

CONSIDERATIONS ON THE RETAIL CREDIT MARKET IN ROMANIA

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Abstract: The rhythm of significant growth of the credit, as well as the conduction of it preponderantly towards the population represents characteristics met in Romania until middle of 2008 year. Before these evolutions, the Romanian banks appeared to have found the necessary instruments for a corresponding management of the crediting process. Since October of last year, the event fund the consequences of international financial crisis, witnessing a phenomenon to halt the credit. Among the products that I estimate that the Romanian banking sector will preponderantly use are: credits designated to the acquisition of goods of long term use; credit cards; mortgage credits; derived financial instruments.

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If a few years ago the big European banks were trying to orientate towards more complex structures of financial-banking entities, meant to ensure a total coverage of the clients' necessities, these have gradually reached to the conclusion, certified by practice, that reveals the necessity of concentration upon the basic activities with the highest rank of performance and, implicitly, profitable. A lot of European banks have reached the conclusion that the activity of retail fulfills all these characteristics, being, in crisis conditions, an essential protection for the population's incomes, and, in conditions of economic boom, a gold mine that possesses an important potential, not yet exploited.

The implication in the retail activity, even on certain segments or market recesses, including of some banks with well known dispositions for the corporations' sector, may represent another signal of the tendency of the last years, reflected by the middle of last year, when the international financial crisis are felt in our country.

The standardization of European banking legislation at the accountancy level, of regulations and even of banking risks, by the so called Basel II agreement, could ensure the supplementary elements for the reposition of the strategic priorities in order to continue the banking consolidation, which will determine a special increase of competitiveness, with implications over the trend of interest rates. The reduction of the neat margins from interests obliges the retail banks to create solutions for the global improvement of the incomes by other profitable activities, a better control of costs¹⁸.

¹⁸ Dănilă, N - Retail banking, Publishing House Expert, Bucharest, 2004, pg. 157

Both in Europe and Romania, the concept of banking retail is considered to be crossing a period of consolidation. Retail banking or banking activity with physical persons refers to the non-commercial operations realized by the population regarding the administration of own resources, the realization of cashing and payments in cash, operations of the account, the contracting of credits or guarantees for personal scopes, electronic payments, operations on the capital market, the offering of banking conciliation.

Any Romanian or foreign physical person, resident or non-resident in Romania, of at least 18 years old and who fulfills the following main cumulative conditions, can benefit of credits:

- to be employed with working contract for an undetermined period of time and to realize concrete incomes, with permanent character, which shall ensure the monthly payment of the credit rates and the afferent interests;
- to open a current account to the bank in which shall deposit initially the minimum solicited advance as own source, if it is the case, and, subsequently, the total monthly payments to be reimbursed;
- to guarantee the reimbursement of the solicited credits and the afferent interests with the incomes that realizes and, by case, with real and personal guarantees;
- to accept that the payments from the credit account be effectuated by transfer (an exception are the treasury credits);
- not to have debts or other unpaid obligations that are due towards the bank and tertiary;
- to participate at the realization of the project (business) with own sources whose minimum quantum is established by the bank for each category of credits (the proof of constitution of own resources can be done by the solicitor either by account extract or partial payment in advance of the pro forma invoice).

The retail clients who can beneficiate of products of credit type are: physical persons, resident or non-resident, of at least 18 years old; independent physical persons and family associations authorized to develop economic activities independently, in all fields, jobs and occupations, according an authorization; physical persons who exercise professions according some special laws.

The activity of retail banking presents a series of characteristics, thus:

- it ensures the services for a large number of clients, a very large number of operations which imposes increased operability and simple working tools;
- it presupposes the adoption of some special politics by the banks who effectuate such operations to attract clients;
- the operations have commercial character.

The activity of retail banking is profitable enough; due to the big volume of products and services offered there are cashed incomes coming immediately from commissions and interests; the risk is more reduced than in the case of juridical persons. In what regards the products and offered services, it is observed lately a personalization of them, launching product packages and services that are the object of some marketing actions through which they want to conquer new segments of market. Also, there have been transformations not only in the field of dynamics of the credit granted to physical persons and the number of solicitor clients and credit beneficiaries, but also in what regards the diversity of the granted credits, the operability in granting, the way of guarantee, all these movements being in favor of the credit beneficiary. Thus, the system of gages was replaced, where it was possible, with the guarantee of the

insurance companies pleased by the bank, the risk of crediting being sometimes overtaken almost integrally by the insurance-reinsurance companies, the bank benefiting of a guarantee that can become immediately liquidated. In this way it is solved the problem of non-performing credits placed to physical persons, that no longer engrave the bank's portfolio, does not require provisions and does not loads the costs of exploitation.

