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**Increasing consumer loan transparency.
The role of the annual percentage rate of charge**

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About the German Economic Team Moldova

The German Economic Team Moldova (GET Moldova) advises the Moldovan government and other Moldovan state authorities such as the National Bank on a wide range of economic policy issues. Our analytical work is presented and discussed during regular meetings with high-level decision makers. GET Moldova is financed by the German Federal Ministry of Economics and Energy. Our publications are publicly available at our website (www.get-moldova.de).

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Increasing consumer loan transparency – the role of the annual percentage rate of charge

Executive Summary

Transparency in advertising of consumer loans is not only important for consumer protection reasons, but also for the stability of the financial sector. The average percentage rate of charge (APR) is, in this regard, a highly useful tool as it includes all the costs of a credit and expresses them in a single number, thus makes different loan offers easily comparable for borrowers. In this policy paper we analyse the transparency situation in the Moldovan consumer credit market with a focus on appropriate use of the APR in advertising.

As a benchmark to the situation in Moldova we use two EU member states – Germany and Austria. The comparison is possible because the regulation of consumer credit advertisement in all three countries is based on the same EU Directive 2008/48/EC. It was created to align the regulation in the EU in order to increase consumer protection and create a level playing field. It serves as minimum, which all EU member states and Moldova have to fulfil.

The analysis of the German regulation shows: In addition to the requirement of the Directive, Germany has formulated provisions which go far beyond the standards of the EU Directive. As a result the practical implementation of advertising consumer loans in Germany is very transparent. In particular the competition is focusing on the APR. The APR is mostly shown in first place in advertising, which makes it easy to assess the cost of the credit and compare credit agreements.

In Austria the regulation is very close to the EU Directive and no additional provisions for consumer loans advertising are made. The practice of advertising consumer loans is different from Germany, there is not such a strong focus on the APR. It has to be shown in advertisement but it is often hidden in small print. Therefore, it tends to be harder for consumers to assess the cost of a credit and to compare loans offers.

The analysis of the regulation in Moldova shows a picture close to the regulation in Austria. The requirements of the Directive are fulfilled but there are no substantial further requirements. The analysis of practical implementation shows that the transparency is far from ideal. First there is not much of a focus on the APR. We also find that it is used in a misleading way or is missing completely, which is against the law. Therefore, in Moldova we see not only a relatively weak regulation – compared to Germany - but also a weak supervision. What makes matters worse is that the consumer loans segment is growing very fast and has reached an amount, which, in connection with non-transparent lending, could pose a potential risk for financial stability.

To increase transparency in consumer lending we see a need to tighten the regulation. Based on the German experience we suggest to include the following provisions into the regulation:

- every communication concerning advertisement shall be fair, clear and not misleading
- formulations are not allowed which lead to wrong expectations regarding costs of the credit
- show the APR at least as prominent as any other rate
- APR should be stated immediately before or after the nominal interest rate

But a stricter regulation can be only one part on the way to more transparent consumer lending. The government also needs to strengthen capacities for supervision of consumer lending.

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1 Introduction

In the recent years the types of credit offered to consumers evolved strongly and they continue to develop. As a result of this development, it has become increasingly difficult for consumers to understand and assess the cost of credits. For consumer protection, for fair competition and also for long-term financial stability it is necessary to make the lending process and the costs of the credit as transparent as possible. In particular, the borrowers should be able to compare the cost of credits in a simple way without much economic background.

A widely used instrument to compare different loan offers is the **annual percentage rate of charge (APR)**. The APR is a standardised and legally defined term that includes all the costs of the credit and expresses them as annual interest rate of the amount of the credit. These costs include the nominal interest rate of the credit, commissions, taxes and any other fees connected to the credit known to the lender. The big advantage of APR is that using this concept all the credit offers become easily comparable for the borrower, independent of the value and time period of the credit.

The Research question of this analysis is to find out, whether the APR is used appropriately in Moldova to ensure consumer protection, fair competition and financial stability.

Before looking at the specific situation in Moldova, we first take a look at the use of the APR in some EU member states – namely Germany and Austria. These two countries had to implement the EU Directive that defines standards in consumer lending regulation just like Moldova.

2 Experience in EU member countries

2.1 EU regulation on consumer loan transparency

Consumer credit agreements are regulated on EU-level by Directive 2008/48/EC. The rationale of the directive is to unify the laws and consumer protection mechanisms among the member countries. The goal is also to ensure sufficient consumer protection and consumer confidence in the EU as well as to stop distortions in competition based on different regulations.

