

THE IMPACT OF THE FINANCIAL CRISIS ON THE ROMANIAN CAPITAL MARKET

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Abstract:

The capital market is essential to any economy. A well-functioning at the macroeconomic level implies a well-rounded capital market which can allow meeting the partial or total needs of funding the issuers of securities.

Key words: the capital market, the crisis, the stock indices

JEL classification: E 44

Introduction

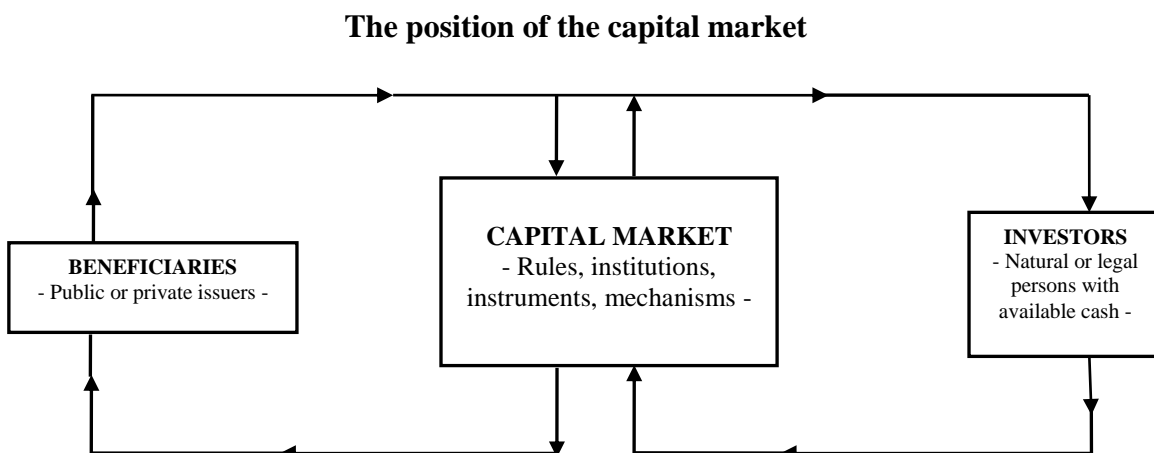
National economies are characterized by the existence and functioning of some monetary and capital markets, more or less developed. These two types of markets mutually coalesce and inter-condition, allowing financing under different conditions and at different prices of the respective economies.

In the authors' conception *the capital market* is: *a complex set of rules, institutions, instruments and mechanisms through which the surplus monetary funds are mobilized and transferred from natural and legal persons to public or private entities (issuers) whose funds do not cover the need for funding*. At the basis of this idea is the keynesist theory according to which the excess of income from covering the consumption is directed towards investment or saving ($V=C+I$ or $V=C+S$; I =Income, C =Consumption, I =Investments or I =Income, C =Consumption, S =Savings).

Main text

Basically, the capital market creates the link between the issuers of securities and those of other financial instruments and the potential investors. The role of intermediary rests with the companies of financial investments services (CFIS).

Chart no. 1



Source: made by the authors

In Romania, according to law 297/2007 on capital market, the latter is organized and operates on two levels: on the first one the National Committee of Securities and on the second one the carriers of supply and demand of capital and the intermediates. Via this law, the Romanian capital market is trying to align and carry out the functions of the developed markets from the European Union.

Regarding the evolution of the Romanian capital market in the period 1997 to 2008 (until the triggering of the global crisis), we can say that it has provided returns more than reasonable for the investors, placing itself on the top positions in the region, but also globally.

