NATIONAL BANK OF ROMANIA

Financial Stability Report

– Overview –

2013

1 OVERVIEW

Financial stability has remained robust since the release of the previous Report, in September 2012. Financial stability has stood up to the ongoing challenges amid the further difficult international environment, the improvement in the balance of risks generated by domestic macroeconomic developments notwithstanding. The major weaknesses of the banking sector, namely the significant level of non-performing loans – in the context of the negative dynamics of lending to the private sector – and the faster cross-border deleveraging, are further manageable. Solvency, provisioning and liquidity levels have continued to be adequate, enabling the banking sector to overcome any moderately unfavourable developments without major difficulties. The main challenges to financial stability over the period ahead are posed, the same as in most EU economies, by the sustainable resumption of lending, against the background of ongoing and even faster deleveraging internationally, and the adequate management of bank asset quality, also by striking a functional balance between the costs and benefits of various alternatives in addressing non-performing exposures.

The successful completion of the precautionary financing arrangement with the European Union, the International Monetary Fund and the World Bank and the signing of a similar agreement conducive to the furthering of reforms meant to consolidate domestic macrostability and the Romanian financial system contribute to the preservation of financial stability.

The domestic banking sector has continued to be well insulated against detrimental developments both locally and internationally. ***Firstly***, the level and quality of own funds has remained adequate: (i) the solvency ratio stood at a comfortable 14.7 percent in June 2013, considerably above the minimum required value of 8 percent, (ii) own funds consist mainly of items with a high and very high loss-absorption capacity (Tier 1 capital ratio of 13.6 percent in June 2013), and (iii) the NBR decided to keep in place prudential filters when calculating own funds and bank prudential indicators throughout 2013 (so that, *de facto*, the solvency indicators continue to be around 4 percentage points higher than the reported levels), before gradually phasing out these filters during 2014-2017, following the implementation of Basel III additional capital requirements.

The results of the banking sector solvency ***stress test*** spanning 2013 Q3-2015 Q2 show that, overall, credit institutions remain resilient to significant adverse macroeconomic shocks, further maintaining an adequate level of the solvency ratio. Under an adverse scenario, incorporating a depreciation of the domestic currency by over 20 percent and a prolonged recession, assuming default rates comparable to those seen during 2009, the solvency ratio of the Romanian banking system (at aggregate level) would decrease by approximately 4 percentage points to 10.8 percent, remaining above the prudential threshold set by the NBR. As regards a few small-sized credit institutions, their lower share of interest-bearing assets in total assets, together with their strategy of covering fixed costs via above-average interest margins, amid a riskier loan portfolio structure (meaning that the ratio of risk-weighted assets to total assets is considerably higher for these banks compared to the rest of the sector) as well as some specific issues relating to the management of interest rate risk, could call for additional capital or taking steps towards reducing the level of risk-weighted assets.

Secondly, the degree of NPL coverage with IFRS provisions and prudential filters has remained at a comfortable level, i.e. 89.5 percent as of August 2013, one of the highest readings in the region. Such a prudent stance adds to the constraints still affecting credit institutions' financial results.

In 2012, the domestic banking sector incurred losses (lei 2.3 billion), owing to the considerable increase in the volume of credit risk provisions, against the backdrop of higher NPL volumes and collateral revaluation. Nevertheless, the profitability levels of larger banks generally stayed in positive territory. At the end of August 2013, the domestic banking sector reported a profit of lei 1.5 billion on account of lower provisioning costs when compared to the same period of the previous year, as well as the reduction in financing costs amid the improvement in Romania's sovereign risk perception. The ROA and ROE profitability indicators returned to positive territory, i.e. 0.6 percent and 5.9 percent respectively. The sustainable resumption of lending to the private sector is, however, the key prerequisite for financial results to remain positive over the longer term.

