

Gent Sejko: The economy and banks, present and future challenges

Speech by Mr Gent Sejko, Governor of the Bank of Albania, at the round table on “The economy and banks, present and future challenges”, organised by the Bank of Albania and Government of Albania with the banking system, Tirana, 16 September 2015.

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Your Excellency Prime Minister,

Honoured representatives of international institutions,

Dear bank executives and representatives,

This meeting seeks to once again draw the attention on non-performing loans, an issue that has been discussed extensively over the recent years. It aims at fostering the shared and concrete commitment to reduce the stock of non-performing loans, increase the financial intermediation by the banking sector and underpin Albania’s economic growth.

Following, I would like to list some facts.

The high level of non-performing loans has not affected the banking sector’s stability. Liquidity and capitalisation indicators remain adequate and the financial performance has been positive and improving.

But, the still-high percentage of non-performing loans has contributed to a higher perception of risk by banks; in turn, they have adopted a more conservative approach to lending.

Our survey data point to tightened lending standards; meanwhile, the lending volume, albeit positive, is still considered as low.

The credit quality has improved during this year. The non-performing loans ratio, after peaking 25%, fell to around 21% in July 2015. We believe this improvement reflects the measures taken in the last 2–3 years, of which I would like to single out:

- a) Amendments to the law “On income tax” at the end of 2013, to facilitate the loan loss write off from the balance sheet;
- b) Amendments to the Code of Civil Procedures in September 2013, to improve the collateral execution process;
- c) Entry into force of a regulation of the Bank of Albania, which renders obligatory the write off of loans classified by banks as “loss” for a period longer than 3 years;
- d) the work accomplished in cooperation with the commercial banks to restructure loans when the borrowers are exposed to more than one bank;

Albeit the number of non-performing loans subject to the execution process has been significantly up, the improvement of the credit quality reflects mainly the loan loss write offs from banks’ balance sheet.

For the first half of 2015, its value amounted to around ALL 11 billion. The write off from bank’s balance sheet is both healthy for the bank and useful for the economy, as it:

- provides a more realistic picture of the banks’ loan portfolio, releases the capital and improves their financial balance;
- improves bank processes, thanks to a more efficient use of human, financial and technical resources, and redirects the focus of the bank toward new loans;
- improves the overall functioning of the financial market, as it contributes to the market “exit” of non-competitive businesses.

- contributes positively to the market participants' assessment of the banking sector (ratings) and, subsequently, to the assessment of Albania's economy;
- provides conditions to better manage debt collection, **but always accompanied with the necessary message that this does not imply forgiving the borrowers debt.**

In our case, the process of loan loss write off from banks' balance sheet is not a detached process from real developments. On the contrary, it reflects the gradual improvement in non-performing loans.

In concrete terms, over the last two years, the growth rate of non-performing loans has decelerated at extraordinary rates, banks' annual spending for provisions has fallen, and new loans, especially those denominated in lek, have been stable.

On their side, banks have been increasingly committed to this process. Usually, it happens when the effectiveness of the process improves and/or banks expectations for lending improve.

Ladies and gentlemen,

I would like to point out that although the credit quality has improved, the level of non-performing loans is considered as still high, and it should be lowered at a faster pace. This is a complex process that puts to test the adequacy of the legal framework, as well as the coordination and consistent implementation of institutional policies.

These challenges were identified in the Annual Forum organised in June. Some of them acknowledge the need for improving the legal framework. Others point to unifying, in a single law, important stipulations about the execution of executive title, which are currently envisaged across several laws.

We should be aware that a part of the difficulties arise from the dimensions of this problem; also, until a while ago, the justice system lacked the experience and specialised expertise on these matters and is still facing inadequate capacities to handle such practices. However, inadequate legal provisions and their inconsistent implementation in practice render the collateral execution process tedious, uncertain and costly for the parties involved.

The coordination of institutional policies is another key process to respond to various problems in a timely and appropriate fashion. For example, the recent Action Plan for the resolution of non-performing loans represents a new level of communication and commitment of public institutions and the Bank of Albania to find a sustainable solution.

Many of the issues concerning the banking industry, which the Bank of Albania considers as crucial, have been incorporated in this Plan. For example, the preparation of the draft law "On bankruptcy", a commendable effort by the Ministry of Justice represents a significant development and unique opportunity to render the resolution of a financial obligation as an enforceable, predictable, and efficient process.

Concluding, I would like to underline that reducing the level of non-performing loans is closely related to the magnitude of financial intermediation by the banking sector.

The need to redirect private investments towards new sectors in the economy, the small market size, problems related to the low quality of financial reporting by private entities, and slowdown of economic growth rates in Albania have dictated an unstable private demand for loans .

Therefore, it is important to find, in addition to macroeconomic policies, new alternatives to boost domestic demand, promote optimism in the economy and contribute positively to businesses and consumer expectations. The acceleration of economic growth would provide the conditions for faster and steadier improvement in the level of non-performing loans.

Thank you!