

ASPECTS AND TRENDS OF CREDITING THE ROMANIAN ECONOMY IN LEI AND FOREIGN CURRENCY DURING THE PRE- AND POST-ACCESSION PERIODS

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A*bstract: The paper analyses the relationship between credits with denomination in lei and euro in the Romanian economy in the pre and post-accession periods, trying to highlight some structural characteristics of different types of deposits and loans from the viewpoint of interest rate levels and agreed maturity in the case of households and population. The main problem is related to the impact and vulnerabilities of predominance of credits denominated in euro in a national economy where the leu is the official currency.*

The bank lending is decomposed into lending to enterprises and lending to households in order to find out their important characteristics in an international comparative context. Which could be the optimal relationship between crediting in euro and crediting in lei?

Keywords: bank loans, credits and deposits denominated in euro versus national currency leu, vulnerabilities of euro credits, types of deposit and loan, interest rate.

JEL Classification: E43,E51, G21.

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¹ This transfer of public assets from the ownership of a State to the one of another State cannot be called "privatisation", because it does not presuppose the shift of an asset of the State from the public sector to the private one.

One of the major theoretical and practical issues of outward opening of Romania's economy, also widely disputed in the domestic and foreign literature is the **financing/crediting of the economy in the national currency and, respectively in foreign currency.**

The two crediting modalities are complementary, satisfying to various extents the financing needs of the national economy, generating equal or unequal benefits to all involved parties, or does one form undermine the other, etc. ?!

Once the negotiations on chapters of the Community Acquis were initiated in 2000 between EU and Romania, on one hand, an increased interest was shown by countries with market economy in Romania, and, on the other hand, the process of transition to a market economy continued, in particular based on promoting and, sometimes, even on imposing according to the programmes agreed with Romania by IMF or other international institutions, the privatisation of some large state entities of the processing industry, of the banking system and of the insurance or utilities ones. It is obvious that the cases of privatisation "at any price" weren't acknowledged, nor will they ever be officially acknowledged probably, as they were non-transparent, imposed by interests from abroad or domestic ones, despite their onerous or disqualifying character for the Romanian state, which declined, practically, its competence by entrusting through ownership transfer¹ its assets of strategic significance to other Member-States of the EU. In the favourable economic context generated by Romania's pre-accession to the EU, within the banking system of our country important structural changes occurred regarding the proportions and relationships between banks with foreign capital and the ones with either public or private domestic capital.

Table 1. Structural indicators of Romania's banking system

	2005	2006	2007	2008	2009	2010	2011	2012
1	2	3	4	5	6	7	8	9
1. Number of credit institutions	40	39	62	43	42	42	41	41
2. Number of banks with majority foreign capital	30	33	36	37	35	34	34	34
3. Weight (%) in total assets of banks with foreign capital	62.2	88.6	88	88.2	85.3	85	83	81.2
4. Weight of the first five banks in total assets	58.8	60.3	56.3	54.3	52.4	52.7	54.6	55.2

Source: Financial Stability Report, NBR, 2012.

In the pre-accession period 2005-2006, the number of banks in Romania increased from 30 to 37, and the weight of their assets in total assets from 62.2% to 88%, and in the **post-accession period** (2007-2012) a diminution occurred both in the number of foreign banks to 34 and in their weight to 81.2% from total banking assets, as a result, in particular, of the negative impact of the economic and financial crisis. We would like to emphasise that both in the pre-accession period and in the post-accession one, the weight of the foreign capital within Romania's banking system was very high, which indicates, at least for a certain period, the operation of foreign banks' subsidiaries in Romania under very profitable conditions.

The banking system of Romania is currently **dominated by the subsidiaries of five large foreign banks** which in 2012 held a weight of 55.2%, as the remaining assets are distributed between several banks of relatively small size and modest financial power.

One of the issues of the banking strategy and policies at the level of the entire national economy refers to the share of domestic and foreign banks in the banking capital market in Romania.

In our opinion, this share is important, in general, especially during critical periods of the national economy (for instance, in a crisis), when banks with Romanian capital, either private or State capital, must and should play a larger role in solving the difficult issues of the economy, as compared with foreign banks that have an interest in the host country to make profit "at any price", the effect of "spillover" (positive externalities) being considered only a factor for increasing the own profit generation potential of the respective banks.

In other words, the predominance of foreign banking capital in Romania is a general characteristic of all developed or developing economies, or is our country next to other countries one particular case...?

To this end, we resorted to an international comparative analysis (Table 2) regarding the market share and the number of foreign banks in some EU member countries, in order to find similarities and peculiarities.

Table 2. Market share and number of credit institutions with foreign capital

Country	Market share (%)	Number of credit institutions	Country	Market share (%)	Number of credit institutions
1	2	3	4	5	6
Romania	81	41	Italy	11	105
Austria	19	28	The Netherlands	13	63
Bulgaria	76	10	Poland	65	45
Czech R.	84	17	Portugal	21	37
France	9	92	Slovakia	92	25
Germany	10	69	Spain	10	135
Greece	21	...	Hungary	60	30

Source: Financial Stability Report 2012.

From Table 2, we can draw the following important conclusions:

- in EU developed member countries, the weight of foreign banking capital varies between 9% and 21%, that is **minority** weight, which means, ipso facto, a **comfortable majority** of the national banking capital (public and/or private);
- on the contrary, in the new EU member countries, the foreign banking capital accounts for 60% and 92%, the **domestic banking capital being in the minority**;
- in Romania and Slovakia, the foreign banking capital is predominant quasi-exclusively.

