
THE ANALYSIS OF THE ROMANIAN BANKING SYSTEM EVOLUTION IN THE IMPORTANT MILESTONES FROM ITS HISTORY

SBÂRCEA Ioana

Lucian Blaga University of Sibiu, Romania

Abstract:

One of the national systems most often marked by various internal and international macroeconomic evolutions over time was the banking system. In this paper I intend to analyze the main developments of the banking system in the outstanding moments in its history, starting with a brief characterization of the banking system before 1990, moving then towards an analysis of the developments recorded in the watershed years (1992, 1998, 2007) and getting to the current situation using several representative indicators. This analysis allows me to place in historical and current coordinates, the subject of a more extensive research aimed at highlighting the impact that Basel III will have on Romanian commercial banks.

Key words: *banking system, solvency indicator, non-performing loans*

1. Introduction

This work is part of a broader research approach that aims to end an impact study regarding the implementation of Basel III Agreement in the Romanian commercial banks; a study that cannot be achieved without a dynamic placement of the Romanian banking system in the current coordinates, an aspect that I am following through this work.

The Romanian banking system has had to face many challenges throughout history, challenges that have taken into account both the national and international financial-economic context. In this paper I propose to realize an analysis of the turning points in the evolution of the Romanian banking system, starting from a short presentation of the outstanding moments before 1990 and then continuing with an overview of some indicators which I consider relevant in the evolutionary analysis of the banking system in 4 years that I consider outstanding, respectively, 1992, 1998, 2007 and 2012.

2. Approach of the outstanding moments in the evolution of the Romanian banking system before 1990.

The banking activity, both nationally and internationally, has appeared as a double necessity on the part of those who made savings and storage their wealth, and on the other side on those who lacked wealth looking only to satisfying their needs.

Regarding the Romanian banking activity, its emergence is related to the activity of the money-changers who began buying and selling currencies in order to achieve gains (Dardac, N, Vascu, T., ASE Digital Library). As the trade, the economic relations were developing, the money-changers have developed lending activities, the lending principle being one which has been preserved until today, and that was that money could be borrowed only in exchange for an interest at the time called usury (the money-changers turning to moneylenders). However, what determined for a banking system to be created, that required a general framework for banks to operate, was the level at which usury reached, namely from 12% -24% at the beginning of lending activities to much higher levels, with development of the usurious activities. The level of the interest rates has led to the impoverishment of *those seeking such loans, from peasants to landowners, and even treasure clergy*. The interest could be even paid in nature, in work or in products by the customers from rural areas, for these recording the highest level, up to 300%. In a more difficult situation were the peasants who were allowed to have only one creditor in the person of their master on whose land they had their household. (Pintea, A., Ruscanu, G., 1995). The beginning of the nineteenth century was marked by a series of banking projects in major regions of Romania, projects that drafted banking activity as being mainly an activity of depositing values, discounting (purchasing bills before maturity) and crediting.

The first project that was done was the creation of the first credit institution in 1864, respectively the **Savings and Records House** that had an activity geared towards attracting financial resources from the public and placing them in government securities. The following years were characterized by the opening of more banks with local capital, namely: the Romanian Bank (1865); Albina Bank (1872), The Land, Rural and Urban Loan (1873-1875), the Marmorosch Bank (1874).

A highlight moment of the Romanian banking system evolution was on *July 1, 1880*, when based on a project initiated by the Finance Minister at that time, IC Brătianu, the **National Bank of Romania** began its work with a majority private capital.

The following period was characterized mainly by a *development of the Romanian banking system*, as evidenced by the large number of bank institutions that have been opened. Thus, if in 1900, eight banks were operating in Romania, their number reached 237 in 1916, 1102 in 1930, respectively 1204 units in 1934.

