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CREDIT POLICY OF A COMMERCIAL BANK IN CONDITIONS OF UNCERTAINTY OF THE ECONOMIC ENVIRONMENT

Abstract. The article examines the concept of «credit policy» through the prism of the functions outlined in the development strategy of the banking institution, which is primarily aimed at maximizing resources for rapid response to uncertainties of the external and internal environment. The complex of identified key characteristics allowed to form a holistic view of the nature and specific features of the commercial bank's credit policy.

The article underlines that in conditions of uncertainty, the bank should take into account external and internal environmental factors that have a direct impact on the dynamics of lending to individuals and businesses, and need to be considered at the stage of strategic financial planning, monitoring the implementation of set tasks and in order to timely adjust the policy according to the banking institution's needs for financial and economic security. The systematised factors are interrelated and interdependent and can have a multifaceted impact on the current state of the credit services of banking institutions' market and such market's trends.

The article establishes the role of analysis and monitoring of banking institutions' credit operations in the context of ensuring the effective results of the commercial bank's credit policy.

It is identified that credit risk is now in the spotlight of banking institutions along with the risks of capital adequacy and legal risks, due to the general decline in economic activity of consumers of financial services as a result of the epidemiological crisis and the introduction of quarantine restrictions, which reduced household incomes and negatively affected the financial situation of enterprises. The dynamics of changes in the share of NPLs by groups of banks is analysed, revealing foreign banks' active work with NPLs.

The study pays attention to the use of analytical tools of the commercial bank's credit policy as a means of managing its financial and economic security in conditions of uncertainty, which concerns constant monitoring of loan portfolio quality and timely detection of NPLs. It also suggests the sequence of lending steps specifying practical aspects of use of analytical tools of credit policy.

Keywords: credit policy, commercial bank, management, uncertainty, economic environment, analytical tools, financial market.

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КРЕДИТНА ПОЛІТИКА КОМЕРЦІЙНОГО БАНКУ В УМОВАХ НЕВИЗНАЧЕНОСТІ ЕКОНОМІЧНОГО СЕРЕДОВИЩА

Анотація. На основі проведених досліджень проаналізовано сутність кредитної політики крізь призму функцій, що окреслені у стратегії розвитку банківської установи, яка передусім спрямована на максимізацію ресурсів для оперативного реагування на чинники невизначеності зовнішнього і внутрішнього економічного середовища. Комплекс виявлених ключових характеристик дозволив сформуванати цілісне уявлення щодо змістовного наповнення та особливостей побудови кредитної політики комерційного банку.

Наголошено, що в умовах невизначеності банку слід урахувувати фактори зовнішнього і внутрішнього середовища, які мають безпосередній вплив на динаміку процесів кредитування фізичних осіб та бізнесу, і потребують обліку на етапі стратегічного фінансового планування, контролю за виконанням поставлених завдань та з метою своєчасної зміни політики відповідно до потреб забезпечення фінансово-економічної безпеки банківської установи. Систематизовано фактори впливу, що перебувають у взаємозв'язку і взаємообумовленості та можуть чинити різноспрямований вплив на актуальний стан і тенденції розвитку ринку кредитних послуг банківських установ.

Визначено роль реалізації завдань аналізу та моніторингу кредитних операцій банківських установ у контексті забезпечення результативних підсумків провадження кредитної політики комерційного банку.

Виокремлено місце кредитного ризику в карті ризиків банківського сектору, який перебуває сьогодні в центрі уваги банківських установ поряд із ризиками достатності капіталу та юридичними ризиками, що зумовлено загальним зниженням економічної активності споживачів фінансових послуг як результат епідеміологічної кризи і впровадження карантинних обмежень, що скоротило як доходи домогосподарств, так і негативним чином позначилось на фінансовому стані підприємств. Проаналізовано динаміку зміни частки NPL-кредитів за групами банків, що дозволило побачити активну роботу з NPL-кредитами в розрізі іноземних банків.

Приділено увагу актуальності використання аналітичних інструментів кредитної політики комерційного банку як засобів управління його фінансово-економічною безпекою в умовах невизначеності, що зводиться до постійного моніторингу якості кредитного портфеля та своєчасного виявлення NPL-кредитів. Запропоновано схему послідовності надання кредиту, що уточнює прикладні аспекти використання аналітичних інструментів кредитної політики.

