

## Impact of Financial Crisis on Lending in Romania. Analysis for the Period 2007-2012

Lavinia Maria Nețoiu<sup>1</sup>, Titu Nețoiu<sup>2</sup>, Nela Loredana Meiță<sup>3</sup>

<sup>1,2,3</sup> University of Craiova

lnetoiu@yahoo.com, loredanameita@yahoo.co.uk

**Abstract:** *Non-performing loans are a reality of Romanian economy. The period 2006-2009 was characterized by easy crediting conditions and a boom in terms of personal loans and mortgages, which were followed by the economic crisis that struck Romania and triggered the emergence of bad loans and their growth in a rhythm described as alarming. Banks, under these conditions, proceeded to refinance, to reduce on savings' interest, to reschedule the payment terms, their final aim being to reduce the number of bad loans that threaten banks' performance. Immediate economic developments tend to worsen the situation of the debts Romanians have to banks and their efforts to recover them are still higher. At present the relationship between bank and clients is characterized by a special attention given to the determination of a certain client's trustworthiness and the fact individual clients are more temperate in accessing credits, even if banks have tempting offers.*

**Keywords:** loans, crisis, outstanding, performing, caution

**JEL Classification:** G23, G32

### 1. Introduction

The economy of Romania was provided with plenty of foreign capitals before being struck by the wave of international financial crisis. The abounding external financing allowed the practice of some instalments reduced by interests on deposits and loans and at the same time practicing an average rate of interests on the interbank money market.

The financial crisis<sup>\*</sup> has revealed new dimensions of the concept of systemic risk in banking. Thus, "the risk of a chain reaction of falling interconnected institutions" (Kaufman, 1995) has expanded to include work "shadow banking system" (Dăianu, 2008) - an unregulated sector designed to avoid typical strict regulation of banks.

### 2. Impact of Financial Crisis on the Romanian Banking Activity

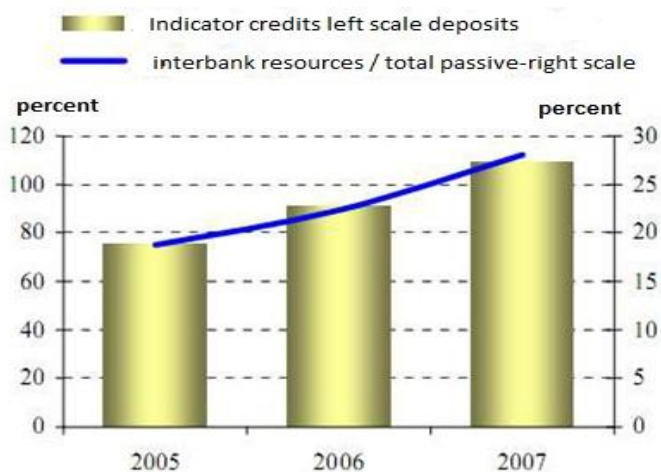
Traditionally, the effect of spill over occurs by means of two channels (De Bandt, 2000, p.18):

- *Channel exposure* - which refers to the potential for the emergence of the "domino effect", potential exposures given real interbank markets and payment systems and clearing / settlement.

- *Channel information* - which refers to the massive and contagious cash withdrawals by depositors imperfectly informed about the type of shocks affecting banks and mutual physical exposures.

In Romania, systemic risk can occur in relation to the liquidity of credit institutions as a result of widening the behaviour of banks to finance the growth strategy targeting resources interbank loans. Dynamics alert lending superior on

deposits from non-bank customers in 2006-2007 induced increase in the indicator credits deposits from 91.1% in 2006 to 109% in 2007 (Figure 2). Accordingly, the balance sheet was maintained by increasing the total resources interbank liabilities from 22.3% in 2006 to 28% in 2007, increasing at the time dependence of the Romanian banking system resources with potential for volatility. The concentration and increasing the value of their largest such increase in the time exposure of credit institutions to liquidity shocks, due to possible changes in the negative sense of institutional investors on investment prospects in the Romanian banking system. We present further indicator development loans versus deposits in total liabilities interbank share resources.