In the structure of the banking system, at that time, were working both large commercial banks (Agricultural Bank, Bank of Commerce of Craiova, Romania Discount Bank, Romanian Bank, Romanian General Bank, Bank of Romanian Credit, Romanian Commercial Bank) and small credit institutions for small rural and urban households, known as the **People's Bank, cooperatives or credit unions**, which

aimed at granting loans to those with limited financial possibilities. In the year 1915, the Romanian banks were owned by banks with Romanian capital in proportion of 38.05% and by banks with foreign capital in proportion of 61.95%. Although the presence of a majority foreign capital in the banking system was beneficial for Romania, later, the externally funded banks helped to drain profits from the industrial and commercial enterprises credited by them or to which these banks held shares. (Pintea, A., Ruscanu, G., 1995).

The First World War period was characterized primarily by an increase in the social capital of the Romanian banks, in order to support the increased needs of the country.

Another turning point in the structure of the Romanian banking system was marked by the **economic crisis of 1929-1933**. This event has mainly affected the small banks and those that functioned in the countryside because the falling prices of agricultural products and reduced harvest of 1928 dramatically affected the farmers' ability to repay loans, thus limiting the banks' ability to cope with cash withdrawals from depositors. Thus, *some of the banks went bankrupt*, which caused a reduction in the number of commercial banks by 20.4%.

The Romanian economy then experienced a period of economic growth that was also felt in the banking system, which in the period 1934-1941 witnessed a significant development, reflected also by an increase in the capital of banking institutions. This period is also relevant in terms of banking law given the fact that on **May 8, 1934, Law no. 70 for the organization and regulation of bank trading** was adopted (www.cdep.ro). The bank, according to this law, was defined as being "any commercial enterprise whose main objective is to perform any kind of operations on the amounts of money in cash on credit, on credits, on the effects of trading, on the various negotiable securities and also on any other operations related to them." Another feature of this period was the high concentration of the Romanian capital. Thus, in the year 1941, 52% of the total balance sheet assets were held by 1.8% of the existing banks (Dardac, N., Barbu, T., 2005).

The period of the Second World War was characterized mainly by the National Bank of Romania trying to conduct a healthy banking activity, while making great efforts to support both the needs of the economy and to cover up the country's war expenses.

In the immediate period of the Second World War, namely **1944-1946**, the Romanian banking system consisted of the National Bank of Romania and 232 private active banks. This system went through a period of boosting the necessary credits for reviving the key economic sectors that were devastated during the war.

The year **1947**, however, led to a fundamental change in the Romanian banking system, with the *nationalization of the National Bank of Romania*, renamed the People's Republic Romanian Bank, from that time the Romanian state became the sole shareholder, the sole decider of the way of conducting the activity of this institution. Thus, the period 1947 - 1989 was characterized by an annihilation of the competition in the banking sector, competition that has been eliminated completely

once with the nationalization of all banks that have remained in the system (in 1948 only the National Bank of Romania, the Bank of Credit Investment, Home Savings Bank were functioning, to which were added in 1968 the Romanian Bank for Foreign Trade and the Bank for Agriculture and Industry). Thus, during this period the Romanian banking system consisted of:

- The National Bank of Romania, which aimed to mobilize the resources in the economy and direct them towards the priority actions of the state;
- Specialized banks, which aimed to achieve the state policy in the financial-banking field as well as providing banking services in the following priority sectors for the economy: agriculture, foreign trade and investment.

Analyzing the key events in the evolution of the banking system until 1990, we can see that *this system has undergone a continuous process of development*, in some periods, *and adaptation to adverse economic conditions in other periods*. Thus, the banking activity was conducted at the beginning by money-changers, and then, to be carried out via more than 1,000 banks and later becoming an activity carried on only by a few bank institutions. These events have left their mark on what is today's banking system, through the lessons learned from the good things or from the mistakes that were made in the Romanian banking system over time.