Ключові слова: кредитна політика, комерційний банк, управління, невизначеність, економічне середовище, аналітичні інструменти, фінансовий ринок.

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Introduction. In the modern economy, a large proportion of banks experience a decrease in profitability and investment attractiveness owing to high risks in the credit segment of the financial market, which are due to the uncertainty of the economic environment and quarantine restrictions.

The credit segment of the financial market is a dynamic component of the country's financial system development. It is this segment exactly that requires research and rethinking of the approaches to the conceptual and managerial components of the credit policy of a commercial bank as part of its strategy for sustainable economic growth.

That is why the clarification of the strategic goals of credit policy, factors of influence and its analytical tools is a priority area of research in the uncertain economic environment and the key to the stability of the banking system of Ukraine.

The imperfection of the analytical tools of the commercial bank's credit policy necessitates the identification of areas for improvement of credit management of a financial institution operating in the credit segment of the financial market.

Literature review and the problem statement. Research into the commercial bank's credit policy implementation issues in the uncertainty of the economic environment has recently received

increasing attention from scientists, financial analysts, and banking market experts. In our opinion, the works of such scientists as Setiawan R., Abu-Rumman A., Cavaliere L. P. L., P. Ratna Mary Ch., Pachala V. V., Khan A., Sankaran D. [1], Lysenok O. V. [2], Stepanenko K. R. [3], Prokopenko O. V., Biloshkurska N. V., Biloshkurskyi M. V., Omelyanenko V. A. [4], Yanenkova I., Nehoda Y., Drobyazko S., Zavorodnii A., Berezovska L. [5], Baudino P. [6] and others deserve attention. The scientific works of these and many other researchers consider various theoretical and practical aspects of the formation and implementation of the commercial bank's credit policy, as well as key system-forming factors that influence the operation of the credit segment of the financial market. However, it should be noted that the works of these scholars do not sufficiently disclose the research subject and do not detail the analytical management issues of the commercial bank's credit policy. Thus, more in-depth scientific inquiry, especially in the field of methodological support of credit management, is identified as a topical research direction.

The purpose of the article is to study the impact of economic uncertainty on the current features of the commercial bank's credit policy, analyze the current state of credit risks in the banking system, and identify the macro- and micro-factors that determine management decisions within lending and the specific use of analytics tools supporting credit policy.

Methodology and research methods. In the process of writing the article, we processed and generalized the material of a theoretical and practical nature using general scientific and specific research methods.

Methods such as analysis, synthesis, comparison in the study of theoretical developments of Ukrainian and foreign scientists related to the research topic were effective. Structural analysis was used for systematization of strategic goals and identification of macro- and micro-factors influencing formation of commercial bank's credit policy. Analytical method and method of expert analysis for giving the characteristics of the main benchmarks and indicators of credit policy of a commercial bank in conditions of uncertainty of the economic environment. Schematic representation of commercial bank's lending process is based on the system method.

Research results. Lending has a special role and importance among the variety of commercial banks' financial services, as its accessibility determines the possibilities of market economy development by meeting the temporary needs of some entities in additional funds at the expense of other entities' temporary surplus. Availability of free capital or resources is the basis of innovation and investment activities' implementation by the subjects in the market environment [7, p. 222].

To form a quality structure of credit assets, commercial banks create their internal credit policy based on prudent approaches to the formation of the credit resource values, security and balance according to the criteria of risk and credit period.

Among scientists, there is no unified understanding when it comes to the economic nature of the concept of «credit policy», which led to the debatable nature of this phenomenon and makes topical the consideration of its key conceptual features:

- a) the strategy and tactics of a commercial bank;
- b) an internal document of a commercial bank, which it follows when forming a loan portfolio;
- c) the system of rules, measures and actions of the bank in the field of lending to its customers;
- d) directions, priorities, principles and goals of a commercial bank;
- e) the general approach and concept of lending;
- f) an integral part of the commercial bank's general policy.

