



***Financial and Banking Services Market***

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**FACILITATING MECHANISM  
OF THE CREDIT PORTFOLIO QUALITY  
AND CREDIT RISK MANAGEMENT  
OF THE BANK IN THE PERIOD  
OF CRISIS DEVELOPMENTS  
IN ECONOMIC SPHERE**

**Abstract**

The improvement trends of the facilitating mechanism of the credit portfolio quality and credit risks management through the definition of the evaluation criterion of the credit quality, creating the credit portfolio of the bank are proved. The creation of the credit portfolio structure in accordance with the group size, classified by the degree of the credit quality, the monitoring of the credit risk, the creation of provisions and adjustment in credit portfolio structure is defined. Special attention is paid to the optimization of the methodology of provisions calculation in order of loan loss provision.

**Key words:**

Credit financing, credit portfolio, provisions, bank, financial crisis, credit risk, credit policy.

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## Introduction

The peculiarities of the economic process in the period of crisis phenomena on the global financial markets not only define the production difficulties and realization of products in the certain sectors and branches of economy, but also are negatively designated on the operational environment of the all market entities, taking into account the fact that the financial sector through the mechanisms of the cash flows and bank lending comprehends nearly all spheres of the public production. The problems, providing the banking system activity, are the main obstacle to overcome recession, inasmuch as the lack of the credit support in the production and economic activities doesn't create the initial possibilities for the natural process of the expended reproduction and changes of the capital at all stages.

Therefore, the questions, concerning the quality supply of the credit portfolio, based on the appropriate assessment of the credit risks level, obtain the special sharpness and actuality. Insofar as the banking system of Ukraine is able to restore the provision of crediting on the level, close to the pre-crisis one, the success in policy of overcoming of the production decrease and reaching of the macroeconomic stabilization will depend on it. Nearly all the negative aspects of the commercial banks functioning, which preceded the crisis phenomena development in Ukrainian economy were connected with their credit activities, whereas the effect of such factors as excessive concentration of the provision of crediting, irrational structure of the credit portfolio, priority choice of the credit financing to the benefit of the credit market consumer segment, inadequate evaluation of the credit risks, domination of currency credits in the structure of the provision of crediting together with the factors of external negative influence on the too open domestic economy was the immediate realization of the crisis potential, being accumulated during the last period.

As a conclusion, the banking institutions of Ukraine cooperate with the real sector of economy and course the significant growth of the total volume of the pass-due indebtedness of banking credits. Some of these banks can deprave the financial standing that leads to the failure and bankruptcy. Such a situation requires the banking institutions to assume such measures: to reconsider the increasing of the evaluation, concerning the risks level and requirements to the prospective borrowers; to determine the higher rates of interest on credit; to increase the different types of banker's commission; to strengthen the demands, concerning provision of loans; to increase the volumes of reservation for the loan loss provisions.

It is obviously, that such events don't course the activization of the credit financing; hereupon the banks are forced to place the bigger part of their assets into the least speculative investments and thereafter to reduce their own credit portfolios, which on practice, deprave the possibilities of overcoming the crisis and production decrease. That is why, according to the present financial crisis, one of the most important components of the formation process of the commercial banks portfolio is the realization of the events, connected with the immediate decision-making, concerning the performing of the lending transactions and optimization of the corresponding structure of the provision of crediting portfolio on the base of the chosen criteria of their quality. This research paper aims to prove the development of those mechanisms which define the tasks of the internal banking management, concerning the organization of lending operations and cooperation between customers, as a consequence, the formation of the optimal structure of the bank's credit portfolio, its high quality and effectiveness of the credit risk management.

### **Presentation of the main material**

The given aspect of the banking institutions activity should comprehend such components: 1) the definition of the evaluation criterion of the credit quality, creating the credit portfolio of the bank; 2) the creation of the credit portfolio structure in accordance with the group size, classified by the degree of the credit quality; 3) the monitoring of the credit risk, the creation of provisions and adjustment in credit portfolio structure.

**The definition of the evaluation criterion of the credit quality, creating the credit portfolio of the bank** is the requirement for its optimization together with the further tasks for the banking management, concerning adjustment of the structure and development of the strategy of the banking institution credit activity. It should be realized due to the analysis of loans, which as a rule forms the credit portfolio and includes such system of criteria: the purpose of credit, the category of loan, the loan sum, the loan term, the amount of the interest rate, the repayment structure of loan, the economic expediency of the credit accommodation, the borrower's branch belonging, the proprietary form of the enterprise, the rate of the borrower according to the authorized capital or annual turnover of finances, the financial standing of borrower, the profitable level of his activity, the means of the credit reimbursement.