The relatively high non-performing loan ratio, which has a detrimental impact on bank profitability, is also due to bank portfolios further comprising a significant share of borrowers with overdue loans, including those with a proven very low likelihood of repayment. For instance, as regards the portfolio of household loans, around 70 percent of non-performing borrowers (recipients of either real-estate credit or mortgage-backed consumer credit) had been in a state of default for more than a year or had recorded multiple defaults as of June 2013. Banks resorted on a relatively wide scale to loan restructuring/rescheduling and foreclosure, yet the effectiveness of these NPL management techniques has so far remained below potential. Other two alternatives, i.e. disposal and write-off of claims, were less resorted to, although they might prove more effective in cleaning up credit institutions' balance sheets. The most visible positive effect of a wider recourse to the aforementioned solutions would be the improved image of the domestic banking sector via a reduction in the volume of low-quality assets. For example, the removal from the balance sheet of any non-performing exposures vis-à-vis the corporate sector (through disposal or write-off of claims) would diminish this sector's NPL ratio from 23.4 percent (the August 2013 reading) to 7.5 percent. This would result from the contraction in the large volume of non-performing loans generated by borrowers with a low likelihood of servicing their debt (loans overdue for more than 365 days amounted to lei 19.7 billion, making up 74 percent of total NPL, as of August 2013).

Thirdly, banks' liquidity position has remained adequate, with sufficient buffers to weather any adverse developments such as a reduction in funding by parent banks or potential shocks related to the early withdrawal of corporate and household deposits. The NBR ensured the adequate management of liquidity across the banking sector, inter alia by supplementing the regulatory framework and providing liquidity via weekly repos. In addition, during 2013 H1, credit institutions' recourse to central bank reserves supplied via repos declined systematically, given the progressive rise in the volume of structural liquidity in the banking system. These developments helped abate the volatility of interbank money market rates and enhance the transmission of monetary policy signals, resulting in the gradual and sustainable narrowing of the spread between lei- and euro-denominated interest rates.

Parent banks' exposure to their subsidiaries in Romania has so far diminished in an orderly manner, although at a faster pace since end-2012, with subsidiaries offsetting the 26.2 percent reduction seen December 2011 through August 2013 (from EUR 20.3 billion to EUR 15 billion) by raising deposits on the domestic market. Deleveraging effects to date have been largely corrective: banks' reliance on external financing has gradually declined, the relatively high degree of household indebtedness has inched down, while the business sectors with the potential to sustainably alter Romania's economic growth pattern have generally received additional funding compared to the other sectors. Assuming the deleveraging process that the major banking groups embarked upon continued to gain pace, entailing liquidity shocks across the domestic banking sector over a short time horizon, the latter would be resilient to these unfavourable developments, certain vulnerabilities notwithstanding.

According to the results of the macro-prudential liquidity stress-testing exercise, challenges relate to fund conversion from lei into euro, certain asset sales and the impact on real sector funding.

The recent events in Cyprus have not exerted a noticeable impact on the domestic financial sector, since the crisis had effects only on banks with Cypriot capital (whose share in total assets of the Romanian banking sector was 1.4 percent in August 2013), with household and corporate deposits witnessing normal fluctuations. Domestic banks owned by financial institutions from euro area countries perceived by international markets as bearing the brunt of the sovereign debt crisis and of its negative feedback loops with investor concerns regarding the quality of banks' balance sheets (the GCIIPS countries – Greece, Cyprus, Italy, Ireland, Portugal and Spain) report overall solvency ratios above the system-wide average, while the provisioning coverage ratio of non-performing loans and the asset quality are close to the system's average. Moreover, the share of short-term external loans in total external loans of banks in this category was significantly below the system-wide average in August 2013. The specific challenges faced by parent banks in their home countries call for attention in assessing risks. The National Bank of Romania further closely monitors local and international developments and acts towards the adequate management of liquidity in the domestic banking sector. Maintaining comfortable liquidity, provisioning and solvency levels is an important prerequisite for the Romanian banking sector to adequately weather any adverse developments, including those triggered abroad.

