

DOI: <https://doi.org/10.53486/9789975359030.25>
CZU: 336.71:338.14(478)

CHALLENGES OF THE FINANCIAL-BANKING SECTOR IN THE POST-PANDEMIC PERIOD

PROVOCĂRILE SECTORULUI FINANCIAR-BANCAR ÎN PERIOADA POST-PANDEMICĂ

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Abstract: Criza COVID-19 a devenit una dintre cele mai mari provocări ale timpului, având un efect sever asupra situației economice mondiale, prin urmare sistemul financiar-bancar fiind direct afectat. Efectele negative ale acestuia au avut un impact simțitor asupra economiei Republicii Moldova, încercând-se prin diverse mijloace, să se asigure stabilitate sectorului bancar, menținerea intermedierei financiare și a funcțiilor băncilor, precum și atenuarea potențialelor efecte de încetinire a creșterii economice. Așadar, în prezentul articol, au fost analizate eventualele riscuri ale sistemului financiar-bancar în perioada actuală post-pandemică, dar și în contextual conflictului militar din Ucraina.

Key words: Sectorul financiar-bancar, Banca Națională a Moldovei, criza pandemică de COVID-19, inflație, datorii de stat, stabilitate financiară.

JEL CLASSIFICATION: G01. G21. E31

INTRODUCTION

In 2020, the global economy was affected by the severe shock of the COVID-19 pandemic. So far, the impact of COVID-19 has been enormous. As a result, economic activity in the Republic of Moldova has also declined sharply as a consequence of COVID-19-related domestic restrictions, and the regional banking system, given its role in financial intermediation. Therefore, the stability of the banking system economic climate affected by the pandemic. The negative effects of the COVID-19 pandemic were felt in all areas of the national economy of the Republic of Moldova and, implicitly, affecting the way and is an indispensable condition for its continuous functioning so as to contribute to the development of the economy. Thus, with the onset of the COVID-19 pandemic, national institutions made efforts to implement measures to mitigate the impact of the crisis, adjusting several monetary policy instruments, relaxing the requirements for capital buffers, and adopting measures to support individuals and legal entities that have contracted loans from banks.

However, the danger still persists, the uncertainty regarding the evolution of the pandemic being accentuated, even more current, the world economy, including the Republic of Moldova, being disturbed by the war in Ukraine. Thus, the main objective of this article is to analyze and identify the

challenges of the financial- banking sector, especially in the Republic of Moldova, in the context of the current post-pandemic economy, and highlight its evolution.

CONTENT

Description of the research methods used

In order to carry out this study, various research methods were used, such as synthesis, analysis, argumentation, comparison, and deduction. Therefore, the study and analysis of the literature were performed, the information basis being the analyses carried out and published by international organizations as well as national ones on the measures taken in the context of the state of emergency generated by the COVID-19 pandemic and their effects in the context of the banking financial system, and other factors that affected this sector.

Literature overview

The world economy, but also of the Republic of Moldova, has gained some momentum in the context of the relaxation of COVID-19 restrictions. Affected by pandemics, our country's economy contracted in 2020, with GDP falling by 7.0 percent [1]. The main factors driving this GDP decline were household consumption, which also declined, followed by investment and stocks. On the supply side, quarantine measures led to a halt in trade and industrial production. In 2021, the economy gradually started to recover, but most short-term indicators are still in the negative zone [1], currently also affected by the military conflict in the neighboring state.

In order to ensure the stability of the banking system by maintaining the critical functions of banks, in 2020, the National Bank of Moldova offered flexibility to banks in dealing with economic agents who have contracted bank loans, by postponing or changing the payment terms and/or the amounts of overdue payments. The NBM has also taken similar actions to support individual consumers of bank loans by providing flexible management of the payment obligations of borrowers. Therefore, during the pandemic crisis, according to the NBM analysis, the financial system of the Republic of Moldova showed resilience, economic and social conditions being characterized by uneven developments and materialization of some risks within the segments of the economy. With a 7% decline in GDP in 2020, Moldova is among the most affected countries in Europe by the COVID-19 pandemic, with a significant effect on households and businesses across the country [2].