3. An approach of the outstanding moments in the evolution of the Romanian banking system after 1990.

The transformations of the Romanian banking system continued after 1990, during which he had to deal with two major challenges, namely, the transition to a market economy and the accession to the European Union. In this context, I will try to show how the Romanian banking system looked like in four years that I consider relevant for the evolution after 1990, namely the year 1992 (to see how the banking system virtually looked immediately after suspending the operation of a centralized banking system respectively immediately after entering into force Law no 33/1991 on banking activity) and then 1998 (the year when the banking system starts to be regulated modernly through the banking Law no. 58/1998), the year 2007 (the year of accession to the European Union and the predecessor year of the international financial crisis) and finally presenting the current period 2012-2013 to see how the banking system looks today, after having faced a multitude of internal and international conjuncture challenges. The indicators over which I will stop in the analysis are the number of banks by social capital origin, the structure of bank assets by origin of capital, the share of overdue loans in total assets, the solvency ratio and the share of nongovernmental loans from GDP. I chose these indicators because I consider them the most important when you want to get an overview of how the Romanian banking system has evolved in the analyzed period.

I will start the analysis from the number of banking institutions in the chosen period, namely the share of the assets according to the origin of capital in the same period (table no. 1)

Table no. 1 - Numerical and structural evolutions in the outstanding moments in the evolution of the banking system after 1990

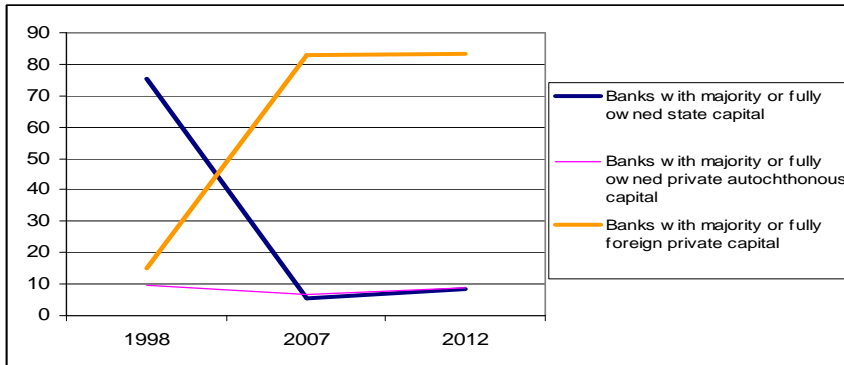
	1992	1998	2007	2012
Total number of banks from which Romanian legal persons :	12	36	32	31
- banks whose capital is fully or state majority owned	7	7	2	2
- banks whose capital is majoritary or integrally private autochthonous owned	5	13	3	3
- banks whose capital is majoritary or fully foreign owned	-	16	26	26
No. of foreign bank branches	5	9	10	8
CREDITCOOP	-	-	1	1
Total number of banking institutions in the Romanian system	17	45	42	40
Structuring the bank assets after the origin of capital (%)				
	1992	1998	2007	2012
Banks with majority or fully owned state capital	-	75,3	5,4	8,2
Banks with majority or fully owned private autochthonous capital	-	9,58	6,7	8,6
Banks with majority or fully foreign private capital	-	15,12	82,9	83,2

Source: Processing by: the Annual reports of NBR 1998, 2007, 2013 and Mugar Isaiescu – The Romanian Banking System - presentation in the Romanian Government Meeting.

Analyzing the number of banking institutions in the 4 years chosen it can be seen a significant increase between the years 1992 and 1998, from 17 to 45 bank institutions, including branches of foreign banks. This is the period when, amid the transition to a market economy the banking system took advantage of the potential that existed in the market in terms of banking activity after a long period of centralized economy, in which the banking activity could not develop. After 1998 there were no significant numerical changes, the Romanian banking system having in recent years around 40 bank institutions, with small changes from year to year depending on the number of foreign branches, which, after joining the European Union could be very easily established or abolished.

If numerically there were no significant changes after 1998, in terms of the origin of the capital, the situation was reversed in 2012 compared to 1998, meaning that the share of the bank assets owned with majority or fully by the state has been replaced almost entirely by the share of banks' assets with foreign private capital. This aspect can also be seen very well in Figure 1, where we practically see the close link that exists between the decrease in the share of state banks' assets in favor of increasing the share of private banks' foreign assets (a very high correlation coefficient of -0.99).