The causes and effects of the existence of such **discrepancy** (dissimilarity) between old and new member countries of the EU constitutes a research field as challenging as it is useful for substantiating strategies and policies for sustainable national development at the interface with the globalisation and integration processes. This holds true, in particular, if we consider that the so-called "institutional convergence" is pursued next to actual and nominal convergence of the EU Member-States' economies. Should this convergence not be manifest also in the field of institutional-banking structures?

The subsidiaries in Romania of the foreign parent-banks which hold the overwhelming majority of the banking assets certainly pursue first to satisfy the crediting, profitability priorities and expectations, and the dividends imposed by the parent-banks and, only then the general interests of sustainable development of the Romanian economy.

The predominance of foreign subsidiaries on the banking market in Romania taking any opportunities for obtaining high profits (probably, most of them are transferred abroad) has the additional inconvenience for Romania that any time

they might cease crediting or operating in Romania if they no longer achieve high shares of profitability as obtained especially before the crisis. The losses “claimed” by many subsidiaries of foreign banks in Romania during the post-accession period represent a threat for the financing of the national economy, but also a reason for transfer to other countries.

In conclusion, we consider that the development of a **banking system with Romanian domestic capital must be a priority of the economic and financial policies** of the Executive, considering that currently the quasi-exclusive weight of foreign banks' subsidiaries within the Romanian economy presents also a series of uncertainties and vulnerabilities, shown especially during the extended period of crisis in our country, when it is more necessary than ever to have sustainable financing of the national economy, which during the period between the two World Wars of capitalist economy had an important number of banks with Romanian capital.

Also, the easy answer given frequently by some leaders whenever the issue of creating banks with Romanian capital is raised – that is, lack of capital! – must be reconsidered. This reason rather proves the lack of professionalism, of responsibility, interest and entrepreneurial spirit for promoting the creation of banks with domestic capital in a country of Romania's size, and economic and social potential. For the time being, the current structure of the banking capital in Romania is faced acutely with large under-financing problems of the economy by credit. Additionally, we mention that in pre-war Romania there was a large number of banks with Romanian capital specialised in fields of activity, next to those with foreign capital.

1. Structures and peculiarities of crediting in Lei and Euro

Considering that Romania's option for a competitive, institutionalised and market economy open towards the world economy, to accession to the EU and to the Euro Area turned into a priority of the economic and social strategy, the full conversion of the national currency (Leu) was one of the first measures for translating into practice the respective option, even if some experts underpinned the fact that our country does not meet the conditions for a transition to full convertibility of the Leu.

Romania's accession to the EU in 2007, after a preparation period of association of 5 years (1995-2000) and a pre-accession period of 6 years (2000-2006) constituted a moment of particular importance for the transition economy. The vast majority of the population (about 80%) was in favour of the integration, hoping that Romania will have a series of favourable premises for achieving its

major objectives of entering the trajectory of sustainable development. Moreover, the EU integration was regarded by many Romanians and especially by decision-makers as a factor of economic and social progress in accordance with the principles of equity, cohesion and social inclusion, of the knowledge- and sustainability-based society, according to the strategic objectives of the EU.

Romania's efforts to European integration aimed at developing the private sector within the economy (by selling state-owned enterprises to foreign and Romanian investors and by creating new private enterprises), promoting direct foreign investments and creating competitive market institutions, among which banking institutions aiming at macroeconomic stabilisation, along with financing investments for overcoming the crisis and re-launching growth.

The transition to full convertibility of the national currency, elimination of state monopoly on foreign trade and promotion of an external opening policy of the Romanian economy represented important steps with respect to the possible denomination in Lei and foreign currency of the various economic, financial and monetary operations, the propensity of the population for savings and consumption in Lei and foreign exchange (in particular Euro after the creation of the Monetary Union).

From 1996 to 2000 Romania faced a new economic decline, after the years 1990-1993 when there was a decline accompanying the beginning of the transition to market economy, associated with galloping destabilising three-digit inflation. This unfavourable evolution of the national economy diminished the confidence in Leu the preference of the population of the companies turning for foreign currency, in particular the US Dollar, including crediting and bank deposits.

Table 3. Structure of non-governmental credits in Lei and free convertible currency in the period 1995-2000

Years	Total non-governmental credits, of which:	Denominated credits	
		In Lei	In free foreign convertible currency
1995	100.0	70.4	29.6
1996	100.0	63.1	36.9
1997	100.0	45.2	54.8
1998	100.0	41.0	59.0
1999	100.0	42.4	57.6
2000	100.0	40.5	59.5

Source: Own calculations based on NBR data.

Thus, if in 1995 and 1996 the non-governmental credit (for population and private companies) was granted predominantly in Lei (Table 3), as of 1997 internal credits granted in free convertible currencies, mainly in US Dollars and Deutsche Marks held the majority volume, **their weight increasing from 54.8% to 59.5% in total credits volume in 2000**. Thus, in Romania, even before the adoption of the European Monetary Unit (Euro), the crediting in foreign currency turned dominant within the national economy.

The question which arises naturally is to what extent is the crediting in foreign currency more advantageous than the one in Lei, the official national currency, intended to fulfil entirely the functions of money? A first answer can be found in the difference between the high interest rates of loans in Lei and the relatively low ones of loans in foreign currency, especially when the inflation “melted” down sensibly the purchasing power of the Leu. Yet, such an answer did not take into account the risk that might be represented by the evolution of the exchange rate in favour of a value increase of the foreign currency against the Leu.