The complex of these characteristics allows to form a holistic view of the nature and peculiarities of the credit policy of a commercial bank. The nature of credit policy should be considered through the prism of the functions outlined in the development strategy of the banking institution, which is primarily aimed at maximizing resources for rapid response to uncertainties of the external and internal environment [1, p. 823].

The strategic goals of the credit policy of a commercial bank are systematized in *Fig. 1*.

The strategic goals of the credit policy of a commercial bank	
→	Actions to change the size and structure of the commercial bank's loan portfolio based on the stage of the credit cycle and the state of the economic system
→	Finding the optimal ratio of elements of the loan portfolio's structure depending on the type of loans, collateral and maturity of loans
→	Prioritizing the development of economic relations with strategic partners
→	Diversification of issued bank loans by sectors of the national economy
→	Maximizing the profitability of credit operations and return on the bank stocks, provided that the risks of lending are minimized
→	Balancing the sources of accumulation of the commercial bank's financial resources and the areas of funds placement in lending
→	Implementation of credit policy on the basis of financial stability as an element of financial and economic security of a banking institution
→	Growth of the client base under the condition of high quality of credit services
→	Levelling of reputational risks and maintaining the position of a reliable bank, a high level of confidence on the part of consumers of the commercial bank's financial services
→	Adherence to the principles of balance and prudence of management decisions on the use of the commercial bank's credit resources

Fig. 1. Systematization of strategic goals of commercial bank's credit policy

Source. Compiled by the authors.

The commercial bank's strategy as an element of lending specifies the development direction and features of financial services in the money and credit market of Ukraine.

Its tactics specifies the list of financial instruments that the bank uses to achieve certain goals in lending, determines the organizational part of the loan granting procedure, and discloses organizational support of lending.

The strategic management of the bank's credit policy concerns the formation of credit strategies of the financial institution, as well as clarification of the purpose and, accordingly, the range of objectives and the choice of methods to achieve them [2, p. 185]. In conditions of uncertainty, the bank should take into account external and internal environmental factors that have a direct impact on the dynamics of lending to individuals and businesses, and need to be considered at the stage of strategic financial planning, monitoring the implementation of tasks and in order to timely adjust the policy according to the needs for financial and economic security.

The study of macro- and micro-factors influencing the formation and implementation of the bank's credit policy is presented in *Fig. 2* and *3*.

