

THE ROMANIAN BANKING COMPETITION AND THE ACCESSION TO EU

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In this study we try to assess banking competition in the Romania for 2001 – 2008, taking into account the evolution of market share of the top five, Herfindahl-Hirschman Index (HHI), performances indicators like ROA and ROE and evolutions of deposit and loans rates. We observed that the competition in the Romanian banking system increases continuously in the last years. The main factors which have influenced this process were: the privatization of the majority of state capital banks and the perspective of accession of our country in the EU. In the period assessed, there are two approaches: in the first period banks have had very good performances due to their market share in a low competitive banking environment and after the privatization of some state capital banks, the leader of the market lost market share in the favor of other bank with greater performances.

Keywords: bank competition, the Structure-Conduct-Performance Hypothesis, Efficient Structure Hypothesis, banking system, European integration

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Introduction

The competition in the Romanian banking system has been growing continuously in the last years. Romania has passed a period of transition to the market based economy from the beginning of the '90. Thus, the Romanian banking system had a period of transition, from a “monobank” banking system, with few specialized institutions to a modern one, based on market economy principles.

In this study we try to assess banking competition in the Romania for 2001 – 2008, underling the main factors which has influenced this phenomenon.

Measuring banking competition

In the literature, there are some empirical approaches concerning the evaluation of the competition, the most known being „the Structure-Conduct-Performance Hypothesis” (SCP) and the „Efficient Structure Hypothesis” (ESH). The first approach, SCP, supposes that higher concentration in the banking market causes less competitive bank conduct and leads to higher bank profitability. The SCP model is originally developed by Bain (1956). The second approach, ESH, developed by Demsetz (1973) and Peltzmann (1977) suggests that the superior performance of the market leaders determines the market structure, implying that higher efficiency produces both higher concentration and greater profitability.

The most common measures of concentration are the Herfindahl-Hirschman Index (HHI) and the n-bank concentration ratio (CR_n). The HHI is defined as the sum of squared market share of the banks in the market. The upper bound of the HHI is 10.000, which indicates a monopoly, and the lower bound is 0 in the situation of an infinite number of banks. A market with a result of less than 1.000 is a competitive marketplace, a result of 1.000 – 1.800 indicates a moderately concentrated marketplace and a result of 1.800 or greater indicates a concentrated marketplace. The n-bank concentration ratio (CR_n) is calculated as the percentage of the market controlled by the top n banks in the market, usually the first three or five banks, and the measure takes the share of deposit, loans or assets.

The profit is measured either by ROA or by ROE and the price of bank product is measure by the value of interest rates or commissions.

The evolution of competition in Romanian banking system 2001 - 2008

The accession to the European Union implies the entering in “the single” European market and the existence of the single banking license. In this context, foreign banks can enter more easily the territory of a member country, which can determine the expansion of competition in the local banking activity. The methods to enter the banking market can be diverse: open branches or subsidiaries; equity investment in the local banks; mergers or acquisitions of local banks.

After the accession of our country to the EU and the liberalization of the service market, a number of 190 foreign institutions have expressed their intention to have direct banking activities on the Romanian territory, out of which 174 are banking institutions, 3 are non-banking financial institutions and 13 e-money providers (NBR, 2008).

Millennium Bank, as this is the name of the local branch of the Portuguese Millenium BCP, is the first example of greenfield investment on the banking market after many years of acquisitions. Millennium Bank started its activity on the Romanian market on October 11, 2007, by simultaneously opening 39 branches in Bucharest and in other eight cities of the country.

Before 2007, there was some foreign entrances in the Romanian banking system after the privatizations of certain Romanian state banks, such as: Banca Română pentru Dezvoltare (BRD-GSG) bought by Soci t  G n rale and Bancpost in 1999, bought by a consortium formed by General Electric Capital Corporation (35%) and Banco Portugues de Investimento (10%); Banca Agricol  bought in 2001 by Raiffeisen Bank and Banca Comercial  Rom n  whose privatization process last between 2003 and 2006, when Erste Bank took the biggest bank of Romania. Also OTP Hungary overtook RoBank in 2004, the first acquisition of a bank with private capital in Romania.

