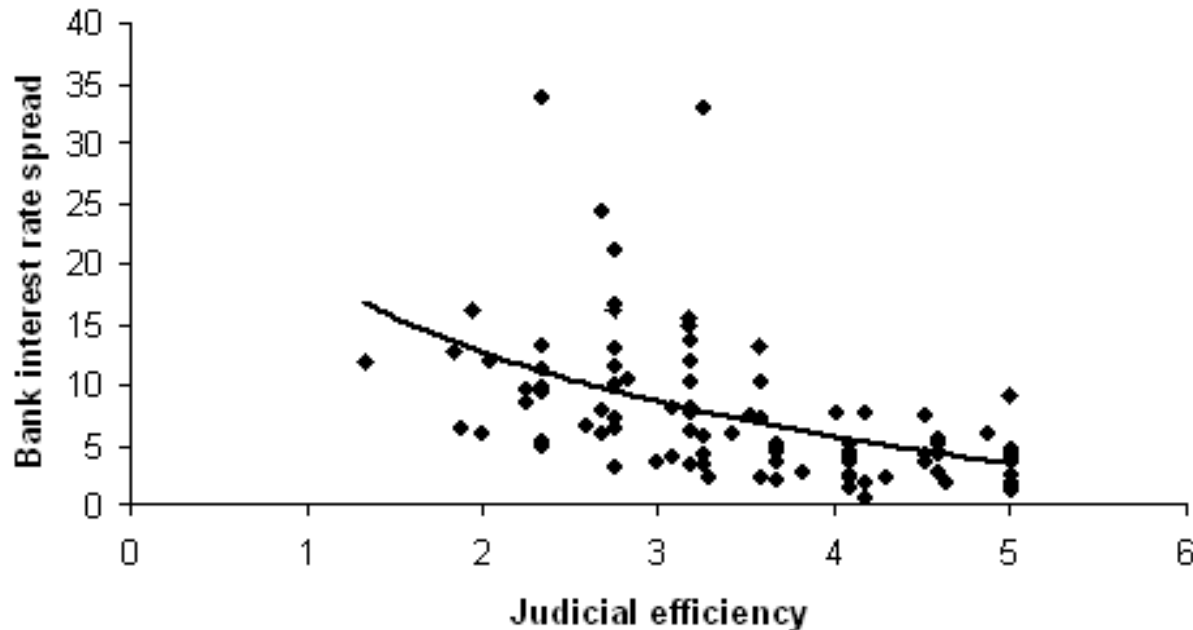
- Improvement of legislation on corporate insolvency & bankruptcy
- Shorter court procedures related to problem loans
- Improvement for execution of collateral

Situation:

- Strong cooperation within IMF program on this field
- Work in progress

International experience

Bank interest rate spread and judicial efficiency



Source: Laeven and Majnoni (2004)

Conclusion: Clear correlation between judicial efficiency and interest rates spreads

