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Steps in the Development of the Romanian Financial System and the Correlation with the Level of Economical Growth

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Introduction

Along the history it has been asserted that among the determinant agents of the economical growth can be also cited the conservation and the endowment with physical, technological and human capital. This thing involves the realization of certain investigations in the infrastructure, development, and innovation, as well as in the education and the formation, that can raise the existent level of these resources in every country and to lead to a growth in the productivity, and in the competition of that country materialized through a higher GDP of a capital. But there is an extremely important factor like the way of financing, the degree of development of the financial system of the economy that leads to economical growth. On a microeconomic level, in what concerns the economical agents, financing is the most important for the development. All in all, no matter how good the product or how efficient the commercialization channels or the correlation level between technology and the human factor may be, if the business does not have an efficient financing politics, regarding the liquidity as well as the solvency and the profitableness, it will crash minimizing the other successfully realized aspects.

Except the fact that it offers an efficient allocation and a reduced cost of the financial services, a well developed financial compartment identifies the potential investors, monitors and gives information regarding the behavior of the beneficiaries of the chartered capital.

The financial system unifies the capital demand and the offer through banks, capital markets, and other financial mediates like mutual funds or pension funds. An efficient financial system mobilizes the collected saving by the unities that, after they satisfy their own objectives of investment and consumption, have a financing capacity for channeling it towards those units that, for realizing their investing objectives, need financing, offer an efficient payment and clearing system, in this way facilitating the financial transactions. An efficient system is the one that realizes an optimum getting in and allocation of the resources, that it has realized in a satisfying manner the remuneration conditions, assurance, and liquidity of the equivalent deposits or the instruments of collecting the resources, and on the other hand, the cost conditions and financing term for the allocated resources. Until short time ago, it was believed that the financial system develops after the contracting sector, channeling towards investments, at the request of the undertaker, the over pluses obtained as a consequence of the economies of the population. Following what Schumpeter first expressed in 1912, recent theories showed that an efficient financial system is a stimulus for the technological innovation identifying and financing the undertakers capable to successfully innovate the product and the production process. One of those who have opted for this kind of thought is Ross Levine who assures the fact that “a theoretical as well as an empirical constant work volume tends to make even the most skeptical to believe that the development of the financial system is a determinant of the economical growth, and not only a passive answer to this growth.” Levine and the others that share his opinion believe that there are inherent relations between financial intermediate and productivity and , as the amelioration of the productivity level produces on a long term benefic effects on the level of economic development, it can be said that also the financial intermediate generates economical growth. Moreover, Levine suggests that the development of the financial system has an important positive effect over the economical growth saying that “it can be eliminated a third of the already existent inequality between the countries with an important growth and those with a slow growth through the development of the financial intermediation for the latter ones until they reach a developing level comparable with the one of the countries with a quick development”. The positive association between the degree of development of the financial system and economical growth was at large analyzed also by Demirguc-Kunt (2006), Levine and King (1993), and Levine and Beck (2004). They get to the conclusion that this correlation stays significant even when other factors of influence are taken into consideration. Moreover, they prove that regarding a

country with a developing financial system, the degree of financial development is correlated not only with the current growth, but also with the future economical growth.

In order to do a thorough analysis of the way in which the Romanian financial system evolved, being correlated with the economical growth of the financing structure of the Romanian economy between 1990 and 2006, we leveled this analysis depending on the mutations that took place during the time in the Romanian economical and financial landscape. We have taken one by one the mutations that took place during this period regarding the Romanian banking system and capital market, as main financial agents, then the macro economical politics and their impact on the development of the financial system, and, least but not last, recent evolutions experienced by the Romanian financial system and regional level (Central and Eastern Europe) and European Union comparisons.

1. The Main Mutations that Took Place in the Romanian Financial Background Between 1990 and 2006

1.1. The Evolution of the Romanian Banking System

At the end of December 1989, in Romania took place the replacement of the socialist system, that had a directional, centralized, planned economy, with a new system based on democracy, decentralization, and oriented towards capitalism, towards the free enterprise, a moment that leaves a mark on the entrance of Romanian in a long transitional period that had as a final objective the entrance and the integration in the European Union structure. The financial system of Romanian was similar to the other centralized economies. In the banking system, BNR combined the functions of a central bank with some of the functions of a trade bank. Next to it, there were also other three banks specialized on different sectors: Romanian Bank of Export Trade (Banca Romana de Comert Exterior) for export trade operations, Investment Bank (Banca de Investitii) for the operations regarding the long term economy financing, Agriculture and Food Industry (Banca pentru Agricultura si Industrie Alimentara) for the operations of that specific field. CEC was the only institution specialized for taking over the available resources of the population. There was no currency market, the national currency was not reversible and the external payments operating were double sided: clearing in the member countries of CAER (leading to regional autarky) and payments in reversible currency with the other countries. The exchange rate was officially assigned. In 1980, a system of multiple courses was introduced (official, commercial, noncommercial) and courses of discount for exports, courses that were actually higher than the unique commercial course and that accentuated the fact that the national coin was strongly over evaluated.

Beginning with 1991 the metamorphosis of the Romanian banking system takes place. At the foundation of these transformations lies the instauration of a system organized on two levels and the legislation regarding BNR and the commercial banks. On the foundation of the ex central bank and from the structures of the specialized financial institutions incipient networks have been formed that were taken over by the current institutions.

So, the reform of the banking system started in 1990-1991 from the elaboration and adopting of a new banking legislation regarding the organization and functioning of the central bank and of the commercial banks. The restructuring reform of the banking sector, which was meant to create a modern banking system on the principles of market economy, started with the approval of the Law of banking activity that was effective during 1991-1997 and the Law of the statute of NBR¹. The new juridical frame encouraged the developing of the private banks and allowed admission on the banking national market of the foreign financial institutions. The banks had been authorized to operate as universal trade banks and, therefore, they could accomplish a large sphere of banking operations in the whole country if it respected the prudential directions emitted by the Central Bank, as it was an authority of banking surveillance.

As consequence of the evolution of the banking system from Romania, the need of alignment with the principles of the market economy and the modification of the ex banking laws was needed.

¹ Is the nr 33/1991 Law and nr. 34/1991 Law

According to these principles, the new appeared laws² that pointed to the statute of BNR, the procedure of the bankruptcy of the banks have approached even more the banking juridical frame from Romania to the modern juridical frame that already existed in the developed countries that had a free enterprise. The new laws have been elaborated concordantly with the references of European Union. All these regulations were meant to positively influence the banking activity, for assuring the economical development and stability.

Once Romania signed The Agreement of European Union Adherence, one of the main objectives of NBR was the taking over of the communitarian *acquis* in its legal framework, objective that was included in the medium term strategy for developing of the banking system, integrant part of The National Strategy of Economical Developing of Romania on medium term.

The general objectives³ that were stated by the strategy, as well as the actions taken for the realization of these objectives and accentuated in the next chart:

OBJECTIVES	ACTIONS
<ul style="list-style-type: none"> • <i>Creating a sector formed only from powerful banks, capable of assuring a financial intermediation based on efficiency and profitability criteria</i> 	<ul style="list-style-type: none"> • a new dimension of the banking system; • amelioration of the resolution procedures of the situation of the insolvent banks; • strengthening of the prudential surveillance activity; • finalizing the state capital banks privatization process; • bringing the credit co-operatives under the regulation and surveillance of BNR; • gaining the public confidence in the banking system and, implicitly, encouraging the savings through a growing in the role of The Fund of Guarantee of Deposits in the banking system; • consolidation of the cooperation with other national and foreign authorities of surveillance.
<ul style="list-style-type: none"> • <i>Diversifying and growing the quality of the financial-banking services</i> 	<ul style="list-style-type: none"> • integration of the banking services with those given by the financial market operators; • creating conditions for developing of some products and services in concordance with the demanding of the market and for implementing modern products and services like hybrid financing instruments, derivatives, services like “e-banking”.
<ul style="list-style-type: none"> • <i>Growing the competition of the banking system</i> 	<ul style="list-style-type: none"> • developing of the markets where the banks operate (money, currency, capital market); • growing of the autonomy of the Central Bank of Romania as authority of regulation and surveillance; eliminating any kind of discriminating treatments already existent in the banking system.

² Law nr. 58, The Banking Law that canceled Law nr 33/1991, Law nr. 101/1998 regarding the statute of The National Bank, which canceled Law nr. 34/1991, Law nr. 83/1998 regarding the procedure of the bank bankruptcy

³ Verdict nr. 455 from 9th of May 2001 regarding the approbation of the action plan of the governing program between 2001 and 2004, published in The Official Gazette, part 1, nr. 267 from 23rd of May 2001

As result of the gradual process of harmonization of the Romanian banking legislation, with the Directive of the European Parliament and the European Union Committee regarding the access to activity and the exercise of the profession by the credit institutions⁴ and also taking into consideration the principles emitted by Banking Surveillance Committee from Basel regarding the banking surveillance, it was felt the need of modification of the existent legal framework.

First of all, this modification pointed the activity sphere and ameliorating of the conditions for the significant stockholders⁵, assurance of the information linked to the activity, reputation, and moral integrity of the persons that intend to become significant stockholders, including the provenience of the funds meant for obtaining the participation, and if they correspond to the legal demands, the realizing of a cautious and healthy administration of the banking system, that can allow efficient surveillance of the central bank⁶. Also, new prudence in connection with endowment capital of the branches from Romania of the foreign banks has been introduced⁷.