While the definition of the evaluation criterion of the credit quality we can use all the mentioned criteria or some of them, which exactly represent the orientation of the banking credit policy, the peculiarities of the customers' serving and the correspondence of the criteria to the strategic goals of the banking institution credit activity.

The credit portfolio quality of the commercial bank represents the correspondence of the structure of its provision of crediting to the basic principles of the credit financing organization in the context of the provision of repayment, duration and payment of the monetary funds, assigned for temporary use. As a whole, these parameters show the degree of the credit risk and the profitability of the bank's lending transactions, which are the strategic goals of its credit policy. So then, the credit portfolio quality means the formation of such structure of the bank, which can provide the appropriate level of its liquidity, and the maximum level of the banking institution profitability in the course of the minimum level of the credit risk. In general, the quality of the credit portfolio, formed by the bank, can be represented by means of the indexes, which characterize its profitability and credibility.

To begin with, we should define the necessity of use of the certain integral index, which would show the profitability of the credit portfolio from the viewpoint of the effective credit activity of the bank. This index should depict the net interest margin with the consideration of the credit risk. It is calculated as a ratio of the net interest, adjusted on the amount of the credit loss to the amount of the credit portfolio of the banking institution:

$$C_{nm} = \frac{A_i - TI - L}{A_{pc}},$$

where  $C_{nm}$  – the coefficient of the net interest margin;  $A_i$  – the amount of the interests on lending transactions;  $TI$  – the total interest bearing expenses of the bank, according to the involved resources;  $L$  – credit losses;  $A_{pc}$  – the amount of the provision of crediting, that is to say, the total sum of the indebtedness on the whole number of bank's loans.

The given index can be used for the effective evaluation of the commercial bank credit portfolio management in the context of credit risk minimization, taking into account the probable losses. Moreover, the coefficient of the net interest margin shows the profitability of the bank's lending transactions, considering the expenses, needed for the creation of resources. What about the credit losses, their amount can be characterized by the number of other indexes, which depict the charge-off of the bad loans from the bank return, as well as expenses, connected with the availability of the nonearning loans of credit portfolio. For such evaluation of the credit portfolio quality, the other indexes can be used.

The question is about the coefficient that depicts the installment of the nonearning loan in the general credit portfolio:

$$C_{nl} = \frac{A_{nl}}{A_{pc}},$$

where  $C_{nl}$  – the coefficient of the nonearning loans;  $A_{nl}$  – the amount of nonearning loans, originated by the bank;  $A_{pc}$  – the amount of the provision of crediting.

The given index depicts not only the effectiveness of the credit policy and the efficiency of the bank measurement, concerning credit risk management, but also the effectiveness of the interest rate policy, able to provide the supportable level of profitableness, according to the all types of the provision of crediting of the commercial bank. Besides it, in order of such evaluation, the coefficients, characterizing the level of the credit reimbursement can be used. In particular, the question is about the coefficient of the untimely credit reimbursement, which is calculated as:

$$C_{cr} = \frac{T_c}{A_{pc}},$$

where  $C_{cr}$  – the coefficient of the untimely credit reimbursement;  $T_c$  – the total of the bank's loans, the repayment of which during the analyzed period was characterized by the nonobservance of time, which is distinguished in the credit agreement;  $A_{pc}$  – the amount of the bank's provision of crediting, that is to sat, the total volume of its credit portfolio.

The given coefficient shows the quality result of the commercial bank's lending transactions during the analyzed period, indicating the bank's problems, concerning loan repayment and trends in reference to the discharge of the customers' obligations, concerning credit reimbursement.

For the dependable evaluation of the bank's credit portfolio we may use the indexes, which show the sufficiency of the loss provisions, concerning credit risks. In particular, the question is about the index, which depicts the ratio of the provisions, formed by the bank, and the amount of the credit:

$$C_{cr} = \frac{R_{lt}}{A_{pc}},$$

where  $C_{cr}$  – the coefficient of the protection from the credit risk;  $R_{lt}$  – the amount of the loan loss provision on lending transactions;  $A_{pc}$  – the general volume of the bank's the provision of crediting.

