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Romania: new consumer finance limits

On 31 July 2008, the public consultation period concerning a new draft regulation initiated by the National Bank of Romania (NBR) for limiting consumer credit-related risks has lapsed.

The draft seems to emerge from NBR's efforts to slow down the rapid growth of retail credit, after a first measure (i.e. the increase of the reference interest) proved ineffective.

In fact, despite the reference interest rate increase, in July 2008, credit retail volumes grew by 77% over the last twelve months. Recent statistics actually place Romania on top of European retail credit in the mortgage sector, with consumer credit accounting for more of GDP than the average of European Union member states. Bad debts also kept up a growing pace in the retail sector.

Despite NBR's concerns, the draft regulation raised vivid criticism from banks, whose targets for increased revenues out of retail credits will be significantly impacted by the expected decrease of the number of clients meeting the more restrictive lending conditions.

As such, among other conditions provided for in the draft regulation, banks will be required to compute the solvency of retail clients based on permanent revenues, and up to the level recorded in the previous year's tax return plus a maximum increase of 20%. Accordingly, evidence of revenues consisting of an employer's statement confirming the salary level shall not suffice any more for retail loans.

Also with a view to assessing the insolvency risks of retail clients, banks will be required to conduct a stress test using the highest interest rate or exchange rate or commission level over the previous 18 months. However, the effects of this condition were questionable, since the banks would only account for past interest rates, while future fluctuations would not be factored in (thus leaving a room for banks to actually increase the credit costs on the retail sector).

As a result of its consultations with stakeholders, NBR signalled a potential compromise: the stress test requirement could be transformed into a client category risk test which will be done for different categories of retail clients (depending on their range of revenues), rather than to each individual client, while banks will be allowed to have their own set of risk matrices.

Previously, via enactment of Regulation no. 3/2007 on limitation of retail credit risk, NBR created the conditions for consumer finance relaxation, by removing the requirement to provide credit security or a down-payment of at least 25% of the loan value, as well as the tight eligibility limits (i.e. monthly payment commitments respectively of up to 30% of the net family income, in case of regular consumer finance, and 35% in case of mortgage-backed loans).

As a result, currently, most banks work on the basis of 70% as the maximum admissible debt-to-equity ratio of retail clients, and with no down-payment requirement. These conditions would be changed as a result of the draft regulation, at least on what concerns less-used currencies, bankers estimating a decrease of 10 to 20% in the volume of credit granted to retail clients.

As per recent NBR statements, the draft regulation could be approved by the NBR Board in the upcoming two weeks and enforced as soon as 45 days thereafter.

A clearer assessment as to whether the new rules will work as a remedy (as sought by the NBR) and not as an impediment (as alleged by banks) should be possible rather quickly. ■

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