Another important step in developing the regulative frame has been made through including in the surveillance of the central bank and of the co-operative credit organizations, in this way regulating their authorization and surveillance⁸. The legal framework built up in 2000, completed and modified in 2002, assured the meeting of certain standards and exigencies aligned to the communitarian prudence regarding this aspects. In this period, have been settled the bases of the regulation framework adapted to the specificity of these credit institutions, through issuing by NBR of prudential regulation regarding:

- authorizing the credit co-operative organizations; minimum level of the capital of credit co-operative organizations and minimum aggregated capital of the credit co-operative networks;
- methodology of reporting their own funds.

NBR continued to be concerned about the harmonization of the regulations and practices in the field of banking surveillance to the base principles settled by The Banking Surveillance Committee from Basel, from which we exemplify:

- the actions taken in order to increase the powers for NBR regarding its activity of authorization and surveillance of the rights of owner acquisition and transfer of the capital of the banks including certain operations realized by groups of persons with the aim of avoiding reaching the level of the authorization threshold for the significant participations (5%) and to be allowed to establish through regulations more strict criteria of eligibility for the stockholders and leaders⁹;
- the amendment of the legislation regarding the bankruptcy of the banks with the objective of creating a more efficient mechanism of eliminating insolvable banks from the system and maintaining the public confidence in them¹⁰;
- modification of the legislation regarding The Fund of Guaranteeing of the Deposits in the Banking System in the sense of raising the role of this fund in the process of eliminating insolvable banks from the system.

I consider that in the period 1990-2002 the financial and monetary system was strongly dominated by the banking sector, the last one being the most important financial intermediary. In this period the Romanian banking system was characterized through a low level of monetarism and financial

⁴ Is the Norm 2000/12/CE modified through The Norm of the European Parliament and the Council of European Union nr. 2000/28/CE

⁵ Law nr. 58/1998 was partially harmonized with the stipulations of the Norm nr. 2000/12/CE

⁶ These ameliorations had at their basis The Order nr. 137/2001 of modification of the banking law

⁷ Is the Order nr.56/2000

⁸ The stipulations of the Law 58/1998 for which reason the Romanian Government issued the Order nr. 97/2000

⁹ Through the modifications and completions to the Law nr. 58-1998

¹⁰ OUG nr. 138/2001. Through it was followed up the harmonization of the existent stipulations with the European Union legislation; it partially took over some stipulations from the Norm 2001/24/ce of the European Parliament and the Counsel from 4th of April 2001 and the regulation of the legal frame regarding the bankruptcy of the credit corporatist organizations as art. 242 from the Judge's Oder nr. 97/2000

intermediation. The dominant place of the banking sector in the Romanian financial and monetary system has as explanation the insufficient development of the capital market and the inheritance of the central planned economy where the banks accounted the activity of economical company without financial independence. Recent evolution of the banking sector shows that the situation of this sector has visibly ameliorated in the last years. At 31st of December 2006, NBR authorized 40 Romanian private capital owned banks for doing banking services in national currency and 6 branches of foreign banks. The evolution of Romanian banking system during 1996-2006 is presented in the following chart (table I.1):

Table nr. I.1
Dinamics of Romanian banks, by capital type and the branches of foreign banks in the period 1996-2006

SPECIFICATION	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006
I. Number of Romanian banks from which:	31	33	36	34	33	33	31	29	30	32	40
a) state-owned capital	7	7	7	4	4	3	3	2	2	2	2
b) majority private capital:	24	26	29	30	29	30	28	27	28	30	38
-majority domestic capital	14	13	13	11	8	6	4	4	5	6	8
-majority foreign capital	10	13	16	19	21	24	24	23	23	24	30
II. Number of branches of the foreign banks	9	10	9	7	8	8	8	8	7	6	6
Total banking system (I+II)	40	43	45	41	41	41	39	37	37	38	46

Analyzing the data presented in the chart we can easily see that in this period the number of banks increased from 40 banks in 1996 to 46 in 2006. If we report only the number of banking operators, the growth is not significant but taking into account the new configuration of the banking system regarding the allocation of the banking operators on the type of the capital, we notice a significant difference. If at the end of 1996 there were 40 functional banks, of which 7 with state owned capital and 24 with private owned capital, of which 14 with majority domestic capital and only 10 with majority of foreign capital, at the end of 2006 the structure is completely changed. The state owned capital banks are very few, as a result of important privatizations, getting to a number of only 2 banking operators, more precisely CEC and Exim Bank and the banks with the majority private capital have not only overwhelmed the state owned capital banks, but they also experienced a spectacular development, especially in 2004-2006, with the approaching of the moment of Romania's adherence to the European Union. Among the causes that led to this configuration of the banking system, next to the acquisition by the foreign investors of the majority stock package of some banking operators is also the significant number of bankruptcies, for example banks like Albina, Credit Bank, Bankoap, or Columna Bank in 1999 or getting out of the market in 2002 of 4 banks through the the bankruptcy of Romanian Discount Bank and Turkish-Romanian Bank, The Bank of Investment and Development and the fusion of the Raiffeisen Bank with Agricultural Bank. This reconfiguration of the banking system also meant the growth of the capacity of distribution of the products and services through a powerful development of the banking unities network, especially in urban areas, with a population with over 250.000 inhabitants, the use of some alternative channels (ATMs, POSs or some sophisticated services as Internet banking, self banking, mobile banking), as well as selling mobile units. All these contributed to the intensifying of the market competition.

The economical conditions between 2000 and 2006 were characterized through a growth of the macro economical performances as a consequence of the succession of structural reforms and of macro

economical equilibrated politics that influenced the evolution of the Romanian banking system. The banks developed and adapted their offer depending on the demand imposed by the exogenous factors impact on the real economy, as well as the more and more obvious pressure of the competition regarding the Romanian banking and financial market. In conclusion, the evolution of the banking system was characterized by the development and diversity of the banking products and services, the growth of the speed and diversity of the discount instruments, the modernization of the evidence and control system, the important changes in upgrading the electronic infrastructure for transmitting accountancy, statistics, and transfer process data. Also the efforts of capitalization as well as the competitive pressure determined the banks to create or to modernize the territorial network¹¹. All these things reflected in the performance of the Romanian banking system and in the rhythm of growth of its assets from one year to another. As we can notice in the following chart, in 2005, Romania had one of the highest rhythms of growth of the banking assets from Central and Eastern Europe. (Figure I.1, I.2).

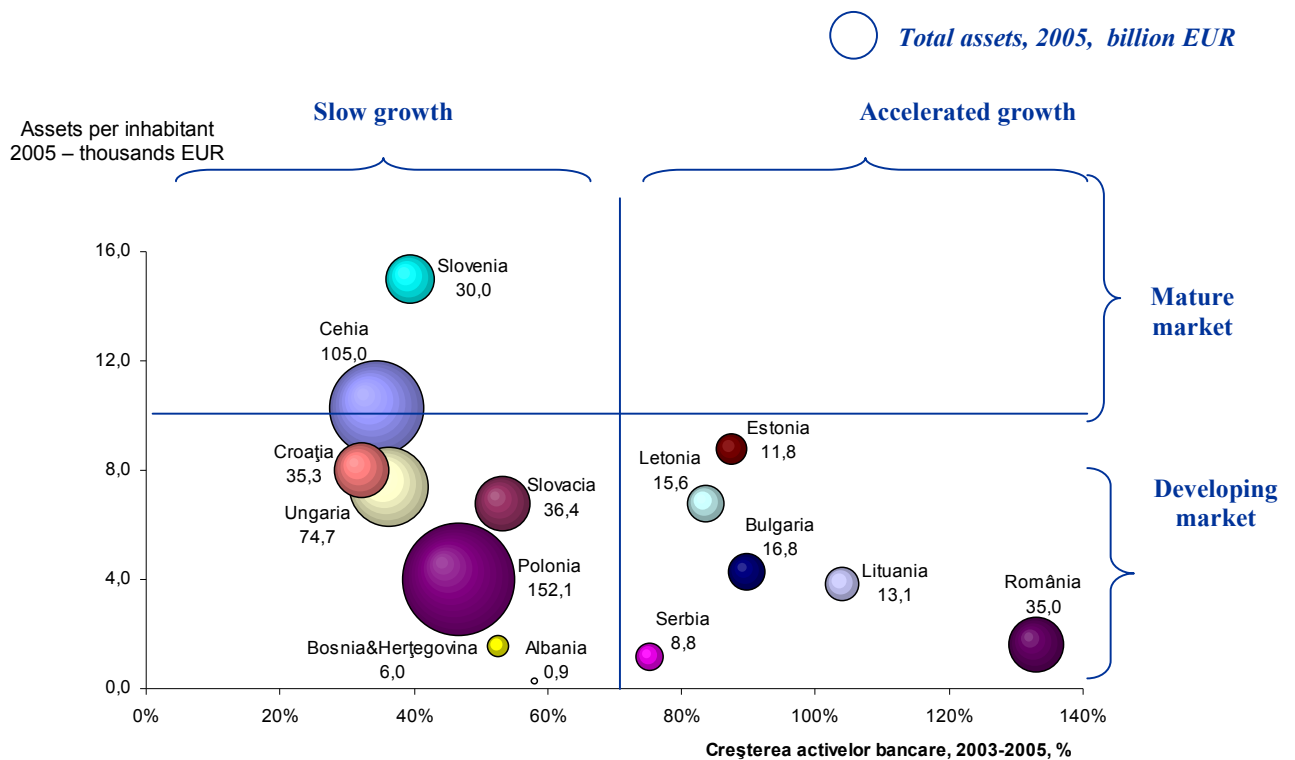


Figure I.1 - Rate of growth of banking assets in the period 2003-2005 in countries from Central and Eastern Europe

