

Regulatory Impact Assessment

- Main Findings and Policy Recommendations -

Regulation

“On Credit Risk Administration”

Proposing Authority
Bank of Albania

Tirana
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Working Group Composition

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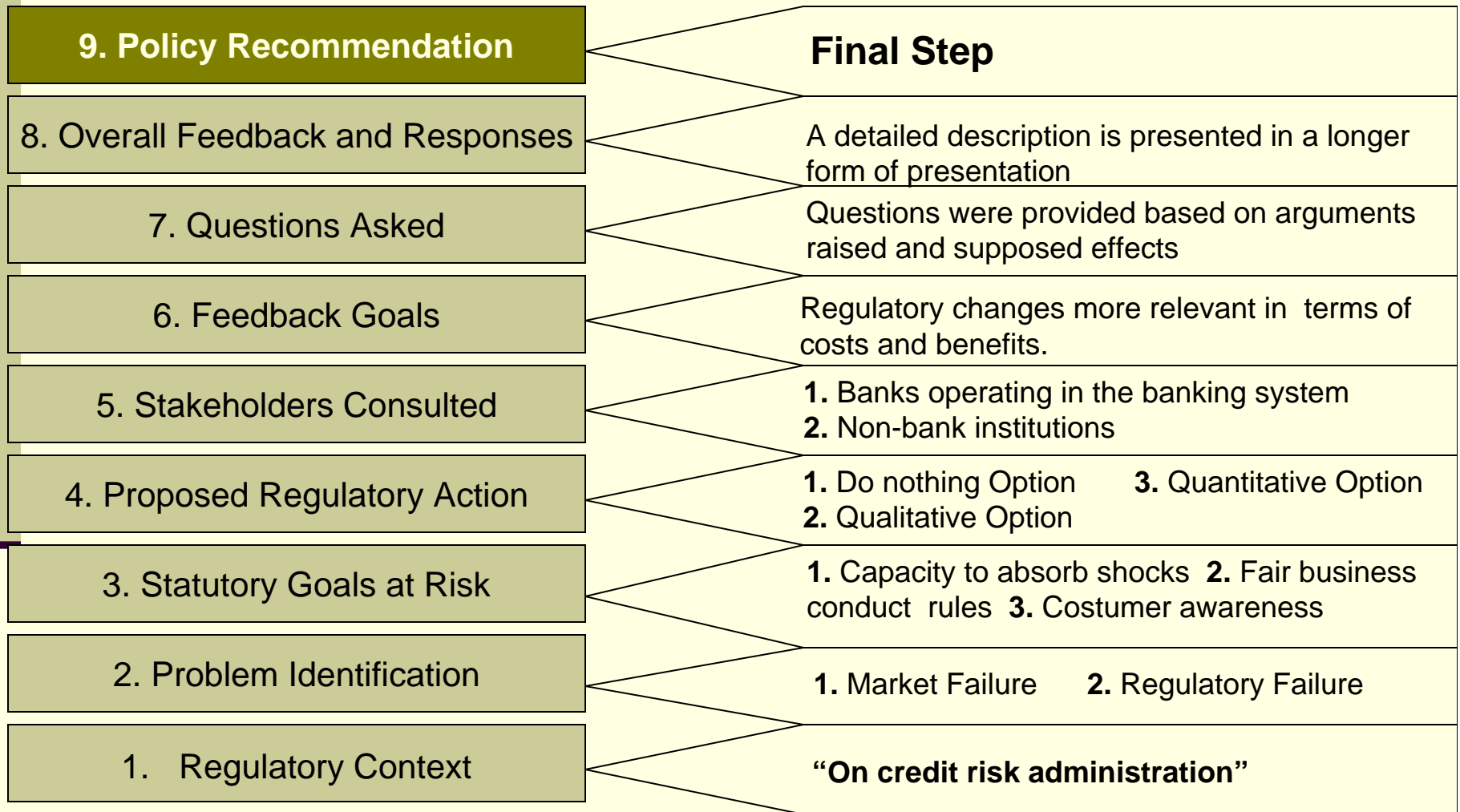
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Impact Assessment Process



Main Findings Overview



1. Regulatory Context

Regulation “ On Credit Risk Administration”.

- It is aimed at improving requirements for reducing credit risk exposures, especially to foreign currency loans issued to unhedged customers.
- Other regulations or guidelines might be identified for further improvement in respect to the identified issue.



2. Problem Identification

Credit expansion has raised concerns over specific risks issue. Our focus is especially on foreign currency loans provided to unhedged customers. At the end of 2007, credit to unhedged customers over total portfolio is at 44.5%. The risks of foreign exchange rate fluctuation especially of American currency the last years is a matter of unease which needs intervention.

The problem addresses the following:

Market Failure

1. Asymmetric Information
 - between stakeholders
2. Negative External Factors
 - explanation

Regulatory Failure

In the past we have had weaknesses in regulatory enforcement regarding transparency issues; as well as the absence of regulatory requirements regarding the creation of specific structures for product design and monitoring.

3. Statutory Goals

Statutory Goals at risk:

Capacity to absorb shocks
(loan portfolio quality)

Fair business conduct rules

Customer awareness

4. Proposed Regulatory Actions

1. “Do nothing” option

We considered the effects to the 3 goals stated.

2. Qualitative Options

- *Establishment of a special unit for risk management and economic analysis;*
- *Restricting rules for Board of Directors in order to secure an improved process of credit risk management and mitigation and setting of transparency prerequisites for minimum information provided to the customers.*

3. Quantitative Options

Limit growth of loans to unhedged customers

- *make each loan more expensive
(e.g. provisions, risk weighting)*
- *quantitative restrictions (e.g. install./income ratio)*
- *make loans beyond a threshold less feasible (e.g. % of reg. cap.)*

6. Feedback Goals

*Understanding how the proposed regulatory changes would impact the firms operating in the Albanian banking sector.
What is their overall opinion on the raised issue and what are their proposed actions.*

- Which are the costs related to possible regulatory changes and what is their impact on the firms activity and to the customers?
- What regulatory choices are more relevant in terms of costs and benefits?

9. Policy Recommendations

- WG suggests that both qualitative and quantitative options should be included in the regulatory change.
- It is essential for banks to have a unit / function for risk management and economic analysis. We agree with the small banks which concern about the costs related to the implementation of this unit, but its size should match the bank's size and type of activity.
- Banks do all agree with the fact that more transparency requirements are needed.
- 5% of increased provisions for each category for new loans to unhedged costumers will increase the interest rate for this type of loans at least of 4% (if all costs are passed to costumers). This raises the comparability of loans in foreign currency and local currency.
- Some of the banks are near the limit of 400% of regulatory capital (loans in foreign currency to unhedged costumers/regulatory capital). This limit will discourage banks to raise the amount of loans in foreign currency to unhedged costumers or will encourage them to raise the capital. In both cases the systems' stability benefits.



THANK YOU