According to this directive all EU countries have to fulfil certain minimum standards and to use the same definitions. These definitions e.g. state what costs need to be included in the APR calculation and what formula is used to calculate the APR. The directive also defines what information has to be included in advertisement for consumer loans, what information has to be provided to the consumer before the agreement (so called pre-contractual information) and what information has to be included in the agreement. The directive additionally provides standardised forms, which need to be used in the credit agreements and the pre-contractual information. Since 2010, all EU member states are obliged to fulfil these requirements of consumer loan transparency by transforming this regulation in national law.

For advertisements, the directive defines: Any advertising concerning credit agreements which indicates an interest rate or any figures relating to the cost of the credit to the consumer shall include standard information. The standard information shall specify in a clear, concise and prominent way by means of a representative example:

- the borrowing rate (nominal interest rate), plus any additional charges included in the total cost
- the total amount of credit;
- the APR;
- the duration of the credit agreement;
- the total amount payable by the consumer;
- the amount of the instalments

We will now analyse how the directive was translated in national law for Germany and Austria and afterwards look at the practical implementation. For implementation analysis we will focus on advertisement as it is much more vivid and easier comparable as other information provided by lenders.

2.2 The case of Germany

2.2.1 Regulation in Germany

Just like all other member states Germany fully fulfils the requirements demanded by the Directive 2008/48/EC, this also applies to advertising. According to German law everyone who advertises credit agreements, interest rates or other numbers concerning the cost of a credit shall provide in clear, concise and prominent way the following standard information:

- the total amount of credit, plus any additional charges included in the total cost
- the nominal interest rate,
- the APR,
- the total amount payable by the consumer,
- the duration of the credit agreement,
- the amount of instalments

Additionally to this standard information the German regulation makes further requirements. These are in particular:

- every communication concerning advertisement shall be fair, clear and not misleading
- formulations which lead to wrong expectations regarding costs of the credit are not allowed
- the APR must be at least as stressed as any other rate

Finally, the German regulation also states that

- the advertisement has to include an example for the APR for which the lender expects that 2/3 of the contracts concluded on the basis of this advertising should have the advertised rate or a better one

The 2/3 clause is unique to Germany as far as we know and was included in the regulation after it was found that the often-advertised rates are of no practical relevance as almost no borrowers were able to get such favourable conditions. We evaluate it as very advanced as it demands from the lender to make assessments about what clients he will attract by advertisement.

Now we will look at practical examples from German consumer loans advertising.

2.2.2 Practical examples of advertisement in Germany

The first examples taken from the website of the Deutsche Bank.

Figure 1

Advertising example from Germany: Deutsche Bank

Nettodarlehensbetrag	8.000 EUR
Effektiver Jahreszins	3,99 %
Fester Sollzinssatz p. a.	3,92 %
Monatliche Rate	180,34 EUR
Laufzeit in Monaten / Anzahl Raten	48
Zu zahlender Gesamtbetrag	8.656,42 EUR

Der Zinssatz ist bonitätsabhängig. Darlehensgeber ist die Deutsche Bank Privat- und Geschäftskunden AG, Theodor-Heuss-Allee 72, 60486 Frankfurt am Main.

Standard-Konditionen: Nettodarlehensbetrag von 1.000 Euro bis 75.000 Euro; effektiver Jahreszins von 3,49% bis 7,49%; fester Sollzinssatz p.a. von 3,44% bis 7,24% ; Laufzeit von 12 bis 84 Monaten. Bonität vorausgesetzt.

Source: <https://www.deutsche-bank.de/pk/kredit/kredit-im-ueberblick/privatkredit.html>

Shown is the total amount of credit (8,000 EUR), the APR (“effektiver Jahreszins”: 3.99%), the nominal interest rate (3.92%), the amount per rate, the duration of the credit and the total amount to be paid by the consumer. Further below the identity of the lender is shown, the minimum and maximum amounts of the credit, the range of the APR and the nominal rates and the possible duration of the credit.

Interesting in this example is that the APR is stated before the nominal interest rate and that there is visual proximity between the rates. This does not result directly from regulation. It would also be possible to first state the nominal rate and the APR behind it. But the APR has to be in the same field of vision and at least as prominent as the nominal rate.

Another result from this example is the relatively high advertised APR. It is higher than the theoretically possible minimum rate (which is 3.49%). This follows from the German specific regulation that the advertised APR should be applicable to 2/3 of the consumers.

The second example from Germany is from comdirect which is an online bank and a subsidiary of the Commerzbank, one of the big banks in Germany.