¹¹ Hetes-Gavra I., Buglea A., Hetes R. – Management bancar , Orizonturi universitare Publishing Press, Timisoara, 2004

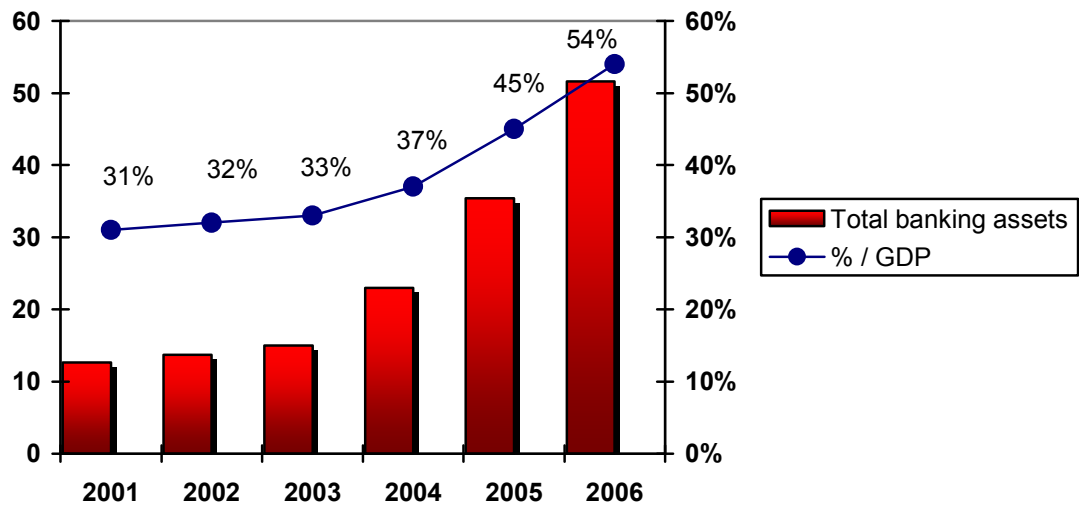


Figure I.2 - Total banking assets as percent of GDP

The percent of the banking assets in GDP, as a measure of the performance of the banking system, grew from one year to another, so from a value of 31% in 2001 it got to a value of 54% in 2006, a significant growth, but if we refer to banking assets/inhabitant indicator we notice that this is very reduced, almost 5 times smaller than that of the Euro area and almost 10 times smaller than in the Central and Eastern Europe. So, the process of developing the banking sector has to continue, for eliminating the disparities from the other countries members of European Union.

As a conclusion, in my opinion, the most important mutations of the considered period were:

- *organization of the banking system on 2 levels*, a model specific for the countries with market economy;
- *reorganization of the banks existent till 1990, simultaneously with the growth of the dimensions of the Romanian banking sector* as a consequence of the coming out of private owned capital banks;
- *the radical change of the role of the banks in society and economy, generally*, Romanian commercial banks enlarging their assets or the sources from which they collect their funds;
- *the entrance of Romania in the European Union*, fact that influenced the appearance on the market of new banking operators, that enriched the competition and led to more efficacy of the banking system, with implicit benefits for the users of this system and for economical growth generally speaking.

These mutations pointed to significant changes of the Romanian banking system – not only the way in which it was organized and its dimensions were changed but also the role of banking instruments in economy and the variety of banking operations offered to the clients experienced some good changes.

1.2. Steps of setting up and development of the Romanian exchange market.

In Romania, the reason for the appearance of the capital market was that of creating of an alternative market that could answer to the necessities of financing and investment of the entities from the economy, as well as for its role played in the process of privatization and reorganization.

After a gap period of 50 years¹² The Stock Exchange from Bucharest opened again its gates at 23rd of June 1995, through the foundation of The Association of the Exchange by 24 security societies. In

¹² The traditions of the stock exchange institution are older than 100 years in Romania and there were also periods of great effervescence and international resonance of the local stock activity. The grade list from that period was formed from the trade

the summer of 1994 it was also authorized by the constitution of the Romanian National Securities Commission, central institution of the Romanian capital market, with essential regulative, authorizing, and surveillance attributions, that concentrated on fundamental; attributions like:

- The promotion of the principle of protection of the investors on the capital market;
- Instauration of the principle of transparency in the activity of the issuing of securities and of institution operating on the capital market;
- Education of the public and its familiarization with the issues, instruments, and mechanisms of the capital market.

The fact that Romania did not have an exchange market for half a century made the process of its development starting from zero, without benefiting from its own experience in the field. After the approval of the regulations and functioning and operating procedures, BVB effectively began its activity realizing its first transactions at 20th of November 1995.

The normative main document that regulated the Romanian exchange market between 1994 and 2002 was the Law of the Securities and Stock Exchange¹³. Before it appeared, a series of other documents had an important impact on the local capital market. The normative frame for setting up BVB regarded the over take in the Romanian legislation of the European principles, so the Romanian exchange market could participate to the realization of an integrated European market of the securities. So, the Law of Trading Company¹⁴ also created the first conditions for the appearance of the capital market. The law, realized, in the beginning, the role of legal frame of creation and evolution of the capital society, in the same time regulating also the running of the main products on the market. The Law of Privatization of trading companies¹⁵ was the second important step, through introducing on the capital market the property certificates which were meant to familiarize the public with these financial instruments and demonstrated, the same time, the necessity of building up an institutionalized frame for their sale and purchase. After the Law of Privatization and until the appearance of the legislation of the stock exchange, a series of other legal documents were the support of the development of the capital market, and among the most significant are:

- The regulation of the non-exchange transactions with securities and the organization of some financial intermediaries;
- The regulation of constituting and functioning of the mutual funds and of the investment companies as institutions of financial intermediation.

After its debut in 1995, between 1996 and 2000 the exchange market from Romania could hardly get to better local performances in an economy where the growing rate of PIB was negative, the investments – including the foreign ones – were falling down in 1999 unlike the two years before, the economies decreased towards the minimum records, the inflation went constantly beyond predictions, and the exchange deficit stimulated the covering of the public debt through mutual loans to interests that were superior to any exchange performance, general or local.

In the context of the tight dependency on the lack of performance of the real economy, the Romanian exchange was losing, between 1996 and 2000, the moment of the transactional growth recorded on some of the East European markets. The exchange activity continued, though, to make constant steps in defining the infrastructure and institutions, the insurance of the regulation framework, the implementation of the technical operation system, the surveillance of the activities and developing new instruments taking into account the needs of the operators. Among the important events that were in favor of the development of the capital market during 1996-2002 is also the launching of the three exchange indexes BET, BET-C, and BET-FI that offered, together, a complete image on the general evolution of the market, functioning as a barometer of the performance of the capital market. Also, in this same period, BVB concluded cooperation agreements with various similar organizations and made all the efforts to become a full right member in organizations like FEAS (Euro-Asian Federation of Stock Exchange), FESE (European Federation of Stock Exchange), or EECSDA (Depositary and Compensation Houses Association from Central and Eastern Europe), this thing leading to the extension of the visibility of the Romanian capital market and its framing in the globalization and regional cooperation tendencies that assert on an international scale.

exchanges and, in the same time, some kind of exchange agents that were then the equivalent of the brokers. The agriculture and transports made Romania once to have the most important position on the exchange market of the South-East of Europe.

¹³ Law nr. 52/1994 regarding the securities and the stock exchange

¹⁴ Law nr. 31/1990 regarding the trade companies

¹⁵ Law nr. 58/1991 regarding the privatization of the trade companies

In 2002, the new law package was promoted and it was meant to initiate the harmonization of the legislative Romanian system with European Union demands. The new law package¹⁶ regulated the activity from the regulated commodity exchange and derivatives market as well as the collective investments organisms.

The modification of the legislative framework led to a growing in the interest of the investors for the securities issued by the Romanian trading companies. Doing these changes led also to the consolidation of the capital market preparing the entrance to European Union. In 2003, RASDAQ became The Electronic Exchange Rasdaq (BER), as joint-stock company. In the same time, BVB elaborated a fusion plan with BER, a very long process that had various steps.

In the context of European Union adherence negotiations, Romanian National Securities Commission contributed to the issuing of “The Free Circulation of the Services”, where were presented measures for transposing the communitarian acquis for the financial sector. There was a need of issuing a new capital market law. As a result, in June 2004 a new law of the capital market¹⁷ was issued that assured the development of the legislative framework necessary for creating new institutions, the access of the capital market brokers from Romania on the single European market, as well as the creation of a viable capital market that allows the transaction of certain modern financial instruments. In the same time, the law had some stipulations regarding the setting up of a compensatory fund of the investors with the role of indemnifying the investors if an agent or an investment administration society cannot pay, regarding the setting up of the operators on the market, of the central depository, of the central counterpart. In this way it assures a unitary analysis of the rules applicable to the setting up and the functioning of these entities, from the sight of obtaining the European passport, after Romania’s entrance to the European Union and transposing a series of norms incident to the capital market issued by European Union between 1993 and 2003.