ii. Establishment of effective credit bureaus

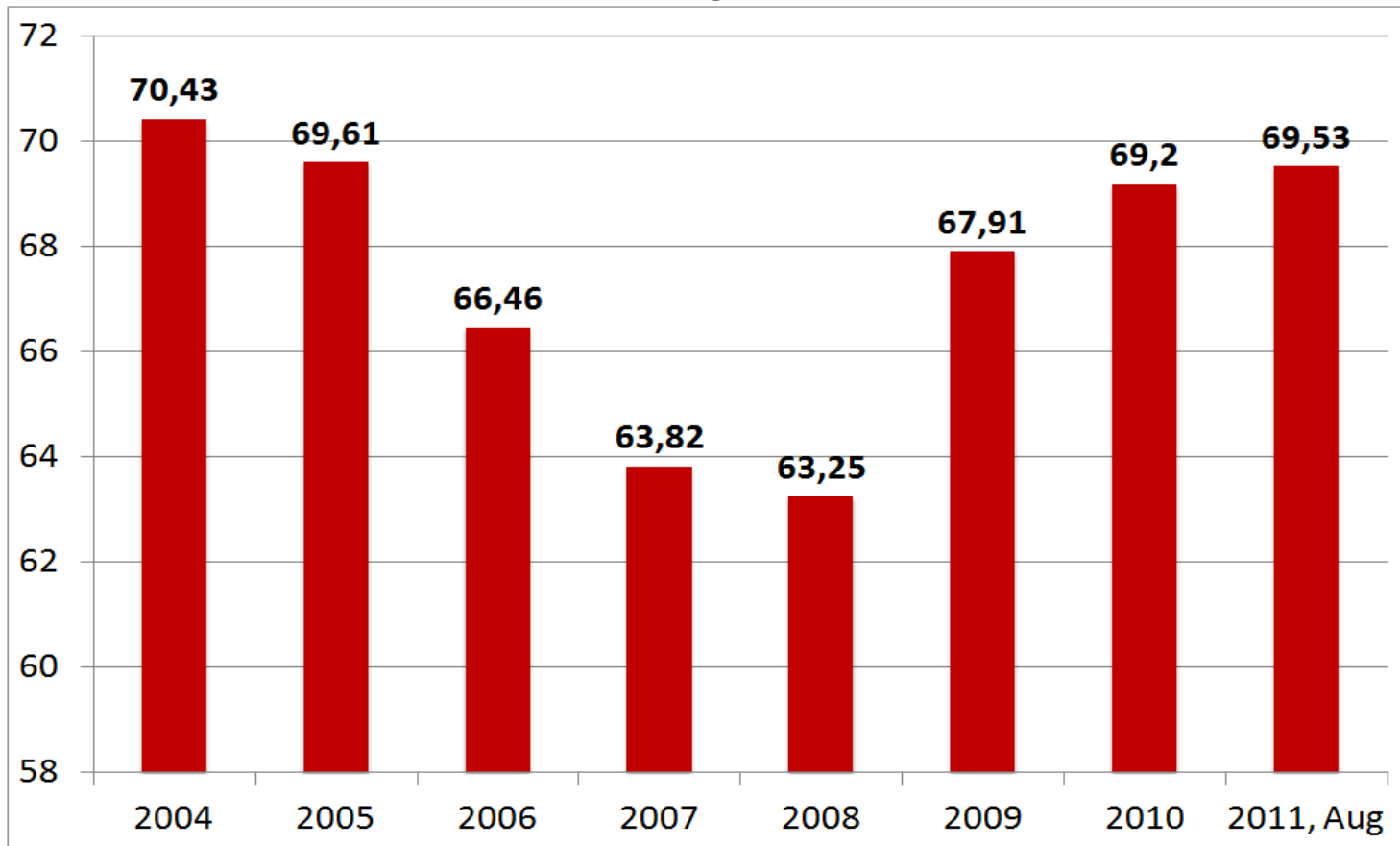
- As of today: Two credit bureaus
 - IMC Infocredit (founded in 2004)
 - "Biroul de Credit" founded by the Bank's Association of Moldova
- But: Databases of credit bureaus are still very limited; much room for improvement
- Reasons:
 - The mechanisms for data collection are not working properly
 - The banks and other financial institutions are reluctant to share the information about their borrowers

iii. Guarantee fund for SME loans

- Idea: Lack of collateral should be mitigated by credit guarantees from a Guarantee Fund
- As of today: Guarantee Fund formally in place, but extremely limited resources and institutional problems
- In particular: 100% state-owned institution
- On top: No participation of commercial banks in the management of the Fund
- Necessary: Reform and substantial recapitalisation of existing Guarantee Fund or establishment of new institution
- Possible: Participation of foreign donors with both technical and financial assistance