Figure 2

Advertising example from Germany: Comdirect

Ein Blick - Alle Produkte ▾

Große Pläne, kleiner Zins:
Der comdirect Ratenkredit

Zum Kreditrechner

Ab **2,45%**
eff. Jahreszins

Nettodarlehensbetrag	Laufzeit
EUR 10.000	Monate 84 ▾

Monatsrate	134,80 EUR
Gesamtbetrag	11.322,40 EUR
Gebundener Sollzinssatz	3,59 % p. a.
Effektiver Jahreszins	3,65 % p. a.

Jetzt Wunschkredit abschließen

Source: <https://www.comdirect.de/kredit/ratenkredit.html#kreditrechner>

In this example the first and most prominent rate shown is the APR. Precisely it states “average percentage rate of charge starting from 2.45%”. So the main focus of the advertisement is again the APR. Below all other information requested by law is shown. Total amount of credit (10,000 EUR), the monthly rate, the total amount to be paid by the consumer, the nominal rate (3.59%) and the APR (3.65%). This APR is higher than above as the example has to fulfil the 2/3 principle mentioned in section 2.2.1.

We see again, the first rate that is used is the APR rate, not the nominal rate. It seems that the competition on consumer credit in Germany is focusing on the APR not on the nominal rate. This is not only the case in these examples but in all examples found from other banks and also from non-bank financial institutions. The APR is mostly shown before the nominal interest rate. If only one interest rate is shown, it is the APR. If nominal interest rate is shown, it is immediately followed by APR. Not only in advertisement are these two rates always standing one after the other. The difference between the nominal interest rate and the APR is quite small in Germany – a result of transparent advertising.

Result: In Germany competition focuses on the APR. There is high transparency and comparability for consumers. The APR is used appropriately. Additionally to the focus on the APR, Germany has the 2/3 rule that ensures that the advertised APR is also realistic.

2.3 The case of Austria

As in Germany, the regulation in Austria fulfils requirements of the EU Directive. The relevant law is in fact very close to the EU directive and the part concerning advertisement is almost identical to the text of the directive. Our focus is again the regulation of advertising and its implementation.

2.3.1 Regulation in Austria

According to Austrian law any advertising concerning credit agreements, interest rates or other numbers concerning the cost of a credit shall include standard information. This information shall be provided in clear, concise and prominent way by means of representative example. It must show:

- the nominal interest rate, plus any additional charges included in the total cost
- total amount of credit,
- the APR
- the duration of the credit agreement,
- the total amount payable by the consumer and the amount of instalments

In contrast to Germany, Austria has no additional provisions which go beyond the requirements defined by the directive.

2.3.2 Practical examples of advertisement in Austria

Now we will look on the practical examples of implementation of this regulation in Austria. The first example is from a branch of a big international bank specialised in retail lending.

Figure 3

Advertising example from Austria: Santander

The advertisement for Santander's 'JetztSofort Kredit' features a woman in a red plaid shirt and jeans standing on a log over a lake, with her arms raised. The text 'JetztSofort Kredit Vom Minus ins Plus' is prominently displayed. A 'Budgetrechner' (calculator) is overlaid on the right, showing a loan amount of € 8,000, a term of 60 months, and a monthly rate of € 143,84. The ad also includes icons for 'Schnelligkeit', 'Maßgeschneiderte Lösungen', 'Freier Verwendungszweck', and 'Zusätzliche Absicherungsmöglichkeiten'.

1) Sollzinssatz bonitätsabhängig ab 2,99 % p.a. (Sonderkondition gültig für Neukunden bei Onlineantrag); Repräsentatives Berechnungsbeispiel: 2,99 % p.a. Sollzinssatz 3,07 % Effektivzinssatz 3,07 %, Erhebungsgebühr, € 0,- Lohnvermerkgebühr, 0,00 % Bearbeitungsgebühr, € 0,00 monatliche Kontoführungsgebühr (bei Einziehungsauftrag), Laufzeit: 60 Monate, monatliche Rate: € 143,84, Gesamtkreditbetrag: € 8.000, zu zahlender Gesamtbetrag: € 8.630,40. Angebot gültig bis 31.03.2018. Erfüllung banküblicher Bonitätskriterien vorausgesetzt. Produktangaben: Laufzeit 24 - 120 Monate

Source: <https://www.santanderconsumer.at/>

First shown in this example is the total amount of the credit (8,000 EUR), the duration of the credit (60 month) and monthly rate (143.84 EUR). The other information regarding the cost of the credit is in the small print. Shown is the nominal interest rate, followed by the APR, different fees, which are all zero and again the duration of the credit, the monthly rate, the total amount of the credit, the total amount payable by the consumer and possible time periods.