In July 2003, in The Forum of the Capital Market from Balvanyos the consolidation of the Romanian capital market through setting up a single market was the main objective of BVB and BER. This thing implied realizing a single well capitalized and liquid market with a modern registry, transactional, compensatory, and discount system and with regulations compatible with other European capital markets, that could answer better to a new competition. This unification could be realized in two steps, due to the fact that the two entities had different juridical forms, like: first, the juridical form of BVB has changed from public interest institutions to joint-stock company, and then, in the second step, took place the unification itself. At 30th of November 2005, took place the fusion through absorption, BVB, in its quality of absorbing institution took the control over BER. Although the importance of the Romanian exchange increased after this extremely important decision, it was not enough to assure the qualitative and quantitative step that was necessary to eliminate the differences to get to the other regional exchanges. The fusion was just a step in the long process of developing the Romanian capital market.

In my opinion, the main negative factors that made harder the developing of the capital market from this period were:

- *Economical recession*, that minimized the individual capacity of the economical agents and reduced the rhythm of the investments;
- *The high inflation rates*, that reduced the interest of the investors for this market;
- *Low rhythm of the privatization*;
- *High interest rates* practiced by the banking sector, that oriented the population’s economies towards this sector.
- *Low profitability of the economical environment*, that reduced the potential of the growing of the nominal value of the stocks;
- *The bankruptcy of some mutual funds* that reduced the trust of the individual investors in the capital market.

Romanian capital market crossed a long and hard road looking for a well defined place in the national economy. The dynamics and the levels the main quantitative indicators of BVB are very important for developments perspectives because the activity of the exchange market depends on a great extend on the dimension it reached and on the liquidity it offers to those with the excess capital.

¹⁶ Law nr.297/2004 regarding capital market

¹⁷ Annual BVB Report 2006

Another phenomenon that brings joy and that is associated with the Romanian capital market, noticed by the statistics, is the fact that in the last period took place a growth in the number of companies relevant for the issuers from the regulative market: reducing the concentration of the capitalization of the market. The concentration of the market capitalization is one of the characteristics to the emergent capital markets, category where are also included the capital markets from Central and Eastern Europe. The year 2006 followed a tendency imprinted 2 years before. If in 2004 the first five listed companies cumulated over 83% from the total of the market capitalization, and in 2005 these cumulated only 80%, at the end of the last year exchange capitalization of the most important five companies from BVB got under 75% from the total of the market¹⁸. With the access on the market of many Romanian companies, there are premises of a higher reduction than these percentages.

The economical growth of Romania, remarkable for the emergent countries had as a consequence the growth of the market capitalization. As we can see in the following figure (Figure I.3), the percent of the market capitalization in GDP as important indicator of the degree of development of the capital market, had an increasing trend along the period 2000-2006, and, as the last annual report of BVB, in 2010 it is being estimated a level of the market capitalization of €40 billions.

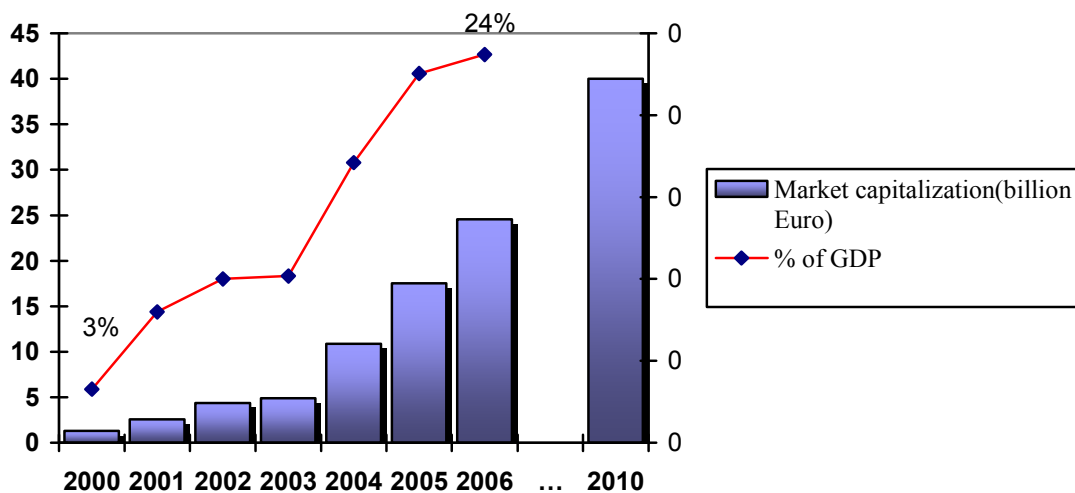


Figure I.3 – Market capitalization as percent of GDP

After this indicator and the one of the value of the transactions, the transactions on the regulated market of the Stock Exchange Bucharest is situated right after the first three exchanges from Central and Eastern Europe. The growing potential of the exchange market from Romania is very high, due to the new large companies that are expected to be listed on the stock, to the issuers that will change to the regulated market from Rasdaq market, but also to the growing of the economical-financial performances of the current issuers.

Regarding the structure of the exchange transactions in 2006, in Romania, the only functional market from the point of view of the liquidity, now, is the stock market (Figure I.4).

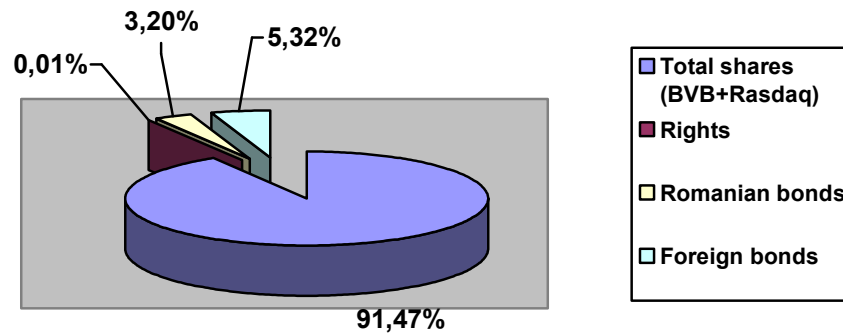


Figure I.4 – Structure of stock transactions (2006)

With a pretty devious evolution, the joint-stock market seems to have got to a certain maturity which can lead to future quantitative, but especially qualitative growth. Regarding the bond market, Romanian capital market is characterized by an insufficient development of the bond primary market and secondary market. In 2007, at The Stock Exchange Bucharest 20 bonds were quoted, of which only 5 corporate bonds, the other 13 municipal bonds and 2 international bonds. Moreover, analyzing the value of the transactions that took place in 2006, we can see that only 8,52% of this is due to the bonds, the listed actions at BVB having a contribution of 91,47%. It is obvious the fact that the bonds transactions are not as far as attractive as the stock ones, thing that determines a reduced liquidity for the investors of this kind of securities. The series of instruments of BVB diversified through introducing in 2007 the first derivative instrument, more precisely future contracts on the stock index BET, but the liquidity of such a market is not very high and it needs an accommodation period with this kind of product that was not available except on the Sibiu Monetary Financial and Commodities Exchange.

Regarding the number of intermediaries on the market, we can say that this grew in the last 3 years from 67 in 2004 to 73 SSIFs in 2006 (Chart I.5) and the number of the issuers grew as well as the transactional market value.

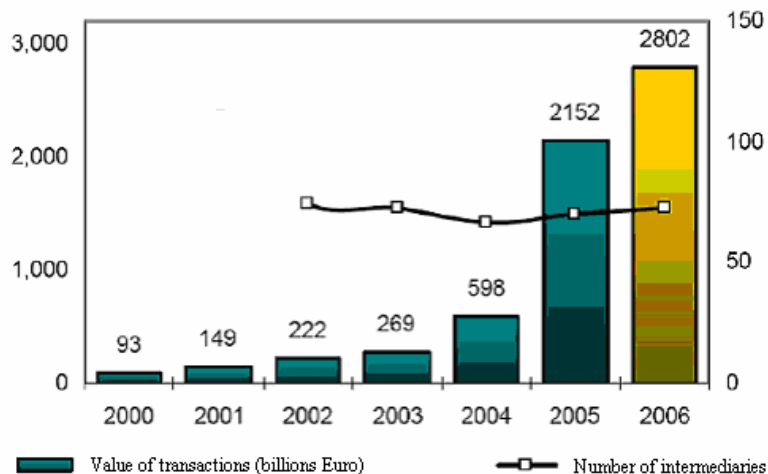


Figure I.5 –Value of transactions and the number of financial intermediaries in the period 2000-2006

In conclusion, the development strategy of the capital market was not felt only through the growth of the market capitalization or of the transactional value from a year to another, but also through the institutionalized consolidation, drawing of new issuers at the Stock Exchange, enlarging the sphere of the transactional products and instruments as well as the growth of the investor public and the improving of BVB visibility for valuing its role and functions by the economical environment.