Aside from the orderly progress in deleveraging, two other preconditions for the sustainable resumption of lending to companies and households are the maintenance of the latest trends in terms of more balanced developments in new loans by currency and the consolidation of sustainable structural changes in banks' business model as regards lending to non-financial corporations. Keener demand for loans in domestic currency and the new steps taken by the NBR starting 2011, prompted both by the currency risk likely to impact unhedged borrowers' capacity to service loans and by the need to comply with the relevant ESRB recommendations, have contributed to more balanced dynamics of the flow of new business since the release of the previous Report. For instance, the share of new EUR-denominated loans to households shrank considerably in the case of consumer loans (from 35.7 percent in 2011 to 10.3 percent December 2011 through August 2013) and to a lesser extent when looking at housing loans (from 97.8 percent in 2011 to 86.4 percent during December 2011 – August 2013). The non-performing loan ratio for foreign currency loans stood at 11.1 percent in June 2013 (versus 8.9 percent for lei-denominated credit), up 2.5 percentage points from December 2011. The volume of non-performing corporate loans in foreign currency soared 73.7 percent December 2011 through August 2013, while that of non-performing loans in lei expanded by 53 percent during the same period. After reaching 4.3 percentage points at end-2011, the gap between NPL ratios in domestic and foreign currencies was bridged in August 2013, when they came in at 23.4 percent and 23.5 percent respectively. The implementation of the "First Home" programme solely for lending in domestic currency starting August 2013 and the lower interest rates on lei-denominated credit, also in response to the central bank's decisions to cut the monetary policy rate by a cumulated 100 basis points July through September 2013, are expected to help alleviate the currency mismatch in the case of housing loans as well. The same trend is also anticipated for corporate lending, since the steps taken by the NBR at end-2012 for better management of credit risk generated by unhedged borrowers are seen leading to more balanced developments in new business by currency.

Corporate funding witnessed favourable structural developments December 2011 through June 2013, the most noteworthy being: (i) lending to firms producing high value added goods (medium high-tech and high-tech) went up 4.3 percent, whereas the volume of loans granted to companies producing lower value added goods (low-tech and medium low-tech) contracted 1 percent; (ii) companies in the tradable sectors reported a 0.6 percent rise in financing, while the non-tradable sectors posted a decline of 1.1 percent; and (iii) looking at the business profile, agriculture reported a 20.9 percent increase in funding, followed by trade and manufacturing with an advance of 3.3 percent and 0.6 percent respectively. Furthermore, SMEs received additional financing from domestic and foreign creditors (up 0.9 percent), with loans extended by domestic banks posting the fastest dynamics (2.5 percent). Conversely, lending to knowledge-intensive services companies dropped 6.2 percent, while the volume of funds channelled to less knowledge-intensive services companies stood 0.2 percent lower (nominal values adjusted for the exchange rate effect).

Financial intermediation, assessed in terms of the financial system's assets as a share in GDP, slightly decreased in 2012, given the slower economic growth rate in Romania and the ongoing tensions on global financial markets. The dominant position of the banking sector weakened at end-2012 and in 2013 H1. The direct contagion risk within the Romanian financial system remains subdued for the banking sector, whereas the other financial institutions may be vulnerable to the concentration of exposures to domestic credit institutions or of funds raised from the latter.

Domestic and external developments had a strong bearing on the ***non-bank components of the financial system***. In particular, the insurance sector witnessed a consolidation during 2012, when the share of gross premiums written in GDP saw its previous years' decline come to a halt. The non-life insurance market recorded positive real dynamics for the first time in the past four years, with a constant share of gross claims paid in total gross premiums written. The profitability of insurance companies remained in negative territory in 2012 as well, despite a slight improvement versus the year-earlier reading.

The private pension system is not exposed to significant risks in terms of financial stability, given the still low level of overall assets held by private pension funds vis-à-vis the rest of the financial system and judging by the investment portfolios, which point to a low risk profile. The performance of pension funds improved in 2012 on account of favourable domestic developments, while the share of foreign exposures in total financial assets continued to narrow.

Non-bank financial institutions (NBFIs) saw their business shrink slightly January 2012 through June 2013. The non-performing loan ratio of NBFIs is further high, yet the provisions set up to cover expected losses help mitigate these entities' credit risk. NBFI profitability returned into positive territory at end-2012, thanks to streamlining operating costs and cutting net expenses with provisions amid the improved domestic macroeconomic context.