Also the structure of credits has become enough diversified. Mainly, there are the following categories of credits granted to physical persons:

- *credit of consume* - designed for the acquisition of goods of long term use, vehicles, for temporary needs, vacations, studies, medical treatments, representing t present the most solicited category of credits. Due to the number of scopes that it offers and to the opening of the market it is estimated a strong competition from part of the local and foreign banks;
- *mortgage credit* - designed for the construction, extension, arrangement, consolidation or buying of accommodations and lands by mortgaging them in favor of the bank, the beneficiary becoming owner only after the integral reimbursement of the credit and payment of the interest. For the credit granted there will be guarantees that will cover its level and the afferent interest to the first year of crediting;
- *credit for activities with productive character* - designed for the acquisition of equipment for private offices, small commercial stores, agrarian machines for the small producers and other activities with productive character. Though they should be very solicited because help to obtain some incomes and so relief the debtor's task, at present these credits have a reduced poise due to the period of economic involution, of the inflation and, moreover, of the interests and big commissions of the banks;
- *the credit lines granted by credit cards* - which are granted according the creditworthiness of each client, according a certain graphic, until there are honored the payments realized by credit cards, even if there are not available in the account. This form of crediting has developed more thanks to the operability in granting and the easy way f using the payment instrument. The incomes obtained by the banks are substantial because of the debtor's sold, exactly in the frame of the graphic, there are perceived very big interests.

The credits granted to the population have had a reduced poise during 1990-1999. The causes were many; among the most important we mention: the heavy access to these credits, the norms and conditions of crediting were inaccessible for a large number of the population, as well as some contracts of exclusiveness that were not legal according the norms of the market economy. The reduced level of credits granted to physical persons was also maintained during the years 2000 and 2001, so that starting with the year 2002 a sudden change to better of the credits granted to the population is registered. A real boom was registered in the year 2003, when the credits granted in lei on mid and long term raised approximately four times than the previous year, respectively 4.5% in the year 2003 than 1.6% in the year 2002. this spectacular evolution was due to the elimination by the B.N.R. of some restrictions and improvement of the conditions for granting credits, from the rise of the poise that the sum to be reimbursed represents in the total of the debtor's incomes when giving up to the guarantor; there were also extended the expiring terms, having as a result the diminishing of the monthly rates to pay.

The significant expansion of the non-governmental credit from the last years was sustained, to a great extent, by the upward dynamic of the credit towards the population (table no.1).

The base from which the growth started (177 millions of euro at the end of the year 2000) was very reduced than the level registered in the same period in other central-European and east-European states (over 8 billions of euro in Czech, 1 billion of euro in Slovakia and over 18 billions of euro in Poland), as well as towards the volume of the credit granted to companies in Romania. The reduced dimension of the credit granted to the population is also relevant by the poise in total of the non-governmental credit, in 2000 this being only 5.7%.

Table no.1. The evolution of the credit granted to the population

	2001	2002	2003	2004	2005	2006	2007
Rhythm of nominal growth	45.2	87.6	161.5	258.9	58.3	52.3	71,0
Rhythm of real growth	3.2	44.6	122.0	214.6	44.8	44.7	60,6

Source: *Financial Stability Report of the B.N.R., 2008*

From the point of view of the financial intermediation, the banks are the main intermediaries that ensure the financing of the population in proportion of 95%. In the conditions in which, during the last years, the credit granted to companies has had a positive evolution, but more reduced in comparison with that of the credit granted to the population, the structure of the non-governmental credit has modified significantly, at the end of the year 2004, the poise of the credit for the population in the total volume rising up to 28.4%. The credit granted to the population continued its expansion coming to represent 48.0% from the non-governmental credit at the end of the year 2007 and has maintained to a higher level than the credits of production or those of investments of the companies.

What is to be remarked is that in the case of Romania is the sudden change of strategy – if in the other east-European countries the orientation towards the retail did not realize so rapidly, in Romania the poise of the credit for the population in the non-governmental credit has increased with 21.6% in the period 2001-2006.

If we take into consideration:

- a. the situation from the euro area, where the medium poise of the credit for the population in the non-governmental credit was of 50.3% in December 2005;
- b. the fact that in Romania the poise of the credit for the population in the GDP was of only 6% at the end of the year 2005, while in other central and east-European countries was superior as far back as 2002 (Hungary 6%, Poland 7%, Czech 8%), we can say that the market of the credit afferent to the population from Romania was far to be saturated.