**Fig. 1.** Evolution of this indicator compared to the share loans on total deposits resources interbank liabilities

Source: NBR Stability Report 2008 ([www.bnro.ro](http://www.bnro.ro)), p. 40

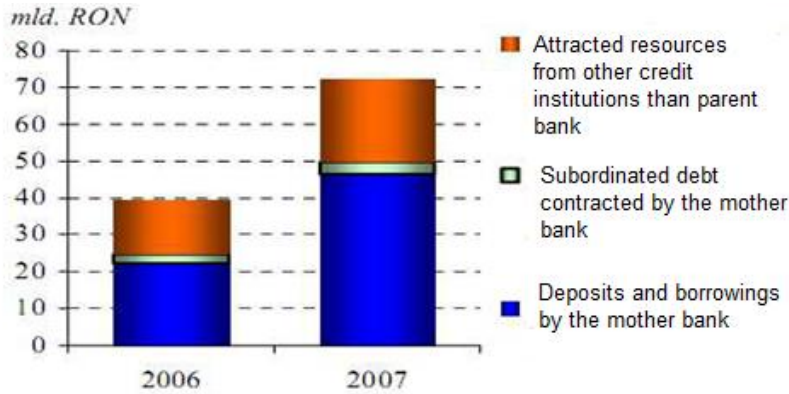
Structural analysis of interbank resources highlights the dominance of external resources, coming mainly from the parent bank. Given that the amounts taken from parent banks represented the end of 2007 approx. 70% of the Interbank resources used by credit institutions in Romania, the risk occurring was that parent banks themselves have been affected by a shortage of liquidity, which subsequently led to restricted financing subsidiaries in Central and Eastern Europe while liquidity crisis became the extremely severe, even if a significant part of their profits came from parent banks such subsidiaries.

Given that the domestic banking sector is dominated by banks in Austria and Greece, which in the period seemed to have difficulties (the first four countries where bank capital holdings in Romania in December 2007 is presented as follows: Austria (22%), Greece (21.7%), Netherlands (7.7%) and France (5%).), the severity of a possible external shock was limited at that time.

In parallel with deepening resource from parent banks, finance domestic money market has been growing. Resistance Romanian banking system domestic interbank contagion risk show that triggering a chain bankruptcy process is highly unlikely, domestic interbank bilateral exposures are generally small in relation to own funds and liquid assets creditor banks .

In addition, although the value of interbank deposits attracted by credit institutions increased in nominal terms by 82% between February 2007 and February 2008 (Figure 3) degree

Concentration of domestic interbank liabilities, calculated based on the Herfindahl - Hirshmann, decreased from 1531 bps to 1258 bps over the same period.

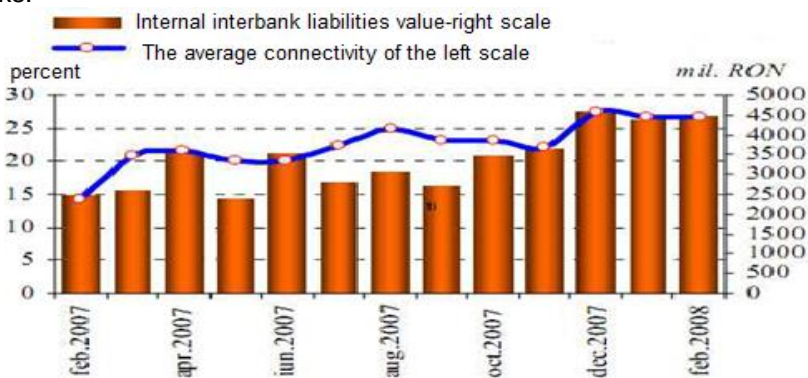


**Fig. 2.** Structural evolution of deposits from other credit institutions  
 Source: NBR Stability Report 2008 (www.bnro.ro), p. 40

This process was justified mainly by increasing interbank connectivity Internal (from 14.11% in February 2007 to 26.81% in February 2008), which allowed increasing amounts owed under the domestic interbank market diversification creditor groups. Simulation results demonstrates that the potential severity of a potential systemic shock not erode banking assets by more than one percent, even in extreme scenario assumptions, the entry into default three credit institutions simultaneously.

We present below the comparative evolution of the value of interbank liabilities related banks, Romanian legal persons and the degree of interbank connectivity.

The financial crisis officially began in September 2008 as in most banking systems in developed countries with low leverage corresponds to a high level of risk, which shows a high exposure to systemic risk. This is because banks hold risky assets in their portfolio, some of which are very toxic assets that led to the collapse of several U.S. banks.



**Fig. 3.** Comparative evolution of the value of banks' interbank liabilities related to the Romanian legal personality and level of interbank connectivity  
 Source: NBR Stability Report 2008 (www.bnro.ro), p. 41

2010 characterized by increasing VAT by 5 percent, reducing salaries by 25%, making available a large number of public sector employees, continuing economic downturn, was the year in which debts to banks soared. Another issue raised in that year is that the loan process is not restarted.

According to data provided by the central bank, credit risk remains the main vulnerability of the banking sector. NPL ratio reached 13.41% in June 2011 compared to 11.9% in December 2010 and 7.9% in December 2009. (Financial 2011 Stability Report, page 7.)