Financial market volatility decreased in the early months of 2013. The decline in investors' risk aversion sent short-term interbank money market rates lower and caused the yields on the government securities market to fall. However, the market saw sharper fluctuations in the period May-June 2013, amid heightened uncertainty over the timing of the start and scale of the tapering of the US Federal Reserve's financial asset purchase programme. CDS prices for Romania's sovereign risk were closely linked to investors' trends across the region as a whole. In 2013, the CDS quotes hovered around 200 basis points, compared with an average of approximately 346 basis points in 2012. In June 2013, global financial market strains also temporarily affected the CDS prices, but the volatility peak remained below the previous years' levels thanks to the improvement in economic fundamentals, which fostered a reduction in the volatility of exposure to Romania compared to other countries and a relative balancing of short-term capital movements.

Lending and risk profile of the financial system were under the mixed impact of the domestic and global macroeconomic environment. The balance of risks stemming from domestic macroeconomic developments improved as against that presented in the previous Report: economic growth stayed in positive territory at 0.7 percent in 2012, even though it was further below potential and lower than the 2011 GDP growth of 2.2 percent, under the impact of supply-side shocks, fiscal consolidation carried on, while external accounts witnessed a considerable improvement in 2013 H1. The projections for the years ahead point to moderate, but above EU average, GDP dynamics, thereby underpinning the progress of real convergence, despite the negative output gap narrowing only gradually. The GDP dynamics sustainability is also reflected by the key macroeconomic indicators remaining below the alert threshold in the European Commission's Scoreboard for the surveillance of macroeconomic imbalances.

An essential prerequisite in the coming years is to ***preserve domestic macroeconomic stability*** amid the consolidation of financial stability with a view to strengthening the confidence of the main stakeholders (resident and non-resident investors, consumers, the financial system, etc.) in the Romanian economy. In order to maintain and enhance macrostability and financial stability, structural reforms in the economy should continue, labour market conditions should improve, the absorption rate for EU funds should increase, innovation should play a more prominent role in economic development, fiscal consolidation should carry on, and payment discipline should tighten for all system participants. The general government deficit narrowed to 2.9 percent of GDP (according to ESA95 methodology) in 2012 versus 5.6 percent of GDP a year earlier, so that the EU Council approved the abrogation of the excessive deficit procedure for Romania in June 2013. For 2013, the government envisages to bring the deficit down to 2.4 percent of GDP (according to ESA95 methodology), or 2.3 percent of GDP (according to national methodology), and to cut the structural deficit to 1.7 percent of GDP from 2.7 percent of GDP in 2012.

Public finance sustainability is reflected by the developments in and composition of public debt, which accounted for 37 percent of GDP in May 2013 (according to ESA95 methodology), well below the 60 percent reference value in the Treaty on European Union and one of the lowest readings across the EU. In 2012, the Romanian government started to issue USD-denominated bonds, thus diversifying its investor base. The maturity breakdown remains comfortable (the share of medium- and long-term debt widened to 84 percent of total debt in 2012 and 92 percent in May 2013, from 77 percent in 2011), the share of lei-denominated public debt remains elevated at 41 percent in May 2013, down slightly against 2011, and the bulk of sovereign debt is held by residents. Non-resident investors' participation in the domestic market for debt securities (in lei and euro) issued by the Romanian government went up sharply in 2012 and the first seven months of 2013 (these investors accounted for 24.5 percent of the securities outstanding at end-July 2013, compared with 14 percent at end-2012 and 11.7 percent at end-2011), but remained well below the levels seen in other countries in the region (53 percent in Hungary, 36 percent in Poland). With a view to dealing with any unfavourable developments in the access to funding, the Romanian government moved to establish a foreign currency buffer as early as 2010, so that budget financing requirements are met for a period of at least four months, and intends to preserve it in the years ahead as well.