The volume of the credit for the population has increased significantly starting with the end of the year 2002, the component with the biggest dynamism being the credit for consume. This was represented approximately three quarters from the total of credits for the population, situation that is obviously different from that of the countries from the euro area, where two thirds are designated to the immobile financings.

The credit for consume has raised with 93.7% (84.7% in real terms) in 2005, with 19.8% (12.5% in real terms) in 2007 and with 37.6% (29.2% in real terms) in 2008.

The mortgage credit has increased with 53% (45.9% in real terms) also in 2005, in comparison with 57.4% (44.8% in real terms) in the previous year, but in 2007 and

2008 were registered increases of 88.6% (77.1% in real terms), respectively 49.7% (40.6% in real terms).

The credit for consume was dominated by the component in lei, whose poise registered a light decreasing tendency in 2008 than 2007 (52.7% than 58.3% at the end of the previous year), in exchange, in the case of the mortgage credit, the majority position continues to be held by the component in foreign currency, the share of loans in euro was approximately constant (76.2% in 2006, 76.4% in 2007 and 75.6% in 2008).

The increase of the credit offer in this period was explained not only by the expansionist politics within this domain of the credit institutions, but also by the proliferation, in the last years, especially by the practice by the big stores of offering goods of long term use in the rate system. On the side of demand, the explanations have origin in the increase of the purchase power of the population, the modification of the consume behavior, as well as in the low level of endowment with goods for consume.

A more frequent phenomenon in the last years on the Romanian market was constituted by the continuous extension of the maturity of credits granted to the population, as consequence of the unprecedented development of the mortgage credit and of the credit for acquiring goods of long term use. This expansion can also be in some measure artificial, and considered to be one of the solutions identified by the banks for elude of administrative measures impose for the limitation of the debt service of the population according the available income.

In what concerns the denomination currency of the credits granted to the population, it was remarked the preference for foreign currency. The orientation towards the foreign currency was occurred:

- on the background of the maturity expansion of the credits granted to the population;
- as a result of some interests more reduced for the credits in foreign currency than for those in the national currency;
- as consequence of the appreciation of the national currency in the period 2006-2007;
- thanks to the relative euro-icing of the prices in some sectors (the real, of the transportation means, etc.).

The rhythm of increase of the credit for the population on long term, determined by the process of convergence to the EU, corroborated with the growing needs for goods of consume and real estates of the population, was induced a rhythm of significant growth afferent to this segment of crediting.

In the context of globalization, at present, the European banking system is yet influenced by the problem of mortgage credits sub-prime from the USA. The increased poises of the non-performing credits with high level of risk, according to which there were granted titles of value, has determined a crisis on the financial markets, enhancing the fears for the instability of the global financial sector and the toughen of the crediting conditions, which led to the intervention of the central banks on the financial markets in order to avoid a crisis of liquidities.

Although the estimate that the European markets, and especially the emergent markets, will overcome with success the crisis from the credit sector extended to the international level, taking into account the limited exposure on the mortgage credit market with high risk from the USA and the increased economic rhythm, however, by the consequences of international financial crisis have been reflected on a global scale, including in Romania, through the parent banks with foreign capital, which have drastically reduced funding, and by compression of export opportunities in the countries

directly involved. Few investors are convinced that the problems appeared on the market of mortgage credits from the USA have come to an end too soon, the analysts warning about the risks of the economic growth. The volatility on the financial markets was affected the global economic growth, because the effects of slowing the American economy was perceived in the commercial exchanges, thus other economies were also affected. The countries with emergent economy have dealt well until middle of 2008.

The market crisis had three main components:

- the reevaluation of the credits' risks;
- the testing in crisis conditions of some new components of the market of financial instruments on the basis of actives;
- the growth of the fears regarding the risks recorded by partners.

The lack of transparency caused the appearance of fears that also other institutions could suffer, leading to the appearance of the liquidity crisis on the market.

Romania does not confront itself at this moment with the risks that could generate a financial crisis such as that from the USA, determined by the cheap mortgage credits, but the rapid growth of the credits granted to the population could lead, in the previous period resulted, to the increase of the number of non-performing loans, thus rising the credit risk, against the improvement of the banking surveillance.

The investigation of the financial behavior of the population and the market evolution of the credit from the countries new members of the EU concluded in the case of Romania the following:

- Romania is the country with the lowest level of debts per citizen from the region, but also with the lowest level of financial income;
- the mortgage credit and the immobile one represents only 25% from the total of Romania's population debts, less than in the other countries from the New Europe (it includes four states from Central and East Europe, new members of the EU and other candidate countries or oriented towards the EU);
- the sustainability on mid and long term of the growth of the market of credits for physical persons depends on a good administration of risks, at the banking system as well as at the level of the macro-economy;
- at the international level, during the last decade, there were structural changes on the credit market that were reflected in the growth of relevance of the retail market by the expansion of the credit for consume, followed by a rapid growth of the market of immobile and mortgage credit.