Table 4. Non-governmental credits, denominated in Lei and foreign currencies, 2008-2013

- bill. Lei, end of the period -

Period	Total	%	Denomination currency							
			Lei	%	Euro	%	US Dollar	%	Other foreign currencies	%
2008	234.1	100.0	83.7	35.3	131.2	56.0	7.8	3.3	12.4	5.3
2009	238.1	100.0	81.9	34.4	137.7	57.8	5.9	2.5	12.6	5.3
2010	253.7	100.0	85.7	33.8	149.4	58.9	5.7	2.2	12.9	5.1
2011	276.4	100.0	92.9	33.6	163.2	59.0	7.3	2.6	13.0	4.7
2012	286.1	100.0	98.9	34.6	167.6	58.6	7.0	2.4	12.6	4.4
2013 March	285.9	100.0	99.2	34.7	167.6	58.6	6.6	2.3	12.4	4.3

Source: primary NBR data and own calculations.

The weight of internal non-governmental credits in foreign currency was 62.5% in 2013, March, against 64.6% in 2008, showing a slight decreasing trend along with the **increasing trend of crediting denominated in Euro** from 56.0% to 58.6% (Table 4). During the same period there was a slight decrease in the weight of crediting in Lei and US Dollars.

Thus, in Romania, the crediting with the highest weight in the total volume of non-governmental credit is held by credits with denomination in Euro and other foreign currencies

The question which is partly rhetorical is whether this situation is or isn't (!) in contradiction with a "golden rule" of crediting according to which the grant of credits **must be done in the currency** in which the population and economic agents achieve mainly their incomes. For the time being, the incomes, to their largest extent, in Romania are realised in Lei, with all the functions of the moneys, and crediting is done mainly in Euro which we don't know very well whether officially or not, started to gain the functions of moneys in Romania in "competition" with the Leu but without having the legal prerogatives to this end.

Table 5. Types of non-governmental credits for non-financial beneficiaries denominated in Lei and foreign currency, on short-, medium- and long-term, Dec.2009 - Dec.2012

- bill. Lei, end of the period -

Type of credit	Dec. 2009	%	Dec. 2010	%	Dec. 2011	%	Dec. 2012	%
Total credits, of which:	246.6	100.0	270.6	100.0	293.9	100.0	304.7	100.0
• Total private sector, of which:	199.8	81.2	209.2	77.3	223.0	75.9	225.8	74.1
TOTAL CREDITS IN LEI, of which:	79.7	32.3	77.3	28.6	81.6	27.8	84.7	27.8
• Short term	26.0	10.5	25.7	9.5	30.1	10.2	33.4	10.9
-non-financial company	20.8	8.4	20.5	7.6	24.1	8.2	27.6	9.0
-households	4.5	1.8	4.6	1.7	4.5	1.5	4.9	1.6
• Medium term	19.5	7.9	19.3	7.1	19.5	6.6	22.1	7.3
-non-financial company	9.9	4.0	10.0	3.7	10.7	3.6	11.3	3.7
-households	9.0	4.0	8.6	3.2	8.5	2.8	10.4	3.4
• Long term	34.0	13.8	32.3	11.9	32.0	10.8	29.1	9.6
-non-financial company	8.4	3.4	9.3	3.4	9.7	3.3	9.7	3.2
-households	25.2	10.2	22.6	8.4	21.9	7.4	18.9	6.2
TOTAL CREDITS IN FOREIGN CURRENCY, of which:	120.1	48.7	131.9	48.7	141.3	48.1	141.1	46.3
• Short term	19.7	7.9	20.1	7.4	22.6	7.7	21.3	6.9
-non-financial company	18.6	7.5	19.0	7.0	20.9	7.1	20.7	6.8
-households	0.8	0.4	0.9	0.3	1.4	0.5	0.4	0.1
• Medium term	20.4	8.3	23.3	8.6	24.8	8.4	24.7	8.1

Type of credit	Dec. 2009	%	Dec. 2010	%	Dec. 2011	%	Dec. 2012	%
-non-financial company	16.6	6.7	19.9	7.4	21.4	7.3	20.5	6.7
-households	3.0	1.2	2.8	1.0	2.7	0.9	3.4	1.1
• Long term	79.9	32.4	88.4	32.7	93.8	31.9	95.0	31.2
-non-financial company	21.7	8.7	25.6	9.4	28.3	9.6	28.5	9.4
-households	57.5	23.7	62.3	23.0	65.0	22.1	66.1	21.7

Source: NBR data, Monthly Statistical Bulletin, April 2013.

From the total volume of credits granted by the banking system in Romania, about 74% were in the year 2013 for the private sector, of which 27.8% in Lei, and 46.3% in foreign currency (Table 5), which highlights a decreasing trend against the year 2009, when the following weights were registered: 81.2%; 32.3%; 48.7%.

In the case of credits in Lei and foreign currency, long-term crediting held the highest weight, in 2012, for households, 6.2% and respectively 21.7%, while non-financial companies held **higher weights for short- and medium-term crediting**. This weight difference highlights the fact that the activities within industry, in particular within the **processing industry and the infrastructure benefit to smaller extent from long-term crediting**, which is absolutely necessary for investments with a realisation term of over 5 years. Long-term crediting is riskier, reason for which the banks show reluctance to denominate it in Euros and not in the Lei. Hence, it is necessary to make a comparison between **the advantages and vulnerabilities for each type of crediting denomination in Romania**. As far as we know, several prestigious experts warn about the “vulnerabilities of crediting with denomination in Euro, promoting at the same time the Lei credits¹.”

For better understanding the issue concerning the ratio of credits in Lei to credits ones in foreign currency, we shall analyse the non-governmental crediting in Lei and Euro in Romania by types of borrower on various time horizons and

¹ The ‘Financial Stability Report 2012’, NBR, p. 102 mentions that “vulnerabilities included by the high level of foreign currency lending were maintained, but perspectives suggest a certain improvement as a result of harmonised implementation at the EU level of the recommendations of the European Systemic Risk Bank (ESRB) regarding foreign currency lending, and also due to the increasingly imperative necessity from a macro-prudential perspective of diminishing the mismatch between banks’ assets and liabilities by currencies.

depending on the size of the interest rate. The analysis refers to data from the post-accession period 2009-2012.