This example differs from the German cases. Advertisement does not focus on the APR, it is hidden in the small print. For unaware consumers it is generally more difficult to find it and compare it to other offers if they do not know what to look for.

The next example is from an Austrian online bank.

Figure 4

Advertising example from Austria: Easybank

Bei einem Nettodarlehensbetrag von EUR 10.000,00 und einer Laufzeit von 84 Monaten erhalten Kunden der easybank AG einen Nominalzinssatz in Höhe von 4,25% p.a. variabel, kein Bearbeitungsentgelt, Kontoführungsentgelt gesamt EUR 390,60, Zinsen gesamt EUR 1.574,26, **effektivzinssatz 5,5% p.a.** Gesamtrückzahlung EUR 11.964,86

In this advertisement the most prominent number is the nominal interest rate (4.25%). In the text on the right the possible credit amounts, possible time periods and further characteristics of the credit are stated additionally. The information of the obligatory example is hidden in the small print. Shown are the total amount of the credit (10,000 EUR), the time period (84 month), the nominal interest rate (4.25%) additional fees, total interest payments, the APR (5.5%) and the total amount to be paid by the consumer.

In contrast to the previous example this advertisement stresses the nominal interest rate, not the monthly payment. The from our perspective important APR is hidden in the small print. Even so, all obligations of the directive and the Austrian law are fulfilled. This advertisement would not be allowed in Germany, because the APR is less prominent than the nominal interest rate.

These and other Austrian examples we looked at, show that advertisement in Austria often stresses nominal interest rates or monthly payments. The APR is mostly hidden in the small print. The difference between the nominal interest rate and the APR is usually higher than in Germany.

Result: In Austria regulation fulfils EU directive but is weaker than in Germany, APR mostly less prominent than in Germany, more efforts and knowledge needed for consumers to compare and understand credit offers. APR is used less appropriately than in Germany.

2.4 Results of EU experience

The goal of the EU directive was to align regulation inside EU, to increase consumer protection and to make competition fairer. This goal was reached insofar as the directive defines minimum standards, which all members have to fulfil. The analysis of regulation and practice in Germany and Austria show, however, that differences between countries still exist.

Austria more or less copied the EU directive. In Germany, the regulation is more advanced. It entails all the requirements listed in the regulations but has additional provisions. In detail:

- Every communication concerning advertisement shall be fair, clear and not misleading
- Formulations are not allowed which lead to wrong expectations regarding costs of the credit
- The APR must be at least as stressed as any other rate.
- The advertisement has to include an example for the APR for which the lender expects that 2/3 of the contracts concluded on the basis of this advertising should have the advertised rate or a better one

These additional provisions result in a more consumer friendly advertisement than in other EU countries. One big advantage from the perspective of consumer protection is that the competition in Germany focuses on the APR, making it difficult for lenders to hide additional costs.

3 Regulation and implementation in Moldova

After looking at the situation in the EU we now focus on the regulation and implementation in Moldova.

3.1 Regulation in Moldova

The Moldovan law for consumer credit is also based on the EU Directive. It was adopted in 2013 (Law Number 202 from 12.07.2013) and is in force since 2014.

The law should therefore meet the EU requirements and should be comparable to that of EU countries.

We again focus mainly on advertisement regulation. Here is what Moldovan law says:

Any advertising concerning credit agreements, which show interest rates or other numbers concerning the cost of a credit shall include standard information. This information shall be provided in clear, concise and prominent way in the **same field of vision and with symbols of the same size** by means of representative example. It must show:

- the nominal rate, plus all the charges that are included in the cost of the credit
- total amount of credit,
- the APR
- the duration of the credit agreement,
- the total amount to be paid by the consumer and the amount of instalments

In addition to the directive, in Moldova one provision is made to make advertisement more transparent. The provided information shall all be in the same size and field of vision, which is not demanded by the directive. At the same time, regulation is far less strict than in Germany. It does not require that every communication shall not mislead, it does not explicitly forbid formulations which lead to wrong expectations regarding costs of the credit, it does not state that the APR must be at least as stressed as any other rate and it also does not have the 2/3 rule for realistic advertised rates.

Result: The Moldovan regulation is a bit stricter than in Austria but far less strict than in Germany.

What effects has this regulation on implementation and is the APR used appropriately in Moldova?

3.2 Examples of advertisement in Moldova

The first example is from a bank.