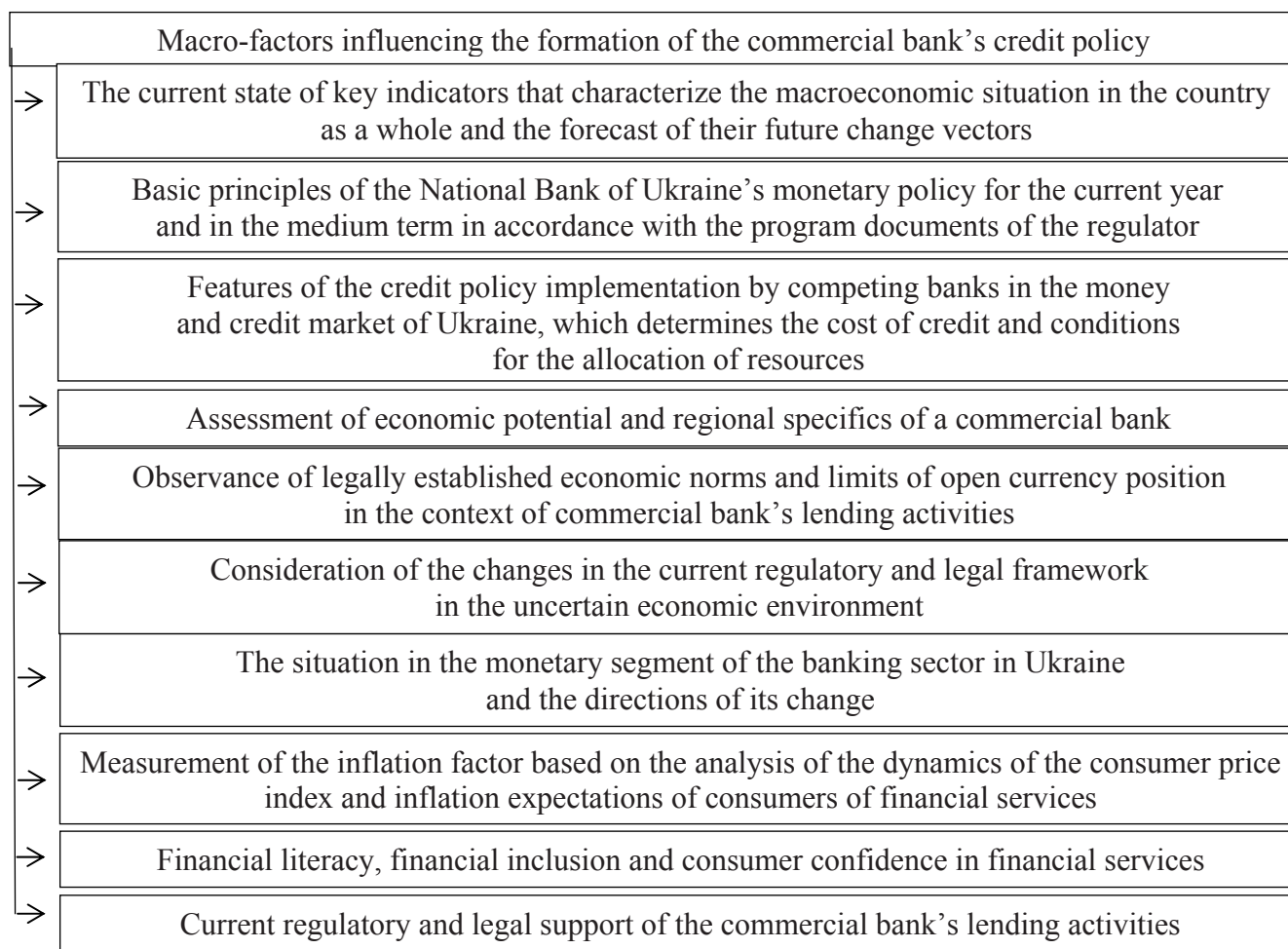


Fig. 2. Macro-factors influencing formation of commercial bank’s credit policy
 Source. Compiled by the authors.