In my opinion, the following years will be decisive in establishing the alliances and the merger processes. The Bucharest Stock Exchange has to reach a sufficient development and maturity level to allow it an equality position with any other regional exchange operator, capitalizing the growing potential that it has. Once Romania became a member of the European Union, this effort seems to have been concretized in setting some real and solid growing bases. Although it still have, on certain segments, a lower position than the other capital markets from Central Europe, the Romanian capital market begins to get the attention through the sustained growing rhythms and through its extraordinary hidden potential.

2. THE INFLUENCE OF THE MACRO ECONOMICAL POLICY ON THE ROMANIAN FINANCIAL SYSTEM

The capital dimension in economy and the financial system development are being continuously influenced by the monetary policy of the state and by the way the fiscal or economic policy was elaborated and applied. The change along the time of some macro economic variables as inflation, market interest rate, or exchange rate, but also the taxing level of different capital gains had a great impact on the concentration of the surplus capital towards one or another financial way of investment and on the microeconomic financing decision. Further we will try to analyze in which way these factors influenced the Romanian financial system.

2.1. The influence of the monetary policy over the financial system

By means of the monetary policy operated by NBR, the state interfered in the economy to ensure the surveillance over the economical liquidity, thus pursuing its contribution to price and exchange stability as well as to fulfill the state economical policy. The ground rule that has motivated NBR even since 1990 was and still is that of ensuring the stability of the national currency, a phenomenon that would have a strong impact over the financial system. The means used by NBR to achieve this purpose were: the discount tax, the open- market policy, the compulsory minimum reserve system, the refunding interest and gathering of deposits from trade banks. We will not focus on the manner in which these instruments were used, but on the impact that they had over certain macroeconomic variables as the inflation rate, the interest rate, and the exchange rate – all these having themselves an influence over the entire financial system.

The inflation represented a sensitive problem for the Romanian transitional economy, with negative effects over the viable implementation of a long-term reliable financial policy and also, with negative effects over price stability as premises for a constant economical growth. Regarding the financial sector, not only the banking sector, but also the stock market has been seriously damaged by the oscillating annual inflation evolution. (Table II.1)

Table nr.II.1

Year	Average annual rate of inflation¹⁹
<i>1990</i>	5,1
<i>1991</i>	170,2
<i>1992</i>	210,4
<i>1993</i>	256,1
<i>1994</i>	136,7
<i>1995</i>	32,3
<i>1996</i>	38,8
<i>1997</i>	154,8
<i>1998</i>	59,1
<i>1999</i>	45,8

By studying the rates registered by the inflation rate in the chart above, we can see that this had registered extremely high annual rates during certain periods of time, as between 1991-1994 and then 1997. In these circumstances, it becomes visible the reason why, during these periods of time most of the stock listed companies had registered real negative earning performance rates. A considerable number of economical agents had ended financial exercises in loss, even if these were societies evaluated at Tier I or Tier II of the Bucharest Stock Exchange, that are companies representative for the Romanian economy. The motivation of depositing savings was lost, because the large inflation rates affected the real interest rates in such a way, that these inflation rates had determined not only a buying power decline for fund holders, but indeed, during some periods, they caused great casualty for those holders. Thus, the banks experienced actual difficulties in attracting medium or long-term reserves and this led to a faulty credit activity.

The need for shaping and applying of a monetary policy that could lead to a significant diminution of the inflation rate was strongly felt and it began to be visibly applied beginning with 1999. The bearish levels of inflation from between 2000-2006 explain themselves through this monetary policy approach, which has not been applied until 2005, though its starting had been anticipated in the National approach of medium-term development in the year 2000 and acknowledged by Pre-adhering Economic Programs (PEP) from 2002, 2003, 2004 and 2005.

By approving, in 2005, the strategy of direct targeting of inflation, The National Bank of Romania has put across its clear mandate regarding the goal of price stability by shaping and applying the monetary policy within the strategy of direct targeting of inflation. This strategy has been widely applied and was characterized by close monitoring and by applying the evolutions at macroeconomic and financial balance level, in order to keep this from contradicting long-term sustainability of the process which combats inflation.

As we can observe from the following chart, this policy has been successfully accomplished. (Figure II. 1)

¹⁹ Average rate of inflation (current year) in comparison with the previous year (%)

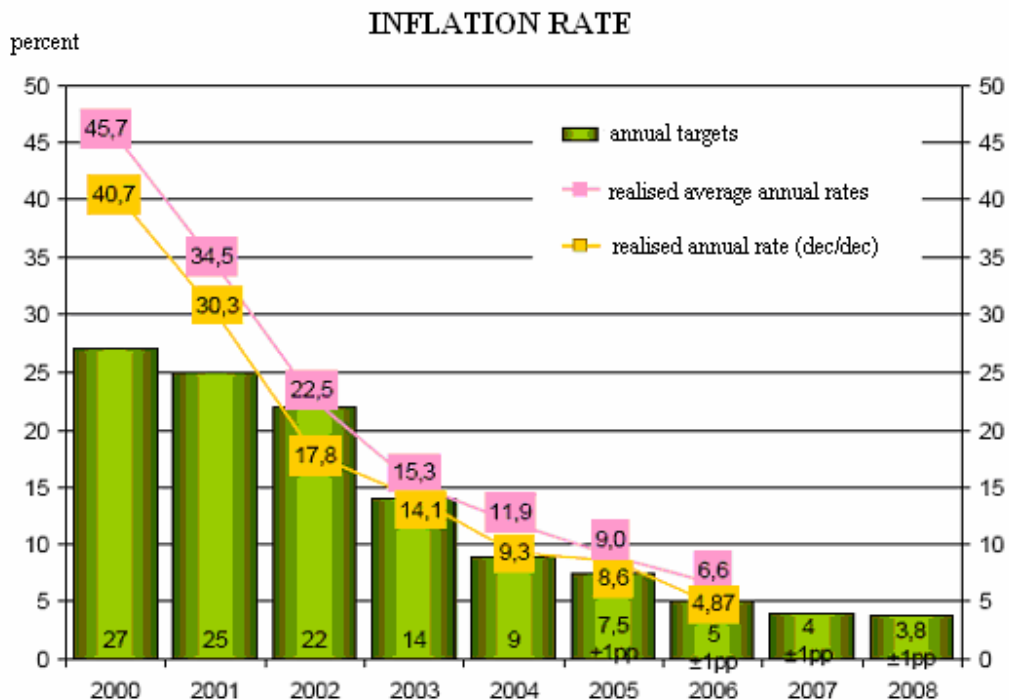


Figure II.1 – Evolution of inflation rate in the period 2000-2008

The complete liberalization of capital account, in September 2006, corroborated with the improved perception over the country risk, induced by Romania's imminent entrance in the European Union's structures, had led to capital entrance, and which, due to the effect of Romanian currency's appreciation, contributed to the inflation rate takedown. As a result, the entire financial system was privileged by the inflation rate evolution.

Another important predictor that influences the financing decision is the interest rate. The interest rate represents an important factor when establishing the functional connections in what concerns the accumulation and investment and in that of ask and bid of financial means. The modification of the interest rate influences the decisions of the economical agents because the factors that influence it are extremely numerous. Between the capital offer and the interest rate is a direct relation which means that when the interest rate is growing, the capital offer is getting higher because the individuals and the companies are more disposed to sacrifice their present consumption for getting a higher sum of money in the future. The interest has to have economic stimuli, without which the financing system cannot function. The investment demand evolves inverse from the interest rate: more reduced the interest rate will be, more higher the investment volume will be. For the creditor the interest is, indeed, a stimulating compensation for giving up using for himself the borrowed funds and for the debtor the paid interest is a stimulus for the growth of the efficiency of the use of own and borrowed funds. Credit offer in economy is determined by the level of economies which is determined by the level of the passive interest and the level of the income. When passive interest level rises, the individuals seek to create bank deposits as to benefit from extra incomes. But the vivid rising of the passive interest does not lead to a similar rising for the savings, because a certain level does not permit the rising of the savings volume, regardless of the interest level (we can include here the preference for liquidities). The credit bid is influenced by the active interest rate. When the active interest is reduced the credits become more accessible and the decision for investing through the banking market becomes easy to be taken.

At macroeconomic level, we can depict at least two arguments for which interest rate on the market is a useful predictor for the individual as well as for the bank:

- the stockholders of a company compare the earning capacity rate offered by the company from its own activities with the deposit interest rate, and if the company does not offer an

earning capacity superior to that obtained from bank deposits, this could mean the loss of financing power from personal capital

- for the indebted companies, the interest rate determines the debt's cost, and this directly influences the capital average weight cost.

In between 1990-2006, the inflation rates negatively influenced the market real interest rates. We can say that the real interest is directly proportional with the nominal interest and inverse proportional with the inflation rate.