**Figure 1 - Structural changes in the banking system
(share of bank assets according to the origin of the capital in total assets -%)**



Source: My own processing by the data in Table 1

A relatively constant evolution during the period analyzed had the share of the bank's assets whose capital is majoritary private autochthonous owned, even though their number diminished from 5 in 1992 to 2 in 2012.

Regarding the other indicators that I have decided to analyze, namely the share of bad loans in total loans, the capital adequacy ratio (also called the solvency ratio), calculated as level 1 funds reported to risk-weighted assets (the calculation method of this indicator has varied over the period analyzed: thus in 1998, this ratio was calculated according to the Basel I provisions, which took into consideration only the credit risk in weighted assets, while in 2007 and 2012, the calculation method of this indicator complied with the provisions of the Basel II in 2004 respectively the share of the assets according to the credit risk, the market risk and the operational risk) (Sbarcea, I, 2014).

I considered these two indicators to be relevant to place them in the context of the contribution that the non-governmental loan had at the formation of the GDP, therefore in table no. 2 are also presented in addition to the non-performing loans the solvency ratio and the nongovernmental credit share in the GDP (for the year 1992, this information is not available, the NBR being at the beginning of publishing these indicators).

Table no. 2 - Evolution of indicators for assessing the significance and quality of the Romanian banking system

	1998	2007	2012
% of the nongovernmental loan in GDP	10,6	35,6	38,4
% of the nonperforming loans in total loans	16,2	2,75	20,93
The capital adequacy ratio (which should be higher than 8% according to international regulations)	10,3	13,78	14,94

Source: Mugur Isărescu - Romania: Banking System - present and future, presentation at the FINFAIR event. My own processing after the statistical section of NBR, data sets, Reports on financial stability, the financial system and its risks, statistical data used in charts, in 2011 and 2013 <http://www.bnro.ro/Seturi-de-date-628.aspx>

Analyzing the international and regional context through which the Romanian banking system has gone in the period analyzed, we can see a rampant growth of the share of the nongovernmental credit in GDP between 1998 and 2007, the economical development which Romania has known in the mentioned period, the progress made by the Romanian banking system for its integration in the European banking system, the infusion of foreign capital in Romanian banks are only three of the factors that contributed to this increase. But the growth rhythm has slowed after 2007, the onset of the international financial crisis diminishing both the momentum of the commercial banks for granting loans and also the possibility for the people and companies to contract loans.

We notice opposite developments at the share of bad loans in total loans. Thus, if in the period 1998 - 2007, the loan portfolio of the commercial banks was "cleaned", the share of the nonperforming loans to total loans reached a comfortable level of 2.75, the situation has worsened considerably since the onset of the crisis. In the period 2007-2012, due to the financial problems faced by the debit companies and due to lowering the repayment capacity of the population due to the loss of work places by many Romanian and the increase exchange rate of leu / euro, the ratio of the nonperforming loans to total loans increased by almost 8 times, the pressure exerted on commercial banks is quite high, an aspect which can explain their distrust to granting new loans. However, the banking system as a whole looks good in terms of capitalization, so that throughout the period analyzed, the solvency ratio experienced a comfortable level, which always exceeded the minimum required level imposed by the Basel agreements of 8%. A contribution in this respect had the signing in 2009 by the NBR officials of the agreement from Vienna with 9 of the foreign banks with the biggest stakes in Romanian commercial banks to maintain the level of exposure on the Romanian market in March and the solvency rate of the branches over 10%.

4. Conclusions

Looking at the overall banking system, and its dynamics, from its apparition and to the present and scoring it remarkable evolution moments, we can say that although it has been through many challenges, we can speak today of a relative stability. We can also say that the banking system has on the one hand reacted to the European and international financial and economic context, and on the other hand has aligned with the international prudential requirements, and even if it went through a major financial crisis that has left serious traces (a share of bad loans in total loans of 20.93%), it continued to maintain its soundness, through permanent capitalization and recapitalization (the solvency ratio of 14.94% being well above the minimum required level of 8%). This is the context in which the scientific research is placed through which I intend to highlight the impact that the implementation of a new agreement regarding the prudential banking regulations (Basel III) may have on the Romanian commercial banks.

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