Companies' financial position improved slightly in 2012, against the background of the modest 0.7 percent increase in real GDP and a still tension-ridden global environment, pointing to the frailty of this improvement. Corporate performance was mixed, but the sustainable change in the economic growth pattern carried on gradually. Payment discipline however remained loose for a significant number of companies and insolvency became increasingly pronounced starting 2012. The measures taken by the authorities to address this situation were aimed at tightening the discipline in filing for insolvency as well as the payment discipline for all participants in the system, but there is still a need for hard budget constraints, also on private companies. In this vein, the legislative framework governing commercial, fiscal and accounting matters should be further improved in order to enhance commercial and financial discipline across the real sector, which is expected to support banking system soundness and stability as well as the public finance and the financial sector as a whole. The relatively high heterogeneity of the corporate sector has led to the fact that, although microeconomic fundamentals improved on an aggregate basis, the companies that grappled with difficulties in the past have generally failed to surmount them; as a result, companies' capacity to service their bank debts was further constrained (the non-performing loan ratio rose to 23.4 percent in August 2013 from 14.4 percent at end-2011). The outlook for the non-performing loan ratio reveals that, in the absence of more comprehensive measures taken by banks to clean up their balance sheets, its worsening will most likely continue in the period ahead, albeit at a slower pace. Credit institutions report adequate capital and provision levels to cover the risks related to corporate financing and have available risk management techniques, which are yet to be used to the fullest. Furthermore, the National Bank of Romania took additional prudential steps to preserve solvency and provision buffers, addressing unhedged borrowers in particular, in line with EU-wide recommendations in the field. Moreover, the new 24-month economic programme concluded with the European Union and the International Monetary Fund provides for further implementation of structural reforms in the economy, which is expected to alleviate the vulnerabilities of non-financial corporations.

The risks arising from ***households' balance sheets*** posted a balanced evolution, while the strongest vulnerability of this sector, i.e. high indebtedness, especially in foreign currency, followed a slightly downward path, in line with deleveraging moving gradually ahead for this category of debtors. The positive developments were uneven across households' income classes, as low-income and very-low-income groups broadly reported a deterioration of their financial standing. The ability of this sector as a whole to service its bank debt kept diminishing, albeit at a slower pace than in the previous period, and prospects are mixed. The non-performing loan ratio went up by 2.2 percentage points in December 2011-June 2013 to 10.4 percent from 8.2 percent, while the volume of non-performing loans increased by 28 percent over the same period. The Romanian banking sector is adequately covered against risks stemming from household lending: (i) capital adequacy ratio remains significantly above the minimum required level, (ii) expected risks from household lending are almost entirely covered by IFRS provisions, including prudential filters (96.3 percent in August 2013), and (iii) the value of collateral in banks' portfolio remains high enough to cover the risks stemming from renewed unfavourable developments (the loan-to-value – LTV – ratio for housing loans reached roughly 85 percent in June 2013, with this increase being also driven by collateral revaluation).

The prospects for the developments in households' repayment capacity are mixed, but indicate a future slowdown in the growth of the non-performing loan ratio (or even a lower ratio provided that banks will take stronger balance sheet clean-up measures). The non-performing loan portfolio breakdown reveals three vulnerabilities, also identified in the previous Report, which are closely connected to the challenges to household indebtedness structure. First, credit risk associated with foreign currency-denominated loans continued to increase, at a faster pace than that of the risk posed by lei-denominated loans. Second, borrowers with a net income lower than the whole-economy average are still the most vulnerable category across the banking sector, accounting for about 70 percent of total non-performing loans. Third, the loans granted under looser terms and conditions during the pre-crisis years put further pressure on bank asset quality. The riskiest loan portfolios are those extended in the period 2007-2008, with the volume of non-performing loans making up roughly 70 percent of total non-performing loans in June 2013. The non-performing loan ratio for these exposures is considerably above the average (15.4 percent and 18.4 percent for the loans extended in 2007 and 2008 respectively, compared with 10.4 percent on average in June 2013) and is still rising quicker than the average. These figures are further evidence that lending should resume on a sustainable basis, as the credit institutions' loosening of lending standards in the period preceding the financial crisis led to a build-up of vulnerabilities.