As we can see in the Table 1, the concentration of the Romanian banking system has been decreasing continuously from 2001 to 2008. This means that the competition in the Romanian banking system has increased yearly, especially due to diminishing of the state capital and entering of foreign capital.

Also the performances indicators declined, being closer to the average value of this indicator. At end-2008, the key profitability indicators (ROA – return on assets and ROE – return on equity) showed a significantly higher level (1,56% and 17,04%) compared to that reported at end-2007 (1.01% and 9.43%). This development was due mainly to the sale of participating interests held by four banks in the equity capital of an insurance company, on the one hand, and to the higher net interest income, on the other.

Table 1. Bank concentration and profitability in the Romanian banking system (2005 – 2008)

	Dec. 2001	Dec. 2002	Dec. 2003	Dec. 2004	Dec. 2005	Dec. 2006	Dec. 2007	Dec. 2008
Number of banks	41	39	39	40	40	39	42	43
Market share of the top five banks in total assets (%)	66,1	62,8	63,9	59,2	58,8	60,3	56,3	54,4
Market share of the top five banks in total loans (%)	59,78	56,2	57,1	55,7	61,1	57,1	63,5	53,5
Market share of the top five banks in total deposits (%)	66,12	63,0	64,9	59,5	57,0	60,0	58,3	54,1
Market share of the top five banks in total equity (%)	n.a.	64,5	61,2	60,5	55,1	52,5	53,3	48,5
Market share of the top five banks in total profits (%)	78,46	68,71	60,94	51,49	83,13	84,1	85,0	n.a.
Herfindahl-Hirschmann index	1.427	1.381	1.264	1.120	1.124	1.171	1.046	926
ROA	3,17	2,64	2,40	2,15	1,65	1,31	1,01	1,56
ROE	21,38	18,27	17,72	16,79	12,64	10,41	9,4	17,04

Source: NBR, banks, Pia a financiar 

The leader of the market was continuously Banca Comercială Română (BCR), which was the biggest state bank until 2006, when the process of privatization was completed and it was bought by Erste Bank. In 2001 BCR owned about one third of the market in total assets, loans, deposits, equity and profits. Also, the ROA and ROE accounted a value over the average of the market. Even if his market share decreased during the period of 2001 – 2008, the evolution of performances indicators had a sinuous evolution. Between 2001 and 2006 these indicators decreased, but after 2006, the year of privatization, the profitability of the bank started increasing. In 2007 BCR lost his position in the share of market in total of profits in the favor of the next competitor BRD-GSG.

Tabel 2. Bank concentration and profitability of the leader of the Romanian banking system (2005 – 2008)

	2001	2002	2003	2004	2005	2006	2007	2008
Leader of the market	BCR	BCR	BCR	BCR	BCR	BCR	BCR	BCR
Market share in total assets (%)	31,27	31,51	29,42	26,30	25,7	26,2	23,8	20,4
Market share in total loans (%)	28,78	28,65	27,21	25,32	26,4	26,6	23,5	22,7
Market share in total deposits (%)	31,61	32,82	31,99	27,81	26,4	23,9	20,5	20,4
Market share in total profits (%)	42,75	43,02	35,49	34,28	35,15	33,3	18,0*	41,7
ROA	4,28	3,73	n.a.	2,73	2,3	1,6	1,45	2,94
ROE	24,22	20,93	16,6	18,6	16,9	18,8	20,6	38,2

* the leader was BRD with 33,5%

Source: NBR, banks, Piața financiară

The second competitor of the market in this period was BRD – GSG, the rest of the positions in top 5 changing in every year. In the period 2003 - 2007 the third competitor was Raiffeisen Bank, which has lost his position in 2008 in favor of Volksbank. BRD – GSG had a relative constant market share in contrast with the first competitor, which has lost market share continuously. Even if some banks was in the top 5, their deposit market share was very low, because their low interest in attracting deposits from Romanian market, in the context of receiving funds from their parent undertakings (e.g. HVB, Volksbank).

