

# **CZECH UNIVERSITY OF LIFE SCIENCES PRAGUE**

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## **Final Internship Report Commercial Bank 'Banca Sociala' Joint Stock Company**

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**Grenoble Ecole de Management  
Ecole Supérieure de Commerce  
Master in Management**

**Final Report on Internship**

**Commercial Bank 'Banca Sociala' Joint Stock Company**



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## **Introduction/General presentation**

My name is Denis Moraru, I'm about to Graduate from Grenoble Ecole de Management. One of the conditions to obtain a diploma is to apply the knowledge received at school into the real business. In order to do that, I started to look for an internship at banking industry.

While analyzing the banking industry in Moldova, at my home country, I came across the CB 'Banca Sociala' JSC, a bank which is focused on supporting agriculture and communities. This bank is also trying to promote competitiveness among businesses and granting loans on those purposes with very low interest rates. These credits are generally issued from the resources of World Bank and European Bank for Reconstruction and Development. This cooperation also had an effect on my choice of the company.

I did my internship in a credit department at one of the branches in Banca Sociala. My internship lasted for almost 4 months, from June 27, 2011, till October 17, 2011.

The first part of this report will provide the reader with some general information on the Banca Sociala. In this part I would like to focus on information related to the crediting policy of the bank and types of credits, since it was relevant to my internship. In the second part of my report I would like to describe the work I've done, I would like to discuss some of the tasks I've completed during my internship. At the end of my report I would like to talk about my usefulness to the company. I will also discuss what I've learnt during this internship, and then I will conclude my report.

## **‘Banca Sociala’ in General and Crediting Policy of the Bank**

### **CB ‘Banca Sociala’ JSC**

Commercial bank ‘Banca Sociala’ is functioning at the market of Moldova for around 20 years. During this time Banca Sociala expanded quality and range of services, and gained loyalty of customers. Today Bank has branches and representations in most cities of Moldova.

Bank provides services to corporate clients, individuals, financial organizations and other banks. Among those services are:

- Lending to legal entities and individuals,
- Operations with securities,
- Regular accounts,
- Transfer services (Western Union, MoneyGram etc.)
- Exchange services and others.

With respect to the crediting policies and conditions, Banca Sociala is one of the most competitive banks on the market. At the very beginning, when bank was just established, Banca Sociala was positioning itself as financial organization which grants credits to agriculture and communities on very competitive conditions. Banca Sociala continued to develop that strategy, and now the company may offer different credits with low interest rates, supported by the sources of European Bank for Reconstruction and Development and the World Bank. But most clients of the bank are enterprises unrelated to the sector of agriculture.

### **Strategic directions of bank’s operations**

CB “Banca Sociala” has two main strategic goals – maintaining the position of one of the leading banks in Moldova and remaining at the top of liability, liquidity and stability through persistent controls and improvement initiatives.

Banca Sociala is improving its visibility at the markets where it is already present due to transparency of the provided services, and clear

understanding of the market needs in terms of bank products' quality and quantity. It aims to be competitive in a highly competitive banking sector in Moldova and to be consistent with the requirements set by reputable international financial institutes.

The main objective of the bank related to lending policy is to define a high yield credit portfolio based on minimization and diversification of credit risks.

Another goal is to encourage the development of modern forms of bank lending through the introduction of new products and the expansion of already existing credit products, such as express lending to micro and small businesses when applying the system of scoring, mortgage lending, factoring, multicurrency credit lines, diverse consumer lending to individuals.

Bank continues to balance the structure of assets and liabilities, and aims to develop the resource base by

- Attracting new customers as well as economic agents - exporters;
- Development of new kinds of deposits for legal entities and individuals in national and foreign currencies with attractive conditions and different retention periods;
- Providing new services that would facilitate the flow of funds: accepting all kinds of payments, and expanding the range of services related to international operations.

Bank is continuously cooperating with various international financial organizations in order to obtain additional resources and foster the development of small and medium businesses in Moldova.

It also seeks to promote the import-export operations in Moldova through the involvement and funding of various new projects related to modern trade financing schemes with the active participation of foreign banks and insurance companies. The foreign banks and insurance companies allocate to the bank additional credit lines for financing the trade for confirmation of documentary operations.

Optimization and expansion of the “retail” segment is another goal to achieve. Bank widens the range of exchange services in each particular affiliate and regularly investigates on local market developments [price and quality of similar services provided by the competition].

The bank broadened the range of training and retraining programs, especially for middle level managers. Banca Sociala involves the specialists of international organizations, follows advices of internal and external audit inspections and consulting companies. Personnel policy should be given a priority in order to ensure maximum effectiveness of the staff, including thorough selection of top-management. Also there should be available effective tools for the appraisal of personnel along with the development of motivation and remuneration methods.

Bank seeks for risk-free operations in order to compensate the ones that are both high-risk and highly profitable. Necessary controls should be in place, as it's the prerequisite of success in the prevention and efforts against money laundering.

Payment cards (credit and debit) should be used more extensively by economic agents (legal entities and individuals) not only for international transactions, but also for daily operations.

The modern automated banking system "Va-Bank" should be further applied. There should be ensured proper level of protection of confidential banking information from unauthorized access of computer viruses that may cause serious damage.

Clients are the most valuable asset, and it's crucial to be able to address their needs timely and offer most modern technologies and services on the ongoing basis.

Maintaining effective organizational structure of the Bank, developing in line with the modern banking institutions around the world, ensuring internal integrity and high level of controls along with persistent investigations on the possible fields of improvements are the key strategies that require to be given the highest priority on daily basis.