Most of the loans granted to companies and households are mortgage-backed (67 percent or lei 147.4 billion in June 2013), whereas real-estate market weakness over the past few years has posed three challenges to the bank loan portfolio, as follows: (i) to preserve mortgage collateral at an appropriate value; (ii) to adequately manage the growing risk relative to mortgage-backed lending, also by ensuring a functional balance between costs and benefits of various solutions to manage non-performing loans; and (iii) to review bank policy effectiveness in terms of the type of collateralisation given the pro-cyclical tightening of lending standards.

The recent housing price downward correction has led to a decline in the collateral coverage of housing loans to households, as reflected by developments in the LTV ratio, which climbed from almost 78 percent in December 2011 to 85 percent in June 2013. As for corporate loans, the LTV ratio also worsened, nearing 90 percent as against 79 percent (June 2013 versus end-2011). Empirical evidence shows that the LTV ratio is an important element of debt servicing, which calls for credit institutions to maintain it at prudent levels. The National Bank of Romania took steps so that the LTV ratio for new business should be adequate and the LTV ratio for the outstanding loans should capture the decline in the prices of real-estate assets held by banks as collateral.

Domestic macro-stability strengthened amid a still intricate global environment characterised by: i) weaker-than-expected growth both of the world economy and the EU's advanced economies; ii) the ongoing balance sheet adjustment by the major European banking groups, including from a cross-border perspective, along with the efforts made towards an early fulfilment of the new capital requirements, liquidity requirements and for identifying sources to cover bail-in-able capital tranches, as well as by iii) the uncertainty surrounding the potential capital movements where the major central banks around the world would decide to gradually taper their far-reaching non-standard monetary policy measures implemented thus far. The key consequences of the tension-ridden global environment on Romania have materialised in challenges to preserving an orderly deleveraging process across the local banking sector, strengthening resilience to foreign capital flow volatility and containing the adverse effects of modest economic growth in Romania's main trading partners.

The delay in resuming growth in major EU economies, Romania's main trading partners, has a detrimental impact on domestic economic growth and may affect foreign trade companies' ability to withstand various unfavourable developments. So far, such risks have been contained particularly by: (i) exporters' capacity to diversify their markets, reducing their exposure to euro area countries in relative terms (down 1.5 percentage points in 2012) by switching to new foreign markets, (ii) preserving foreign trade companies' access to funding (e.g., non-resident parent undertakings increased the loan volume to local net exporting companies by 10.6 percent in the period December 2011 – June 2013), and (iii) maintaining the economic and financial standing of foreign trade companies at a satisfactory level, above the economy-wide average. Romania's exports with high value added and innovative technology have remained on an upward path. Thus, medium-high technology products, making up the bulk of domestic companies' exports, have advanced markedly of late. As a matter of fact, providing incentives to innovative industries is a key goal, as mentioned in the Europe 2020 Strategy currently under implementation. Its achievement should be regarded as a priority and it would represent a potential advantage, as these industries proved their capacity to weather the crisis better than other sectors, with their share of value added increasing economy-wide, amid reasonable profit margins and considerable investment efforts.

In turn, enhanced resilience to the possible heightening of capital flow volatility calls for strengthening external debt service sustainability so as, together with maintaining domestic macro-stability, to preserve the access to external funding under adequate conditions and improve the structure of external financing flows, thereby contributing to the sustainable change in the growth pattern for the Romanian economy.

Potential risks to financial stability associated with the dynamics or structure of external capital flows have remained manageable and are expected to retain the same features. Following some capital outflows in the period May-June 2013, occurring simultaneously with similar events on other emerging markets, portfolio investments in Romania bounced back to levels close to those seen prior to the reduction in exposure to emerging economies in terms of asset class. This evolution validates the fact that capital flows are further directed particularly towards the economies where the major macroeconomic equilibria have already been adjusted or their adjustment is underway, as well as towards the countries implementing structural reform programmes.

First, Romania's short-term external debt followed a downward path, contracting by more than 12 percent in the period December 2011 – June 2013 (from EUR 22.8 billion to EUR 19.9 billion). Furthermore, the official foreign currency reserve provides an adequate coverage for the short-term external debt, the best across the region. Second, the companies generating the country's private external debt enjoy a satisfactory economic and financial standing, which enables them to withstand moderately unfavourable developments.