In the Financial Stability Report for 2020 [2], the NBM concluded that the Moldovan economy was hit by the pandemic that caused a global recession as a result of the economic shutdown in order to slow the spread of the virus. In addition to the internal lockdown, the recession was also influenced by multiple external factors, such as the economic contraction in the EU and its main partners in the CIS, as well as the limitation of the movement of people and goods, thus reducing both imports and exports. Against the background of the government measures taken, the budget deficit widened and the state debt increased as shown in *Table 1*. So, according to *Figure 1*, as of September 30, 2021, the balance of state debt amounted to 72 394.7 million lei, of which domestic state debt - 45.4% and foreign government debt - 54.6% of the total. The increase in the balance of state debt by MDL 4,574.0 million compared to the values at the end of the previous year was influenced by positive net financing both domestic and foreign. According to the data on projected GDP for 2021, the share of state debt at nominal value in GDP decreased compared to the situation at the end of 2020 [3].

Table 1. The evolution of state debt to GDP, 30.09.2020 - 30.09.2021, (%)

| Debt balance, MDL million | 30 sep. 2020 | 31 dec. 2020 | 30 sep. 2021 |
|---------------------------|--------------|--------------|--------------|
| Domestic state data | 28 161.4 | 29 235.6 | 32 857.4 |
| Foreign state debt | 34 072.5 | 38 585.1 | 39 537.3 |
| Total state debt | 62 234.0 | 67 820.7 | 72 394.7 |
| GDP (million lei) | 206 352.0* | 206 352.0* | 232 500.0 |

* Operating GDP for 2020

Source: Elaborated by the author based on information from the Ministry of Finance

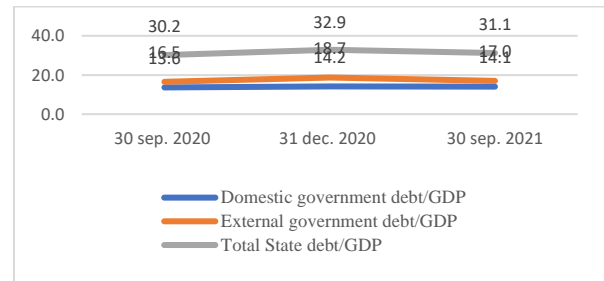


Figure 1. Evolution of state debt to GDP, 30.09.2020 - 30.09.2021, (%)

Source: Elaborated by the author based on information from the Ministry of Finance

Also, based on Inflation Report no.1, February 2022, of the NBM [4], we note, according to Figure 2, that in the fourth quarter of 2021 the annual inflation rate continued at a higher pace than expected (Inflation Report no. 4, 2021), the upward trajectory attested since the first part of 2021. Thus, it increased from 6.7 percent in September 2021 to 13.9 percent in December 2021. As a result, in the fourth quarter of 2021, it was above the upper limit of the range of 5.0 % \pm 1.5 percentage points. The acceleration being driven by the increase in food, oil, natural gas, and other commodity prices on the international market, which also led to the increase in prices of these products on the local market, but, more importantly, in the adjustment of gas and heat tariffs in November 2021 [5].

