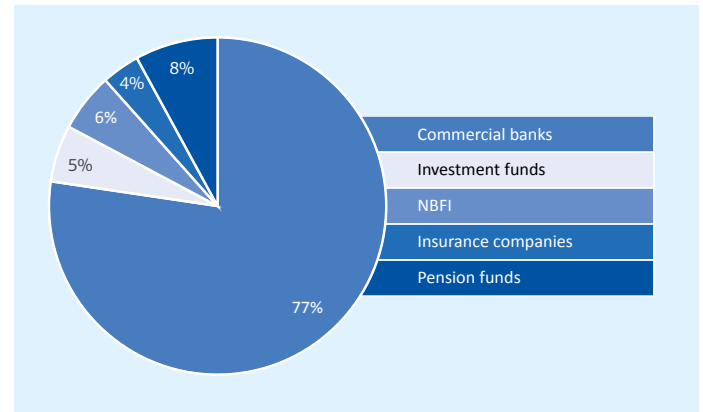


Overview of the financial sector in Romania



Commercial banks account for the largest part of the financial sector in Romania with a 77% share in the total assets. The importance of private pension funds has increased recently and by the end of 2020 they held around 8% of total financial sector assets. Non-bank financial institutions mostly provide short term loans to the market and hold 6% of total assets in the sector. Investment funds in Romania manage around 5% of the total financial sector's assets. Around 43% of investment funds assets are invested in equity and 36% in fixed income securities.

Figure 1. The structure of the financial sector in Romania, December 2020

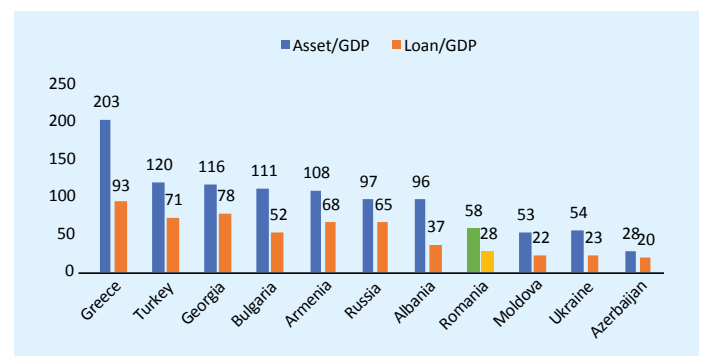


Source: National Bank of Romania

Currently, 34 commercial banks operate in Romania with a large foreign participation in the shareholding. More than 70% of the total banking sector's assets are owned by non-residents. Commercial banks are predominantly privately owned, and they account for around 90% of total banking sector assets. The banking sector in Romania is competitive with the largest bank holding less than 20%, and the 3 largest banks holding only 40% of banking sector assets. The HHI index of concentration is low at 9%, highlighting the low level of concentration and a competitive market structure.

The size of the banking sector relative to the economy in Romania has shrunk over the 10 years prior to 2020. 2019 was the first year since 2010 that the size of the banking sector increased more than nominal GDP grew, with the ratio of total assets to GDP reaching 58%. However, this is still a relatively low level compared to other countries in the region. Romania is near the bottom among BSTDB countries in terms of credit outstanding relative to the economy, with the ratio of total loans to GDP at 28% at end 2020.

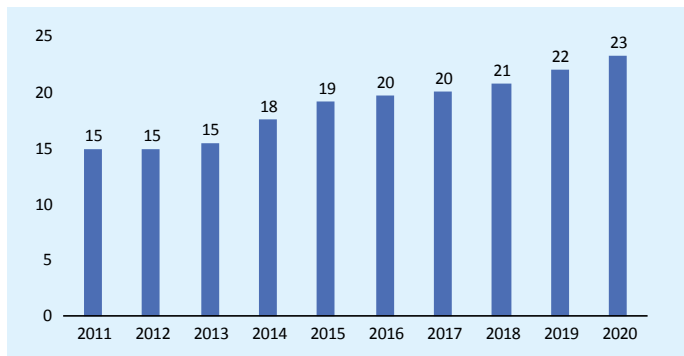
Figure 2. The size of the banking sector relative to the economy, December 2020



Source: National Bank of Romania

The banking sector in Romania is well capitalized. The capital adequacy ratio (CAR) has increased steadily over the last 10 years and stands above the required minimum. By the end of 2020 the CAR had reached 23% of risk weighted assets. Large capital buffers are an indication of the strong shock absorbing capacity of the system.