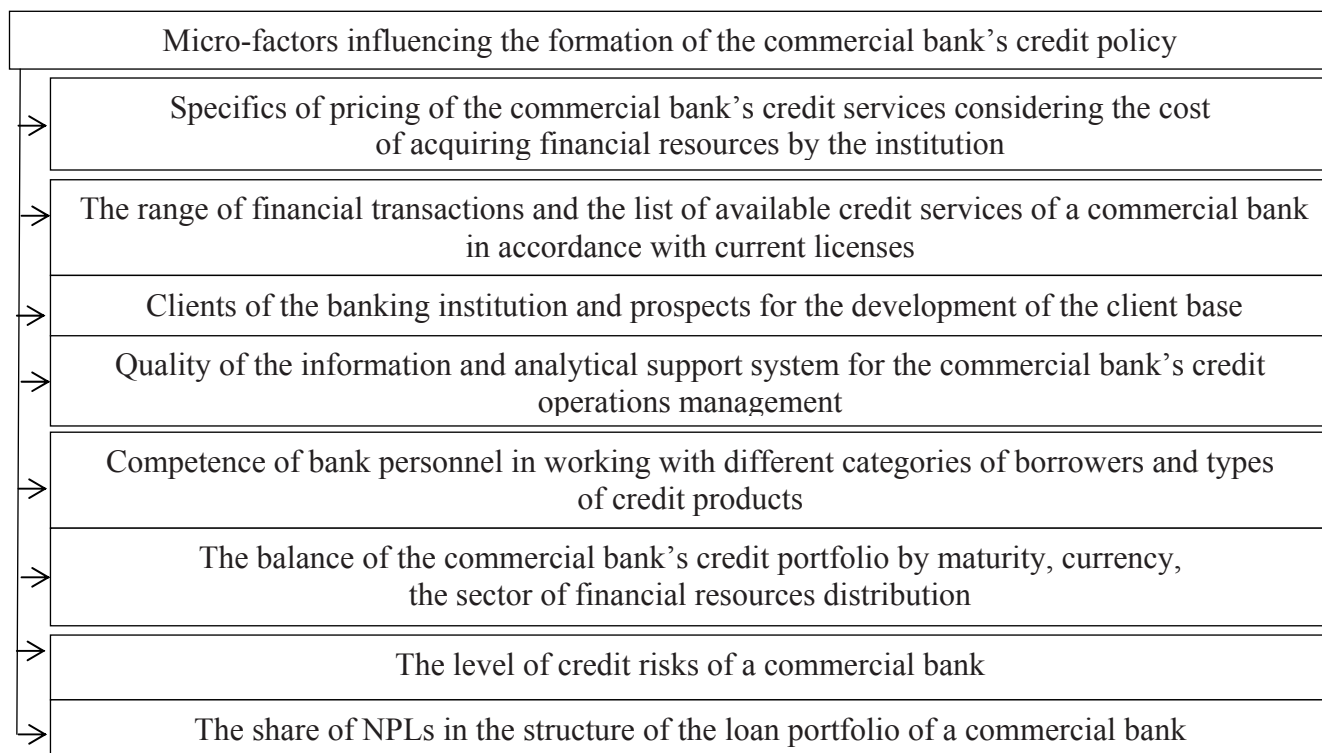


Fig. 3. Micro-factors influencing formation of commercial bank’s credit policy
 Source. Compiled by the authors.

Macroeconomic factors form a group of systematic risks, which a commercial bank cannot directly influence, but which it must consider when lending. In particular, attention is required to the price factor of credit policy in order to maximize the profit of lending activities [8, p. 83]. Also, the interregional features of the incomes of consumers of credit services and their needs have to be taken into account by the management of the commercial bank [9, p. 31]. It is emphasized by the problems of uneven distribution of incomes between regions, the difference in the rates of growth in production, unemployment rates, and social indexes [10, p. 39]. Regarding micro-factors, a commercial bank has leverage to influence possible risks that pose a threat to its financial and economic security.

The classification of micro-factors influencing credit policy is shown in *Fig. 3*.

The identified factors are interrelated and interdependent and can have a multifaceted impact on the current state of the credit services of banking institutions' market and such market's trends.

A credit department should continuously monitor the factors influencing the entire cycle of the banking institution's lending strategy implementation, considering the uncertainty and turbulence of the financial environment as a risk management is a key element of the strategic activities of any organization [11, p. 6047].

Ensuring the effective results of credit policy is possible, provided that analysis and monitoring of the banking institutions' credit operations are implemented. This task can be performed using analytical tools to assess the quality of the loan portfolio with the appropriate information support, which includes a complex of statistical information, overall accounting and operational accounting data, regulations and recommendations of the banking system's regulator.

Turning to the concept of «loan portfolio», we consider the definition given in the work of K. R. Stepanenko, based on its consideration as a tool for managing active operations of the bank, the purpose of which is to increase profits and efficiency, achieved by providing loans in various areas of lending, taking into account the requirements of credit policy of the bank and banking supervisors [3, p. 112].

The use of certain analytical tools of credit policy should consider simultaneous interaction of several levels of analysis, namely:

- a) the use of a group of indicators at the level of analysis of the banking system;
- b) application of methodological approaches to the analysis at the commercial bank level, which concerns the assessment and work with both a separate loan and the loan portfolio as a whole.

The defined approach creates a systematic vision of the application of analytical instruments of the commercial bank's credit policy as a means of managing the entity's financial and economic security in conditions of uncertainty.

Considering the macro-factors presented in *Fig. 2* is the basis for assessing the place of a commercial bank in the money and credit market, both at a certain reporting date and in the dynamics, which asks for:

- a) monitoring the current state of economic system's development and, accordingly, the study of business and individual expectations of the prospects for the implementation of credit services. As at the level of domestic banks, more attention should be paid to the development and implementation of new credit technologies [4, p. 31].
- b) tracking the peculiarities and innovations of the monetary policy of the NBU in the reporting year and in the future;
- c) the study of the impact of the international financial market participants on the current demand, supply and price of credit services, etc.

Thus, the tasks at the level of analysis of the banking system concern the regulatory and legal framework research and statistical analysis of key indicators of the banks' credit and financial performance at the macro level.