Table II.2

Average interest rates practiced by banks in the period 1992-2006 (percent)

YEAR	INFLATION RATE ²⁰	NOMINAL INTEREST RATE ²¹	
		Activă	Pasivă
1992	201,5	43,60	32,90
1993	256,1	86,40	42,50
1994	60,0	61,80	49,50
1995	27,80	47,50	32,40
1996	57,50	55,80	38,10
1997	151,40	63,70	51,60
1998	49,50	56,90	38,30
1999	54,80	65,90	45,40
2000	40,70	53,48	32,74
2001	30,30	45,74	26,16
2002	17,80	35,65	18,39
2003	14,10	26,19	10,78
2004	9,30	25,81	11,34
2005	8,60	19,19	6,22

From the data in the table, we can conclude that, regarding the entire period of time, the bank interest rate has a similar trend with the inflation rate. Because of the fact that the inflation combating process did not continue, due to some outbreak periods, this made the interest rate practiced by the national bank to raise, this rate being the main tool for inflation combating used by BNR to determine the rising of the interest rate practiced by trade banks. Even though the nominal interest rate registered important denomination, the real interest rate was, generally, negative, meaning that the trade banks, as well as the deposit holders registered money buying power loss.

In between 1993 and 1995 the interest rate registered a downward evolution, diminishing by almost 50% accountable to 1993. The interest rate extremely high percentage is due to the inflation rate, which, in 1993 has reached the record of 256, 1 %, a hyperinflation feature, but also a feature of the distortions inside the Romanian economical system, especially in the banking system, at its incipient level. The interest rates practiced by banks until 1998 did not reflect the monetary resources ask-bid relation, and they were the result of the operator's inflationist anticipation, the central bank's inability of controlling more than one variables at a time, the poor saving level and the public sector deficit from internal sources.

In between 1998 and 1999, the average interest rates registered a rising of 5-6 points, especially due to the securities cost increase for the outside clients. The main reasons were the devaluation of the leu and the banks' attempt to recuperate the loss induced by the compulsory minimum reserve and by the

²⁰ Level registered in current december in comparison with the december of the previous year (%)

²¹ Interest rates practiced by banks for non-banking clients

doubtful banks financing possibilities disappearance, at high interests. The National Bank decision of increasing the compulsory minimum reserve rate was meant to discourage the banks to make deposits in the system and it was followed by an increase of the passive interest rate for the outside clients' deposits, as to attract those clients' deposits.

Beginning with the year 2000, the apprehended and discounted interest rates diminished, due to the monetary market relative improvement and due to a monetary policy relaxation during the first and the last part of the year.

For the consolidation of the central bank's credibility, the saving encouragement and the public confidence in the national currency, as well as to prevent a higher internal request, NBR has preserved a cautious attitude, by not allowing a deposit interest rate proportionate reduction.

On the other side, from the economic agent's perspective, the relation between the active interest rate and the inflation rate was favorable, because the banks could have considerably increased the nominal interest rates as to cover the great inflation rate. Thus, the banks choose active interest rates below inflation rates (favorable for the economic agent, who needed cheap financial resources), on the account of some passive real negative interest rates (in a normal economy this is not in the favor of economizing level), that did not totally discouraged the money deposits in the banks of a population that was not sufficiently well instructed for a market economy and this thing helped the companies where they remained as investors because they did not find something more attractive.

Another macro economic predictor that can influence the financing decision at a microeconomic level and the whole financial system because it provokes a risk to the financial transactions is the exchange rate of the national currency. The appreciation or depreciation of the national currency produces important changes at the level of the banking system, stimulating or not its active and passive operations in the national currency. In the capital market the changes registered by the exchange rate is being felt also in the volume of the buying or selling directions on the market, thing that strongly influences the expectations of the investors for the national currency and the titles invested in it.

On the other side the exchange rate has consequences on process of saving realized by the economical entities and on the financial system in its important function of collecting of the economized incomes and of their efficient allocation. If we think at the population sector most of the salaries are quantified in the national currency. If this is depreciated the level of their savings is being significantly altered. If we talk about the importer or exporter economic agents, the exchange rate affects their flat result. If the exchange rate leu-euro is higher when cashing than when paying then the difference is favorable for the importers; if it is higher in the moment of the paying than in the moment of cashing then the difference would be unfavorable. On another side, the risk resulted from the essence of the exchange rate is inherent that affects the whole financial system, including the persons who take a financing decision. In the figure II.2 is illustrated the evolution of the leu in comparison with the dollar.

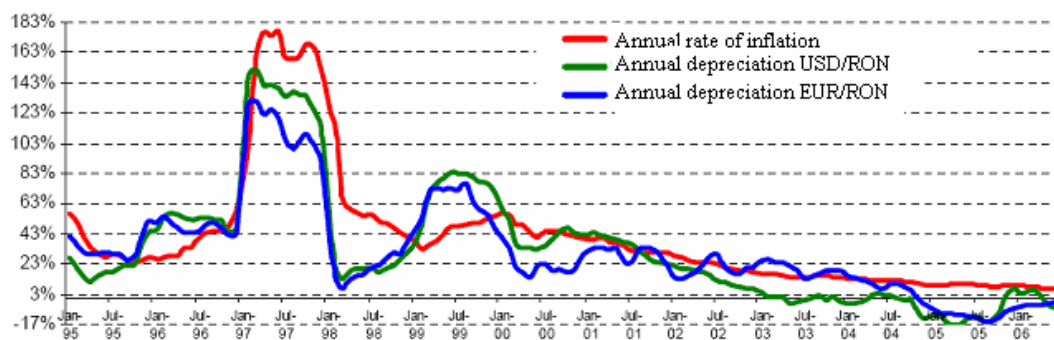


Figure II.2 – Evolution of the exchange rate in the period 1995-2006²²

We can notice from this chart that between 1990 and 2003 was a continuous depreciation of the national coin compared with the US dollar and the euro. This period was favorable to those that had

incomes from exports. In 2004 the leu gained little compared with the dollar and the reason was the depreciation of the dollar for the European coin. The empower of the leu at the beginning of 2005 appeared maybe because of the development level Romania got but also because of the policy of NBR led for the inflation.

2.2 The Influence of the State Economic Policy over the Financial System

Another important element when talking about the support of the development of the financial system is the economic policy promoted by the government.

The state can encourage or discourage the economic activities through the growth or diminution of the level of public expenditures for economical reasons in the total of the volume of effectuated public expenditures. Reducing the amounts dedicated for the economic actions, easily noticed in the table below, is a normal evolution generated by the withdrawal of the state from economy.

Table nr.II.3

Percent of expenditures for economical actions in total public expenditures

(%)

YEAR	PERCENT OF EXPENDITURES FOR ECONOMICAL ACTIONS IN TOTAL PUBLIC EXPENDITURES
1990	43,63
1991	33
1992	39,57
1993	35,54
1994	32,94
1995	28,94
1996	25,57
1997	14,71
1998	13,79
1999	14,84
2000	16,36
2001	17,79
2002	18,8
2003	24,52
2004	24,31

If we look carefully at the data from the table II.3, that present the evolution of the economic expenditures between 1990 and 2004, we can notice here as well a devious evolution. We get to the conclusion that, though the general tendency is to reduce these expenditures (the amount decreased almost to half of them), they are still high enough, even recording an easy growth in the past years. These things are concordantly with the things expressed by IMF (International Monetary Fund) and Romanian Government, the subvention mechanism of the public sector exerts negative influences on the correct functioning of the Romanian economy because it does not encourage the entities that received subventions to get an optimum financial structure through the financial system, for the maximizing of the value of the company.

Fiscal policy is viewed as an integrant part of the economic policy, and is in a continuous adaptation to the economic and social development conditions of the country. So, the taxation policy plays a decisive role in the financing decision of the entities from economy. The existence of a different taxation policy of the incomes from the interests and dividends, or on the incomes from the transactions that take place on the capital market, as well as the existence of some deductibility of the taxable income for the corporate sector has an effect also on the development of one or another of the financial intermediaries that coexist on the market and on the other hand, on the whole financial system.

When talking about the corporate sector, the calculation technique of the income tax has, first of all, a direct influence on the way of their financing. For the diminution of the taxable profit, they will seek for the appropriate financing alternative (the emission of bonds or the contraction of banking loans) depending on the deductibility of the interest expenditures. As a general rule, in Romania, are considered deductible those expenditures effectuated with the aim of realizing the taxable incomes including those regulated by the operative normative indentures. When referring to the interest incomes, the Fiscal Code says that these are deductible if the degree of debt of the capital of the entity is lower or equals three.

The interest taxation also influences the incomes of the individuals, influencing their motivation in choosing a financial intermediary or another. The quotes of taxation the bank interests incomes increased from 5% to 10%, from 1st of June 2005 and from 1st of January 2006 lined to the single rate of taxation of 16%. If we take into account the decrease of the deposit interest rates from the last time, that was determined by the necessity of reducing the difference from the domestic and international interest rate, as an action for stopping the entrance of speculative capitals, we can conclude that a change in the sense of increasing the level of taxation quote, can determine a growth of the consumption and a decrease of the savings, that has effects on the banking system's activity and on the general financial stability. The growth of the interest taxation next to the tendency of growth of the banking interests was a stimulus for finding investment alternatives for those with surplus capital.

If we take into consideration the incomes from the capital market, we can notice a growth in the fiscal pressure regarding *the taxation of the income originated by dividends*, the perceived taxation quote increasing from 5% in 1999 to 16% in 2005. The sums received for the participation to the closed investment fund titles come with 16% from the total. At the titles of value's transfer the taxation is calculated by applying 16% to the flat gain from the transfer of the titles of value gained at 1st of June 2005 and lost at 1st of January 2006 through applying a smaller share than 1% to the flat gain from the transfer of the titles of value got at 1st of June 2005 and lost in a period smaller than 365 days. The differentiate taxation's effect is obvious – the diminution of *the speculative transactions*. But the practice from the Romanian capital market shows that, if there is a consolidation of the capital market, the decrease and increase periods of the shares become more and more rare, thing that makes the investors to mark more and more often the profit in spite of the higher taxation rate of 16%.

