

# HAVE THE RECENT CRISIS AFFECTED FOREIGN BANKS' POSITIONS IN CENTRAL AND EASTERN EUROPE? (II – FOCUS ON ROMANIA)

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*The aim of this paper is to investigate the extension to what foreign banks reacted during recent crisis in supporting their Romanian subsidiaries and thus the local economy. The analysis focuses on the interpretation of foreign claims broken by maturity, sector, local versus foreign denomination currency, and liabilities. The data were completed with a brief analysis of internal credit (governmental and non-governmental) and finally with an analysis of the behavior of foreign banks located in Romania on the basis of the parent bank's country of origin.*

*Key words: foreign banks, economic crisis, Romania*

*JEL Classification: E5, G21*

## 1. Introduction

Following the methodology and approach developed in the first part of the paper, we will try to extend the research on foreign banks' behaviour regarding the support they provided to their subsidiaries their during crisis time, in the case of Romania. We are interested an evolutive, sectoral perspective, combining data regarding the evolutions of total foreign claims, internal credit (governmental and non-governmental) and liabilities. Finally, we are interested to find out if the banks originated in certain countries had a more unstable action comparing with others.

## 2. The analysis of foreign claims

Starting with the general findings about the evolution of foreign claims in several selected Central and Eastern European countries, we have to further develop the analysis by taking into consideration the developments of foreign claims, on a quarter basis, since Q4 2005 to the most recent available data. Table 1 summarises the data by maturities, sectors and claim type.

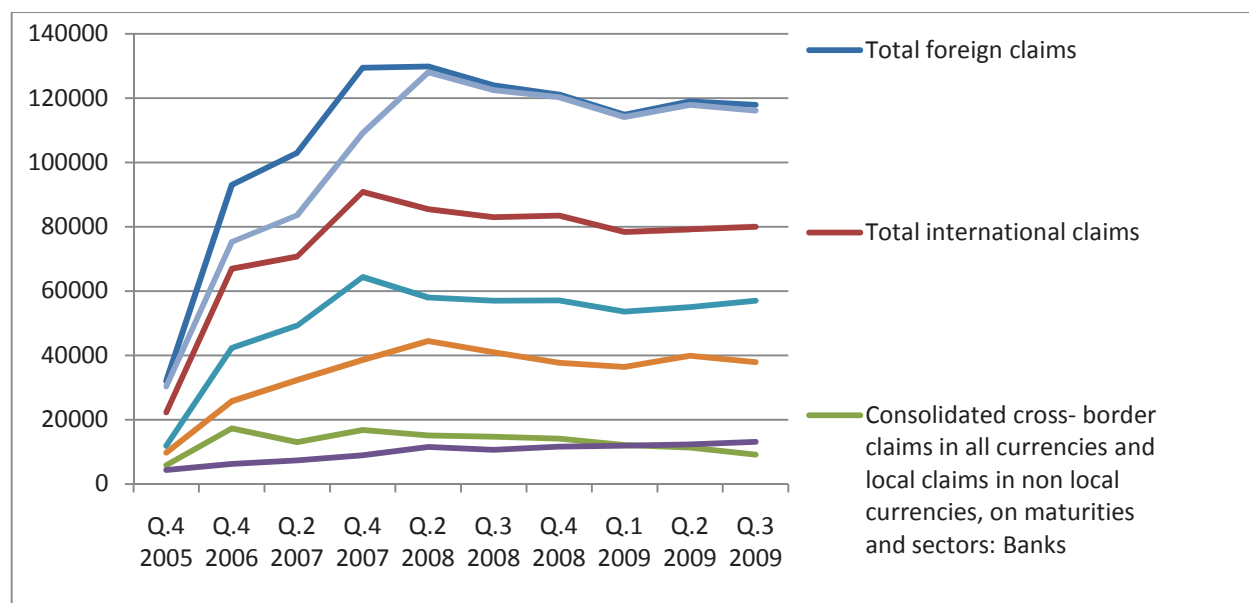
This information related to Romanian banking system shows that the indicators on foreign banks – both on cross border credit and on local credit grant by implanted banks – show a significant increase in the third quarter of 2009 comparing with December 2005, but considerably inferior to the amount registered in the maximum periods (end of 2007 until September 2008). Decreases go from 9-10% for total external credit to 39% for cross border credit.