In the case of short-term credits in Lei, the non-financial companies held a weight of 8.5% against only 1.7% for households. This underpins the fact that banks grant more short-term credits to non-commercial companies for payments and cashing between enterprises, which are safer and profitable.

On the contrary, **long-term credits in Lei and foreign currency** prefer as beneficiaries the population households for building and repairing real estates, buying consumer goods, etc.

Table 6. The annual average weight in total credits of non-governmental credits denominated in Lei and foreign currency on short-, medium- and long-term, non-financial companies and households, Dec. 2009-Dec. 2012

Type of credit	Annual average weight Dec.2009 – Dec.2012 (%)
Total credits, of which:	100.0
• Total private sector, of which	77.1
TOTAL CREDITS IN LEI, of which:	29.1
• Short-term	10.3
- non-financial company	8.3
- households	1.7
• Medium-term	7.2
- non-financial company	2.9
- households	3.3
• Long-term	11.5
- non-financial company	3.3
- households	8.2
TOTAL CREDITS IN FOREIGN CURRENCY , of which:	47.9
• Short-term	7.5
- non-financial company	7.1
- households	0.8
• Medium-term	7.9
- non-financial company	0.4
- households	7.5
• Long-term	32.1
- non-financial company	9.3
- households	22.8

Source: Own calculations based on primary NBR data.

2. Deposits of population and non-financial companies in the period 2009-2012

One of the main sources of crediting economic agents in Romania is represented by the bank deposits of the population and of non-financial companies in Lei and foreign currency.

The volume of banking deposits depends on the interest rates for various categories of deposits and on the level of the savings realised by the population and the economic agents.

**Table 7. Bank deposits of population and non-financial companies,
2009-2012**

- bill. Lei, end of the period -

	Period				
	Dec. 2009	Dec. 2010	Dec. 2011	Dec. 2012	March 2013
Total, of which:	167.7	177.4	187.2	197.2	200.8
- Lei	102.6	113.4	124.5	125.4	127.4
- foreign currency	65.0	63.9	62.7	71.8	73.3
Population					
Total	97.3	104.1	112.7	122.2	125.8
- Lei	59.1	64.2	72.0	74.7	76.9
- foreign currency	38.1	39.8	40.6	47.4	48.9
Non-financial companies					
Total	58.0	62.3	62.3	61.1	60.8
- Lei	36.4	41.5	43.3	41.1	40.7
- foreign currency	21.5	20.8	19.0	19.9	20.1

Source: NBR Monthly Bulletin, April 2013, p.28.

According to the data in Table 7, the main conclusions that can be detached with respect to bank deposits, for the analysed period, are the following:

- in total bank deposits (Lei + foreign currency) of the population and of the businesses, the highest weight is held by deposits in Lei (63.4%) against deposits in foreign currency (36.6%), this situation being completely different in the case of credits in foreign currency, which is explained by the fact that depositors in Romania realise incomes in Lei to the largest extent;
- **Lei deposits of the population** increased 1.29 times, and the ones in foreign currency 1.28 times, while for non-financial companies the deposits in

Lei increased 1.13 times, and the deposits in foreign currency **decreased** by 2 percentage points in the period 2009-2012;

- **the weight of the Lei deposits of the population** in total deposits (Lei and foreign currency) were 62.6% in March 2012 and those of the non-financial companies 37.4%, which highlights that the first source of financing bank credits is represented by population deposits, to a larger extent than the deposits of non-financial companies.;
- **the weight of foreign currency deposits of the population in total bank deposits** (Lei and foreign currency) in March 2013 was 24% and that of non-financial companies only 10%, resulting that also for foreign currency deposits the first place is held by the population.

Table 8. Structure of non-financial companies' deposits on term in Lei and Euro, for one year and over

- bill. Lei -

	Dec.2012	%	March 2013	%
Total, of which:	61.1	100.0	60.8	100.0
Overnight deposits, of which:	31.6	51.7	29.7	48.8
-Lei	22.0	36.0	20.7	34.0
-Euro	7.2	11.7	7.0	11.5
-other foreign currencies	2.3	3.7	1.8	2.9
Deposits on term, of which:	29.5	48.3	31.1	51.1
-Lei total, of which:	19.1	31.2	19.9	32.7
• one year term	18.0	29.4	18.8	30.9
• over one year	1.1	1.8	1.0	1.6
-Euro total, of which:	8.8	14.4	9.1	14.9
• one year term	8.1	13.3	8.4	13.8
• over one year	0.7	1.1	0.7	1.1

Source: NBR data and own calculations.

In the case of non-financial companies, in March 2013, deposits on sight in Lei (34.0%) exceeded by more than two times the ones in foreign currency (14.4%), ascertaining the rule of the predominance of deposits in the currency in which incomes are mostly earned. The same structure is found also in the case of deposits on term, that is, the prevalence in weight of the deposits in Lei.

Another conclusion refers to the fact that trading companies which, to their vast majority are represented by subsidiaries of multinational corporations, **do not make deposits in Euro** in Romania, but in a very small share.

3. Interest rates on credits and bank deposits

The level of the interest rates on credits has a primordial importance for re-launching economic growth in Romania, because depending on their size, investment crediting can be realised to a larger or lesser extent. As already known, without investments, overcoming the crisis and re-launching economic growth are less probable.