## **Risk management related to the bank's operating activities**

Banks are exposed to the various risks as they are highly dependent on the debt capital. Economy of each particular country experience tough times, when any of those risks related to the banks' operating activities are realized. That is why banking activities are subject to special state regulations and controls.

The entrance barriers to the banking sector are continuously growing: the level of minimum capital is increasing and the requirements to the reputation of the banks' top-management are continuously expanding. The requirements that have to be met in order to obtain the license for realization of financial activities are set by National Bank of Moldova. These requirements tend to be quite high and aim to limit or/and decrease the risk of uncompetitive and weak banks entering the banking system. There exist special obligatory guidelines that commercial banks should follow and report the results and/or progress to the National Bank of Moldova on regular basis.

Banca Sociala has created its own analytic base on the macroeconomic and banking system indicators that help to follow the dynamics of banking system development against national economy. It allows implementation or/and adopting new methods of risk management timely.

Risk management is backed-up by enormous number of control points, requirements and guidelines, but human factor is always present and can be crucial. Banca Sociala pays particular attention to the personnel training programs, professional development programs, raising the feeling of belonging to the bank and its activities [corporate spirit].

In Banca Sociala there exist and function the Committee responsible for assets and liabilities' management, Credit Committee of Banca Sociala and its affiliates, etc. The higher the value of the banking operation is, the more and higher authority level will be involved in the decision-making process in order to diminish the level risk related to that operation.

### *Risk related to bank's liquidity*

Traditionally a significant part of banks' assets are accommodated as government securities. Bank is required to check on its liquidity on daily basis and report to the National Bank of Moldova on monthly basis.

Bank has to ensure required reserves are held. Also Bank has access to interbank resource market, where it can attract or/and accommodate some resources, in necessary.

The appraisal of potential operational cash flows is essential part of liquidity controls.

Bank defines the difference between the inflow and outflow of resources according to nine time periods. Depending on the result of real liquidity appraisal, the bank adjusts the banking policy related to the attraction and allocation of funds.

*Capital adequacy* is realized through:

- management of factors that have direct impact on net effective income of the bank;
- formation and maintenance of sufficient and necessary reserve funds;
- decisions on the issuance of new bank shares, shares buyout;
- decisions on the bank's participation in the capital of other financial organizations in Republic of Moldova;
- bank dividend policy (capitalization, payment or/and non-payment; volume or/and level). The higher the level of dividend payments is, the lower the decrease of bank capital is, but at the same time the value of the shares is growing;
- diversification of bank assets;
- management decisions on the structure of credit portfolio;
- ensuring high quality of credit portfolio,

- decisions on bank guarantees issuance, as well as letters of credit and accepting the risks related to the issuance of letters of credit,
- different kinds of securities, and
- optimization of banks assets.

*Credit risk* is realized through:

- meeting the requirements set by the National Central Bank of Moldova,
- properly following internal procedures of Banca Sociala related to the mechanism of making decisions on granting credits, issuance of liquid securities, such as bank guarantees and letters of credit;
- making forecasts on dynamics and structure of credit portfolio, aggregate normative bank capital and other ratios,
- diversification of credits among industries, currencies and types of securities provided to cover Bank's exposure;
- setting limits on possible credit lines that can be provided by particular Banca Sociala affiliate. Decisions on credit lines higher than allowed by internal guidelines should be escalated to the Credit Committee of CB Banca Sociala JSC;
- very high credit lines should be only managed by the Board of the Bank;
- mixed facilities/means to cover the risks related to a particular operation,
- usage of external experts advices on the definition of the market value of the collateral;
- classification of credit lines according to the requirements set by National Central Bank of Moldova and internal Bank Code (2%-standard, 5%-under surveillance, 30% - substandard, 60% - doubtful receivables, 100% - bad debts) – will be discussed in detail further;

- identifying the maximum credit line that can be obtained by an individual or group of individuals, as well as controls on the lines available for particular affiliated offices and bank employees;
- implementation of credit monitoring systems;
- informing competent authorities about doubtful receivables and possible bad debts, cooperation with legal authorities, such as Courts, Bank lawyers; and Bank security team.

*Risks related to the exchange rates*

- operations on interbank market through purchase and sale of currencies to clients at the internal auction;
- regulation of structure and dynamics of assets and liabilities related to exchange rates;
- setting particular rates of interest for foreign exchange credits and deposits;
- following the guidelines on the normative for remittances;
- setting certain internal limits on the operations that involve different currencies;
- hedging forward operations.

*Risks related to different rates of interest*

Bank is treating such risks carefully and on the regular basis through:

- setting rates of interest for Bank's assets and liabilities;
- proper choice on the type of interest: fixed or floating interest rate;
- assessing the structure of working assets against the structure of paid liabilities;
- monthly identification and tight controls on the dynamics of spread, absolute cumulative gap, as well as a range of relative indicators of interest related risks and their trends;

- reporting to the Bank's top management on the trends identified, measures taken, and actions to be further taken and changes to be applied on quarterly basis.

*Operational risk* is managed through:

- maintaining a copy of databases used in daily operations at the reserve server;
- availability of uninterrupted power supply unit, emergency generators;
- limited access to the information both at the hardware and the software levels;
- applying digital signature that is available in the system Client-Bank,
- continuous renewal of technical base, update of software.