Figure 5

Advertising example from Moldova

Informații generale despre credit	
Suma creditului solicitat	10000.00
Comision unic	200.00
Taxa administrativă	100.00
Suma dobânzii	494.80
Comision de administrare	232.00
Total spre plată	11026.80
DAE	19.00

* Calculul estimativ realizat prin intermediul calculatorului de rate online este orientativ si nu are valoare contractuala

What is shown first in this example is the nominal interest rate (9.0%), it is followed by the total amount of the credit (10,000 LEU), different additional fees, total interest payments, the total amount to be paid by the consumer and the APR at the very end. The example on the website also showed the duration of the credit agreement and the amount per instalment and number of instalments. We did not include it due to reasons of space.

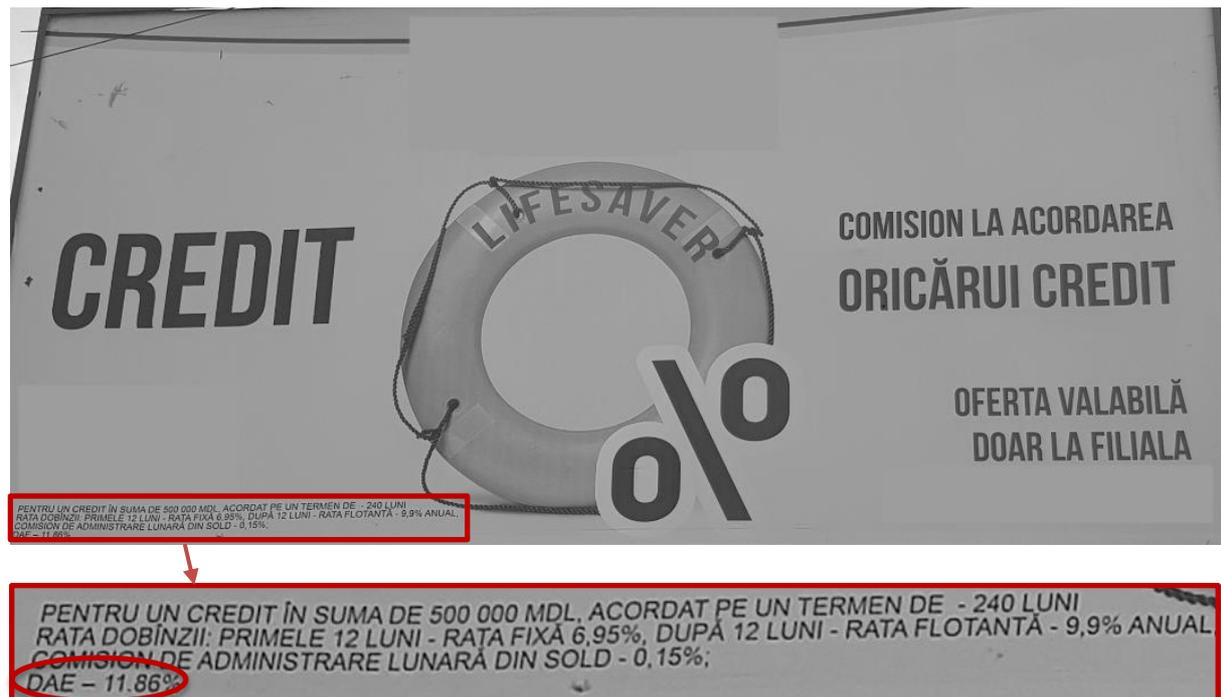
The first result from looking on this example is that all necessary information is shown. At the same time the advertisement focuses on the nominal interest, it is the first number shown. The APR, the number we are most interested in, is shown as the last number. This example is comparable to the second Austrian example, which has shown the APR at the last place. It has to be noted that it is at least not hidden in the small print – a result of the stricter Moldova regulation (all numbers in the example have to have the same size). Nevertheless, a more prominent position of the APR would promote transparency.

However, another problem we see in this example is the presentation of the APR as abbreviation. We suspect that not every consumer understands what it means. An assumption we could confirm by asking people in Moldova. A further problem with this example is the missing “%” sign after the APR number. It could easily be interpreted wrongly – an assumption which was confirmed by experts from the German Federal Financial Services Regulatory Authority (BaFin) that also looked at this example. At the same time, we see a huge difference between the nominal interest rate and the APR, which is more than twice as high as the nominal rate.

The second example from a bank is taken from a street advertisement.

Figure 6

Advertising example from Moldova: Street advertisement



Advertised is a 0% commission for a credit in a specific branch of the bank. In the small print is the information demanded by law: the total amount of the credit, the duration of the credit, the nominal interest rates, the monthly management fee and the APR.