The given index shows the level of the bank's protection from the credit risk. Let's estimate the effectiveness of the credit policy from the viewpoint of the provisions, which can be directed on the loan loss provisions and then show the confidence of its credit portfolio in general. Also the amount of the bank provision can be compared through the coefficient system with one or other groups of the problem loans in particular with those, which don't bring income or are overdue or problem. Moreover, the coefficient of the completeness of the creation of provisions as a ratio of the actually created bank's loan loss provisions to the calculation amount of the provision, by reference to the amount of the credit risk can be calculated.

To estimate the quality of credits, which form the credit portfolio of the commercial bank, the other indexes can be used and depict the tendency of the banking institution credit policy. In particular, they are: the volume and dynamics of the overdue and problem loans; the amount and structure of the loans without interest payment; the volume of credit agreements, drawn up with the insiders; the amount of the considerable credit (the volume of which is more than 5% of the bank capital); the growth rates of the provision of crediting in general and according to the groups of credits, classified in accordance with their quality; the ratio of the short-received interests according to the granted credits in the total volume of the interest income of the bank.

One more index, which characterizes the quality of the credit portfolio from the viewpoint of its competitiveness is the degree of its renewal. It means the change of the customer base in the certain period. The connection between the credit portfolio quality and the dynamics of its renewal is defined by means of the time lag, during of which the portfolio of loans can restore its initial volume. In fact, the degree of the constancy of the customer base directly influences on the riskiness of the lending transactions and then on the level of their profitability. The credit portfolio volume according to the one or another date can be different due to the movement of the debt service obligations. Moreover, both the low and high velocity of renewal is undesirable. The low velocity can course the reduction of the credit portfolio yield, and high velocity can show the undeliberate and unjustified decision-making, concerning loan extension, which increase the riskiness of the lending transactions and reduce the probability of the profit-making and assets repayment. Zero power of renewal shows the complete closure of the credit portfolio that courses the loss of competitiveness of the bank. Due to the strategic plan, it means the termination of the bank's development. At the same time, the too high level of renewal shows the unstable structure of the credit portfolio and the probability of the increasing of the credit risk.

In general, the offered indexes should be compared with the certain criterion values, developed by the commercial bank on the base of the statistical array of the actual value of the every coefficient for the last periods. At that, the evaluation of the credit portfolio quality can be made on the base of the comparison of the actual value of the certain indexes with the world standards or the commercial bank's standards, defined in the credit policy and on the base of the comparison of the actual values in the corresponding coefficients with their values in the other analogical banks. On that ground, the direction of the bank accepts a decision concerning changes in the structure of the credit portfolio for the purpose of increasing the investment profitability and optimization of the situation, concerning repayment of loans.

The other important element of the facilitating mechanism of the credit portfolio quality is **the creation of the credit portfolio structure in accordance with the group size, classified by the degree of the credit quality**. Such aspect of the credit portfolio creation envisages that managerial solutions, which are accepted on the base of the system of indexes of the credit portfolio quality, and are directed on the change or correction of the credit policy in the plan of the

reorientation of its priorities between different classified groups by means of which the provision of crediting is diversified.

The types of the classified groups of the credit portfolio can be chosen according to the one or other crucial criteria to define the actual and objective structure of the provision of crediting. Such criteria are the next: the risks profile of the granted credits (standard, under control, subprime, problem, loss loans); the branch feature of the belonging of different groups of borrowers according to the sphere of their professional activity; the types of the granted credits depending on credit financing of the current or investment activity; the terms of lending transactions performing, which differ by the advance of funds, put out on loan for the period from some months to some years; forms of currency, performing the provision of crediting into the bank; the volumes of the lending transactions depending on the amount of the loans granted.

The quantitative analysis of the credit portfolio structure according to the given criteria provides the study of the dynamics during some periods of time (as a rule during some years) and structure of the general volume of the bank's provision of crediting. The structural analysis aims to discover the level of lending transactions concentration in one or another classified group, the ratio of the considerable credit in it and then the degree of the credit risk of the bank in the process of the credit portfolio creation. Accordingly, the relations of the bank can be corrected with every borrower or certain groups of borrowers, whereas their activity, concerning the usage of their loans granted and loan requests don't correspond to the general strategy of the bank, concerning the profitability support of the credit portfolio and providing the acceptable level of the provision of crediting liquidity.