### **Principles of Lending Policy**

Loans are available to solvent borrowers if they have real resources for credit repayment, as well as robust security in the form stipulated by law and the relevant banking practice.

The basic principles of crediting are:

*1. Minimizing the risk of not returning the loan.* The entire system of credit management, including the stage of loan applications processing, issuance of a loan and monitoring of credit, should contribute to achieving this goal.

*2. Targeted use of credit.* Credit must be used in strict accordance with its purpose stated in the loan agreement and the documentation submitted by the borrower on the activity he/she is financing.

*3. Provision of credit.* Each loan must be assured by a loan guarantee, which must comply with the laws of the Republic of Moldova.

*4. Interest rate.* Interest rate must cover expenses on crediting the customer and provide the bank with optimal profit. Interest rate is determined with respect to the purposes of the loan, terms of its use, risk level, costs of resources and other factors. Interest payments are made within the deadline

stipulated by the loan agreement (daily, monthly or in other terms). In addition to interest, the borrower pays the commission for processing of loan application, loan management and other commission rates in accordance with the procedure for paying commissions on lending activities.

5. *Creditworthiness of the Borrower.* The credit is granted to applicants who have positive indicators of solvency within the limits set out in this policy rules. Those indicators must ensure return of loans, interest payments and commission on them in time.

6. *Term of loan.* Loans are granted for specified in the loan agreement time.

### **Marketing in the Bank's Lending Policy**

Marketing policy of the bank is designed in order to attract customers, to expand sales of its services and sales of new services, at the same time increasing effectiveness of work.

Marketing objectives are: on the one hand - to attract customers as depositors of the bank, on the other hand – to direct bank credit resources towards companies/individuals who will use them with higher efficiency for the bank and for the borrowers themselves.

The bank's main marketing tool is the interest rate policy directed towards effective crediting of the customers, at the same time encouraging the accumulation of their own financial resources, which are the basis of deposits in the bank.

Marketing is constantly focused on determining the degree of possible risk in granting loans.

Bank is granting loans to businesses which are carried out in various sectors of the economy, trying to cover all major groups of customers: corporate businesses, SMEs, legal entities, communities, local public authorities, thereby contributing to the development of the economic situation within the country.

Based on the main strategic directions of the Bank's marketing policy, lending policy is developed and approved on the yearly basis by the board of directors.

The main strategic directions of lending policy are:

- Continuous focus of all the services of the Bank to achieve the benchmarks required for a good rating, while ensuring the profitability and keeping sufficient level of the capital at the Bank;
- Keeping up on the positions of the Bank at the resources and services market. The main tool for it is using the competitive interest rate policy;
- Increasing degree of liquidity of investments;
- Determining of the strategic customers with respect to their role for the national economic development;
- Maintaining quality of banking services at the level acceptable by the shareholders and depositors;
- Improving the information database in order to achieve more profitable level of managing the bank strategy, and to be able to react fast to changes that appear on the market;
- Ensuring continuous improvement of organizational structure of the bank;
- Running training programs for bank personnel.

Based on the main strategic directions of the Bank's marketing policy, lending policy is developed and approved on the yearly basis by the board of directors.

### **Types of Loans**

There are several types of loans granted by the Bank. We will discuss those types briefly.

Bank loans are classified according to the term of loan, loan value, form of assurance of loan and purpose of loan.

1. *Depending on loan term* loans can be of 3 types:

- Short term - up to 1 year;
- Mid-term - from 1 to 5 years;
- Long term - over 5 years.

Specific terms for a loan are determined with respect to the objectives of the loan and the payback period of credited event/project.

Repayment is made in accordance with the timetable:

- Equal installments (monthly, quarterly, or at any other time),
- Annuity (equal to the amount of repayment, including loan amount and accrued interest),
- With the establishment of a grace period (investment loans, enterprises with the seasonal nature of production, etc.),
- Irregular schedule (taking into account the specifics of the client).

Priority is given to high-performance transactions and projects with short payback periods and medium and low risk of default on the loan.

2. *Depending on the loan value* credits are classified as follows:

- "Large" - over 10% of the total regulatory capital. These loans must be approved by the Board of the bank;
- Over the limit - below 10% of the total regulatory capital, but exceeding the limit of the branch. Those loans must be approved by the general credit committee of the bank;
- Within limit – loan value is within the limits set by the branch and approved by the decision of the credit committee of the branch.

3. *Depending on the accepted forms of assurance* of credit:

- Secured;



-Unsecured.

In turn, secured loans are classified according to the admitted forms of security:

- a). Pledge (real estate, fixed assets, current assets, receivables, securities, bank deposits, etc., in accordance with the laws of the pledge and mortgage);
- b) Guarantee, surety of the legal entity or natural person, guarantee issued by the Government;
- a) Providing a mixed assurance form, i.e. securing the loan with several types of assurance.

Forms of securing the loan obligations are determined in each case separately, taking into account the nature of the financed activities and financial condition of the borrower. To reduce the risk, the bank prefers to use few forms of securing the loan. In addition, each of those assurance forms should secure the entire amount of debt.

4. *Depending on the purpose of loans*, credits are divided into the following types:

- Agricultural loans /loans to the food industry - issued to finance the costs of agricultural production and food industry, including loans to farmers, loans for the cultivation and storage of the harvest, loans for the sale or storage of agricultural products by farmers, and loans for culturing, feeding or selling of livestock. This type of loans includes financing of fishing and forestry, loans to farmers for the purchase of inventory and equipment, loans to cover costs of running a farm, etc.