This example is probably in line with the law, because all the obligatory information for the credit example are given in the small print which also have the same letter size. Nevertheless, this example is misleading. The zero rate associates with a zero interest rate and the small print is too small to be read.

To prevent such cases a stricter regulation could help. Such advertising would probably not be possible in Germany as it is misleading and it could contradict the rule that the APR should be at least as prominent as any other shown rate.

The next example is from a micro financial institution.

Figure 7

Advertising example from Moldova

Условия кредита

- ✓ Условия кредита
 - 2 000 - 30 000 MDL
- ✓ Срок кредита
 - от 1 до 12 месяцев
- ✓ Переплата и проценты
 - 12% годовых +
ежемесячный комиссион

Необходимые документы

- ✓ Работающие официально
 - Булетин (вместе с вкладышем)
- ✓ Работающие неофициально
 - Булетин (вместе с вкладышем)
- ✓ Пенсионеры
 - Булетин (вместе с вкладышем)
 - Пенсионное удостоверение

APR is missing

This example shows on the left side some condition for the credit, e.g. the possible total amounts of the credit, the possible duration of the credit agreement and the borrowing rate plus an additional not specified fee. On the right side are the necessary documents listed for different groups of customers: officially employed, unofficially employed and pensioners. The problem with this example is that it does not show an APR, which is against the law.

The last example is again from micro financial institution. It is a street advertisement.

Figure 8

Advertising example from Moldova: Street advertisement



The example advertises a zero interest rate credit for the first five days of the credit. This example is also highly problematic from legal point of view, because none information obligatory by law is shown. There is an exception in the law for short term agreements which have to be repaid within three months. But the exception only applies if only insignificant charges are payable. This is not the case here as a significant interest is charged after the 5 days and the shortest credit duration is 7 days.

The advertisement examples have shown some problematic issues. In the case of banks, most advertisements and offers are ok from a legal viewpoint, but there are rather confusing indications which are of little use for consumers. We see these problems especially in the use of the APR. In most cases the APR is only shown as abbreviation and is not explained and sometimes not even recognisable as what it is. Thus, consumers without a proper financial background will have a hard time to understand and compare credit offers. In other cases the APR is not shown at all, which in our understanding is a clear breach of the Moldovan law.

Another observation of the Moldovan examples is the high difference between the nominal rate and the APR. There are many fees and commissions that we do not observe in Austria and Germany. In Moldova the APR is often twice as high and sometimes ten times as high as the nominal interest rate, which makes it even more necessary to stress and explain this rate in advertisements.

3.3 Transparency during loan application

The problematic practices apply not only to advertisement. We performed field trials to see how transparent the dialogue with the consumer is. According to law, lenders are obliged to:

- In good time before the consumer is bound by any credit agreement provide the consumer with the information needed to compare different offers in order to take an informed decision on whether to conclude a credit agreement
- provide adequate explanations to the consumer, in order to place the consumer in a position enabling him to assess whether the proposed credit agreement is adapted to his needs and to his financial situation, where appropriate by explaining the pre-contractual information, the essential characteristics of the products proposed and the specific effects they may have on the consumer, including the consequences of default in payment by the consumer
- assess the consumer's creditworthiness on the basis of sufficient information, where appropriately obtained from the consumer and, where necessary, on the basis of a consultation of the relevant database

However, credit is often available in a very short period of time (half an hour) and it is difficult to ensure proper explanations about the cost of the credit. Our experience is that lenders, especially micro financial institutions, offer lending without explaining all the subtleties of a credit contract to clients.

Once the client has decided to contract a consumer loan, creditors provide him the pre-contractual information. At this stage, usually, the provided information is incomplete, and more details are provided only on request. At the same time, in many cases at the pre-contractual stage, micro financial institutions do not present a copy of the contract to the client. The client will be invited to sign the contract afterwards and only then he will be able to become acquainted with its provisions.

Also, at the pre-contractual stage, a list of documents is required from the client, in dependence to the amount and term of the loan he asks for. As a rule, the credit of a value that ranges between MDL 1 to 8 thsd. can be perfected in one hour and only on the basis of the ID card. The presence of the salary certificate is not a necessary condition.

We found breaches of law more often in micro financial institutions as banks conduct a much more professional dialogue with customers. This significant difference in the approach is also a problem, because if one lender wants to be fair, they will face disadvantages in competition.

Thus, we can conclude that the lending activity of individuals lacks the necessary transparency that is mandatory for ensuring consumer protection. Moreover, there also seem to be a weakness in supervision as deceitful advertisement and consumer dialogue seems to be quite common.