Table 9. Average interest rates on credits, 2008-2012

Type of credit	Years				
	2008	2009	2010	2011	2013 Feb.
Credit balance in Lei,					
-population	16.59	17.11	14.83	14.00	13.36
-non-financial companies	18.34	16.06	10.57	10.45	10.10
New credits in Lei					
-population	17.64	16.58	11.68	12.66	12.64
-non-financial companies	19.51	15.40	9.40	9.74	9.58
Credit balance in Euro					
-population	8.65	7.65	7.08	7.11	5.54
-non-financial companies	7.63	5.97	5.63	5.73	4.75
New credits in Euro					
-population	8.05	6.06	5.89	5.90	4.57
-non-financial companies	7.63	5.92	5.02	5.64	5.02

Source: Monthly Bulletin no..2/2013, NBR.

The credit interest policy is mainly **the attribute of foreign parent-banks** with subsidiaries in Romania, and to a lesser extent it depends on the demand and supply of credits inside the country.

According to Table 9, it results that:

- in the period 2008 – Feb. 2013 a **diminution** took place in the average level of the interest rates for credits in Lei by about 3 – 5 pp, and by 4 pp for the ones in Euro;
- **the level of the interests on credits to the population is higher than the one on credits to non-financial companies** (save for new credits in Euro, in the years 2011 and 2013) which can be explained by higher credit needs of the population;
- as compared to the interest rate for bank credits granted in developed countries, in Romania they are much higher.

Table 10. Average rates of interests on deposits, 2008-2012

Type of deposit	2008	2009	2010	2011	2012
Deposits balance in Lei					
-population	12.2	9.56	7.18	6.24	5.31
-non-financial companies	14.81	9.07	5.47	5.59	4.94
New deposits in Lei					
-population	15.27	9.91	7.62	6.59	5.64
-non-financial companies	16.01	9.17	5.36	5.78	5.15
Deposits balance in Euro					
-population	5.36	3.51	3.19	3.29	3.12
-non-financial companies	6.12	2.90	2.27	2.14	1.67
New deposits in Euro					
-population	6.36	3.35	3.44	3.47	3.39
-non-financial companies	6.32	2.48	2.45	2.38	1.97

Source: Monthly Bulletin no.2/2013, NBR.

From the data of table 10 it results that:

- the average interest rates of deposits in Lei are higher than the ones of the deposits in Euro;
- a diminishing trend occurred for the interest rates of the deposits in Lei and in Euro, while new deposits benefited from rates somewhat higher than balance deposits;
- against developed countries, the average rates of the bank deposits in foreign currency are somewhat higher in conditions of a larger gap between the assets and liabilities interest.

The differentiation of average rates of interest on the credits in Lei and foreign currency, granted in Romania by the subsidiaries of foreign banks is, in general, substantiated by the **higher country risk**.

This argument was completely negated by the current economic and financial crisis which led several banks from developed countries to bankruptcy while, in Romania, no large systemic bank went bankrupt. It would be interesting if, in the case of bankruptcy/insolvency of a large bank from Romania, the **protectionist-interventionist solution** would have been applied **by the state** (investment

injections by the state or purchasing shares by the state) based on the idea “**too big to fail**”.

Table 10A1 we calculate the average interest rates on deposits (new business) as a percentage per annum of households (population) and non-financial corporation in 2012 and 2013 with different agreed maturity in countries belonging to the Eurozone. It results that the level of interest rates is lower in the case of households in comparison with non-financial corporations. That is different from the situation in Romania and indicates a policy promoting deposits of non-financial corporations which have a stronger financial power.

In the case of loans to households (table 10A2), ECB **stimulates lending for house purchase** by using a lower interest rate for new business in comparison with consumer credit interest rates.

Table 10A. MFI interest rates on euro/denominated deposits from and loans to euro area residents in Eurozone (percentage per annum, end of month)

1. Interest rates on deposits (new business)

	Deposits by households				Deposits by non-financial corporations			
	overnight	with an agreed maturity of			overnight	with an agreed maturity of		
		Up to 1 year	Over 1 and up to 2 years	Over 2 years		Up to 1 year	Over 1 and up to 2 years	Over 2 years
Monthly average March-Dec.2012	0.45	2.75	2.74	2.59	3.07	1.12	2.27	2.55
Monthly average Jan.-Febr.2013	0.37	2.52	2.30	2.35	2.19	0.39	2.17	2.01

2. Interest rates on loan to households (new business)

Interest rate	Consumer credits ¹⁾			Lending for house purchase ¹⁾			
	Floating rate and up to 1 year	Over 1 year and up to 5 years	Over 5 years	Floating rate and up to 1 year	Over 1 and up to 5 years	Over 5 and up to 10 years	Over 10 years
Monthly average March-Dec.2012	5.61	6.24	7.25	3.03	3.67	3.02	3.63
Monthly average Jan.-Febr.2013	5.79	6.08	7.75	2.86	3.18	3.04	3.35

¹⁾ By initial fixation.

Source: ECB, European Commission, Monthly Bulletin May 2013.

Interest rates for non-financial corporations (new businesses) by credit size (Table 10B) show that ECB encourages especially loans of over EUR 1 million over 3 months up to 1 year and over 5 and up to 10 years.

Another interesting aspect of the size of interest rates on loans to non-financial corporations in the Eurozone consists in a policy of diminishing the level of interest rate in 2013 as compared with year 2012 for the new businesses.

Reducing the interest rate for new businesses is an important factor for overcoming the crisis and relaunching the economic growth. In Romania, as a rule, interest rates on new credits are higher in comparison with old credits.