**Table 1. Claims of BIS reporting banks on Romania (2005-2009)**

Period	Total foreign claims	Total international claims	Consolidated cross- border claims in all currencies and local claims in non local currencies, on maturities and sectors:						Claims in local currency of reporting banks' foreign offices with local residents	Total foreign claims
			<1 year	1-2 years	>2 years	Banks	Public sector	Non-bank private sector		
	A + L	A	B	C	D	F	G	H	L	R = A+L+Q
Q.4 2005	31984	22240	10599	1145	9050	5851	4358	11749	9744	30272
Q.4	92956	66898	40395	2560	18165	17272	6254	42249	25698	75313

2006										
Q.2 2007	102990	70711	41447	3738	22954	13028	7330	49248	32279	83543
Q.4 2007	129381	90799	49785	4984	33392	16777	8955	64292	38582	109108
Q.2 2008	129810	85401	38132	8775	35003	15082	11451	58007	44409	128034
Q.3 2008	123930	82948	38327	8071	33247	14659	10623	56945	40982	122432
Q.4 2008	121089	83463	37934	7660	34718	14039	11593	57049	37626	120249
Q.1 2009	114759	78334	34885	7817	32837	12140	11901	53613	36425	114080
Q.2 2009	118999	79169	38389	7909	31860	11290	12246	54964	39830	117863
Q.3 2009	117835	79924	30768	8700	37136	9126	13048	56996	37911	116073

Source: own calculation based on BIS data, different years



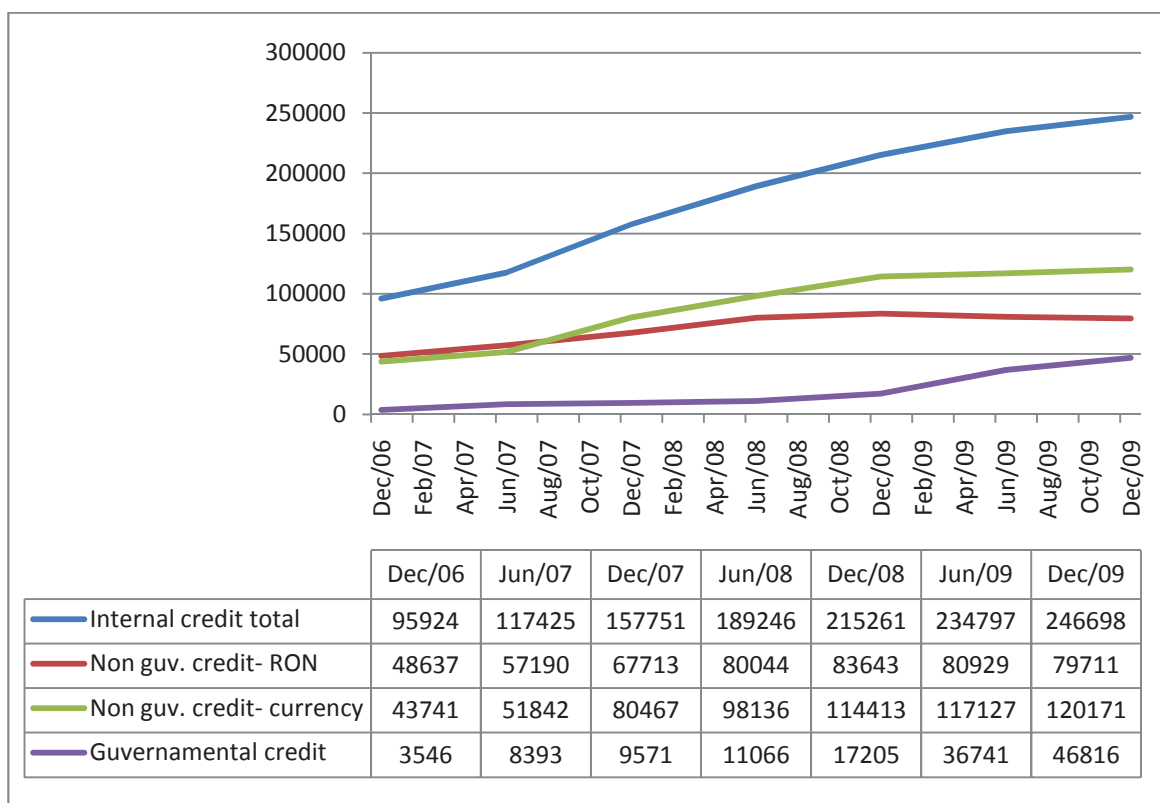
**Chart 1. Claims of BIS reporting banks on Romania (2005-2009)**