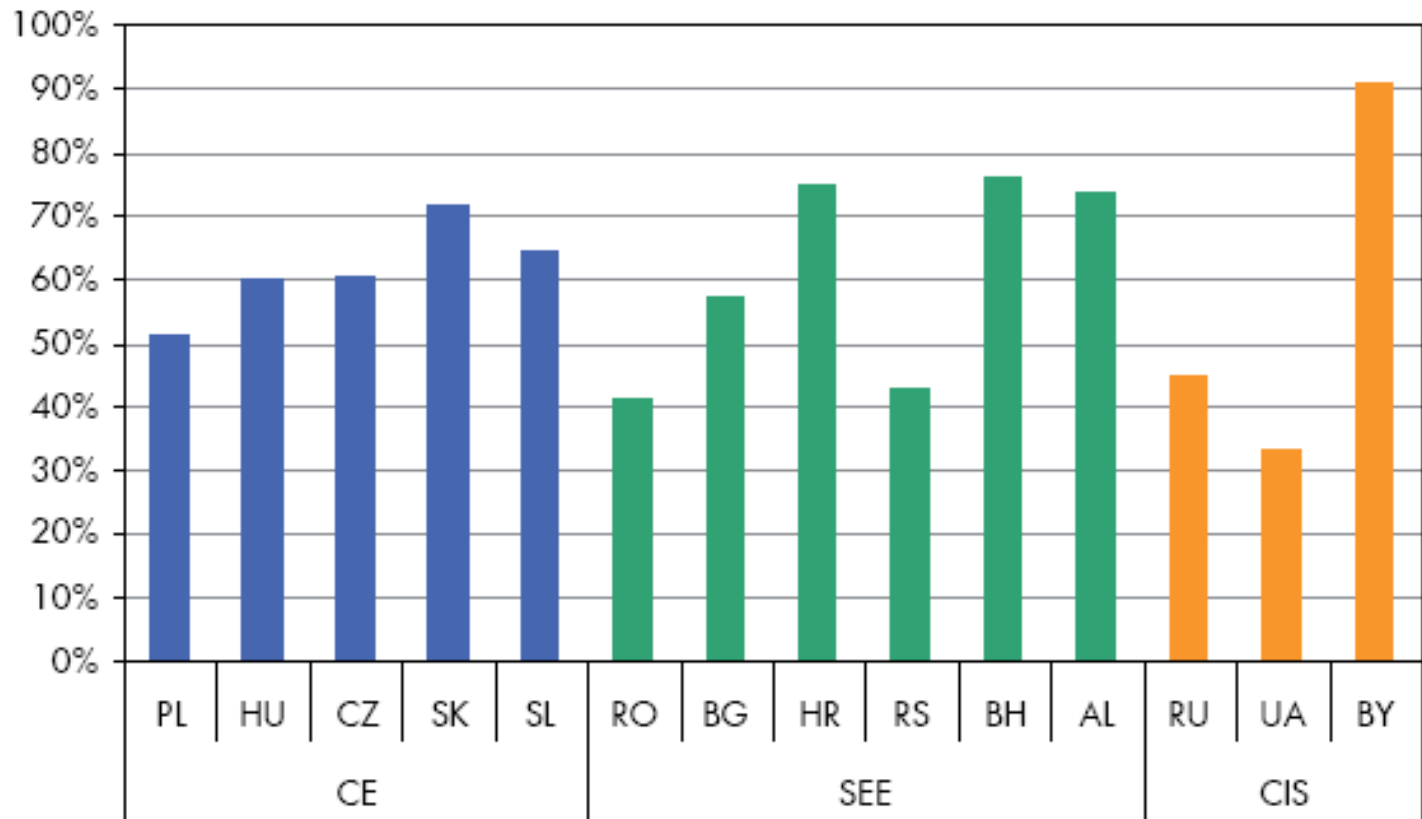
iv. Moderate competition/high concentration