Thus, the given aspect of the commercial bank's work defines the content of the credit portfolio management, which is connected with such directions: 1) the realization of the optimal methods of the disbursement and repayment of loan and choosing of the most acceptable methods of credit financing for the customers of the bank; 2) the analysis of the bank's credit portfolio condition as a whole and some of its parts in particular; 3) the usage of the different approaches of the increasing of the provision of crediting profitability and minimization of risks due to the lending transactions; 4) the development of the actions concerning improvement of problem and loss loans.

The result of this activity is the total of those managerial solutions, concerning credit portfolio, which open up opportunities for:

- Firstly, to establish a border of the credit portfolio on the basis of the developed parameters of the credit policy and define the ratio of the bank's resources, which can be used for the loan granted, types of credits, which can be granted and what part of the credit portfolio they should comprehend;

- Secondly, to grant credits only to those borrowers, who correspond to the acceptable parameters of risk, which are approved by the credit policy of the bank;
- Thirdly, to form the credit portfolio on the base of the group classification, depending on the financial standing of the customer and parameters of his development. This enables to distinguish and develop the certain events concerning minimization and prevention of the credit risks;
- The fourth, to create the certain prediction for the bank, concerning its credit portfolio and predict the main indexes of its activity on the basis of the empirical data, concerning credit risks prevention.

One more element of the facilitating mechanism of the credit portfolio quality as it was mentioned is **the monitoring of the credit risk, the creation of provisions and the adjustment of the credit portfolio structure**. The given aspect of the banking management envisages the monitoring of compliance of the given credit portfolio structure and the correspondence of it to the objectives, concerning risks reduction, profitability provision and avoidance of the losses, crucial for the provision of the liquidity. The question is about the estimation of the credit portfolio quality and adjustment of its structure in accordance with market changes, which define the possibilities of the customers, concerning settle obligations before the commercial bank.

The continual analysis of the credit relations with each several borrower should be in the basis of this research paper – in other words the process of credit monitoring, concerning the estimation of the changes in the customer's competitiveness and definition of the necessary events, in course of the problems arise, particularly, the new loan modification and limitations of the further credit financing or debt acceleration. In this context, the question is about the control of granting and using of the given loans. With the consideration of the last years' events we can surely say that the lack of such control courses the crisis phenomena in the financial sector inasmuch as not only the loans were granted to those economic agencies, which don't have a good reason for this, taking into account the parameters of the credit risk and don't provide any control on the part of the bank due to their proper use.

For that purpose, the credit portfolio control should foresee the possibility of deterioration in the financial position of the borrower and timely realization of the measures, concerning repayment of the granted loans. Such measures abreast each several transaction is the complex of approaches to provide the credit reimbursement to its benchmark that is to say to the bank. The leading role here is played by such traditional measures as collateral, guarantee, and insurance.



The complex use of the mentioned approaches and methods of credits reimbursement is considered as methods of risk management of the certain credit, inasmuch as their final course is minimization of the probability of the granted loan repayment to the bank. Special attention, while holding the activities, concerning credit risk management abreast the certain borrower should be paid to such trends of the banking activity as monitoring and control. The control and steady monitoring of the bank's lending transactions is the first-order condition of the successful introduction of the banking loan programs. The constant control helps managers to find out the problem loans in advance and to check up the correspondence of the credit workers to the main requirements of the banking credit policy. It is necessary to underline the incredible significance of the control function of the bank, which should be performed on the each stage of the credit process. The systematic monitoring of the credit process position should be combined with the continuous analysis of the credit portfolio quality. The main task of this work for the bank management is the development of the urgent practical recommendations and propositions, concerning the crediting improvement in the commercial bank.

At the same time, the monitoring of the whole credit portfolio should envisage the implementation of the specific principles and methods of minimization of the lending transactions risk profile, concerning diversification, establishment of the interbank limits and loan loss provision of the commercial banks.

The method of diversification is the method of minimization of the credit portfolio risks which says that the credit portfolio should be formed by means of credits which: firstly, are granted to the borrowers, which work in the different branches of economy (branch diversification); secondly, are granted to borrowers, which work in different regions (regional and geographical diversification); thirdly, are granted to borrowers, which differ by the form of property; the fourth, are granted to borrowers, which differ by the capital dimension.