**Table 10B. Interest rates to non-financial corporations
(new businesses) in the Eurozone**

- percentage per annum, end of month -

	Monthly average March-Dec.2012	Monthly average Jan.-Febr.2013
Revolving loans and overdrafts:	4.31	4.20
• Other loans up to EUR 0.25 million by initial rate fixation:		
-floating rate and up to 3 months	4.78	4.68
-over 3 months and up to 1 year	4.95	4.70
-over 1 and up to 3 years	4.43	4.04
-over 3 and up to 5 years	4.58	4.21
-over 5 and up to 10 years	4.13	3.66
-over 10 years	4.13	3.66
• Other loans of over EUR 1 million by initial rate fixation:		
-floating rate and up to 3 months	2.24	2.08
-over 3 months and up to 1 year	3.11	2.86
-over 1 and up to 3 years	3.29	3.22
-over 3 and up to 5 years	3.17	4.35
-over 5 and up to 10 years	3.17	2.94
-over 10 years	3.26	3.08

Source: ECB, European Commission, Monthly Bulletin May 2013.

Table 10C. Long-term government bond yield as a percentage per annum; period average

Years	Bulgaria	Czech Republic	Denmark	Latvia	Lithuania	Hungary	Poland	Romania	Sweden	United Kingdom
2012										
-Oct.	3.39	2.24	1.29	3.52	4.32	6.94	4.57	6.85	1.54	1.54
-Nov.	3.22	1.92	1.11	3.32	4.11	6.87	4.18	6.84	1.46	1.55
-Dec.	3.44	1.92	1.07	3.24	4.00	6.44	3.88	6.65	1.51	1.60
2013										
-Jan.	3.27	1.96	1.61	3.21	3.97	6.23	3.91	5.90	1.80	1.82
-Feb.	3.25	2.01	1.73	3.22	4.06	6.29	3.99	5.72	2.00	1.92
-Mar.	3.54	1.98	1.59	3.17	4.15	6.38	3.93	5.86	1.92	1.65

Source: ECB, European Commission, Monthly Bulletin May 2013.

Table 10D. 3-month interest rate as a percentage per annum; period average

Years	Bulgaria	Czech Republic	Denmark	Latvia	Lithuania	Hungary	Poland	Romania	Sweden	United Kingdom
2012										
-Oct.	1.56	0.71	0.33	0.52	0.76	6.84	4.82	5.46	1.51	0.54
-Nov.	1.45	0.54	0.30	0.54	0.73	-	4.62	5.64	1.46	0.52
-Dec.	1.39	0.50	0.28	0.53	0.70	-	4.26	5.79	1.37	0.52
2013										
-Jan.	1.27	0.50	0.30	0.50	0.53	5.80	4.03	5.71	1.21	0.51
-Feb.	1.23	0.50	0.33	0.49	0.47	-	3.80	5.60	1.19	0.51
-Mar.	1.23	0.49	0.27	0.47	0.47	-	3.48	5.10	1.25	0.51

Source: ECB, European Commission, Monthly Bulletin May 2013.

The international comparison of long term government bond yield (Table 10C) and 3-month interest rate (Table 10D) in other EU countries not belonging to Eurozone reveals that in Romania (excepting Hungary) the government bond yields are the highest what is inducing greater attractivity for foreign buyers which are beneficiaries of such a good yield in the future (5.86 per cent).

As far as the highest 3-month interest rate is concerned (Table 10D), Romania rank the second after Hungary. Usually a high level of interest rate on loans does not encourage investment and economic growth.

4. Structure of different types of deposits and credits denominated in lei and euro

In our research we try to study some tendencies and structural characteristics of deposits and credits denominated in foreign and domestic currency in order to see how one currency is replacing the other one, their ways of coexistence, competition and complementarity, why the interest rates differ by the denomination, in lei and in euro.

Table 11. Evolution of credit structure denominated in lei for economic agents and population, 2008-2013

%

	Years						Average 2008- 2013
	2008	2009	2010	2011	2012	2013*	
1. Credits with denomination in lei (rd2+rd3=rd4+rd5=rd6+rd7+rd11)	100.0	100.0	100.0	100.0	100.0	100.0	100.0
2. - current	97.8	94.4	90.2	88.6	86.8	85.1	90.48
3. - bad debt	2.2	5.6	9.8	11.4	13.2	14.9	9.52
4. - residents	99.8	99.9	99.8	99.7	99.6	99.8	99.8
5. - non-residents	0.2	0.1	0.2	0.3	0.4	0.2	0.2
6. - economic agents	48.9	49.1	51.7	54.7	57.3	51.6	52.2
7. - population, of which:	48.9	48.7	46.4	42.8	40.3	40.4	44.6
8. - consumption	45.2	45.2	34.3	31.4	28.4	28.2	35.5
9. - housing	1.9	2.1	2.0	1.9	2.1	2.4	2.1
10. - other credits	0.8	0.5	9.3	8.8	8.8	9.0	6.2
11. - others	2.2	2.2	1.9	2.5	1.9	2.0	2.1

* May 2013.

Source: Own calculation based on primary data of NBR.