The analysis of indicators at the individual commercial bank level covers the application of analytical instruments of credit policy at the level of a particular banking institution, which includes a thorough study of the loan portfolio structure (separation of elements according to credit quality,

lending sphere, lending currency), loan portfolio management methods, as well as detailed consideration of the debtor’s creditworthiness in the dynamics.

Particular attention is paid to NPLs and their share in the total loan portfolio of the bank. A significant share of NPLs worsens the financial stability of a commercial bank, reduces the quality of the loan portfolio, and increases credit risks. In this way the level of reliability of a bank is characterized by the adequacy of the capital that the bank has to cope with possible unexpected losses [5, p. 14].

Credit risk is now in the spotlight of banking institutions along with capital adequacy risks and legal risks (*Fig. 4*) due to the general decline in economic activity of consumers of financial services, as a result of the epidemiological crisis and the introduction of quarantine restrictions, which reduced household incomes and negatively affected the financial situation of enterprises [6, p. 1].



Fig. 4. Banking sector Risk Map

Source. [12, p. 20].

According to experts, the reduction in household income and financial income will continue, which creates difficulties in the process of fulfilling loan obligations, as well as affects the quality of the commercial banks’ loan portfolios. In accordance with the NBU’s «June 2020 Financial Stability Report», the credit risk is 7 points, which is quite a high value, 2 points higher than in December 2019. Credit risk reflects the prospects for changes in the share of non-performing loans in the banks’ portfolios and the need for additional reserves for such loans [10, p. 20]. According to the NBU’s estimates, the level of provisions as of the end of 2020 is 98 %, which shifts the consideration of NPLs by banks towards assessing their investment attractiveness, rather than financial performance. The high share of NPL is the result of the credit expansion of past years, when the standards for assessing the solvency of borrowers were low, and the rights of lenders were insufficiently protected. Another reason is the practice of lending to related persons who stopped servicing loans during the crisis. The NBU notes that banks should intensively clean up their balance sheets: NPLs should be restructured, sold or written off.

The banking sector risk map reflects the regulator’s expectations for each type of risk for the next 6 months. The share of NPLs (non-performing loans) is declining rather slowly, but their value is practically unchanged due to the expansion of banks’ loan portfolios. This trend is more pronounced in the segment of retail lending (during the last two reporting years, the share of NPLs decreased by 17 percentage points and amounted to 42.6 %) compared to the segment of corporate lending (the share of NPLs decreased by only 2 percentage points down to 54.9 %).

The distribution of credit debt by the level of the debtor’s income is heterogeneous, according to the NBU. The largest share of borrowers takes up the debtors whose income is up to UAH 7 000, which account for a third of the debt. Debtors with income over UAH 20 000 take out

loans mainly for the purchase of durable goods, including vehicles, which account for almost a third of the debt balance (Fig. 5).

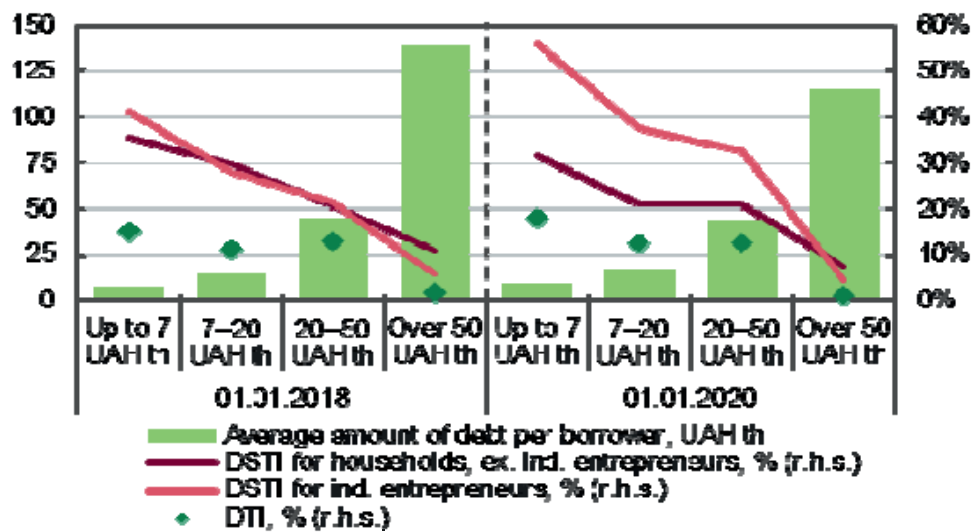


Fig. 5. Debt burden across groups of borrowers, broken down by income
Source. [12].