Table no.1

**The evolution of the stock indices at BSE (Bucharest Stock Exchange)
in absolute and relative value**

An	BET (RON)	BET (%)	BET-C (RON)	BET-C (%)	BET-FI (RON)	BET-FI (%)	ROTX (RON)	ROTX (%)
1997	757,86	N/A	N/A	N/A	N/A	N/A	N/A	N/A
1998	377,63	-50,17	488,57	N/A	N/A	N/A	N/A	N/A
1999	448,53	18,77	472,75	-3,24	N/A	N/A	N/A	N/A
2000	544,72	21,45	510,81	8,05	1.236,84	N/A	N/A	N/A
2001	754,85	38,58	486,07	-4,84	2.700,72	118,36	N/A	N/A
2002	1.659,06	119,79	1.103,12	126,95	6.015,22	122,73	N/A	N/A
2003	2.171,88	30,91	1.390,38	26,04	8.014,17	33,23	N/A	N/A
2004	4.364,71	100,96	2.829,45	103,50	17.289,87	115,74	N/A	N/A
2005	6.586,13	50,90	3.910,88	38,22	47.588,76	175,24	14.238,55	N/A
2006	8.050,18	22,23	5.025,08	28,49	63.011,74	32,41	17.642,77	23,91
2007	9.825,38	22,05	6.665,47	32,64	78.669,68	24,85	21.705,00	23,02
2008	6.857,70	-30,20	4.873,40	-26,89	52.660,71	-33,06	15.092,25	-30,47

Source: www.bvb.ro

The year 2008 marked the onset of the negative evolutions on the international level of the capital markets. The crisis triggered in the U.S. was also rapidly propagated in Europe, Asia and Australia, affecting both national economies and particularly the capital markets.

According to George Soros, the current crisis began more than 20 years ago, it was preceded and reinforced by other smaller crises that were resolved only in appearance, and the result is a very serious one very, which discloses day by day its catastrophic proportions. At the basis of this huge crisis there is the real estate market, which over the last fifty years witnessed a spectacular development. Investments in real estate were considered infallible, causing an expansion of funding and development in this respect.

In these circumstances it is easy to understand that real estate prices began to rise gradually, supported by the increasing demand for houses and by the economic growth linked to the technological boom of those years.

In the environment of an ultra-liberal American economy, the above-mentioned situation led to the loosening of the crediting conditions and to the extreme speculative growth of the prices in real-estate. A real estate property is a safe investment, with perspectives of continuous assessment, therefore we can safely grant credits without major restrictions. Another major cause of the crisis is the way in which wealth is distributed globally: 5% of world population owns more than 90% of the planet's riches.

The impact is even greater as globalization is increasingly being manifested in an obvious way, the national economies being connected as a puzzle. It is enough for one piece to fall to trigger the other ones in motion.

The U.S. financial markets were and are among the largest and most liquid in the world, which is a big advantage in itself. From this point of view, America could under no circumstances be ignored or avoided, as financial partner.

If we were to take only the example of some European banks, these could not have carried out an international financial activity without making use of financial products such as swap, futures, options, and other derivative which inevitably created for them an exposure to the conditions of the U.S. markets.

In the moment when colossi such as Lehman Brothers, Bear Stearns, Merrill Lynch, Fanny May or AIG are on the verge of bankruptcy and the public perception is that of financial panic, it is impossible for banks in various parts of the world not to be affected sooner or later. As if these purely financial effects had not been enough, the real estate bubble seems to have been propagated throughout the world, thus many other countries face problems of speculative growth of prices for real estate (and then sudden collapse or blockage), nevertheless without their savings to fall into collapse, due to some less liberal rules of crediting.

During this period the main stock indices of the representative markets recorded significant decreases: DJ Industrial index has fallen from 12,474 points on January 3, 2007 to only 8,579 points on December 19, 2008 (a significant decrease of 31.22% in just two years). A similar decline was recorded in the case of NASDAQ (a decrease of its value of 37.7% in the last two years) or in the case of S&P 500 (38.3% in the last two years). On the European market we have witnessed a similar decline (FTSE 100 fell by 30.5%, DAX fell by 28.8%). And the same in the case of the Asian market where the decrease appears to be even higher (49.5% for NIKKEI 225, 19.03% for Hang Seng).

The Romanian capital market has also suffered massive losses, the indices depreciating in an accelerated rate during this period.

Thus, at the end of 2008 the BET index was calculated for 2,901 points, 70% below the start value of January. Furthermore, the maximum values in 2008 of all stock indices were achieved during the first trading sessions of the year. The BET - Fi index fell dramatically from approximately 93,000 points at the end of 2007 to 18,000 points in 2008. Neither did Bet - C have a better evolution, with decreases of over 50%.