Table 3. Bank concentration and performances of the top five banks in total assets⁰ (2005 – 2008)

Year	Banks (first 5)	Market share of the top five banks in total assets (%)	Market share in total loans of the top five banks in total assets (%)	Market share in total deposits of the top five banks in total deposits (%)	ROE
2001	BCR	31,27	28,78	31,61	24,22
	BRD	15,74	18,36	16,71	30,7
	CEC	8,63	5,41	10,62	28,34
	ABN AMRO	5,62	3,87	4,39	111,57
	ING Bank	5,27	3,36	2,79	76,44
2002	BCR	31,51	28,65	32,82	20,93
	BRD	13,66	17,07	14,18	30,3
	CEC	7,71	1,82	9,45	7,77
	ABN AMRO	5,36	n.a.	n.a.	n.a.
	Raiffeisen Bank	5,04	5,23	4,95	n.a.
2003	BCR	29,43	27,21	31,99	16,6
	BRD	13,30	16,34	13,86	24,7
	Raiffeisen Bank	7,23	n.a.	n.a.	8,13
	CEC	6,51	2,34	8,24	12,98
	ABN AMRO	5,15	n.a.	n.a.	n.a.
2004	BCR	26,30	25,32	27,81	18,6
	BRD	13,0	15,9	13,7	23

Year	Banks (first 5)	Market share of the top five banks in total assets (%)	Market share in total loans of the top five banks in total assets (%)	Market share in total deposits of the top five banks in total deposits (%)	ROE
	Raiffeisen Bank	9,27	11,47	9,18	21,29
	CEC	5,71	1,58	7,14	15,02
	ING Bank	5,63	n.a.	n.a.	n.a.
2005	BCR	25,7	26,4	26,4	16,9
	BRD	15,0	17,3	17,7	30
	Raiffeisen Bank	8,7	9,3	9,6	20,83
	ING Bank	5,3	n.a.	n.a.	n.a.
	HVB	4,9	5,7	3,3	42,5*
2006	BCR	26,2	26,6	23,9	18,8
	BRD	16,3	20,2	19,1	34
	Raiffeisen Bank	8,3	7,6	10,2	15,69
	HVB Ţiriac	5,1	5,4	4,3	16,9
	Banca Transilvania	4,7	5,3	5,6	17,14
2007	BCR	21,7	23,5	21,7	20,6
	BRD	15,5	16,1	19,5	43
	Raiffeisen Bank	6,0	5,7	9,3	23,79
	Volksbank	5,9	5,3	1,4	8,8**
	Banca Transilvania	5,7	5,7	7,6	28.10
2008	BCR	20,4	22,7	20,4	38,2
	BRD	15,7	16,3	17,6	44
	Volksbank	6,8	6,7	1,4	n.a.
	Raiffeisen Bank	6,0	5,3	9,0	34,31
	Alpha Bank	5,5	8,2	3,6	12,62

* June 2005; ** September 2007

Source: banks, Piața financiară

As we can see, the first competitor BCR had lower performances like the other from top 5. Its performances were improved after the privatization in 2006, being more and more close to BRD, in the first position regarding ROE in the period 2001 - 2008. CEC another state capital bank in the system has lost position continuously and in 2005 it was out of top 5.