The analysis according to types of obligation instruments enhances the existence of some structural differences of the analyzed markets. Unlike the euro area, where the mortgage and immobile credit holds the biggest poise in the volume of debts of the population (70% in 2007), in the area on new EU members the credit for consume contributes mostly to the population's debts, but its relevance diminished from 80% in 2000 to 54% in 2005, on the basis of the more rapid medium annual growth of the market of mortgage credit (49% than 18% in the same period).

The emphasized development of the credit market in the area of the New Europe is due to some factors of demand type, as well as to some factors of offer type.

The analysis of the relationship between the dynamic of consume and that of the credit emphasizes the existence of some constraints of liquidity in Romania, a sign of a crediting potential generated by the necessity to consume satisfy. The analysis of the factors of the micro and macro economy does not allow obtaining a stable

conclusion regarding the sustainability on medium and long term of the expansion of the market of retail credit. What can be said, though, is that there are predicted major risks for certain countries (Romania, Hungary, Bulgaria, Czech Republic, Poland, Baltics) there are some sources of vulnerability (big foreign currency exposure, the growth of the debt service, the enlargement of the external deficits) that can transform into major unbalances.

Romania remains the country with the lowest level of financial income and debt per citizen from the region. At the end of the year 2007, the financial income of the Romanians represented only 38% from the GDP, than 75% which was the average grade in the area of New Europe at that date, while the financial debt reached 12% in comparison to 21% in the area of New Europe.

With a medium annual growth of 18% during the last 5 years, in 2005, the mortgage and immobile credit represented only 25% from the total of debts of the Romanians. This expansion was possible as a consequence of the existence of a reduced level of debts, but also on the basis of the growth of incomes and the positive expectations regarding the future incomes.

For the period of 2007-2008 it was registered a medium annual growth of the financial income of the Romanians of 17% (in comparison with the average grade of 10% from the area of New Europe) as a consequence of the preferential growth for the market of mutual funds and insurances. At the same time, the volume of debts was raised, on an average of 22% per year (than 19% per year from the area of New Europe), the mortgage credit increasing gradually its relevance. Increased emphasis of indebtedness was not devoid of risks, in particular macroeconomic nature (increased exposure to currency and current account deficit), specific periods of transition. Analysis of the relationship between the expansion of retail credit growth and current account deficit indicates, indeed, there was a significant correlation, particularly due to imports of durable goods.

Although the granted credits of the economic agents (including non-residents) has an important role in the deterioration of the deficit of current account, because it generates the growth of the production capacity.

In conclusion, the development of the market of retail credit until the middle of last year reflected, generally, a phenomenon of balance, the expansion of this market from a level almost neglected five years ago to the realization in the context of improving the financial conditions of the population.

After that date, the balance has deteriorated rapidly under the impact of international financial crisis and its consequences (the crisis of liquidity, volatility of securities courses, exchange rate instability, decreases in real estate prices, the compression market, particularly in construction and cars).

In order to reach a full efficiency and to better respond to the needs of its clients, we consider that organization of the Retail Bank must be based upon three key functions: Distribution, Products and Markets.

This pole concentrates the marketing activity (the analysis of behaviors and expectations of the clients, the observation of the market and competitiveness, the creation of new products) and the commercial aspect (the definition of the commercial politics, the establishment of the objectives and their realization). Among the main objectives of this team there are the adaptation and enrichment of the product offer (with products such as leasing and intern factoring), as well as the development of the

alternative channels from the perspective of realizing a multi-channel bank. The reduction of incomes can be compensated by the growth of the volume of sold products, especially in the field of investments, since over 70% from the profit of financial services of retail type from Europe result from economies and investment products. Thus, in order to increase the report between incomes and costs, the banks from Europe that offer financial services of retail type should:

- reduce the basic costs of the banking services of retail type in order to maintain the level of profitability estimated to an average of 10 - 15%;
- to excel in the financial management in order to attract and maintain the most important clients.

The problem consists in improving the relationship with clients to a superior level of facilities offered by the private banking, without raising the costs of distribution in such a way to generate new incomes, while the affluent volume of clients require more and more products. The current process of development, the communication systems and of training the selling force must evolve in order to keep the pace with the introduction of new products.

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