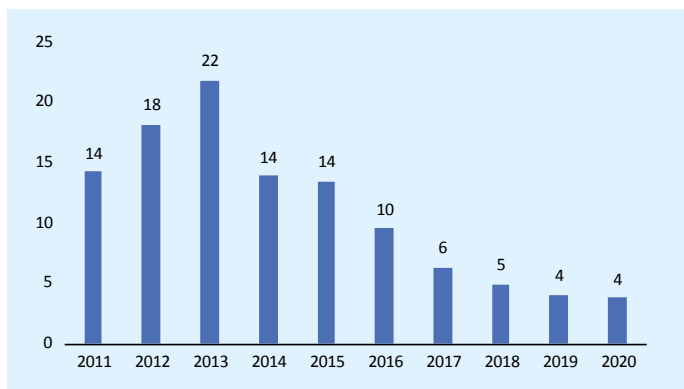
Figure 3. Regulatory capital to risk-weighted assets (%)



Source: Financial Soundness Indicators, IMF database

The performance of the banking sector has improved over the last 7 years. NPLs have declined regularly since 2013 when they reached a record high of 23% of total gross loans. With the quality of the credit portfolio improving significantly, the NPL ratio declined to 4% in 2019. The decline of the NPL ratio was to a large extent driven by actual improvement of asset quality, although credit growth and write-offs of bad loans have also played a role. Despite the pandemic, the NPL ratio in 2020 didn't increase. The effects of the pandemic on the asset quality of banks are probably camouflaged and delayed due to the government's introduction of debt service moratoria at the beginning of the pandemic. Therefore, the full impact of the pandemic on economic activity has yet to be seen.

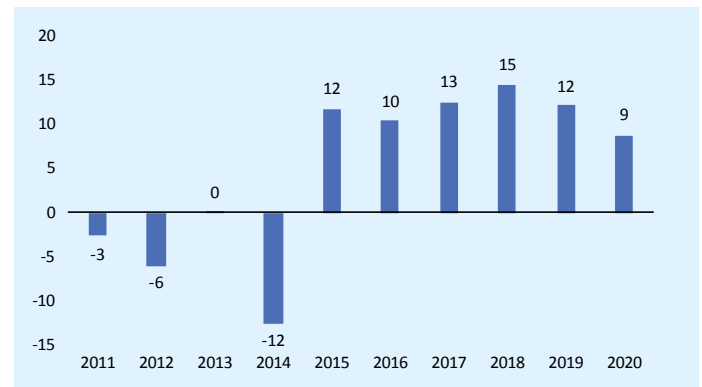
Figure 4. Non-performing loans to total gross loans (%)



Source: Financial Soundness Indicators, IMF database

Together with an improvement in asset quality, the profitability of banks has increased. For the four years prior to 2015, banks incurred losses with ROE negative at -12% in 2014. Since then, however, the trend reversed with banks becoming profitable and reporting double digit ROE. In 2020, as was expected, ROE declined compared to the previous year and stood at 9%. The average ROE for the last 6 years in Romania is around 12%, a figure comparable to other countries with similar credit ratings.