- Loans for construction and land development – loans granted for the construction (construction, reconstruction, demolition) of buildings or residential property, industrial and commercial enterprises, farms, hotels, churches, charitable institutions, recreational areas, etc. This type of loans also includes credits for acquisition and landscaping of land, including improvements of the land quality;

- Consumer loans - issued to individuals for household and personal expenses (purchase of real estate and other immovable property, acquisition of both personal and commercial vehicles, household appliances, furniture, home improvement and reconstruction, expenses on education and health care, vacation expenses, payment of overdrafts, etc.);

- Fuel and energy credits - issued to companies on manufacture, import, export, transportation, distribution, storage and sale of energy in any form (electricity, coal, oil and other fuels), and loans issued to petrol stations;

- Loans to banks – credits issued to other banks;

- Loans to the Government – these credits are granted to the Government for various purposes. It includes loans issued in accordance with applicable law for administrative - territorial units and their subordinate agencies;

- Industrial and commercial loans - issued for industrial or commercial objectives to individual enterprises, associations, corporations and other businesses, as well as for communication enterprises, commerce and service organizations, hospitals, consulting firms and other borrowers, regardless of their organizational and legal forms;

- Loans on real estate - issued for businesses and individuals on acquisition of real estate. These loans are provided for the purchase of houses, land property, and residential areas.

- Loans for transportation and construction of roads - issued to build roads and develop different areas of transportation, enhancing infrastructure of transport.

### **Principles for Establishment of Interest Rate**

Interest rate is one of the most important marketing tools in banking sector. Bank tries to set it in the way to keep maximum profits and attract new customers.

One of the Bank's general strategies is to maintain a position which is:

- Flexible and resilient to anticipated changes in interest rates and inflation,
- directed towards preventing an excess of the average cost of resources of the bank used for granting a credit above the average interest rate on loans.
- Focused on stabilizing and increasing the net interest income of the bank.

The key of successful interest rate policy lies in the correct dealing with the interest rate risk, which, in turn, is defined by:

- The sensitivity of bank assets and liabilities to changes in interest rates;
- Balance between the assets and liabilities which are sensitive to changes in interest rates.

The Bank is constantly monitoring and managing the interest rate risk in order to avoid losses from the lending operations of the bank, to minimize interest rate risk, while maintaining optimal profitability and adequate liquidity for the bank.

In order to comply with the bank's policy and achieve the desired results in determination of interest rates the following factors are taken into consideration:

- Actual cost of raising funds;
- The degree of risk from issuing the loan and interest rate risk;
- The cost of processing the loan and its monitoring (analysis of the borrower's creditworthiness, costs associated with control, implementation, etc.);
- Rates of refinancing of National Bank of Moldova and the range of rates offered by other banks of the country for the same purposes;
- Term of the loan;
- The relationship between the bank and the borrower (Credit history, liability, etc.);

- The rate of profit, which may be obtained by investing in other assets.
- The importance of this entity for the bank;
- External factors (inflation expectations, the level of the average market rate for similar loans, the risk of a specific borrower).

It often happens that the entity is failing to keep up with the conditions of issuing of a credit. For those cases the bank may revise the interest rate and change it (apply the floating interest rate). But it can't be applied for the lending of short periods.

## **My Tasks and Responsibilities as a Trainee**

During my internship I worked at a credit department under the supervision of the head of credit department, Cristina Manoil. Work of the credit department didn't require any communication with other department, so my collaboration at work was limited to the credit department employees, director of our branch and the clients.

First few weeks of my internship I worked over the analysis of the credit applications, I was also working with different documentation required for processing with the credit application and issuing a loan. When we had a big project for almost a month, where I had to prepare a business plan for one of the clients and make a financial analysis. For the rest of my internship I was working over monitoring of the credit use and classification of credits. Now I would like to go in detail on the tasks I've performed during my employment.

### **Analysis of credit applications**

During first few weeks of my internship I did the analysis of the credit applications. My general aim was to get an idea about each document in the credit application so that I could participate in the working process as a regular employee.

I went through the following documents (required to apply for a loan):

1. An application for a loan,
2. Foundation agreement,
3. Certificate of state registration and the assignment of the fiscal code,
4. Extract from the Commercial Register (issued by Registration Chamber of the Ministry of Justice).
5. Approval of the authorized managing body (board, general meeting etc.) for the loan application and the provision of collateral.
6. Letter of appointment of directors.

7. Financial statements (balance sheet, income statement, cash flow statement),
8. A brief description of the enterprise, its products and services, marketing strategy, production plan,
9. Financial forecast of the balance sheet, income statement and cash flow statement,
10. Contracts with suppliers on purchases related to credited event,
11. Description of collateral (pledged property, inventory, mortgage, guarantee etc.),
12. Assessment of the pledge, made by an independent expert organization,
13. ID (internal passport) of director and chief accountant of the company (the Borrower).

### ***Modification of Credit***

In some cases, on a request of the Borrower, it is allowed to change the credit agreement's details (interest rate, terms of payment of interest, maturity, credit etc.). Depending on the financial situation of the client, if the client is facing problems with repayments, bank may renegotiate the interest rates and decrease it. Bank may also decrease the credit repayment amount by prolonging the terms of credit. During my internship we had few clients prolonging their credits. In order to process credit prolongation, we were requesting the following documents from the client:

- Application for extension. In this application, besides regular information, client also had to list the reasons of untimely payments to the Bank, as well as provide the bank with the new terms for repayments.
- Indicating the collateral (same/not same);
- Documents confirming the objectivity of the reasons of temporary financial difficulties faced by Borrower, as well as the measures taken to ensure repayment of debts to the bank with respect to the schedule;
- The client's responsibility is to acknowledge the bank of all changes in contracts with suppliers.