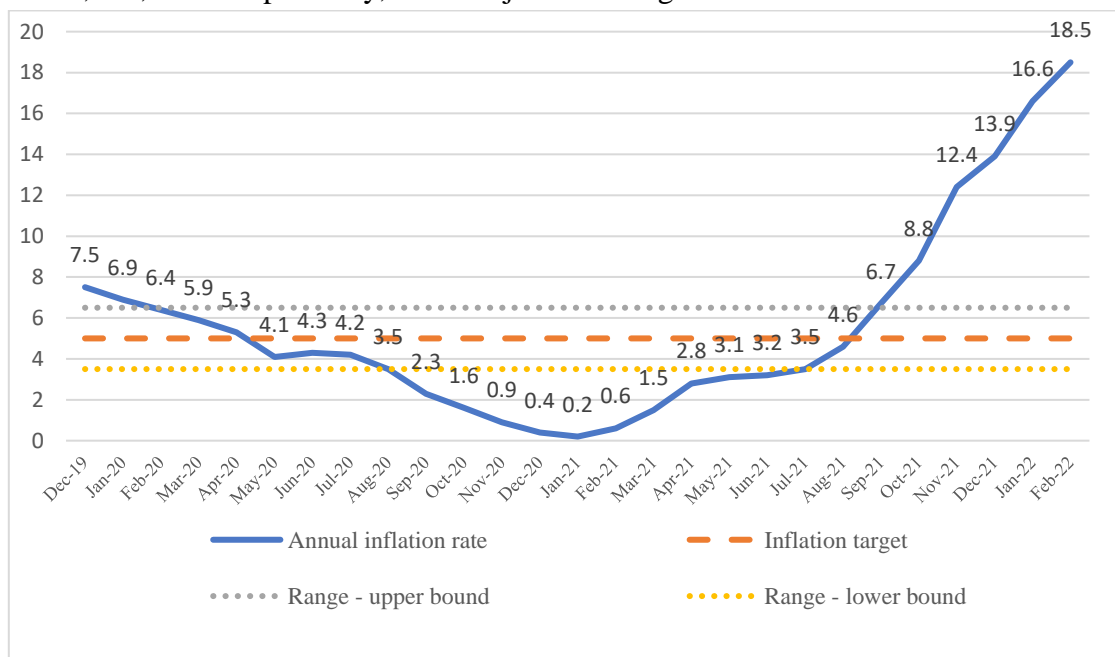


Figure 2. Annual inflation rate, %

Source: Elaborated by the author based on information from www.bnm.md

The significantly high inflation rate increase in the first quarter of the current year of up to 18.5 is also due to the intensification of geopolitical tensions related to the Ukrainian-Russian conflict, which led to the depreciation of both the Ukrainian hryvnia and the Russian ruble. The economic sanctions packages for Russia also have a significant impact on the development of the world economy. Petrol prices rising significantly because in the short-term OPEC+'s capacity to increase petrol production is limited and there is evidence of a delayed reaction to rising global petrol demand [4].

According to the NBM Report on the Financial Situation of the Banking Sector for 2021 [6], the banking sector in 2021, according to the data submitted by the banks, is characterized by high liquidity, growth of assets, loans, own funds, deposits of individuals and legal entities, as shown in *Figure 3*. In addition, the profit for the year compared to the previous year increased to the pre-pandemic size.

Despite the challenges of the period under review, the banking sector continued to perform satisfactorily, maintaining its strong profitability and solvency positions. The banking sector's loan portfolio maintained its growth rhythm. According to NBM [6], the quality indicator recorded an improvement compared to the end of the previous year, due to the higher growth rate of the credit portfolio compared to the growth of non-performing loans. Thus, according to a press opinion [7], in 2021, the loan portfolio in the banking sector increased by MDL 9 136.9 million (20.0 %) to MDL 54 786.1 million. As a consequence, the ratio of non-performing loans to total loans has also decreased, which is shown in *Figure 4* [6]. Credit risk remains the most significant threat to the stability of the banking sector. Furthermore, the credit risk analysis highlights the effectiveness of prudent risk management policies of banks, which have managed to maintain sufficient capital positions in unprecedented crisis conditions.

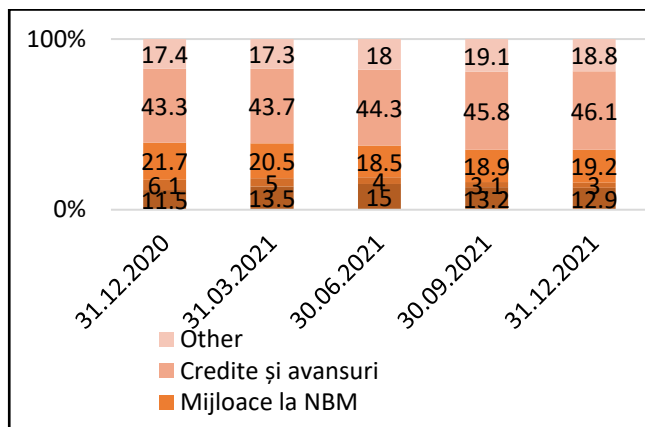


Figure 3. Asset structure %

Source: Elaborated by the author based on information from www.bnm.md

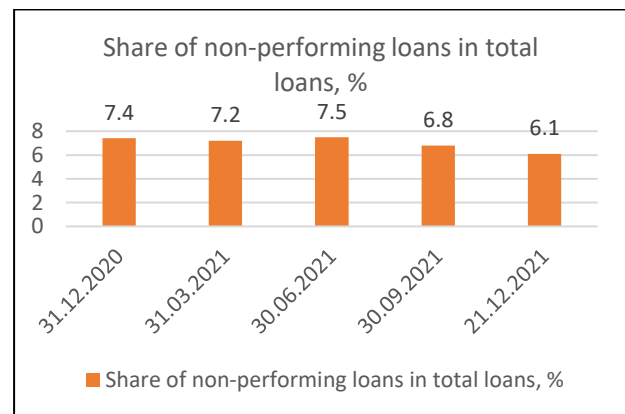


Figure 4. Share of non-performing loans in total loans, %

Source: NBM (National Bank of Moldova)