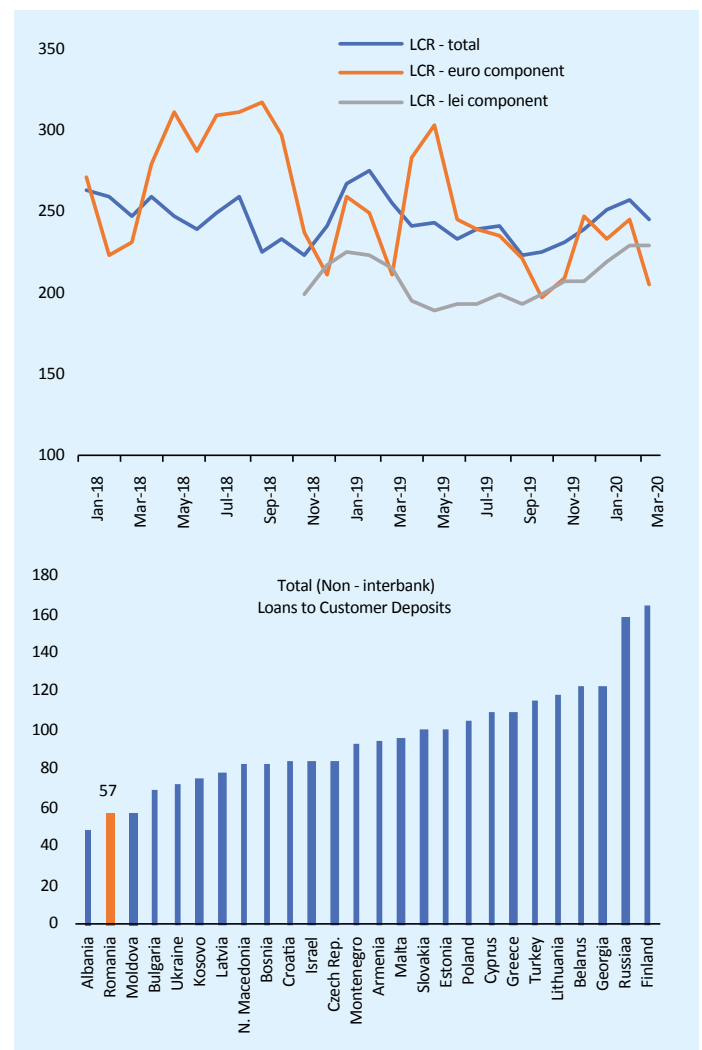
Figure 5. Return on Equity (%)



Source: Financial soundness indicators, IMF database

The banking sector in Romania maintains large liquidity buffers. By the end of 2020, 43% of the total assets in banks' balance sheets were liquid assets, while the share of loans was 49%. The liquidity coverage ratio (LCR) exceeded the 100% limit with a large margin both for local currency and euro liabilities. The funding of banks in Romania almost entirely depends on deposits, which account for more than 90% of total liabilities. Retail deposits, which are considered a more stable source of funding, accounted for around half of the deposit base in 2020. The strong deposit base and lagging loans resulted in ample liquidity in the Romanian banking system. With the loans to deposits ratio at 66%, Romania again stands closer to the lower side among the BSTDB member countries.

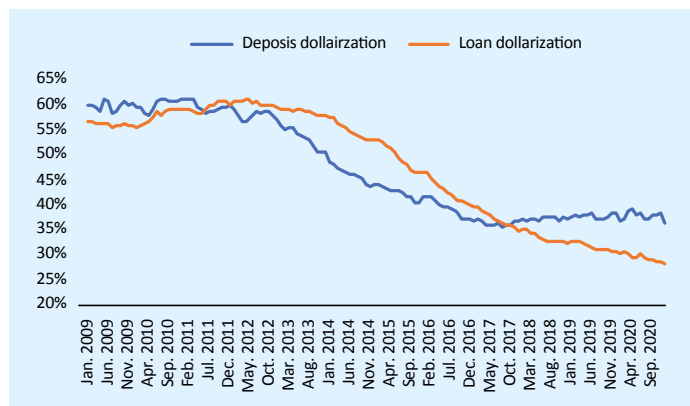
Figure 6. Evolution of LCR for the banking sector in Romania and regional comparison of loan to deposit ratio (%)



Source: Financial Soundness Indicators, IMF database

Similar to many other countries in the region, Romania experienced a high level of dollarization. In 2010 dollarization of the financial sector's balance sheet was around 60%. In the next decade, however, Romania was relatively successful in reducing financial sector dollarization with loan dollarization down to 28% and deposit dollarization to 36% by the end of 2020. Despite this reduction, household loan dollarization remains around 20%, and exposes those who have borrowed in FX to exchange rate fluctuations.