Limitation provides the process of fixing of limit, in other words the ceiling amount of the banking transactions, concerning one or the other borrowers or group of borrowers. As an example, we can demonstrate the ratio of the credit risk, mounted by the National Bank of Ukraine for the commercial banks: the upper limit for one borrower; the ratio of the upper limit for one insider; the ratio of the total credit amount, guarantees, granted to insiders. The limitation is directed on the restriction of the weighted credit risks of the commercial banks. At the same time, we must admit that besides the NBU ratios, abreast the interbank credit policy, the practice of the lending limits establishment was not extended.

What about the loan loss provisions of the commercial banks? The thing is that the loan loss provisions (with the peculiar risk) were considered by the bank not in the moment of debtor's default, but gradually, according to the risk accumulation. In other words, in course of the debtor's default, concerning the lending transactions conditions, the bank weights the principal amount of the debt into the corresponding coefficients. Provisions can be showed as the recognition of expenses in order to depict the real result of the banking activity with

the consideration of the deterioration in asset quality and off-balance sheet liabilities. We can mention conditions, which influence on the volume of the allocations to provision: the financial position of borrower, the collateral position, in accordance with the lending transaction, the debt service quality, the credit history of borrower. The key insight of the credit risk estimation according to such conditions is dynamism, continual consideration of the factors' change, which form the amount of the credit risk. It is explained by means of the fact that the time value of money is not constant, and the amount of funds, available now will never be equivalent to this amount, if we trace all the changes, concerning every lending transaction.

The mechanism of the creation of loan loss provisions influences on the appropriate quality maintain of the credit portfolio of the commercial bank, which should be considered in the context of those tasks of the banking management, which provide the minimization of the credit risk level.

Nowadays, the creation of the corresponding provisions in the domestic banking practice is in fact the main trend in hedging of risks, connected with the wrong control of the credit portfolio. The given provisions are created due to the all types of the credits, granted by the bank to compensate the principal amount of the loan. According to the NBU standards, the loan loss provision is a special provision, stipulated by means of credit risks in banking [1]. The creation of provision to the credit risks is the recognition of expenses to depict the real result of the banking with the consideration of the asset quality deterioration or the increasing of the lending transactions riskiness.

But in order to get to know is the mechanism of creation of the loan loss provision quite effective to provide the credit portfolio quality, we should study the available system of banks' creation of provisions to the credit risks in Ukraine.

The volumes of provisions are defined with the consideration of the total amount of all credits, classified to the degree of risk (each degree has its own corresponding ratio in percentage terms, which represents the level of provision due to the each group). The general indebtedness on lending transactions performs the gross credit risk for the creditors. To calculate the loan loss provisions we should define the net credit risk, by means of reduction of the gross credit risk on the value of the acceptable collateral.

The criteria for the credit portfolio classification according to the group of risks are: 1) the borrower's financial position; 2) the condition of his loan debt operation; 3) the level of the lending transaction provision. In accordance with those criteria, the entire bank's credits due to the current standards of the NBU are divided into prime and nonprime ones. The prime loans are granted to the borrower with stable financial standing and good outlook, which repays the principal and interests at fixed dates. For such of loans, the general loan loss provision, amounting to 1% of net credit risk is formed. The second group of provisions is formed for the nonprime loans, including such subgroups:

- credits under control, granted to the borrowers with stable financial position, but with the shady perspectives, concerning further development, and having the past-due indebtedness (up to 90 days), that is to say, the credit risk is insignificant, but can increase. The level of provision on such credits is 5%;
- sub-prime loans, granted to the borrowers with satisfactory financial position but having tendency toward deterioration and if the past-due indebtedness is no more than 90 days. At that, the credit risk is significant. Provision ratio for this group is 20% of the net credit risk;
- problem loans, granted to the borrowers with bad financial standing and cyclicity in development. Past-due indebtedness can be more than 90 days. Provision ratio for this group is 50%;
- loss loans, granted to the borrowers, financial and operational activity of which says about the losses and the impossibility of repayment of the principal amount of the loan and interests, concerning it. Provision ratio for this group is 100%, that is to say, the risk on such transactions corresponds to the full amount of the credit indebtedness.