Source: own calculation based on BIS data, different years

### 3. Internal credit developments

Based on the National Bank of Romania data for 2009<sup>439</sup>, we can notice that in 2009 the increase of total credit was mainly represented by the government credit (increasing with more than 1,7 times in 2009 versus 2008 and 3,9 ori comparing with 2007), and less on non-government credit (only 1% in 2009 comparing with 2008) – see Chart 2.

<sup>439</sup> National Bank of Romania, *Monthly bulletin*, January 2010, [www.bnr.ro](http://www.bnr.ro)



**Chart 2. Evolution of internal credit, government and non-government between December 2006 and December 2009**

Source: NBR, Monthly bulletin January 2010

Analysing this data together with the data regarding foreign banks' involvement, we can draw the following conclusions:

- Both foreign and domestic banks demonstrated a much reduced interest – comparing with the pre-crisis period – in financing the real economy; they all reported a greater preference in government financing;
- The foreign claims – either referring to cross-border credit or to locally granted credit supplied by the Romanian located subsidiaries of the foreign banks, followed the same pattern; the interest and involvement in the Romanian economy were achieved especially by the financing supplied for the government (in local currency or foreign currency) in the same time with an effective withdrawal from the real economy or population financing;
- The withdrawal of Romanian located foreign banks is confirmed also by the consistent decrease of cross-border credit granted to the Romanian bank sector (decreasing by more than 34%), comprising here the greatest part of the credit supply by parent banks to their own subsidiaries locally implanted in Romania;
- Within the total claims of foreign banks on Romania, the most significant decrease is registered in the case of lending provided in local currency by the subsidiaries of the foreign banks located in Romania, fact indicating a reducing involvement in the Romanian economy and a pro-cyclical action.

In the better possible case, accepting with honest-mindedness the foreign banks' representants statements about their maintained interes regarding the Romanian economy<sup>440</sup>, this fact can be seen as a consequence of the capital re-allocation decisions according to the market oppotunities in risk-aversion conditions.

It worths mentioning that the developments could be much more dramatic then the effective ones, in the absense of international support provided by the EU and the IMF. As Mugur Isarescu, the NBR Governor stated, "the import of credibility from the EU and the IMF determined some private financing not to reduce themselves or to reduce less; this financing positively reflected itself in several directions: relatively larger investment comparing with the situation ob absense of these agreements (with EU and IMF – n.n.); diminishing the depreciation and temperating the foreign exchange rate volatility of the romanian leu relative to euro and other currencies; the Wien agreement on the banks engagement to renew the existing finance lines and to maintain capital adecquation ratios to secure levels"<sup>441</sup>.

#### 4. The liabilities' perspective

Foreign banks' involvement in the economy of developping countries has to be completed with the analysis of local liabilities denominated in local currency. Even the relevance of this indicator seams reduced compared with the measure of credit granted (to bank sector, non-bank private sector, public sector in the host country), it reveals it's importance through several issues.