Once we were getting all documents, we could proceed with the application, and analyze the financial situation of the Borrower as well as his credit situation. If financial and credit situation was acceptable for prolongation, bank had to make sure that the pledged property is in suitable condition, and declared price of property corresponds to the market price. If proposed collateral wasn't covering total value of debt and the interest, the client was required to provide some extra form of securing the loan.

There are some other general rules for prolonging the credit, which we had to obey:

- Extension of credit is usually performed if there is no unpaid interest;
- Extension, as well as another update of the loan contract, is executed as an additional agreement, which stipulates the fees/commissions and increase in the interest rate.

The procedure for approving decisions on the extension of credit terms is similar to a regular credit approval. If you prolong the loan period, regardless of the terms of credit, loan remains in its original status: short-term or medium-term.

### **Business plan and financial analysis**

Writing business plan and financial analysis was one of my first tasks at Banca Sociala. Even though it was a good experience, it wasn't the responsibility of the bank to do the plan and the analysis. Each branch of Banca Sociala has an established 'norm' – the minimal value of lent money. One of our clients, Covali&Co, makes around 70% of this norm. This client is considered as a VIP client, he always has discounts on exchange rates and on interest rates. Banca Sociala is cooperating with the World Bank. WB is providing credits through our bank with low interest rate. That client has requested a credit from resources of World Bank, and among requested documents there are business plan and full financial analysis of the company. The client simply refused to do that, and our management, being afraid of losing this customer, shifted this task to the credit department.

I have completed the followings:

- Full analysis of the competitive environment (Porter's five forces analysis),
- Analysis of the market and of the market share,
- SWOT analysis,
- Financial analysis: Liquidity,  
Profitability,  
Solvency,  
Debt ratios analysis,  
Operating performance ratios.

During that work, knowledge acquired at ESC Grenoble was very useful.

### **Credit Monitoring**

Credit monitoring was one of my main tasks during internship at Banca Sociala. In the bank, credit monitoring was divided into current monitoring, control over the targeted use of credit, and control over the condition of a pledged property. Now I would like to go into details on each of these tasks.

#### ***a). Current monitoring***

Within current monitoring our department was doing general monitoring of the loan, monitoring of credit repayment, and development and adoption of arrangements to fulfill these tasks.

The Bank must be sure that the customer complies with the loan contract and implements his/her obligations. Bank also controls the use of credit, and timely and full repayment of the loan. In order to do this, I, as a credit department employee, had to make a review on the client's business; to analyze what changes happened in the client's enterprise. I also had to make the analysis of the client's financial situation (based on the ratio analysis). Other tasks implemented by our team in current loan monitoring were analysis of client's, cash flow, receivables, payables, balance as a whole, and income statement. Sometimes my team was conducting on-site verification of cash and accounting documents, accounting transactions, the availability and safety of the mortgaged property, the reliability of reports. These checks were



carried out at least once in a year, and more frequently, when required. For the current monitoring, our team was using all kinds of financial and other information received from the Borrower as well as from other sources.

One of the duties of my team was to collect information relevant to assessing the creditworthiness of the client. We also were analyzing this information in order to synthesize it for the future use, because the degree of certainty of the Bank that the Borrower is able and willing to repay the loan in accordance with the terms and conditions of the loan agreement is highly dependent on that information.

While analyzing the balance sheet, its annexes and other statistical reporting, we, as a credit department, tried to find answers for the following questions:

- If the overall financial position of the Borrower is stable, unstable or mean. In fact, a lot of attention was paid to the analysis of financial situation of the Borrower, because it is very important during the whole monitoring process, and it is the base for the classification of loans and determining the necessary value for the risk fund.
- If the client will be able to pay interest and repay the loan at required payment terms;
- Whether the collateral is sufficient to ensure the full coverage of the loan value. If it is not, our team was claiming other additional forms to secure the credit.
- How realistic are enterprise's balance sheet and other financial statements.

In order to get information on creditworthiness we conducted interviews with the Borrower, on-site inspections, etc.

The whole package of documents received during processing of a credit application was systemized by a member of our team and stored in a special folder of that particular client; all the documents were stored in a special order, with respect to the bank regulations on the order of documents in a credit application.

Our team was verifying if the Borrower complied with the terms of his/her own participation in the event credited. Data about their own participation (at least 10-20% of the financed activities) must be specified in the application for requesting the loan, as well as in the business plan. The credit file must contain the documents confirming that the Borrower has fulfilled its obligations of own participation in the event credited.

Throughout the whole period of crediting, our team, on a daily basis, was monitoring cash inflow of all Borrowers' accounts to ensure timely repayment of the loan. Also credit department was systematically making a record on each telephone conversation made and on meetings with each client (with respect to the appendix № 13 of the bank regulations).

Another task related to current monitoring I used to perform during my internship, was to control if client's prognosis on the performance of the credited event complies with the real financial situation of the Borrower. To conduct monitoring there were required financial balance and other sheets, so, with respect to the credit agreement, client of the Bank had to submit financial reports, and any other information about its financial position and economic activity, if requested by the credit officer in charge. All of the documents were submitted on a confidential basis. Upon receipt of the balance, we, as a credit department, were validating if the debt to the Bank is shown correctly in the balance sheet of the client. Afterwards we were analyzing solvency of the Borrower in order to get an idea on how has the customer's financial position changed, and, where necessary, were reacting with respect to the real situation.