Result: Credit advertisements are mostly non-transparent up to deceitful in regard of the use of the APR. There is much room to improve the use of APR to increase the transparency in providing consumer credit. Supervision of these practices seems also to be a weakness.

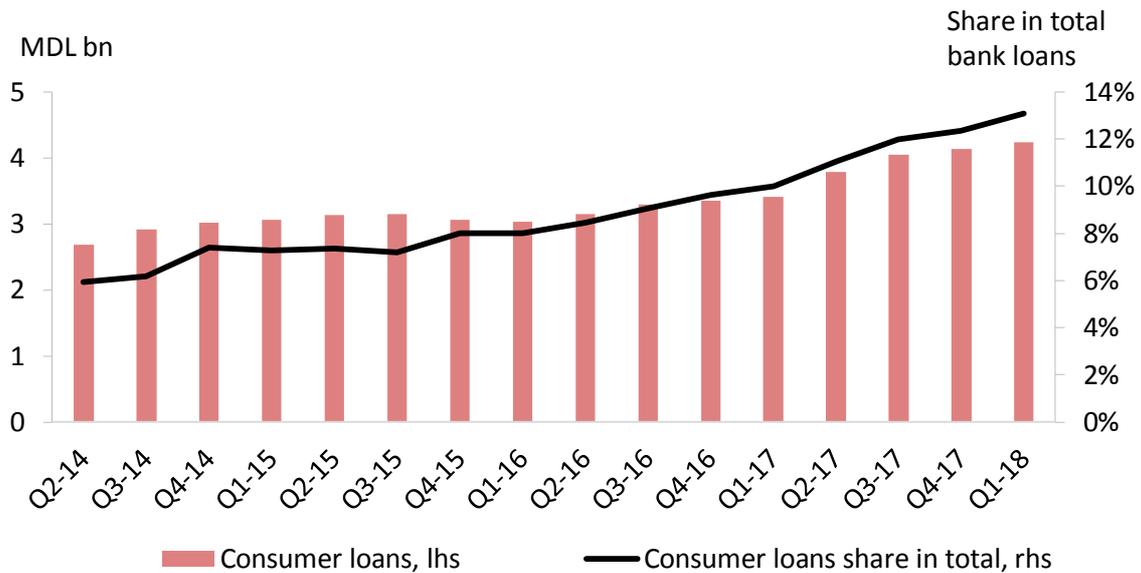
4 Consumer loans and financial stability

To ensure transparency in consumer lending is not only a topic of consumer protection but also has consequences for financial stability. Poor transparency in consumer lending and poor consumer protection can lead to an increase of non-performing loans (NPLs) and thus threaten financial stability in the long-term in Moldova. Thus, in this section we will look at the recent developments of consumer loan growth and NPL growth to see whether there is a potential future risk.

First we look at the development of consumer loan growth compared to total bank loans, see figure 8.

Figure 8

Development of the volume of banks consumer loans 2014-2018



Source: National Bank of Moldova

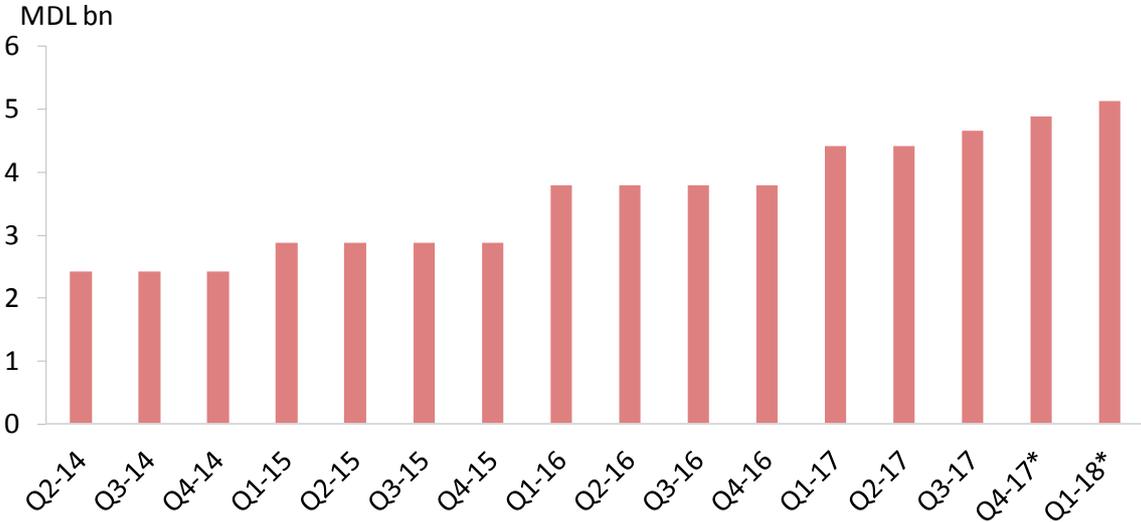
The figure shows a strong growth of consumer loans compared to other loans in the past four years. The amount of consumer loans from banks increased from MDL 2.7 bn in Q2-2014 to MDL 4.2 bn in Q1-2018, an increase of 58%. At the same time the share of consumer loans in total loans increased from 5.9% to 13.1%. The increase in share was higher than in absolute terms because the total amount of loans decreased as a result of the banking fraud in 2014. In fact, consumer loans were the only loan category that significantly increased in this time period and they continue to grow.