On one hand, an important issue is the way in which the capital entried the host country<sup>442</sup>. Where the entrance was achieved by cross-border granted international claims – the involvement in deposit collection is very low and insignificant. In the case of greenfield involvement, the resources' collection from that country's residents – especially in local currency – is limited especially by the network size, type of clients etc. Finally, if the foreign capital entry is achieved by the acquisition of a existing local bank, often with an important market share in the host economy, it is highly possible that the dimensions, size and expertise of the network, and the contact with the local clients rise the availability and willingness of the new entities to continue their involvement also in resource and deposits collection, in local or foreign currency, at the same time with the appeal to the cheaper, foreign currency resources supplied by their parent bank.

On the other hand, the relevance of this measure is shown by the different way in which the foreign banks' subsidiaries approach the effects of the crisis. Starting from de Hass and Lelyveld findings, we can state that the extension and measure in wich a foreign bank involves in resource collection and lending in local currency can generate two possible developments:

- Increasing it's relative independance toward their parent bank regarding the resource supply and thus valorising more rapidly and more effective the growing opportunities in the local market, exceeding the estimations at the time of implantation;
- On other hand, in crisis times, and in the case when parent bank has not a high financial power and/or experiences difficulties on their home market, the parent bank's support to

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<sup>440</sup> Parent groups of the main 9 banks with foreign capital signed in August 2009, bilateral letters of engagement to maintain the exposure level on Romanian market and the solvency ratio to over 10%. The banks signing the agreement – Erste Bank, Raiffeisen International, Eurobank EFG, National Bank of Greece, Societe Generale, Alpha Bank, Volksbank, Piraeus Bank and UniCredit – counted for about 70% of the Romanian banking market

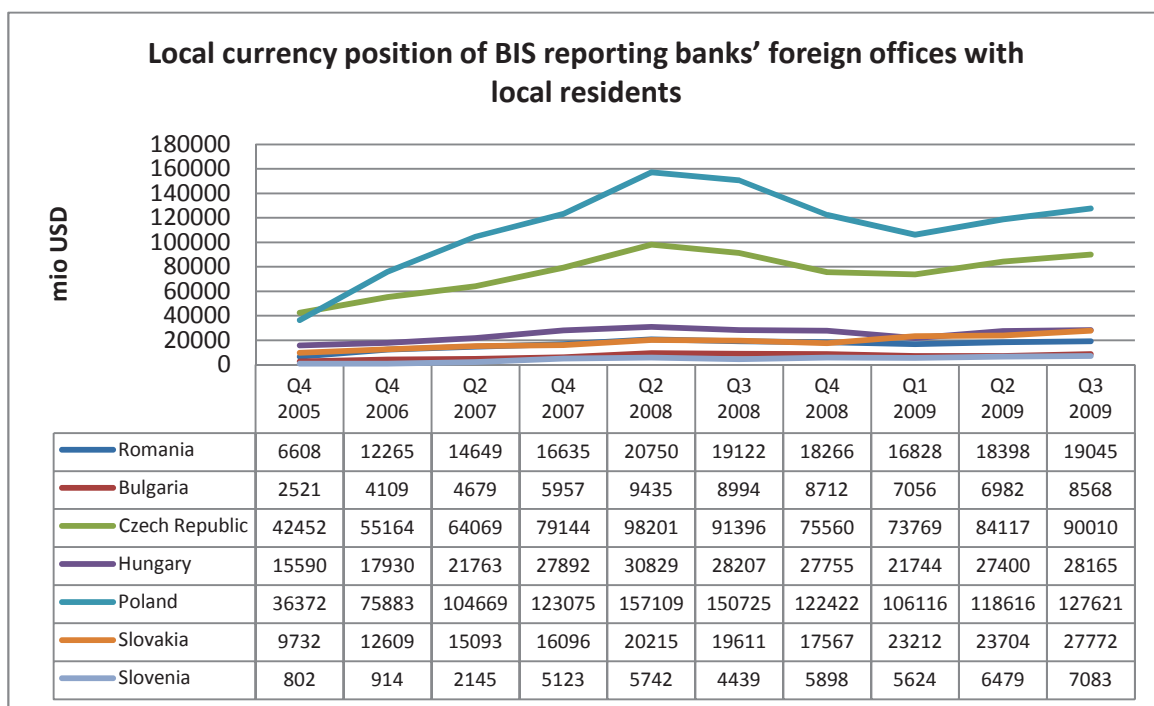
<sup>441</sup> Isarescu Mugur (2009), *Finantarea dezechilibrului extern si ajustarea macroeconomica in conditiile crizei financiare*. Cazul Romaniei, NBR