Another task me and my supervisor used to do was monitoring for any changes in the ownership structure, top management and in status of the Borrower.

In case when the Borrower didn't fulfill his obligations of the credit agreement or in a situation when the Borrower provided us with false financial sheets and statements, our department, in accordance with the terms of the loan agreement, was suspending further disbursement of loan. Together with the disbursement, bank is able to surcharge the remaining debt immediately

through the court, increase the interest rate on remaining part of the loan or apply other measures according to the loan agreement and legislation; however, those measures are applied rarely.

***b). Monitoring the credit use***

Monitoring of the credit use was one of the tasks I used to perform during my internship. It is required in order to check if the client is using borrowed money with respect to the purpose the loan was granted for. It is a general procedure for all banks in Moldova, established by the National Bank in Moldova. Once in three months Bank is obliged to provide National Bank of Moldova with the credit use analysis of any client (upon request on NBM).

In order to conduct the monitoring of the credit use, Borrower must provide the credit department with detailed explanation of intended use of the loan. It is done before credit application is processed. During the application process the Borrower also submits all the contracts with suppliers, which confirm the proper use of credit.

Once all of those documents are submitted and the credit is issued, the following up control is on-site verification of the documents confirming that the deal (among borrower and his supplier) really took place; these documents are transportation and tax papers, card of stock control which shows the movement of commodities, acts on performed work and others in accordance with signed agreements.

After revising all the following documents I was preparing a document with the details of all verified papers (mainly tax invoices). It is important that the amount of money transferred to some specific supplier won't exceed the value on the tax invoice. Simultaneously it is necessary to evaluate the performance of the financed activities and therefore the prospects for repayment of the loan.

In case of detection of misuse of credit, credit department was starting early recovery of the loan, if necessary, using the collateral or other forms of assurance, mentioned in the credit agreement. Borrower may be also subject to penalties perjured in the contract, but generally no one is getting penalized.

### ***c). Control Over the Pledged Property***

Another task that was partially in my responsibility during my internship was control over the pledged property.

Credit department, during the whole crediting period, is obliged to systematically monitor the availability and condition of accepted forms of assuring the loan. At the same time it is important to make sure that the collateral didn't lose its value and may cover the loan and the interest rate in case if Borrower won't be able to repay his debt.

Taking into account probable risk (of falling prices, declining liquidity, etc.) the value of the form used to secure the credit should exceed the amount of loans and interest (in accordance with the standards set in Chapter 3, p. II of the bank regulations). Total value of collateral shouldn't be less than 130% of remaining loan and interest.

When collateral value wasn't enough to secure the loan and the interest, we, as a credit department, with respect to the credit agreement, were asking the Borrower to cover the unsecured value of loan, or to provide us with other property guarantees, like pledging other assets, providing individual warranty (guarantee) or other guarantees that are used in banking practice.

During prolongation of the terms of credit it is mandatory to analyze the form of assuring the loan, and make sure that value of collateral/guarantee is enough to cover extra interest rate coming with the extended period of the loan.

Depending on the form of securing the loan, our department had to consider the followings:

1. If the loan is secured by a guarantee provided by a legal entity, solvency of the guarantor should be checked on a quarterly basis. In order to do that, that accounting body should provide the credit department with the balance sheet, income statement and other financial data. If the guarantee is provided by a natural person, that person should submit to the credit department the information of his/her average earnings of the guarantor, and the information

about all financial means the guarantor is controlling (owns). In the case of worsening of economic and financial situation of a guarantor, we, as a credit department, were asking the Borrower to provide us with additional forms of securing the loan value. If the client didn't do so, we would proceed to early repayment of the loan, bearing in mind the financial condition and cash flows of the Borrower.

2. If the loan is secured by a pledge, in addition to analyzing the pledged property before granting the credit, it is necessary to carry out further checks on the value of collateral periodically. On-site verification of mortgage value is also mandatory during the extension of a credit. It is important to consider liquidity issues while calculating the value of the pledged property, and recalculate it all the time when conducting controls on the collateral. Value of pledge is revised with respect to given tendency of emerging real estate prices and real demand for it.

For the entire crediting period it is mandatory to control if the property rights over the mortgaged assets didn't change.

3. If the loan is secured by the assets (generally, current assets) of the enterprise, it is important to ensure that the incoming revenues from the sale of mortgaged goods (if using raw materials for production purposes – then finished product in the appropriate amount) are directed to repay the loan.

In order to find out the value of a pledged property, first, I conducted the on-site control. It was important to come up with some general description of the property. Then I was checking out newspapers, internet sources and real estate agencies on the prices of similar property. With respect to the market given, it was hard to find the exact price of the property, so I had to find some average approximate value.

### **Loan Classification and Allowance for Loan Losses**

During my internship at credit department I was also classifying loans in order to calculate allowance on those loans for the fund of risk. The classification of loans and contingent liabilities is carried out to assess the credit risk and

therefore the formation of allowances of appropriate value for the loss to provide liquidity, protect bank's shareholders and customers. Credit risk - is the risk of loss by a bank or other crediting institution due to late or incomplete fulfillment of financial obligations to the crediting institution in accordance with the terms of the contract. Since each credit has the risk of being unpaid, the Bank is having a fund of risk for the credits that won't be repaid. With each new credit bank is increasing its risk fund on some particular value. That value depends on several factors, and will be discussed later. This classification is carried out with respect to regulations on the classification of assets and contingent liabilities and the formation of allowances for asset losses and provisions for losses on contingent liabilities, approved by the National Bank of Moldova.