The risk of over-indebtedness of the population and the risk related to foreign currency loans also remain the main challenges associated with the non-bank credit sector. Therefore, according to the data of a survey, conducted in January 2022, by CBS Research, commissioned by the ISPRI "Ioan I.C. Brătianu" of the Romanian Academy and the IDIS "Viitorul" in Moldova, it was found that in 2021 there was an unprecedented increase in the degree of indebtedness of individuals by almost 8 billion MDL more than in 2020 [8]. However, according to the expert, the number is much higher

because Moldovans have two other unofficial sources of financing (Figure 5): relatives and friends; and moneylenders.

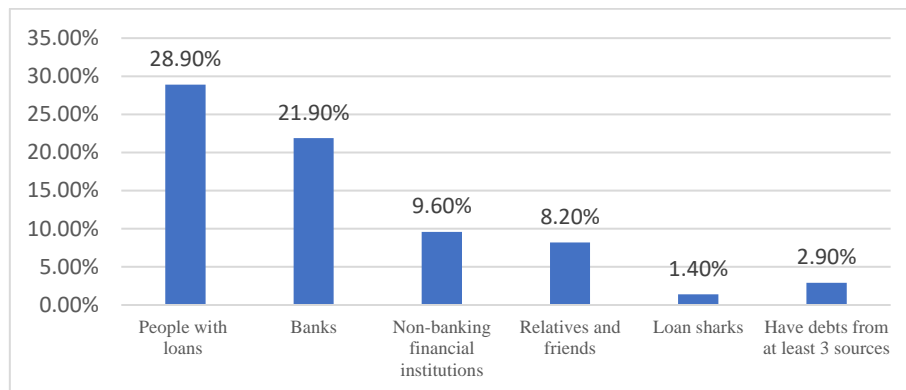


Figure 5. Degree of indebtedness and source of borrowing of individuals

Source: Elaborated by the author based on information from <https://ionita.md/>

Results obtained

The unpredictability of the economic effects of the COVID-19 pandemic and the military conflict in Ukraine in the coming period on the financial-banking sector, requires the National Bank to review its actions in the process of monitoring the activity of banks, in order to focus mainly on those areas where the highest risks may occur. Hence, as a result of the assessment of the main risks and challenges related to the banks' activity, the most important areas to focus on to ensure the stability of the banking sector for 2022 has been established as: (1) Credit risk; (2) Internal governance, risk management, and internal risk capital assessment process; (3) Internal Liquidity Adequacy Assessment Process [9].

CONCLUSIONS/ RECOMMENDATIONS

To conclude, the uncertainties surrounding the evolution of the pandemic and political developments will keep the world economy, including Moldova's, well below its potential. The contribution of key sectors and industries will prove crucial in helping global economies recover from the devastating impact of the coronavirus and more recently in the context of the conflict in Ukraine, and build for the future - with the banking industry a likely benefactor. So, the financial and banking industry has a crucial role to play in helping the global economy to overcome this crisis and return to growth [10]. Despite all these challenges facing commercial banks in the Republic of Moldova, they have the responsibility to ensure continuity in their activities, to maintain stability and customer confidence. In these circumstances, banks are encouraged to continue to promote appropriate policies for the recognition and coverage of non-performing exposures and to carry out proper capital and liquidity planning as well as effective risk management.

Also, the ability to mitigate the impact of the crisis and support economic recovery will depend crucially on external funding, in particular the successful negotiation with the IMF, which will give the Republic of Moldova the best chance of achieving its public health objectives and enabling a solid overall recovery. There is therefore a need for global coordination and cooperation on concrete measures to slow the spread of the pandemic and concrete economic actions to mitigate the economic effects.

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