The most affected sectors are:

a) **the real estate market:** at the end of 2008 transactions have decreased dramatically, and at the beginning of 2009 they were as non-existent. In October, however, the market has almost frozen, under the circumstances in which the financial blockage on the international level was doubled by the new measures to limit crediting required by the National Bank of Romania (BNR). On the other hand, the moderation in price growth in constructions and land - especially in the capital city - was to be expected after the galloping increasing of costs in the past five years. Thus, many real estate developers have interrupted their projects hoping for a return of the prices, and some have started after a while to reduce the profit margins in order to be able to sell. The chain effect was reflected on the real estate agencies, on the producers and distributors of construction materials, on the producers of furniture and interior decorations, but also on those of electrical products and electronics. In addition, many companies were forced to abandon their expansion plans just because of the blocking of the real estate market. Real estate analysts say that because of the international real estate crisis and of the crediting conditions, the prices of the old houses fell on average, since the beginning of the year, by 30%, while for the new apartments the decrease was of 5-10% in 2008. As for the number of real estate transactions, it decreased by 20.8% in October 2008 compared to

the same month last year, to 41,672 units, according to the latest data presented by the National Statistics Institute (NSI).

b) **the auto market:** the automotive industry in Romania - contributes almost 10% of gross domestic product (GDP) of the country, with a turnover of approximately 11.5 billion euros. General Manager of Dacia Renault - Francois Fourmont, estimated at the end of October that the Romanian auto market could fall by 11.5% in 2009 up to the level of 2006. The Ford representatives in Romania claimed at mid-November that the plans of the U.S. car manufacturer were not affected by the financial crisis. It is to be seen, however, if the investments of 675 million euros to modernize the factory in Craiova will indeed take place in January 2009, under the circumstances in which Ford has not received governmental aid from the U.S., unlike its competitors - General Motors and Chrysler.

Dacia Renault was forced to discontinue its activity on 30 and 31 October, and then the management of the company sent the workers home again on 20 November 2008 until 11 January 2009, as a result paying them 85% of the total gross salary. Dacia has announced before that it would not renew the 620 fixed-term contracts approaching the closing date in December 2008 and would reduce the production pace starting with 12 January 2009, as a consequence of the "sharp" fall of the auto market in Romania and in order to reduce the stocks. In addition, the company has cut the investment budget for 2009, from 250 million to 150 million euros. The Dacia suppliers have also announced that they would send the staff in technical unemployment, and afterwards they would decide which would be the next steps, depending on the program of the Romanian leader of the auto market. The sales of new cars have been affected in the recent months also by the massive import of second-hand cars, by the depreciation of the national currency and by the changing of the crediting norms imposed by the National Bank of Romania (BNR), which led to a significant reduction in crediting. In these circumstances, in mid-December, the two major car manufacturers present on the Romanian market - Renault and Ford - have even requested assistance from the Romanian state. Thus, the American car manufacturer, Ford, which has committed to invest 675 million euros in the factory from Craiova, starting with 2009, has asked the Romanian state for loan guarantees of 400 million euros from the European Investment Bank (EIB). Renault has asked in its turn guarantees for a 100-million loan, under the conditions in which it starts operating at Titu, in an early stage, the development of a design centre. According to APIA (Association of Automobile Producers and Importers) data, the global financial crisis has pushed the Romanian auto market towards its lowest level since 1999, the new car registrations of the first 11 months of 2008 decreasing by 53% as compared to the same period of 2007.

c) **the iron and steel industry:** the largest aluminium producer in Central Europe and Eastern Europe, Alro Slatina, has announced also towards the end of December, that it takes into account the reduction of production by up to 50% and the reduction of the number of employees by 1,200 people in 2009, because of the price reduction in aluminium by over 50% since mid July 2008 until now.

d) **agriculture:** in November 2008 Agrostar Federation has asked the Ministry of Labour and the Ministry of Agriculture the entering into technical unemployment of 50,000 employees, and the investments in the bakery industry are affected by the economic crisis, because the aggravation of access to loans. Interagro, the cereal manufacturer, has also announced that in 2009 it made redundant over 90% of the group's employees, respectively 5,500 people, of whom 4,500 from the chemistry field, under the conditions in which the shareholders anticipate that losses of the group will exceed 100 million dollars and hope for a saving intervention from the state.