Evolution of credit structure denominated in lei for economic agents and population (Table 11) over the period 2008-May 2013 highlights the following main aspects:

- a) **increasing share of delayed credits**, especially during the economic crisis years, from 2.2 percent of total credits volume to 14.9 per cent, which is reflecting a reduced capacity of payments both for economic agents and population due to general impact of the economic and financial crisis as well as to the so-called "anti-crisis measures" (25% cutting of the budgetary employees' wages, taxes on pensions) with strong negative effects on demand, noncompensated by other pro-active policies such as employment promoting;

- b) credits to residents for the whole analysed period represented 99.8 per cent as compared with 0.2 per cent to non-residents; in Romania this discrepancy means credits are not attractive to foreigners, first of all, because of the relatively high interest rates and other banking costs;
- c) credits to population registered a declining trend from 48.9 per cent to 40.4 per cent, Romania belonging to the group of developing countries which, unlike developed ones, are characterised by relatively small percentage share of household credits;
- d) consumer credits to the population dropped from 45.2 to 40.4 per cent in the total credit volume indicating a decrease of population consumption and an increase of people living under the poverty threshold.¹

Table 12. Evolution of the structure of credits denominated in free currency (euro) for economic agents and population, 2008- May 2013

%

	Years						
	2008	2009	2010	2011	2012	2013*	Average 2008-2013
1. Credits in foreign currency (rd2+rd3=rd4+rd5=rd6+rd7+rd11)	100.0	100.0	100.0	100.0	100.0	100.0	100.0
2. - current	99.2	96.9	93.4	91.6	87.8	86.2	92.5
3. - bad debt	0.8	3.9	6.4	8.4	12.2	13.8	7.6
4. - residents	99.1	98.9	98.9	98.6	98.5	98.4	98.7
5. - non-residents	0.9	1.1	1.1	1.4	1.5	1.6	1.3
6. - economic agents	46.9	47.6	49.3	50.5	50.9	49.6	49.0
7. - population, of which:	50.7	50.8	49.8	48.5	49.1	49.4	47.7
8. - consumption	31.1	30.5	28.4	25.4	23.7	23.0	27.5
9. - housing	16.7	18.6	20.6	22.3	24.7	25.7	21.4
10. - other credits	2.6	1.4	2.0	0.5	0.5	0.5	1.3
11. - others	2.5	1.6	1.0	1.0	0.8	0.9	1.3

* May 2013.

Source: Own calculation based on primary data of NBR.

¹ According EU Statistics (EU Citizens at Risk of Poverty, year 2010, www.scribd.com/doc) deprived persons in Romania have 1900 euro per year as against 10600 euro per year in Germany, 13.700 euro per year in Norway, 9000 euro per year in Italy. In Romania 23 per cent of total population faces social exclusion, of which 33 per cent for the group aged up to 17 years, 26 per cent for the age over 65 years and 12 per cent for employees in comparison with EU average of 17, 20, 19 and 8 per cent.

Table 12 data are showing some structural changes in Romania's credits denominated in free currency deserving a special attention, as follows:

- current credits in free currency diminished their share by 13 pp in total volume of credits, which represents a corresponding increase in bad debt percentage, as a consequence of the economic crisis and the austerity policy especially for the budgetary sector incomes;
- the share of residents' credits was approximately 98.7 per cent over the whole period;
- the share of non-residents' credits was extremely modest over the entire period, which is explained by non-attractive conditions for loans;
- economic agents and population have around the same percentage share of credits, economic agents exceeding only by 1.3 pp the share of population crediting;
- population credits for consumption decreased from 31.1 per cent in 2008 to 27.5 in May 2013, while credits for house purchase registered an increase by 5 pp over the period 2010-May 2013 as a result of incentives offered for young persons who build their first house.

Table 13. Evolution of total volume of credits denominated in lei and free currency, in the period 2008 – May 2013

mil.lei

	Years					
	2008	2009	2010	2011	2012	May 2013
1. Credits in lei	83746	79788	77455	81825	85079	84122
2. Credits in free currency	115360	121404	133391	143340	143272	139846
3. Relationship (2)/(1)	1.38	1.52	1.72	1.75	1.68	1.66

Source: .Own calculation based on primary data of NBR.

In Romania, the relationship between credits denominated in free currency and lei in the pre-accession period is indicating an increasing trend from 1.38 in 2008 to 1.75 in 2011 and then a decrease to 1.66 in May 2013.

We consider that the above-mentioned relationship is raising a series of theoretical and practical problems concerning the financial and monetary policies of Romania where free currency credits are 1.66 times higher than Lei credits.

Which are the vulnerability/advantages of such a relationship taking into consideration the rule according to which crediting economic agents and population has to be denominated in the currency in which incomes are generated?!

In Romania most of the economic agents' and population's credits are obtained in lei and not in euro. On the other hand crediting denominated in euro is vulnerable to national currency depreciation in relation to euro which is the predominant foreign currency in Romania. And the euro is a stronger currency than the leu.

The preference for the credits denominated in euro versus lei, explained by the apparent advantage of the interest rates can be easily undermined by the unfavourable evolution of forex as well as by pressure generated by rapidly increasing Romania's external foreign debt especially on short term, in combination with medium and long term burden. At the same time it should be taken in consideration that, in the post-accession period, in Romania many foreign debt financing sources have substantially decreased (foreign direct investment, remittances of Romanians working abroad, receipts in foreign currency from state-owned assets privatization, small capacity absorption of EU structural and cohesion funds, etc.).

Table 14. Evolution of percentages structure of deposits denominated in lei for population and economic agents, 2008-May 2013

	Years							2008-2013 average
	2008	2009	2010	2011	2012	May 2013		
1. Overnight deposits denominated in lei	100.0	100.0	100.0	100.0	100.0	100.0	100.0	
2. Economic agents	44.1	51.9	58.9	59.5	58.8	57.7	55.2	
3. Population	51.5	42.5	35.2	34.5	34.0	35.8	38.9	
4. Others	4.4	5.6	5.9	5.9	7.2	6.9	5.9	
5. Term deposits and redeemable at notice deposits denominated in lei	100.0	100.0	100.0	100.0	100.0	100.0	100.0	
6. Economic agents	35.7	25.9	25.1	23.6	21.4	21.9	25.6	
7. Population	50.8	62.5	63.2	65.3	66.9	65.4	62.4	
8. Others	15.5	11.5	11.7	11.1	11.7	12.6	12.0	
9. Overnight, term, redeemable at notice deposits and repo operation denominated in lei	100.0	100.0	100.0	100.0	100.0	100.0	100.0	
10. Residents	97.6	97.7	97.8	97.7	97.6	97.7	97.7	
11. Non-residents	2.4	2.3	2.2	2.3	2.4	2.3	2.3	

Source: Own calculation based on primary data of NBR.