The importance of the fiscal policy on the evolution of the capital market is obvious. Using the fiscal pillars it has, the state can stimulate or not the consumption and the investments. If there is a stimulation of the expenditures, the quantity of the currency that remains for the possible individual investors is reduced and with it is also reduced the capital offer on the capital market and this limits the access of the issuers to the financing sources. Contrary, if the state wants to develop the local capital market, it has to adopt a series of fiscal actions that stimulates the individual investors as well as the institutional investors to increase the invested capitals on this market.

2.3 Recent Evolutions of the Romanian Financial System and the Correlation with the Economical Growth

We concluded, in the last paragraph, that the Romanian financial system suffered, in the last decades, a series of reforms meant to create a more and more competitive environment, for the benefits of the users of this system, and this also led to the development of the economy. As some recent studies say, the growth of the banking assets and market capitalization percent in GDP of a country were constantly positively correlated with the growth of the income for every inhabitant. It is easy to understand this fact taking into account that a significant growth and an efficient functioning of the financial system is necessary for the economic development and the prosperity of a country.

If we take into consideration the stated above and analyze at the level of the current Romanian financial system, we can notice that the activity of the banking system, as well as the one of the Romanian capital market had an upward trend which is correlated with the economic growth of Romania from the last few years. But for having a stable and healthy financial system the non-banking intermediaries as well as the banking ones have to develop for realizing important synergies at a national level. While in Romania the banks are dominant over the financial system, the traded companies, individuals, and the public sector as entities with financing needs have to have a variety of financial instruments in order to reach their financial objectives. Unfortunately, the degree of choosing other financing sources except the traditional ones is very small (Figure II.4, II.5).

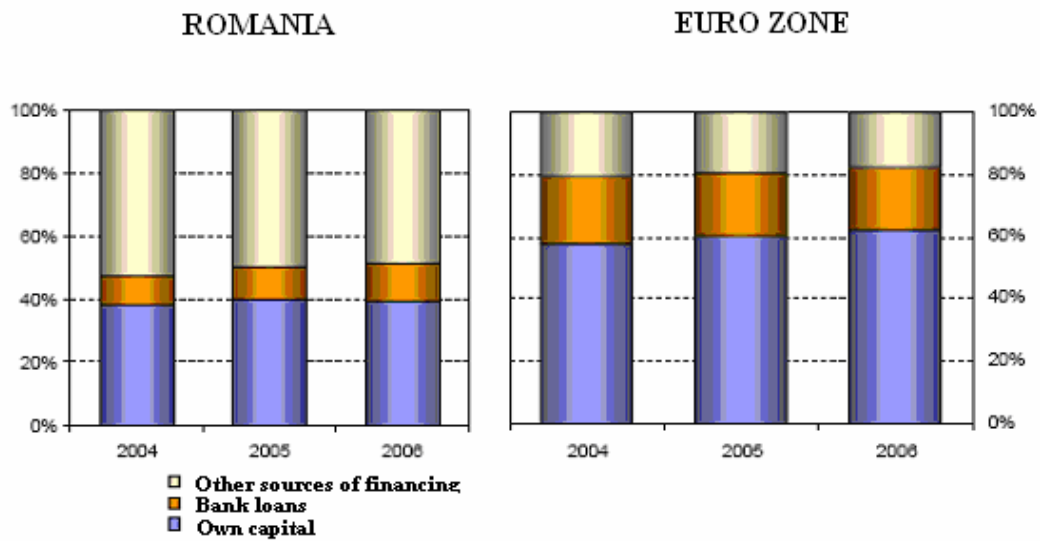


Figure II.4 – The structure of the liabilities of the economical entities

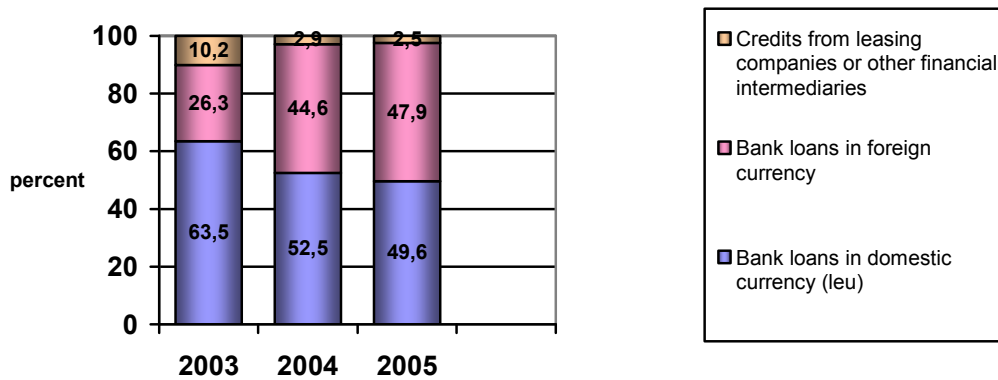


Figure II.5 – The structure of the individuals liabilities

The capital market can and must answer on one side to the demand of financing the national economy, and on the other side to be an advantageous investment alternative for those willing to give up their financial resources. The market capitalization/bank assets ratio is high in most of the European Union's countries, including the countries that entered EU in May 2004 (Figure II.6). In the same time there is a global growing tendency of this ratio.

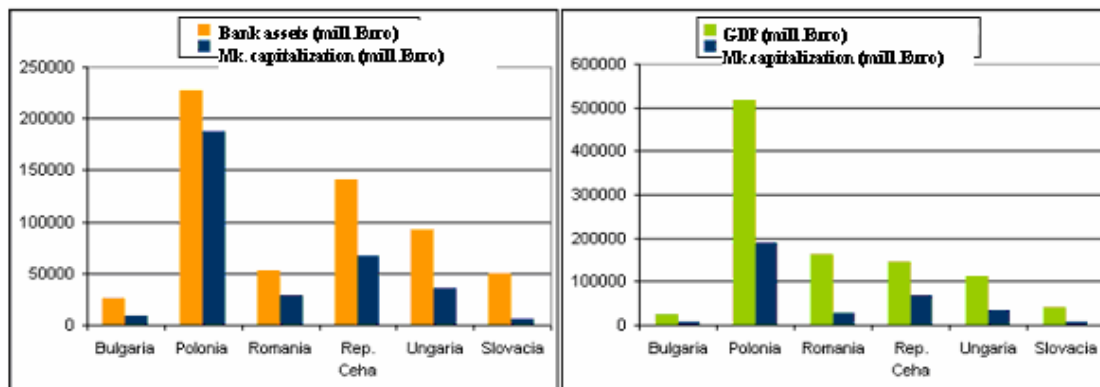


Figure II.6 – Regional comparison on the basis of the bank assets/market capitalization and GDP/capitalization ratios

Although the growth of the level of financial intermediation and activity of the financial affiliates was getting obvious over the time, if we make a brief comparison with the situation of the old member states of the European Union or the regional situation, our country reaches a not quite satisfying level. But we can say that the recorded evolutions from the regional financial markets are more and more correlated, thing seen especially on the stock market.

In our opinion, after a global analysis of the important aspects that define the Romanian financial system through its most significant two representatives (the banking system and the capital market) and the recent tendencies recorded on the global financial market we can say that, currently, the financial system is in transformation having as final objective that of becoming comparable in its structure not only on a regional level, but also European. We assist, on one side, at an institutional and legislative transformation related to the European trends, and on the other side, we cross a quantitative growth in the level of the number of affiliates and the capital in action.

The fact that the Romanian financial market is more and more mature and the trust in its different sectors is constantly growing is also noticeable from the point of view of the reorganization of the assets held by the population. If we look at the below figure (Figure II.7), we can conclude that from the portfolio of the population there is a higher and higher weight towards the acquisition of stocks, bonds, and investment funds titles. This changing was influenced especially by the decreasing tendency of the interest rates. Restructuring the population's assets' portfolio is accompanied by risks and pleads for the need for initiating actions by the authorities for increasing the degree of financial education of the population.