The creation of provisions should be done every month comprehensively in spite of the level of income. Provision to the credit risks is used only to compensate the borrowers' outstanding debt on lending transactions due to the principal amount of the loan, where the indebtedness recovery is impossible. The loss credit indebtedness is written off by the bank by means of provision due to the non-prime indebtedness, according to the bank's decision.

Well then, the main task of the creation of loan loss provisions should be the promotion of the banks to manage their credit portfolios in order to improve the credit portfolios quality and reduce the risk of the probable losses through the nonredemption of loan. And in spite of the imperfection of this mechanism, we may consider that nowadays, such problem as permanent discrepancy of their predicted and actual magnitude is solved (such problem was peculiar in our country in 1990-s). (table 1).

As we can see in the table, during last three years the banks meet all the requirements, concerning creation of provisions in full size. Even in spite of the tripling of the troubled assets with the beginning of the financial crisis in 2008, the provisions on active bank operations were completely formed. But, the increasing of the problem loans volumes depicted only the general trends of the increasing of the amount of credit portfolio in Ukrainian banking institutions. In fact, the relative indexes of the problem loans ratio in the general structure of the credit portfolio show the steady dynamics of their reduction from 11% at the beginning of 2001, to 1,3% at the beginning of 2008. And only with the beginning of crisis phenomena the increasing trend of this index took place, which during the nine months of the year 2009 was nearly 7%.

It means that the practical events, concerning lending transactions management were performed according to the peculiarities of the relationships with every borrower, the main parameters of whom (financial standing, possibilities of quality provision, the level of the credit reimbursement) enable to refer one or the other credit to the specific risk category, which defines the credit portfolio quality. Under such conditions, the commercial bank gets only that credit portfolio, which is made due to the realization of agreements with different borrowers on the base of the individual attention to each of them. As a consequence, the disadvantage of the banking lending transactions is the availability of the great volume of the doubtful, past-due, uncollectible debt in the structure of the credit portfolio of Ukrainian banks.

Table 1

**The dynamics of the credit portfolio volumes and provisions of the Ukrainian commercial banks (mln. hryvnia)**

№	The title of index	1.01. 2001	1.01. 2002	1.01. 2003	1.01. 2004	1.01. 2005	1.01. 2006	1.01. 2007	1.01. 2008	1.01. 2009	1.09. 2009
1.	Credit portfolio	23637	32097	46736	73442	97197	156385	269688	485507	792384	755355
2.	Problem loans (doubtful and overdue)	2679	1863	2113	2500	3145	3379	4456	6357	18015	51418
3.	The ratio of the problem loans in the credit portfolio, %	11,3	5,8	4,5	3,4	3,2	2,2	1,7	1,3	2,2	6,8
4.	Provisions on active transactions of the bank	2737	3194	3905	5355	7250	9370	13289	20188	48409	95447
5.	The interest of implementation of the creation of provisions, %	61,5	85,4	93,3	98,2	99,7	100,1	100,1	100,04	100,1	100,08
6.	Loan loss provision	2336	2963	3575	4631	6367	8328	12246	18477	44502	79820

Source: Herald of NBU. – 2009. – №10. – P. 68.

As a result, concerning the current methodology of the calculation and creation of loan loss provisions, the bank should assume measures to improve it. In fact, the available scientific researches mainly depict the affirmation of the existed mechanism of creation of corresponding provisions [2, 3, 4]. That's why, the first thing, we should mention some problematic aspects of this methodology and ways of solving them to increase the credit portfolio quality of the commercial banks. Those aspects are the next:

Firstly, the order, stipulated by the statutory act of the National Bank of Ukraine, according to which the creation of provisions in accordance with some types of lending operations is not performed (according to financial leasing transactions, if the target of the operation is real estate; according to the funds, which are placed by the bank on conditions of the subordinated debt; according to the credit off-balance sheet liabilities, where the bank shouldn't grant funds as first counterparty's request), and is not always suitable to the available conditions, inasmuch as not all the mentioned transactions are always without risk, as a result, the bank should assume the corresponding measures for creation of provisions.

Secondly, whereas the provisions should be created considering the development of one or the other trends (both positive and negative), we should indicate that in the current methodologies of the credit risk evaluations, a little attention is paid to such important element as the forecasting of the probable change in the financial position, ability to meet payments, and credit capacity of the borrower. As a result, the improvement trends of the settlement procedure of the individual credit risk should be based on the implementation of the different methods concerning cash flow valuation of the bank's customers and forecasting of its change for the future.