Our team had to calculate allowance for losses for the followings:

- a). On all loans (including credit cards, financing of commercial transactions, REPO agreements, guarantees from banks etc.);
- b). For the following contingent liabilities:
  - issued letters of credit and guarantees,
  - Obligations of giving the credit in the future.

Interest on loans, commissions and other income on loans and contingent liabilities are not supposed to be classified and allowance on those for the fund of risk is not formed.

Credit risk is assessed upon issuance of loans when these loans appear on respective balance sheets. Revision of risk is conducted no less than once in a quarter. Allowances for losses are calculated on a monthly basis in an amount not less than the calculated amount of the last reporting date.

Minimum required amount of allowances for losses on loans and contingent liabilities of the bank is based on the classification of loans and contingent liabilities. If loan or contingent liability is secured by the: government securities issued by the Ministry of Finance of RM, securities issued by National Bank of Moldova or other guarantees issued by the government of

Moldova, the value of loan/contingent liability for calculating allowance on losses for fund of risk is decreased by the value of those guarantees. After determining the value of loans and contingent liabilities, subject to adjustments just mentioned, credit department was assessing the risk of each loan / liability and allocating the loan/liability into one of the following categories:

Group A – ‘Standard loan’ - a loan issued to Borrowers with strong financial position and high rating of solvency, adequate cash flow. There is no doubt in the timely return of issued loans and the payment of accrued interest on it. The Borrower complies with all conditions of the loan agreement, has a reliable guarantee of the loan and can present an effective business plan, which brings profits.

Group B - Credit ‘Under the Supervision’ - loan issued for a Borrower with a good financial situation, but some aspects of that financial situation or form of securing the credit is raising some doubts. For example, during the crediting period there has been deterioration in some indicators of economic and financial activity of a credited company: equity and working capital, financial ratios, financial results, etc., or delayed payments to suppliers. If the Borrower was late from 1 to 60 days with credit repayment, he is automatically allocated at group B. Another reason for fitting the customer into group B may be raising doubts that the adopted form of security can guarantee the timely repayment of the loan and interest thereon.

If the debts of the Borrower on his balance sheet exceed the net worth 8 times, that loan/contingent liability is allocated to the group B, even though the client is repaying the loan and interest timely, without any delay.

Loans "under supervision» were under careful attention of the credit department, so that the bank could take urgent measures to address the problems, in order to prevent further deterioration of credit quality and growth of its risk.

Group C - The ‘Sub-prime’ credit - loan provided to the Borrower, whose financial situation or collateral condition is worsening, and therefore increases

the risk of losses on it. Factors showing that the loan has to be allocated in group C are as follows:

- Reduction of cash flows;
- A significant increase in accounts payable and receivable for goods and services, Social Fund payments and others;
- Lack of real buyers for products, lack of contracts;
- The Borrower violates the terms of credit agreement between him and the bank,
- The size and liquidity of the accepted forms of ensuring the repayment are insufficient.

As a result, the Borrower is working with insufficient capital, losses; financial ratios are below the acceptable level.

Loan is classified not lower than the sub-prime (regardless of the financial situation of the Borrower) if it was issued under the unconditional and irrevocable guarantee of the state.

Loan is classified not higher than the sub-prime if:

- The Borrower didn't make any credit repayments for more than 60 days,
- Overdue payment for more than 30 days for credit which was overdue and then was recovered.

Loans classified as "substandard" are under close attention of the head of the credit department, head of our branch and specialists from the main crediting division at headquarters.

Group D – 'Doubtful / Problematic' credit - a loan to a Borrower whose financial situation was very weak at the time of reporting.

The signs that the client might belong to group D are as follows:

- The activities of the Borrower are loss-making,
- Short-term liabilities are not covered by short-term assets,
- Working capital is diverted to cover expenses unrelated to turnover,



- Borrower is failing to cover expenses on raw materials, social fund and others.
- Terms of credit agreement are violated,
- Preservation of collateral is not ensured, its quality and liquidity is deteriorating.
- Bank is not receiving any financial statements from the Borrower, or received statements turn to be false.

Loans at group D create a real threat that in order to collect the debt the bank will have to apply to legal forces. Repayment of the loan in full at this moment in time is unlikely. Adopted form of securing the loan lacks liquidity. The classification of such a loan as uncollectable is postponed until a more accurate determination of the status of the loan. However, there are objective factors that will ensure the return of debts to the bank in the future. Loans at group D have the collateral value which is enough to meet the expenses of the bank.

Loans classified as "doubtful" are controlled directly by the Department of Legal Relations and Problematic Loans. That department is coordinating the work of other services in order to get that credit reimbursed.

Group E – 'Uncollectable' credit - at the time of classification the Borrower does not have a real opportunity to repay the loan. However, the bank continues to recover the debt through the courts and other authorities. The business activities of the Borrower are at a loss for a long time, there is no chance to collect account receivables. There is no income to the bank account of a client. All the legal steps to collect the debt are already taken.

Once the credit was allocated to the group E, it doesn't mean that the department of legal relations and problematic loans stops any work related to the credit. That department still works on the collection of that debt through the courts, law enforcement, as well as through other legal action even though it doesn't seem that real.