Continued economic uncertainty for 2011 and 2012, continuing economic crisis led to higher interest loans and overdue debt service inappropriately, over 90 days late, total loans and interest to sum up a share of 13.4%, so, in which the number of individual debtors, the number reached 720,000 people.

Summarizing the above, the development of non-performing loans is as follows:

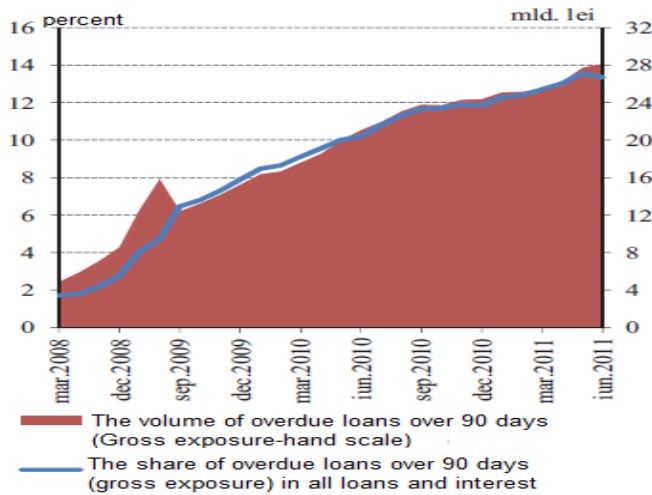


Fig. 4. NPL development, financial stability report on 2011, p. 34  
Source: NBR Stability Report 2008

During this pessimistic tone we can reassure the fact that we are not the only ones faced with such situations. We find that our neighbours Bulgaria have a similar situation, according to the chart below:

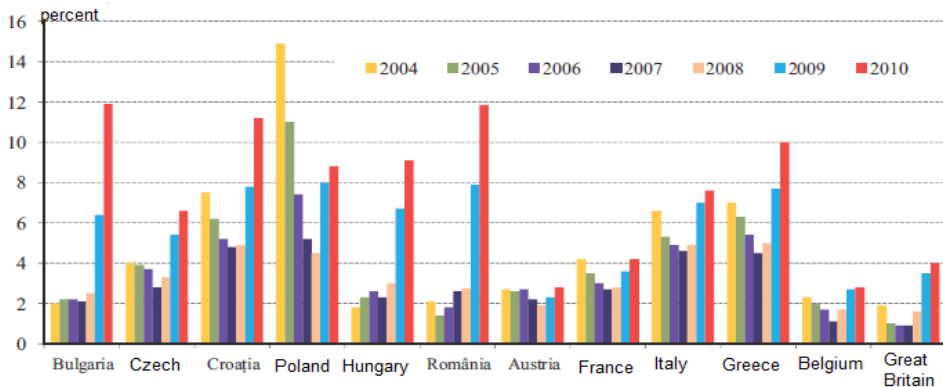
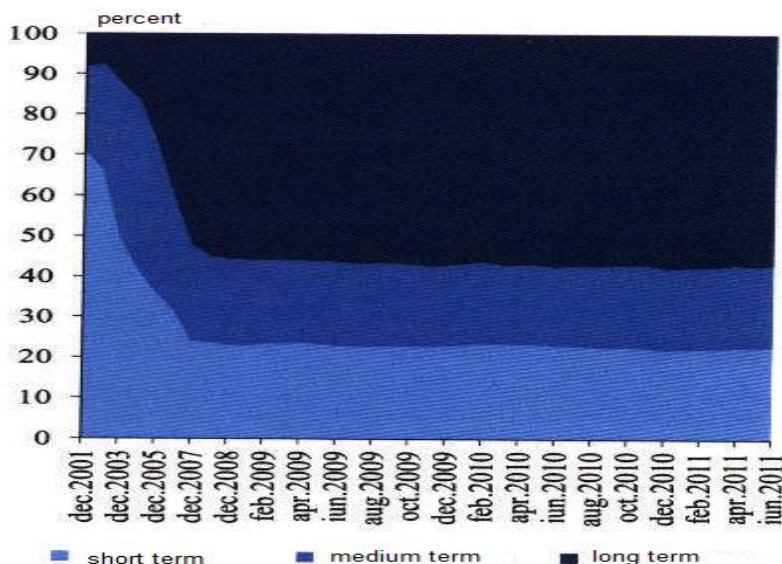


Fig. 5. Financial Stability Report on 2011, p. 48  
Source: NBR Stability Report 2008

2010 marked a marginal increase in normal terms, the volume of bank assets and non-government credit equivalent to a slight compression in real terms. Lending standards were maintained relatively unchanged for companies and households with a marginal tendency to relax for real estate loans and lending terms were slightly relaxed in 2010.