Thirdly, the individual attention in evaluation of the credit risks doesn't enable to consider the probable valuation changes and probability of loss according to the group of borrowers or credit portfolio as a whole. The question is about the situation, when the general macroeconomic development trends in the economic conditions can have the same consequences in the plan of riskiness for the borrowers of the one group (while granting the consumer credit or while credit financing of the small business). At that time, the individual evaluation of the credit risk to calculate the provisions by virtue of the small volume and great number of such loans can be time-taking. That's why the evaluation of the credit risk according to the groups of provisions of crediting in conditions of their suitable classification can be quite effective, considering the possibilities of the bank expenses.

The fourth, the amended in 2003 procedure of creating of provisions under the standard indebtedness, according to which the cash reserve ratio was reduced from 2 to 1%, can be considered as feasible. Because of the fact that the given provisions are created in order to be considered while realization of the lending transactions, probable undesired events, concerning the whole economy of the country, the reduction of the ratio was depicted by means of the too opti-

mistic look on the aspects of the economic development, without consideration of the difficulties of the transition period which still take place in the economy of our country and influence on the borrowers' activity. The given provision should be created to minimize the losses by virtue of the external preconditions for the non-redemption of loan by virtue of one or other macroeconomic trends on the market or political events even if there is no any concern about the borrower's lending capacity.

The fifth, the facilitating mechanism in the process of the credit classification for the creation of provisions has some disadvantages. In particular, the question is about the fact that the provision in different forms (guarantees and collateral) is one of the crucial factors, which are considered during the classification of credits according to the group of risks, which influence on the amount of the created provisions. At that, the requirements of the NBU note that in order to calculate the provision, the amount of the gross credit risk on every lending transaction can be reduced on the value of the accepted collateral. But if the value of the subject of collateral is defined by the bank's whole crediting according to the market value, under conditions of unstable market situation on the real estate market as well as the absence of the positive methodologies of the appraisal of property we can't insist that the corresponding collateral can be the means of reduction of the gross credit risk in order to calculate the corresponding provisions. The solution of the problem should be based on the change of the approaches in the current methodology concerning calculation of the loan loss provisions. The question is about the mechanism of the creation of provisions, which is based on the evaluation of the borrower's financial standing and level of the redemption of the earlier got loans as well as reduction of the interest of hypothecation value, which is considered while the calculation of the net credit risk. It is clear, that ratio of 100% is not acceptable here even in case of the standard indebtedness.

Well then, the solution of the problem aspects in the current methodology of the creation of loan loss provisions should be based on the rising of the credit risk quality in the relationships with the borrowers to distinguish strict requirements in the developed ratios of the NBU, concerning creation of provisions in conditions of financial crisis.

But, the creation of the corresponding provisions is one of the trends, concerning minimization of the credit risk, emerged in the process of the credit portfolio creation. We must understand that a great number of problems in the banks' credit activity (high risks in the investments to the real sector, the low rates of the structural transformations, the investment unpleasantness of the enterprises, the lack of the information, concerning their financial position, the insufficiency of measures, concerning the legal protection of creditors, etc) require to set tasks, concerning optimization and management of the credit portfolio.

## Conclusions

The results of the evaluation and analysis of the credit portfolio on the base of the elements of the facilitating mechanism of its quality enable the bank to reconsider the credit policy and adjust the credit portfolio structure. First of all, the question is about the development of the new conditions for the granting of new loans, setting restrictions on the loans, with the consideration of the condition in the certain branch of economy, district peculiarities and type of borrower, increasing of the provisions to cover the credit risks, development of the procedure of credit's charge-off, elaboration of technology for the repayment of the problem loans, reconsidering of the policy of the credit reimbursement in the part of the usage of collateral, guarantee, warranty, insurance, optimization of the order of decision-making, concerning granting credits.

So, the usage of the feasible elements of the facilitating mechanism of the credit portfolio quality and credit risk management can be considered as an important condition for the realization of the strategic goals of the commercial bank's credit policy in the plan of satisfaction of the market needs, concerning different types of credits and providing of the corresponding competitive positions of the bank to minimize the risks on lending transactions and realize profit. Practical realization of events, concerning creation of the loan loss provisions can promote the credit cooperation between banks and the real sector of economy which is very important in overcoming of the crisis phenomena in economy.

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