Table 14 shows that, in the period 2008-May 2013, economic agents had an average share over 55 per cent of total overnight deposits, while the population contributed to more than 62.4 per cent to the total volume of overnight, term, redeemable at notice deposits and repo operations. It turns out that resident population and economic agents have the higher contribution to the internal source of financing credits in lei in the Romanian banking system. Non-residents are quasi inexistent in this regard. In other words, internal sources of bank financing are mostly stemming from Romania's residents who contribute to profit making by the bank system dominated by subsidiaries of foreign parent banks.

Table 15. Structural percentage evolution of deposits denominated in lei of economic agents and population, 2008-May 2013

%

	Years						
	2008	2009	2010	2011	2012	May 2013	2008-2013 average
1. Overnight deposits denominated in free currency	100.0	100.0	100.0	100.0	100.0	100.0	100.0
2. Economic agents	36.9	45.2	48.3	48.7	46.7	44.6	45.1
3. Population	59.9	50.6	46.2	46.3	47.4	50.4	50.0
4. Others	3.6	4.3	5.4	4.9	5.9	5.0	4.9
5. Term deposits and redeemable at notice deposits denominated in free currency	100.0	100.0	100.0	100.0	100.0	100.0	100.0
6. Economic agents	34.9	27.6	26.1	20.7	18.1	19.9	24.6
7. Population	48.5	55.7	59.9	62.4	65.8	64.6	59.9
8. Others	12.6	16.7	14.0	16.8	16.0	15.5	15.5
9. Overnight, term, redeemable at notice deposits and repo operations denominated in free currency	100.0	100.0	100.0	100.0	100.0	100.0	100.0
10. Residents	88.3	86.1	84.8	84.8	87.3	86.5	86.3
11. Non-residents	11.7	13.9	15.2	15.2	12.7	13.5	13.7

Source: Own calculation based on primary data of NBR.

As it results from Table 15, deposits of the population denominated in free currency represent the main source of funding credits by the Romanian banks, exceeding by far the contribution of economic agents.

Conclusions and recommendations

The banking system of Romania is currently in a **strong dependency relationship** with banks from the Euro Area countries that have de-intermediation plans in the following years (diminishing crediting and selling assets for rendering the capitalisation and the financing structures efficient) which could represent a risk for the banking system of Romania.

From the viewpoint of the market share, the Romanian banking system is nowadays dominated by subsidiaries or branches of foreign banks in a share of over 81% in the year 2012, the first 5 banks by size holding over 55% of all bank assets. In the developed EU countries, the foreign bank capital has a market share of 9% in France, 10% in Spain and Germany, 11% in Italy, 13% in the Netherlands, and 21% in Greece and Portugal. The discrepancy between the New Member States of the EU and the old ones with respect to the percentage structure of the domestic and foreign capital remains an open issue for the EU objectives of **real, nominal and institutional economy convergence, if we take into account the level of the interest rates**, which is smaller by 4-6 pp in the developed EU countries than in the new member countries, for credits in Euro. On the other hand, the largest part of crediting of households and non-financial/non-governmental trading companies in Romania is realised in Euro and not in lei, which is the official denomination currency of the country. From our analyses, it results that for the same amount in Euro, borrowed in developed EU countries, the interest rates are much smaller, in particular during crisis, than in the New Member States, in Romania as well, a fact that puts in unequal conditions of competitiveness and competition the two groups of countries, in the favour of the developed countries.

The explanation of this discrepancy is frequently the **country risk** (the risk margin), which is higher in the New Member States than in the old member states of the EU. But the current crisis showed, undeniably, that in Romania **no important, systemic bank went bankrupt** as against many bankrupted banks or other facing severe liquidity difficulties in developed countries.

The argument of a "higher country risk" seems to be valid rather for the large banks from countries with a mature market economy and not for Romania where

banks practice the most expensive credits and show a diligence sometimes worth of a better cause.

The expensiveness of the new credits as against the ones in the balance represents another difficulty in financing the Romanian economy, considering that in developed countries the new credits are at a very low level of the interest rate.

In the post-accession period of Romania to EU, crediting companies and population was under the threat of a negative impact of **de-intermediation** in the European area, which requires a series of measures regarding re-launching sustainable crediting in Romania, that is a stronger orientation towards the economic sectors generating higher value added or towards those most fit to change the economic growth model of Romania based on “pseudo-tertiary” growth¹.

The high level of the credit stock in foreign currency generates a series of vulnerabilities and risks that to a certain extent can be softened by measures for stimulating the new credits under more advantageous conditions for beneficiaries and safer for the banks.

The main challenging factors for maintaining sustainability of crediting for economic agents and population in Romania are:

- a) managing risks that can be generated by prevalent foreign currency credits, i.e. in Euro, in the context of manifest financial de-intermediation processes, in general, and in the Euro area, in particular;
- b) orientating the real economy financing predominantly towards short-, medium- and long-term credits, which have an acceptable level of the interest rate and of the other expenditures and banking charges.

The banks from the Euro Area have over 80% of the assets of the Romanian banking sector.

¹ By “pseudo-tertiary” growth we understand crediting first of all that side of the services sector that has weak to non-existent relationships with real economic growth and which is “predominantly speculative” or a financial bubble generator, which are apparently profitable on short-term but particularly toxic on medium- and long-term.

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