Prudence banks new loans preference for refinancing operations of existing facilities have maintained the term structure of credit to the private sector (Figure 6.). Dominant position further long-term loans (57% of total non-government credit in June 2011).



**Fig. 6.** Evolution of non-government loans by maturity, p. 43  
Source: NBR, Stability Report 2011

The volume of loans to households recorded a declining trend, while taking credit for the portfolio companies has emerged as a positive counterpart, especially in the second quarter of 2011.

We are not far from the years 2007-2009, when lending recorded a dangerous momentum, found later, when they were talking about, balkanizing Romania "and the exotic currencies for credit, like the Swiss franc. Today we have new rules on bank lending, more drastic, which provide guarantees of 133% of the loan for personal loans in foreign currency, the limitation period for all consumer credit lending to five years, a minimum down payment of 25% for mortgage loans in Euros and 40% for loans in other currencies, but we need to understand better the reality: there is a dangerous size of bad loans.

Following a cautious lending policy, banks have focused primarily on short-term financial products, which led to a progressive increase in private sector credit component with maturities under one year.

For the period June 2011 - June 2012, the main developments reported by interest rates charged by banks for loans and deposits in relation to non-bank customers can be summarized as follows:

- average interest rate on loans in lei decreased by about one percentage point compared to the same period last year;

- average rates on new loans to households have foreign currency recorded a decrease of one percentage point in the range, which encourages demand developments;
- cost deposits in lei was adjusted during the reference period, due domestic macroeconomic conditions improve. If new deposits in foreign currency, interest did not record significant changes compared with the reference period;
- net interest margin of banks operated in relation to population remains significantly lower for loans and deposits in lei from that calculated based on the balance of loans and deposits.

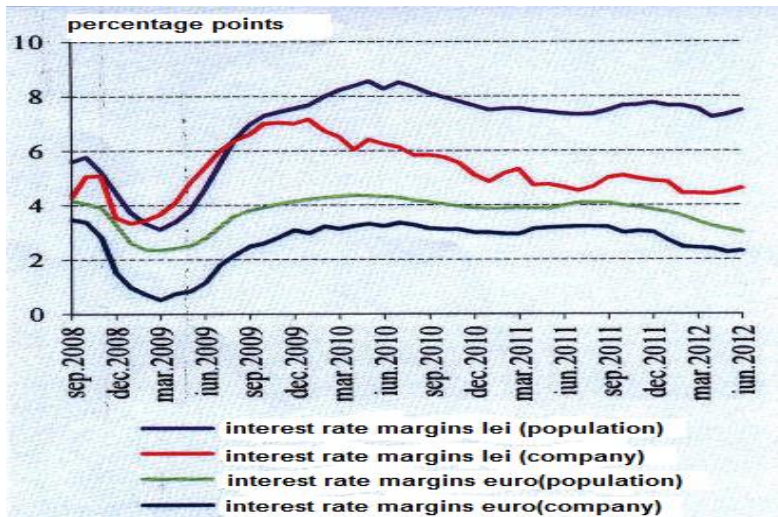


Fig. 7. Evolution interest margins on loans and deposits as Year 2013 is another year in which Romania is talking about the economic crisis.  
 Source: NBR, Stability Report 2012

### 3. Conclusions

Customers of banks, whatever their nature, natural or legal, feel this, are more reluctant when it comes to bank credit at the same time make some money.

In 2013, banks in Romania face, the heavy inheritance "of years is given credit for any" or credits, only bulletin "situations that have generated a 20% non-performing loans on the whole system bank. No further years in which people spoke, Romania balkanizing "when opening new witness and new agencies.

Who is to blame? We cannot blame just for those who contracted loans equally the fault of banks that lent too easily.

Although the U.S. announced in September 2008 that are officially in recession, the wave of the global crisis not yet hit Europe, who still enjoy the few days remaining financial tranquillity. At that time, the Romanians still enjoyed the loans they obtained an ease and banks in Romania promoted an aggressive marketing to urge customers to access credit.

What will happen this year? We must not ignore the socio - economic conditions existing in the public sector and the industrial sector is restructuring large state capacity becomes insolvent. It's easy to understand that these situations will influence bank lending and loans already in progress will have problems. Other problems of

banks in Romania come from parent banks in their home countries where the economic situation is not reassuring.

The existing international financial crisis forces banks to increase social responsibilities and change its behavior which urges on prudence, because when banks were competing in spectacular performances, the state did not have to interfere. Today, when European states charge rate payers with reimbursement of some great losses, banks are the first institutions that have to give signs of straightening and have to convey the signal for taking again the lending.

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