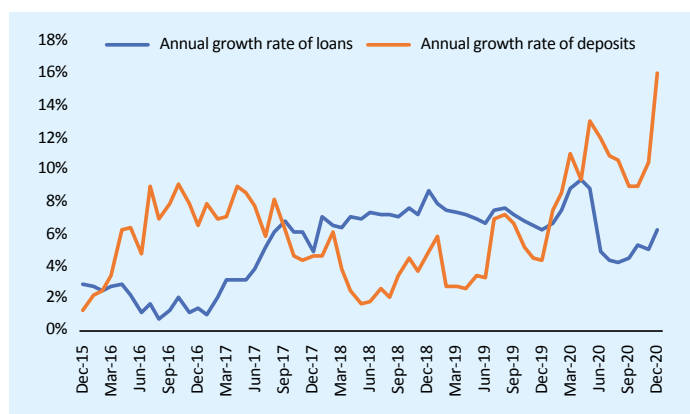
Figure 7. Evolution of dollarization in the banking sector of Romania



Source: National Bank of Romania

Over the past 5 years, the growth of the banking sector in Romania was modest, with deposits growing on average by 6% per annum and credits growing by 5%. In 2020 growth of deposits in the banking sector accelerated and reached 16% by the end of year, while loan growth was only 6%. Expansion of banks' balance sheets in the last year was supported by loose monetary and fiscal policies.

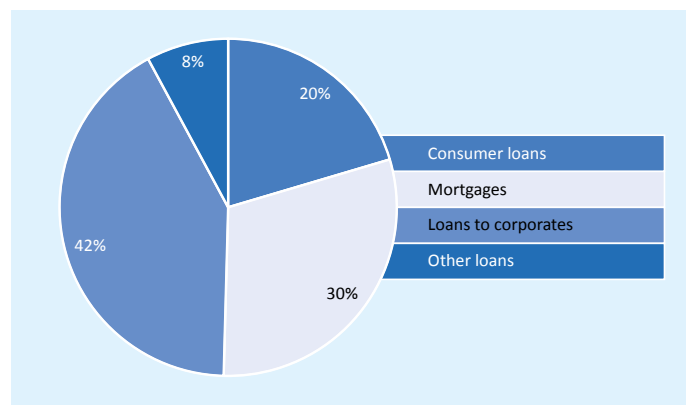
Figure 8. Growth rate of deposits and loans in Romania



Source: National Bank of Romania

The banking sector in Romania is characterized by a relatively low share of corporate borrowers in the total credit portfolio as businesses account for only 42% of total loans. 50% of total credits are granted to households out of which mortgages are 30 percentage points and the rest are consumer loans.

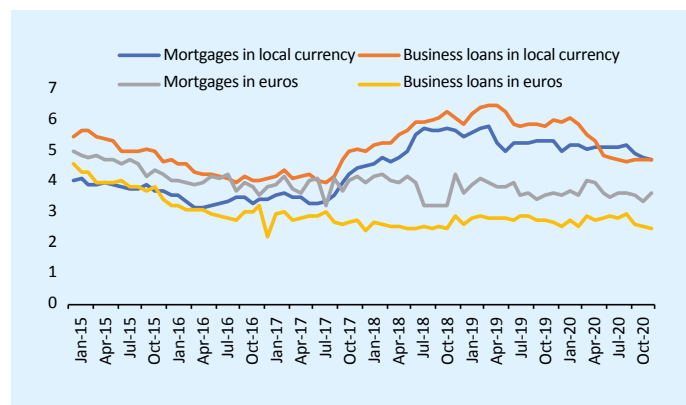
Figure 9. The structure of the credit portfolio



Source: National Bank of Romania

As a result of central bank's tightening of monetary policy, interest rates for local currency loans increased in 2018. Last year, after the central bank cut the policy rate in response to the pandemic, interest rates in local currency followed. Interest rates for euro denominated loans, however, have been low for the last 5 years, mainly driven by global market conditions.

Figure 10. Interest rate for different types of loans



Source: National Bank of Romania

The banking sector in Romania is relatively small with loans accounting for only 28% of GDP. The sector is well capitalized with very strong liquidity buffers. The performance of the sector has improved in the last 7 years as NPLs dropped from 22% down to 4% of total gross loans and profitability improved with the ROE averaging 12% per year. In addition, Romania was able to reduce financial dollarization from around 60% to close to 30%.