In case than the loan / contingent liability may be classified in different ways, and, as a result, in different groups, it should be attributed to the lower group

to prevent any chance of unexpected risks. Modification of the loan in order to avoid adverse classification is not allowed.

Most common loans like consumer loans of up to 30 thousand MDL, and loans to small and medium enterprises of up to 75 thousand MDL, which are not secured by a pledge or other form of security, and whose repayment is based only on the Borrower's liabilities shall be classified as follows:

(1). If the repayment on the loan is carried out at least once a month:

- If the Borrower was late with the payment for up to 30 days, the loan shall be classified no higher than 'under observation';
- If the Borrower was late with the payment from 31 to 60 days, the loan shall be classified no higher than the 'sub-prime';
- If the Borrower was late with payments from 61 to 90 days, the loan shall be classified no higher than 'doubtful';
- If the Borrower was late with the payment for more than 90 days, the loan shall be classified no higher than 'uncollectable'.

(2). If the repayment on the loan is conducted less frequently than once a month, those loans are classified one category lower when the loans described in paragraph (1), with the exception of loans already classified in the category of 'uncollectable'.

Prolonged or renegotiated credit is classified in a different manner. Depending on different conditions, classification may change for any loan or contingent liability. For example, if bank sold a contingent liability to a third party, it is classified no higher than subprime.

*The required amount of funds to be reserved for unpaid loans and contingent liabilities are as follows:*

- 1). For the group A - the group with the lowest risk, called 'Standard', the value of 2% of remaining amount of credit/liability has to be transferred to fund of risk,
- 2). The group B, or credits 'Under Supervision' require the reservation of 5% of the value of remaining credit/liability for the fund of risk,

- 3). For the group C, or 'Subprime' credits, 30% of the value of remaining credit/liability must be transferred to the fund of risk,
- 4). 'Doubtful /Problematic' loans - 60% of remaining loan/liability to the fund of risk,
- 5). 'Uncollectable' loans - 100% of remaining loan/liability to the fund of risk.

### **How useful was I to the company?**

While working at a bank I had a chance to apply my theoretical knowledge, acquired during studies at Grenoble Ecole de Management, into real business. I believe that my knowledge in financial analysis was very useful for the bank. I was able to quickly and effectively analyze financial situation of a client.

During my studies at ESC Grenoble I developed my communication skills, my teamwork and interpersonal skills as well as strong work ethic. These qualities were very useful at my internship, and I managed to develop it further.

Most of the bank's employees, including the director of our branch, were people around 50. They were using old-fashioned approaches to the business and bank's clients, the approaches that were applied in banking system in Soviet Union. I tried my best to share with my colleagues some new insights on work with clients and other strategic issues.

While working on the credit monitoring I have undertaken significant part of work and have developed an excel spreadsheet for the analysis of credit use. I have to mention that most of the similar data were written out manually.

Even though writing a business plan and financial analysis don't fall within credit department responsibilities, I was entitled for an assignment that implied preparation of business plan and financial analysis of a particular company that aimed to obtain some credit line from the resources of the World Bank. The company has got a credit line from the World Bank in the end.

### **What did I get from the company?**

During the 4 months of my internship in Banca Sociala I was cooperating not only with the regular employees, but also with the head of credit department, who was my internship supervisor. It allowed going through the tasks done by the regular employees and work shadowing the head of the department. I had the possibility to see all the chain of granting a credit, starting from first visit of the potential customer and assistance in preparation while preparing documents for application, to the application process along with granting of credit and further monitoring of the loan usage and final repayment of the loan.

I especially appreciated the possibility to ask questions to the head of a department whenever I've had any. I believe that opportunity to take a look on business from the manager point of view is very important for a trainee.

I had the opportunity to improve my communication skills. I was personally engaged in negotiations with customers, and I often had a chance to see how my manager was conducting negotiations with the customers, especially negotiations related to problematic loans.

I've learnt the details of Banca Sociala's credit policy, which is relevant for the most of Moldavian banks. I have been also involved in the analyses of how marketing policy is formed in banking industry and what are the best directions to be implemented, what are its strategic aspects, how bank is promoting and selling its services. At the bank I was able to draw an image about developing industries in Moldova and about general economic situation in the country.

## **Conclusion**

I strongly believe that my personal goal was achieved. I've had a chance to apply my theoretical knowledge into real business. I managed to bring new initiatives that have been happily accepted by the Bank's employees as they reduced the workload significantly. I have widened the knowledge of credit tools and improved understanding of credit policy in the banking industry that has been always very attractive to me. I've tried myself in different roles and I have been never scared of challenging tasks and interactions with clients. I was lucky to be assigned for the project that required complex skills and quite good understanding of the balance between customer needs and its capacity, when applying for a loan from the resources of the World Bank. Furthermore, I have developed a tool that ensures providing proper and timely recommendations regarding credit repayment plan to the potential customers. These calculations were previously requested from the central office in the capital of Moldova, Chisinau, and implied lower level of services provided to the customers as it was time consuming. Due to daily interactions with the clients together with the credit department employees, I have developed my interpersonal, communication and teamwork skills attained at GEM.

Since I've went to the high school till now I was dreaming about a career in banking industry. I believe my internship was very effective simply because now I can understand whether career in this sector or in financial sector as a whole is desirable for me as my career path.

## **Resources**

1. CB 'Banca Sociala' JSC General Code;
2. CB 'Banca Sociala' JSC Lending Code;
3. CB 'Banca Sociala' website: <http://www.socbank.md/ru>