For the rate of non-performing loans (NPL) no long time-data series is available. The share of NPL in banking consumer loans decreased in the last two years from 5.1% to 4.2%. But in the same time there was a strong growth in volume of consumer loans, so in absolute terms, the total NPL consumer loan volume increased from MDL 161 m in Q2-2016 to MDL 177 m in Q1-2018. A negative development from the point of view of financial stability. But banks are not the only institutions providing consumer loans.

Figure 9 shows the development of the credit volume of micro financial institutions in the past four years.

Figure 9

Development of the volume of loans by micro financial institutions



Source: National Commission for Financial Markets; *Estimate based on historical growth rate

For 2014-2016 only yearly data is available, which is why these quarters have the same value. The figure shows a very high loan growth of micro financial institutions. The loan portfolio more than doubled in the time period from end of 2014 to Q1-2018, from MDL 2.4 bn to estimated MDL 5.1 bn. Under the assumption that micro financial institutions provide only consumer loans, the total credit amount from banks and micro-financial institutions consumer loans equals around MDL 9.3 bn. This is about 29% of the total credit volume of the Moldovan banking sector.

Unfortunately, no data could be found on the NPL rate of consumer loans of these institutions, but it could be assumed that it should not be better than that of banks consumer loans. There are much less requirements to get a loan from a micro-financial institution that is why more consumers with a bad credit history will apply for such a credit, which should lead to a higher NPL rate.

Result: High and growing share of consumer loans in total loans, in connection with a non-transparent system of providing consumer loans could pose a threat for financial stability in the long-term.

5 Summary and recommendations for Moldova

5.1 Summary of results

The EU directive 2008/48/EC should increase consumer protection and create a level playing field between EU members. This directive was also implemented by Moldova. However, our analysis shows that there are still differences between countries. This can be explained with the fact that some countries implemented stricter regulation as that of the directive. A good example is Germany, as it implemented regulation for advertisement for consumer credits that goes far beyond the directive. In Germany, the advertisement focuses on the APR, which is transparent and consumer friendly. In Austria this is not the case; the APR is often hidden in the small print - a result of a less strict regulation.

In Moldova the situation in advertisement is similar to that of Austria. There is no focus on the APR in advertisements and it is therefore not used appropriately. The situation needs to be improved.

Consumers are not protected, as it is very difficult to compare offers if you are not an expert. As another consequence, the competition is not fair.

In Moldova we also found several cases that seem to be clear violations of the law. This is not only the case in advertisement but continues in the dialogue with the customer. This implies not only a relatively weak regulation but also a weak supervision. This situation is of relevance not only from the point of view of consumer protection but also in regard of financial stability as the share of consumer loans in total loans is growing fast.

5.2 Recommendations for Moldova

What needs to be done is not an easy question to answer. One element should be an adoption of a stricter regulation for advertisements of consumer loans. Moldova fulfils the requirements of the EU directive but our analysis shows that it makes sense to further improve the regulation. We think that it makes sense to adapt some parts of the German practice. In particular we suggest these additional requirements:

- show the APR at least as prominent as any other rate
- APR should be stated immediately before or after the nominal interest rate

To make the analysis for violations easier, general specifications could be formulated as in Germany:

- every communication concerning advertisement shall be fair, clear and not misleading
- formulations are not allowed which lead to wrong expectations regarding costs of the credit

The most transparent advertisement from our point of view would look like this:

“Annual Percentage Rate of charge (APR) 4,5%; nominal interest rate 4.3%”

Of course a stricter regulation can only solve a part of the problem. There seems to be a problem in supervision. The important questions in this regard are who controls the implementation, what happens if the lender does not comply with the regulation, who checks the calculation of the APR, does the Consumer Protection and Market Surveillance Agency as supervisory body has the capacity to cover the area and what should be done to improve it?

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