Conclusion

Faced with such developments, *anti-crisis measures* are necessary to enable the revival of the national economy and implicitly the repositioning of investors on the capital market.

1. The formation of some public funds as well as public-private ones, in order to support certain financial institutions in difficulty, through the purchase of their shares. For example, at the proposed of the U.S. Treasury (Ministry of Finance) the Law of economic stabilization has been adopted as a matter of urgency (October 2008). This document allows the Treasury to buy back the “toxic assets” of the major financial institutions, but which are in danger of bankruptcy. For these purposes a fund of 700 billion U.S. dollars has been established. For example, the process to buy back the debt securities of two giants of mortgage refinancing in the U.S. was started: Fannie Mae and Freddie Mac. For each of these 100 billion dollars being provided. In South Korea the injection of the amount of 30 billion dollars is provided to stabilize the economy. Out of this amount, 20 billion go to the public Bank “Korea Eximbank” for supporting medium exporters. Another 10 billion dollars are intended to support the national currency which is in depreciation. We remind here that this country, until recently, was situated on the list of countries with the largest reserves of currency in the world.

2. The governments of some countries have actually initiated a process of nationalizations (partial, complete or integral) of several major financial institutions. For example, Great Britain, regarded as Europe’s financial centre, has partially nationalized the first 8 of the country’s banks by purchasing their “toxic” shares: Abbey, Barclays, HBOS, HSBC, Lloyds BTS, Nationwide Building Society, Royal Bank of Scotland, Standard Chartered. The government used for these purposes 50 billion pounds (65 billion euros or 87.5 billion dollars). In this context the intentions of the authorities from the Republic of Moldova (RM) to “privatize” various economic objects are totally unclear. Under crisis circumstances the role of the state in the economy should increase.

3. With a view to avoid/reduce panic, and to withdraw deposits from banks, in most developed countries the ceiling of the respective guaranteed sums have been substantially increased. For example, in the U.S. this indicator has been increased from 100.0 thousand dollars (which provided over 98% of deposits) to 250.0 thousand. It actually means ensuring the bank deposits almost entirely. Similar decisions have been adopted by the EU countries. Most of the EU countries have agreed in October this year on raising the ceiling on guaranteed deposits from a minimum of 20.0 thousand euros, up to at least 50.0 thousand euro. If we take into account the fact that in several states “the old minimum” already covered much over 9/10 of total bank deposits, then we can conclude that the new limit of the guarantee provides almost all the money kept in banks. For example, in Romania the old ceiling (of 20.0 thousand), according to the Fund of Guaranteeing the Deposits in Banking Institutions, it used to cover 99.2% of the previous balance of the total sum of deposits. In some states, the ceilings are still higher. In the UK - 50.0 thousand pounds, in Italy - 103.0 thousand euros etc. In November similar measures were adopted in Switzerland, Australia, etc. The increase of ceilings and the reduction of interstate gaps between them contribute favourably to the reduction/exclusion of money migration, afferent to deposits. (In this context we mention that in the RM the ceiling of guaranteeing deposits is approximately 300 euros or approximately 0.5% of the pan-European “ceiling”).

4. Another anti-crisis measure is the fusion of various economic and financial structures. The growth of the economic and financial potential of the new entity contributes favourably to strengthen their resistance capacity under conditions of instability.

5. An efficient anti-crisis measure is represented by the reduction of interest rates of monetary policy in the base countries and the contribution to increase investments. For

example, Fed has repeatedly decided to decrease (almost weekly) the respective rate, which reached up to 1% (early November). Similar decisions were also taken by the European Central Bank (ECB), the Bank of Japan, the Bank of Canada, and the Bank of Australia.

It is obviously that the actions taken require enormous public and private funds. Along with the increase of public debts (internal), the budget deficit has also significantly increased. For example, the U.S. budget deficit in 2008 (1 October 2007-30 September 2008) reached over 450 billion dollars.

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