<sup>442</sup> see Grubel, H., *A Theory of Multinational Banking*, Banca Nazionale del Lavoro Quarterly Review, nr. 123/1977 Konopielko, L., *Foreign Banks Entry into Central and East European Markets: Motives and Activities*, în "Post-Communist Economies", vol. 11, nr. 4/1999, apud: Badulescu, D. (2007), *Globalizarea si bancile. Cu o privire specială asupra Europei Centrale și de Est și asupra României*, Editura Economica, Bucuresti

its subsidiaries reduces. As a consequence, these subsidiaries masivly involved on the local market through lending and deposits will behave more as a domestic bank, acting pro-cyclicly and suffering the majority of the crisis' effects on the host market. In other words, the consistent support of the parent bank – possible if this parent banks is a powerful multinational bank – is decisive in maintaining the subsidiary as a bank less affected but the crisis in the host country; in a more general approach, this fact justifies the statements regarding the positive effects of foreign banks involvement on the developping countries in the case of entry of powerful banks, originated from developed economies.

Different from the evolution of the indicators analysed in table 2 and 3, the information in Chart 3 shows a similar evolution of local liabilities for all analysed countries; the difference only comes from the lag of starting the crisis or the amplitude of decrease for each country:

- All countries experienced considerable decreases of these liabilities, from -49% in the case of Poland and -42% in Hungary (Q1 2009 versus Q2 2008), -25% – -30 % in the case of Czech Republic, Romania, Bulgaria, or considerably lower in the case of Slovenia (where the foreign capital presence is much less than in other countries cases).
- Even the moment of the decreasing is de-phased in time, it occurs abruptly, and the recover is usually slow; at the moment September 2009, the indicator haven't reach the pre-crisis levels in no country.
- Finally, as a general explanation, confirming the pro-cyclical affection of foreign banks' subsidiaries, is the fact that reducing the amounts of these attracted founds is due to the effects of the profound crisis which affected the real economy, population and firms, government institutions refering to a more extent to the existing liabilities as the access to finance is more and more restrictive and the associated risks higher.



**Chart 3. Local currency position of BIS reporting banks' foreign offices with local residents**

Source: own calculation based on BIS data, different years

## 5. Final Conclusions

We can state that the support and involvement of the foreign banks in Romanian economy is moderate, under certain conditions and selective, explained by:

- a. Over 55% of the foreign capital in Romanian banking system comes from countries very affected by the global financial crisis, as Greece, or from relative consolidated banks but very exposed on Central and Eastern European market (Austria).
- b. Decreasing in total claims on Romania was more pronounced from the country consistently involved in Romanian banking system (Austria -11%, France -11.4%, Netherlands -9.7%, comparing with an average at 9.23%)
- c. The scale of crisis shock on Romanian economy

**Table 2. Foreign claims, total and main reporting BIS countries on Romania**

Period	Total foreign claims	Austria	France	Italy	Netherlands
Dec-06	92596	35467	10135	3282	5186
Sep-07	114637		16128	9989	6483
Jun-08	129810	46457	17640	12948	10999
Sep-09	117835	41460	15629	13149	9932
sep-2009 vs june-2008	-9.23%	-10.76%	-11.40%	1.55%	-9.70%

Source: own calculation based on BIS data, different years

For all Central and Eastern European countries, the global financial crisis is a real, effective test proving the support form multinational banks for their subsidiaries. We can noticed that this involvement has different degrees and extension, explained both by internal particularities of the banks (financial power, complexity and dimension of the abroad networks) and by the particularities of host country economy (crisis effects, economic policy and performance, support from international organizations as IMF, EU etc.).

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