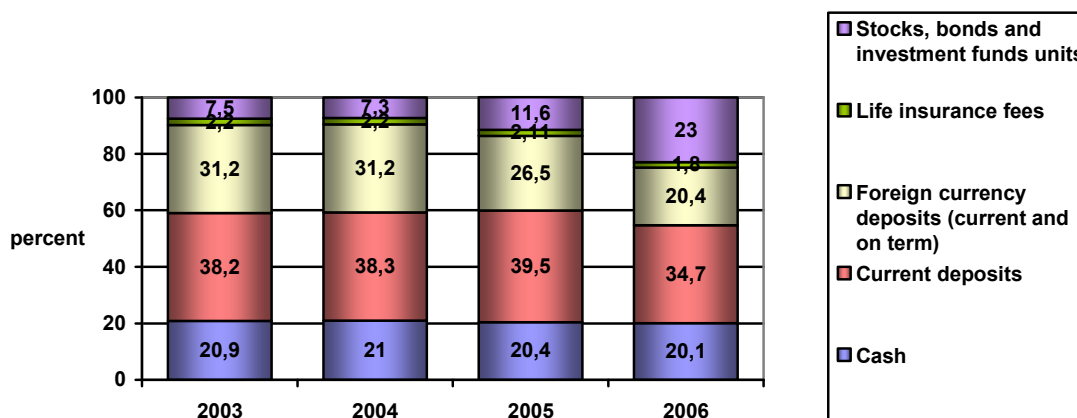


Figure II.7 – Structure of the individuals assets

The capital market started to be attractive for those with surplus capital and this is, lately, a growing tendency favorable to the Romanian economy. In my opinion, this thing was due to the favorable modifications in the local economic environment, to the growth of the incomes of the population and to some rearrangements in the investors' structure. But for encouraging this fact is necessary the growth of the stock market's transparency, sustaining the principles of corporative government, providing a wide and adequate offer of financial instruments on the stock market and the adoption of adequate costs structur. All of these could lead the domestic capital market to a more and more important place in the European stock markets. A more liquid and efficient stock market will allow the Bucharest Stock Exchange to increase its presence between the international financial organizations and to maintain more and more tight contacts with the other European stock markets.

As we said before, the necessity of the financial system development is essential for Romanian economy and implies intensifying the activity of the non-banking financial institutions. Through the delivery of the alternative and diverse financing services, they assure the facilitation of the mean and long-term investments that are many times a challenge for the banking based financial systems. They get into direct competition with the banks in attracting the mean and long-term funds and in this way support the development of the stocks, bond, mortgage, leasing, factoring markets. These institutions that collect the economized incomes allow a better diversifying of the risks, reduce the systemic risk, realize a better allocation of the risk for those who want to endure it, and the appliance of some advanced transaction techniques of the portfolios. Romania would gain from enlarging and deepening of the financial market, capable to offer financial services at a high level.

Unfortunately, if we take a closer look to the chart below, we will notice the low degree of the Romanian non-banking intermediaries activity. (Figure II.8).

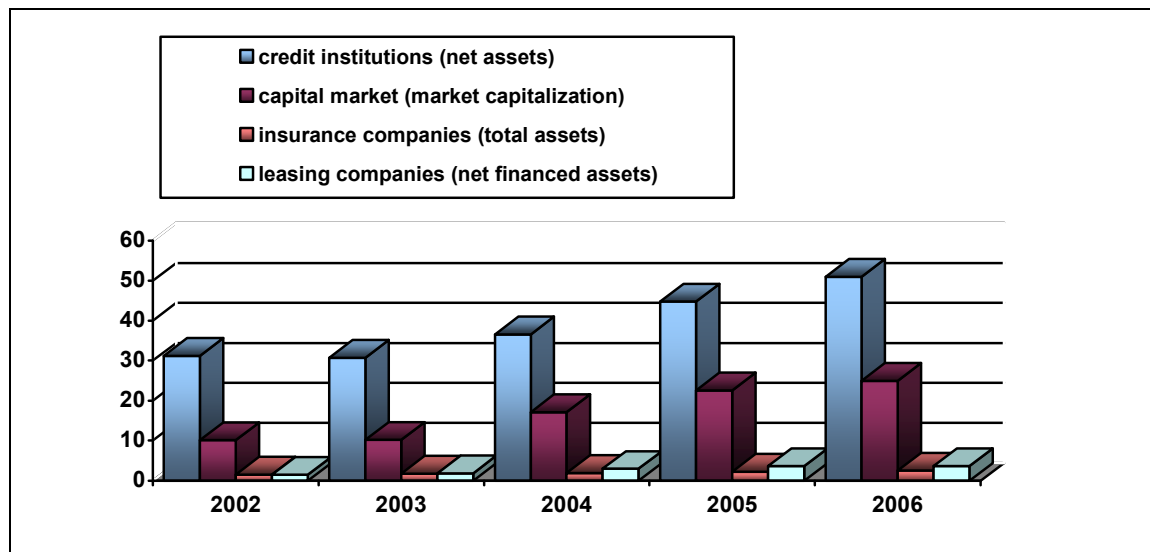


Figure II.8– Principal components of the financial system (% in GDP)

The unsatisfactorily situation revealed by the Romanian non-banking financial intermediaries activity is also presented in the following figure, meant to be a comparative illustration with the main EU-15 non-banking financial intermediaries situation. We notice that in 2004 they had a much more important weight in GDP than the one this sector realizes in Romania (Figure II.9).

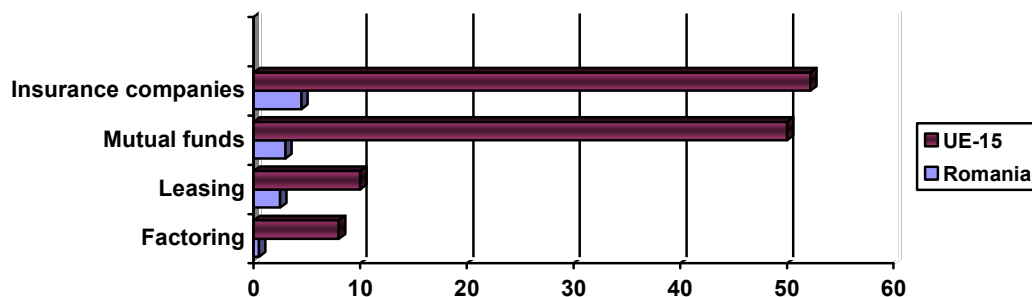


Figure II.9 – Principal categories of non-banking financial intermediaries and the percent of their assets in GDP- comparative analysis Romania-EU-15 (2004)

The situation of the non-banking intermediaries is considerably improving at a national level. The economical growth experienced by Romania in the last years is the main factor that influenced this improvement and it led to a growth of the incomes.

On the leasing market there is a significant development which confirms the statute of the leasing as financial product complementary and competitive to other banking products and capable of sustaining the development of the various sectors of the national economy. Therefore we can say that leasing has become a mean financing source capable to sustain the development of the different sectors of the national economy to competitive financial costs.

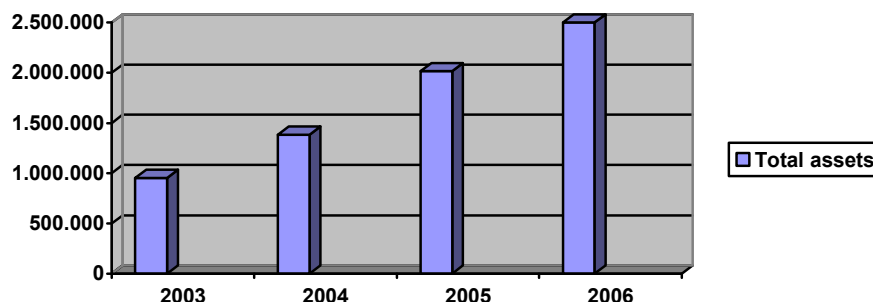


Figure II.10- Evolution of leasing market in Romania between 2003-2006

The factoring is present in the Romanian legislation from 2002 and it is extremely useful especially in import-export operations where the need of liquidities and the recovery in short time of the invested funds are in equilibrium. Through factoring, the companies that make trade transactions also benefit by the fact that they can concentrate on the development of the activity, while the agent follows up the cashing and the evidence of the invoices of the factoring. The Romanian companies started to cope with this kind of market in 2001 because there was a lack of the banking offer and the macro economic conditions were not so good. But the present tendency is of an accentuated growth and the local factoring market is split between BRD (27%), BCR (23%), Raiffeisen (23%), Unicredit (19%), and ABN Amro (12%)²³.

The pension system reform implied the extension of the bases of the pension system through adding another two pension pillars, along the public pension, stimulating the development of the activity of the private pension funds in their try to achieve a higher volume of compulsory and optional private pensions. In 2016 is predicted that the percentage from the monthly income of any employee for the private

pension will increase with 6%. This thing influences also the local capital market. The experience of the other countries shows that the social security system reform has a significant potential influence over the capital market. The existence of the two pillars is a premise of the intensification of the institutional investors' activity embodied in the private pension funds in their try to find adequate investment instruments. This thing inevitably leads to the creation of some diversified instruments on the capital market, the increase of the liquidity on the market, and a deepening of the financial market as well.

Regarding the local market of the mutual funds, it has a high potential although it is on a reduced level in comparison with other countries in the region. With the decrease of the bank interest rates, the mutual funds start to possess a stronger position on the market. Presently, on the Romanian market there are four categories of mutual funds (monetary, bonds-based, diverse, and stock-based), and the efficiency they offer is in high competition with the one offered through bank deposits. The below table (Table nr. II.4) illustrates the predicted growth of the financial assets of the mutual funds between 2006 and 2008, from which we can easily notice that they have the highest growth level predicted for this period.

Table nr. II.4

Annual average growth rate of the financial assets in the period 2006-2008

	Annual average growth rate
Cash	15 %
Bank deposits	17 %
Stocks	17 %
Mutual Funds	44 %
Insurance Funds	29 %
Pension funds	0 %

In conclusion, Romania would gain from the development of the non-banking financial intermediaries, from developing its domestic capital market, and the financial system in general. The reforms from the Romanian financial system have to go on for developing an efficient financial intermediation which is necessary for a sustainable economical growth.

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