PROSPECTS FOR THE USE OF DYNAMIC PROVISIONING IN RUSSIA

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In the article the author considers the possibilities of approbating the dynamic approach to creating the possible credit loss reserves in Russian banking system.

The global financial crisis of 2008-2009 had a negative impact on the Russian banking system. For example, during the II quarter of 2009 year, in the midst of financial crisis, Sberbank losses reached 20 billion rubles. Currently there is the process of restoring the credit system from the consecuences of financial crisis. Only in the period of September-December 2010 the growth rate of loans had average 10.5% in comparison to the previous period. In the post-crisis period it is necessary to analyze the mistakes and make financial reforms of banking system to improve its stability during the periods of possible external shocks in the future. The international community is now actively discussing the reform, which would go to the counter-cyclical regulation of banking system. This approach suggests to differentiate the severity of banking regulations, depending on the stages of credit cycle, with the use of higher requirements for banks in the periods of capital inflows and as a consequence of credit boom. In our view one of these measures to be tested on the Russian financial market can be the use of dynamic provisioning.

Dynamic provisioning means the creation of dynamic reserves during the credit boom.

The dignity of dynamic redundancy is primarily that created reserves take into account not only current losses, but also the long-expected loss when exposed to the banking system of external shocks. Buffers additional reserves for possible losses on loans that are created in periods of expansion capital in the financial market, will serve as collateral sustainability of the sector of financial intermediation in the situation of sudden outflows of capital and stop lending process in the situation of changes in financial market.

The positive contribution of the dynamic redundancy in maintaining the stability of banking system to external shocks has been proved in practice during the global financial crisis in Spain in 2007-2009. Among the countries with developed financial market, Spain since 2000, uses the practice of forming dynamic reserves (statistical provisioning). Spanish banks at the expense of current earnings on a quarterly basis constitute reserves of between 0 and 1, 5%, depending on the category of loan. When you declare a default on the loans for losses, it will be generated from the static reserves. Introduction to the practice of dynamic redundancy in Spain was due to a sharp increase in lending in the pre-crisis years. The banks did not agree with the policy of the regulator to raise contribution rates to reserves for possible losses on loans and advances. Prior to using the practice of dynamic redundancy (2000) in Spain, the ratio of reserves to total loans was less than that of most other OECD countries. Introduction to the practice of payments to the dynamic reserves has radically changed the situation. In early 2008, before the global financial crisis, the total reserves of Spanish banking system were 40 billion euros, or about 200% of all accumulated distressed assets on the balance sheets of Spanish banks. In other EU countries, this figure was at an average of 58%. Thus, the presence of significant reserves accumulated during the credit boom, gave additional stability to the banking system of the country.

Positive experience of the dynamic redundancy in the stabilization of the banking system during the global financial crisis also exists in emerging markets, particularly in India. While credit growth in some sectors was too rapid, the National Bank of India increaseed the rate of contributions to the dynamic reserves. This approach was extended to consumer credit and lending for real estate.

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According to the dynamic approach, the bank begins to create dynamic reserves during the credit boom, until the beginning of the period of credit contraction. During this period, bank losses offset by a previously created dynamic reserves, and due to the standard established during the emergence of arrears.

In terms of banking regulation and supervision, the dynamic reserves will perform three functions:

♦ reducing the pressure on profits and shareholders' equity of credit institutions in times of credit crunch by increasing the backup load during the credit boom, which contribute to long-term stability of banking sector;

♦ limit excessive growth of credit supply by the mandatory rules of dynamic redundancy, depending on the growth of loan portfolio;

♦ controlling the growth of overdue debts by its cancellation in times of crisis due to previously accumulated dynamic reserves.

It is also necessary to model the dynamic redundancy that has been supported by leading organizations. In particular, the new approach supports the Bank of England. Financial Stability Forum recommended that the International Accounting Standarts Boards and US Financial Accounting Standarts Board should consider the alternatives of assessment, using the model of expected losses and dynamic reserves. The initiative of the transition to a dynamic provisioning of banks was also supported by the Expert Group on Financial Supervision, under the leadership of Jacques Lavoisier. The model of dynamic redundancy is also included in the program of measures to reform the financial markets of many developing countries. For example, in Kazakhstan, according to the program of financial sector reforms, the transition of the banking system to model the dynamic reserve is planned for 2012.

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