The dynamics of lending to the corporate sector is presented according to net loans to micro- and small enterprises (MSE's) in Fig. 6, which allows their quality assessment.

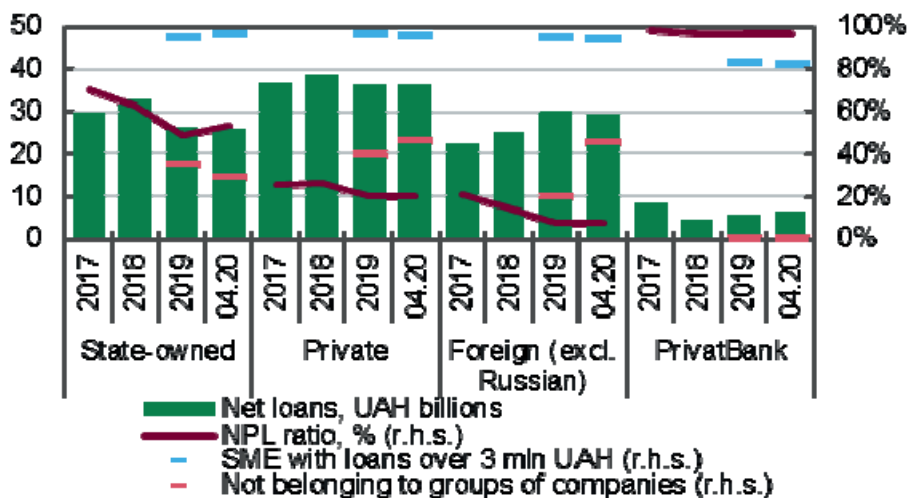


Fig. 6. Net loans to Micro- and Small Enterprises (MSE's) and their quality
Source. [12].

The dynamics of the share of non-performing loans by groups of banks allows us to see active work with NPLs in foreign banks (see Fig. 6). During 2 years, the top 5 of foreign banks' share of NPLs in their total loan portfolios decreased from 34.0 % to 14.3 % [12].

The next steps of foreign banks are write-off measures, sale of problematic loans and voluntary settlement of debts with debtors. Thus, it is difficult to underestimate the relevance of analytical tools of the commercial bank's credit policy as a means of managing its financial and economic security in conditions of uncertainty, which concerns constant monitoring of loan portfolio quality and timely detection of NPLs.

The lending process schematically presented in Fig. 7 clarifies the place of credit policy's analytical instruments in the procedure as the main criterion for obtaining a loan by the company is its financial condition [13, p. 51].