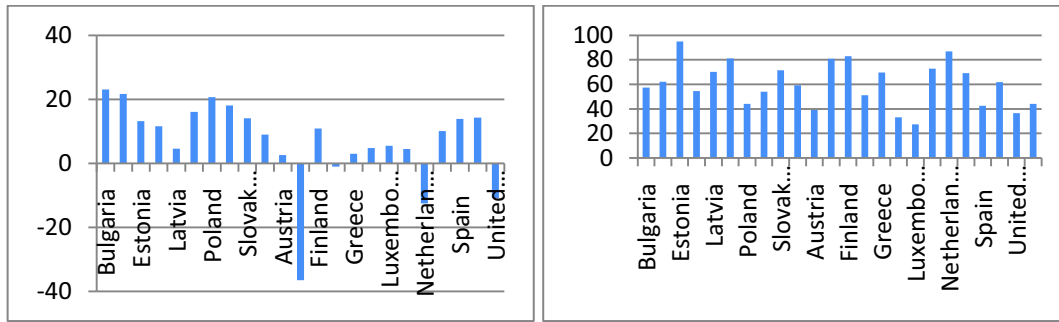
Even though competition in the banking system is continuously increasing the Romanian banking system proves to be concentrated. In 2008, the first 5 banks in Romania according to the value of their assets held 54,4% from the aggregate balance sheet assets, 53,5% from the total of offered loans, 54,1% from the attracted deposits and 51,4% from the equity of Romanian commercial banks, a letdown in comparison with December 2007.

Starting with 2006, the value of Herfindahl-Hirschmann index entered a slightly downward path, still posting a moderate concentration. In 2008 its value came below 1.000, indicating moderate to low concentration and a moderate to high competition.

These indicators demonstrate an improving in bank competition in the Romanian banking system as a consequence of entering in the European single market.

Also we can mention that the value of ROE and market share of the first five banks in total assets is comparable with the European average.

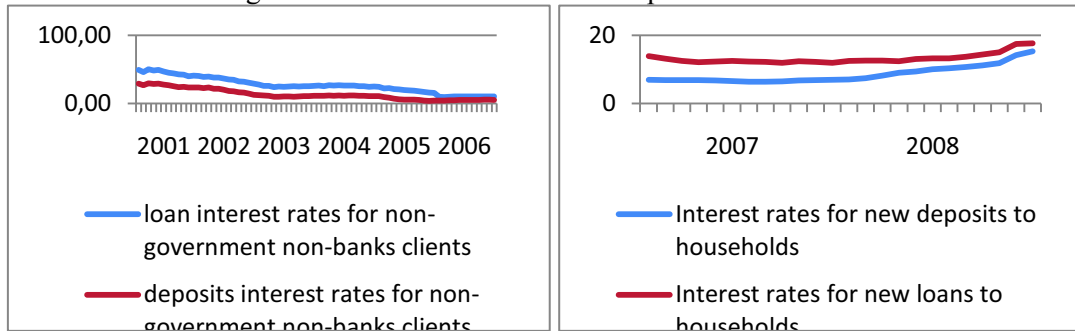
Figure 1. Return on equity (ROE) and concentration ration for the first five banks in total assets in EU, 2008



Source: FMI Global Financial Stability Report, October 2009

As we can see in the next figures, the evolution of deposits and loans interest rates proof a continuously decreases excepting the end of 2008, when the first signs of the financial crises could be found. The spread between deposits and loans rates became more and more tighten. This evolutions proof again the increasing of competition.

Figure 2. Evolutions of loans and deposits interest rates



Source: NBR Monthly Reports 2006-2008

Conclusions

The competition in the Romanian banking system increases continuously in the last years. The main factors which have influenced this process were: the privatization of the majority of state capital banks and the perspective of accession of our country in the EU. In the first period of transition of Romanian economy banks have had very good performances due to their market share in a low competitive banking environment. After the privatization of some state capital banks, the leader of the market lost market share in the favor of other bank with greater performances. Also, the privatization of BCR determined grater performances for it starting with the year 2006. BRD, the second competitor maintained his market share and performances in all this period. As a fact of improving competition we can see a trend of tightening of the spread between deposits and loans rates, and one of loan rates decreasing (excepting the period of the beginning of the actual financial crises in the end of 2008).

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