Share of assets of 5 largest banks in total assets, %



Source: NBM

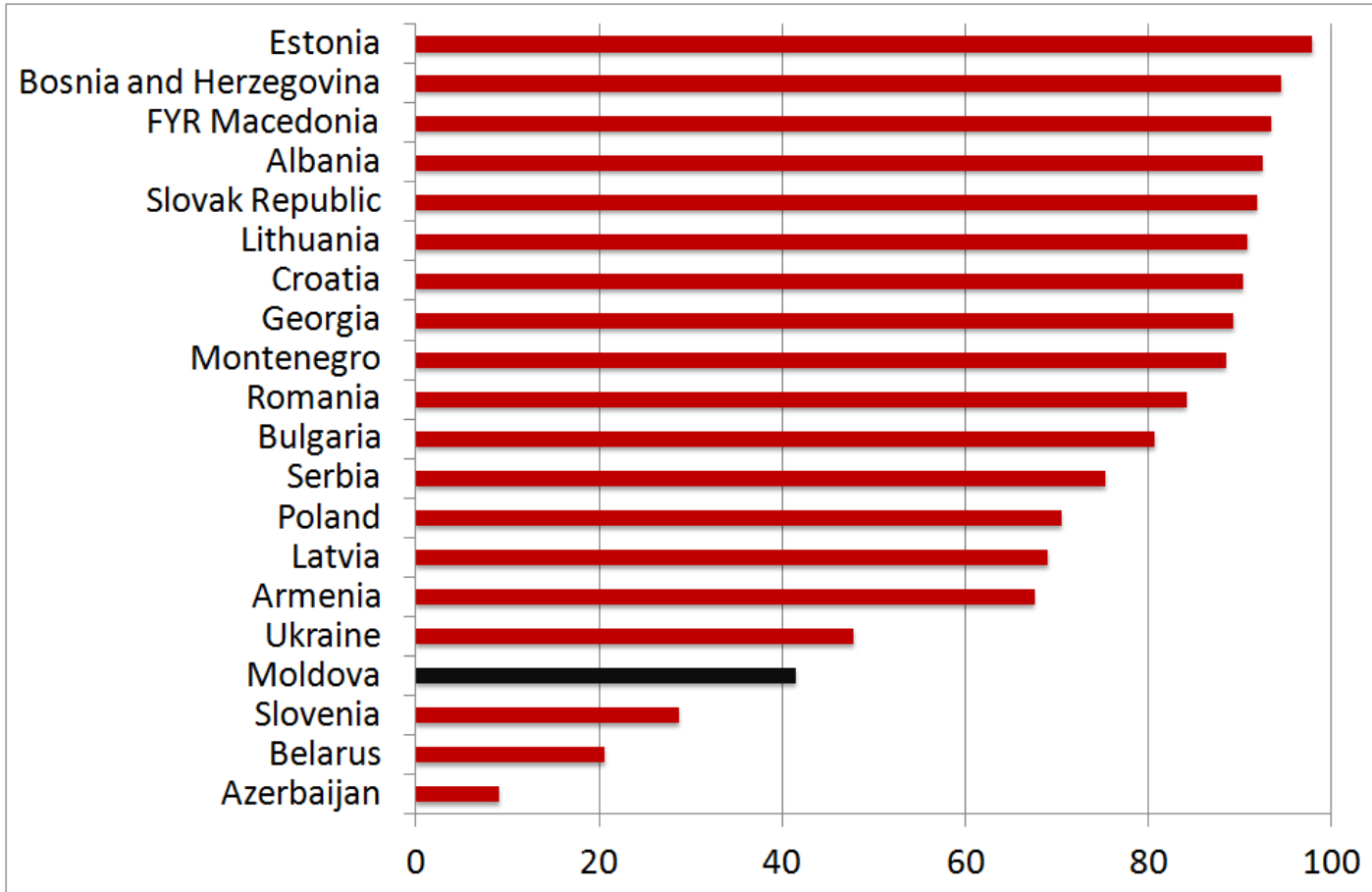
Concentration – International Comparison



Market share of top five banks in % of assets as of end 2009
 Source: Local central banks, Raiffeisen RESEARCH

iv. Low level of FDI attraction

Share of foreign owned banks' assets in total banking assets, % (2010)



Source: EBRD

4. Implications for SME Finance

- SME lending depends on macroeconomic policy and on structural issues regarding bank lending
- Moldova:
 - Adequate monetary and fiscal policy
 - But low speed of reform problematic in the long-term
 - Appropriate monitoring of bank lending by NBM
 - However: Structural deficiencies in banking sector continue to limit access to finance for SME; high interest rates are still a problem
- In short:
 - Current macroeconomic/monetary/banking policy good
 - Lack of structural reforms in the economy and the banking sector remains the main problem

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