Third, the short-term external debt of non-financial corporations is accounted for nearly 60 percent by parent undertakings, with evidence showing that such debt proved among the most stable.

Fourth, medium- and long-term external financing of non-financial corporations provided by creditors in countries perceived on international markets as being more severely hit by the sovereign debt crisis (the GCIIPS, namely Greece, Cyprus, Italy, Ireland, Portugal, and Spain) holds a moderate share in total medium- and long-term external debt (15 percent in June 2013). Assuming adverse developments in financing extended by creditors from those countries, their direct impact on the Romanian economy or the Romanian banking sector via the corporate debtor channel is most likely low, also due to the maturity of the loans.

Fifth, the Romanian banking sector is able to withstand a moderate shock of a failure to roll over foreign borrowings, due to banks' higher stock of liquid assets, their gradual reduction in reliance on external financing (the share of external funding in total bank liabilities net of capital shrank 5 percentage points, while the loan-to-deposit ratio fell from 119.1 percent at end-2011 to 109 percent in August 2013) and to the enforcement of NBR measures aimed at strengthening credit institutions' capacity to cope with adverse developments in foreign capital flows. Among these measures, the following deserve mention: (i) broadening the range of eligible collateral by including foreign currency-denominated securities launched by the Romanian government and lei-denominated bonds issued by financial institutions, (ii) preserving the banking sector's prudential indicators on solvency and the degree of provisioning for non-performing loans at adequate levels, and (iii) ensuring an appropriate amount of eligible collateral by banks for their monetary policy operations in order to make available the necessary liquidity for the banking sector, if required. Last but not least, Romania has signed a new precautionary arrangement with the international financial institutions (the European

Union and the International Monetary Fund) tantamount to approximately EUR 4 billion; the Romanian authorities may draw on the programme only in the case of a serious and unexpected worsening of the economic and/or financial situation triggered by factors outside the scope of domestic decision-makers, should the already in place buffers set up by the authorities prove insufficient.

ReGIS payment system ran smoothly from January 2012 to June 2013, but the value of transactions started to decline at mid-2012. Although the aggregate liquidity available to the participants in the system was higher than the demand for resources, there were slight tensions affecting some participants' liquidity in the course of 2012, which however alleviated in 2013 H1. The value of transactions in ReGIS increased during the first part of 2012, as the central bank expanded its repo operations on the money market and the credit institutions resorted to significant intra-day credit operations; however, the amounts settled via this payment system fell subsequently to 2011 levels. Even though the SENT system experienced some operational incidents, they did not affect its stable and predictable functioning. The incidents had a marginal and isolated impact on the participants in the system. DSClear, RoClear and SaFIR clearing systems also operated smoothly throughout 2012 and in 2013 H1, with the major indicators on system performance remaining at high levels, thereby confirming their robustness.

The step-up in the volume of transactions on the secondary market for government securities, the larger amount of issues launched by the Ministry of Public Finance on the local market as well as the rise in National Bank of Romania's operations translated into an upturn in the number and especially in the value of instructions settled via SaFIR system in the course of 2012. The first half of 2013 witnessed negative growth of the total value of instructions processed as against a year earlier, the further upward trend in the number of settlement instructions notwithstanding. After having assessed the DSClear and RoClear systems in view of the applicable European standards, the National Bank of Romania made several recommendations and the system administrators took tangible steps to correct the identified deficiencies, while relatively minor inadequacies are still to be remedied in the upcoming period.

The micro- and macro-prudential regulatory framework is currently in a process of thorough revision both at EU and national level. The outcome of assessments regarding the impact of the CRD IV/CRR package shows that the credit institutions operating in Romania generally meet the requirements of European regulations. As the key elements of the banking union, namely the single supervisory mechanism, the single resolution mechanism and the national deposit guarantee schemes, are put in place, the segregation of duties between European and national authorities, as well as the sharing of financial obligations among the participating Member States will weigh on the effectiveness of the implemented mechanisms and non-euro area countries' interest in joining them.