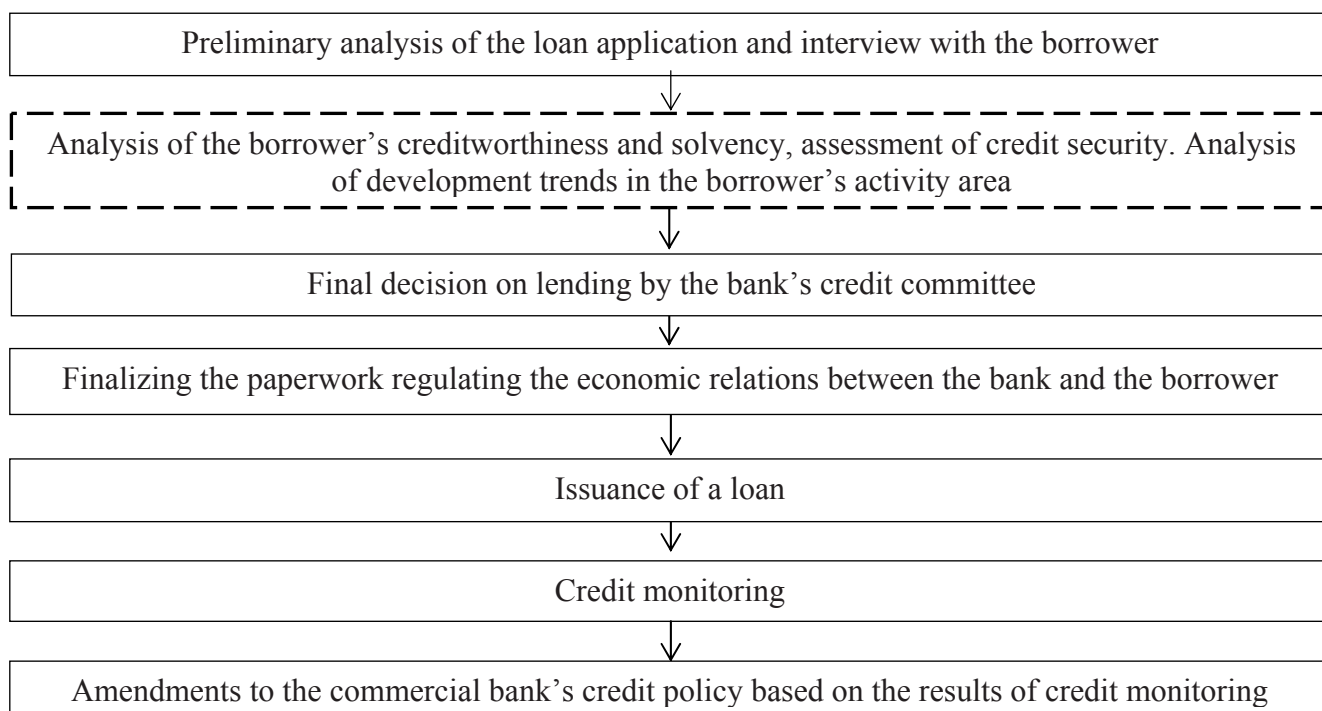


Fig. 7. Schematic representation of commercial bank's lending process
 Source. Compiled by the authors.

Regular review of the borrower's loan information, as well as frequent on-site visit, updating borrower's credit files permits allow to reduce credit risks of the loan portfolio [14, p. 5].

The ratio between liquidity and return on loans is a key parameter for assessing the effectiveness of credit policy in the event of changes in credit risks in conditions of uncertainty. In any case, any of the areas of credit policy that the bank chooses when conducting activities in the money and credit segment of the financial market must be effective and ensure the achievement of the main goal — to make a profit.

Loan portfolio yield indicators that are taken into account, including at the stage of credit monitoring, characterize the dependence of the bank's total income on credit operations, allow to calculate the value of loans granted and assess the profitability of credit operations. Analytical tools for assessing the risk of the loan portfolio provide information on the security of the loan portfolio with equity, the share of borrowed funds in the formation of the bank's loan portfolio and the level of reserves formed for credit operations, as well as analyse the use of customer funds in the loan portfolio.

Thus, the credit policy sets the vectors for the development of the bank's lending activities in regard to the approval of acceptable credit risks, decisions on the selection of reliable borrowers, the urgency and maturity of lending, ways to ensure the fulfilment of credit obligations. This determines the prospect of changes in the profitability and riskiness of the loan portfolio, the competitive position of a commercial bank in the money and credit segment of the financial market.

Conclusions. The uncertainty of the economic environment leads to rethinking of the nature and content of the commercial bank's credit policy, which requires the improvement of analytical tools for credit policy management for a timely response to emerging systematic and specific economic risks.

Factors influencing the credit policy and the loan portfolio of the bank are interrelated and interdependent and can have a multifaceted effect on the current state and trends of the banking institutions' credit services market, taking into account the turbulence of the financial environment. Thus, to ensure the effective results of credit policy implementation, the analysis and continuous monitoring of banking institutions' credit operations are crucial. The proposed approach creates a systematic vision of the application of analytical instruments of the commercial bank's credit

policy as a means of managing the entity's financial and economic security in conditions of uncertainty.

In the current context of quarantine restrictions, the issue of improving the assessment of the borrower's creditworthiness is becoming relevant, which is a future area of research.

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