The National Committee for Macroprudential Oversight

# Annual Report 2017

Year I No. 1

# Annual Report
# of the National Committee
# for Macroprudential Oversight
# for the year 2017

# Cuprins

# Organisation

The National Committee for Macroprudential Oversight (NCMO) comprises:

**The National Bank of Romania**. The NBR has an intrinsic role in maintaining financial stability, given its responsibilities arising from its double capacity as monetary and prudential authority. Financial stability objectives are pursued both by way of its prudential regulatory and supervisory functions exerted on the institutions under its authority, and by the design and efficient transmission of monetary policy measures, as well as by overseeing the smooth functioning of systemically important payment and settlement systems.

**The Financial Supervisory Authority**. The FSA contributes to the consolidation of an integrated framework for the functioning and supervision of non-bank financial markets, of the participants and operations on such markets.

**The Government of Romania, via the Ministry of Public Finance.** The MPF is organised and run as a specialised body of central public administration, with legal status, subordinated to the Government, which implements the strategy and Government Programme in the field of public finance.

# Foreword by the NCMO Chair

The global financial crisis that broke out in 2008 ushered in a number of major changes in policymakers' approach to financial stability. Up to that point, the central banks' primary objective regarding price stability was deemed sufficient to safeguard financial stability. However, the financial crisis showed that financial stability is an endogenous component of the economic equilibrium.

The first action step at EU level taken in this sense was the establishment of the European Systemic Risk Board (ESRB), whose mandate – as the name suggests – is to identify risks that have the capacity to affect the financial sector and the real economy on a large scale. Both by virtue of this approach and in an environment of increasingly complex and close interlinkages globally between the financial systems and real sectors of national economies, the idea was put forward for coordinated action by all authorities in charge at national, regional (European) and world levels.

Specifically, in the EU, Member States have assigned the role of designated macroprudential authority either to a single institution, i.e. the central bank or the supervisory authority or to a board composed of authorities whose actions have a material impact on financial stability, Romania being a case in point. As regards the boards, the ESRB recommends that national central banks have a leading role "because of their expertise and their existing responsibilities in the area of financial stability. This conclusion is further strengthened when central banks are also in charge of microprudential supervision".

The National Committee for Macroprudential Oversight (NCMO) is a forum for discussions among Romanian authorities with a major role in preserving financial stability. In addition, the NCMO also acts as the designated authority in charge of implementing the macroprudential instruments consisting of the capital buffers, Romania, France and the UK being the only EU Member States that chose this option. The other countries mostly opted for leaving at the central bank's disposal the macroprudential instruments in the capital buffers category.

Based on the same mechanism used by the ESRB as well, the NCMO may issue only warnings and recommendations to the NBR and the FSA, in their capacity of national financial supervisory authorities at a sectoral level, as well as recommendations to the Government for the purpose of safeguarding financial stability. The recipients of NCMO recommendations or warnings may adopt the appropriate measures or provide justification for any inaction, based on the "act or explain" principle.

The drafting of the *Annual Report* ensures the NCMO's accountability to the Parliament as regards the macroprudential policy decisions taken. The structure of this *Report* may vary from one year to another, depending on the actual economic conditions and the macroprudential measures adopted. Thus, the *Annual Report* is intended to have a flexible structure that might constitute an unbiased source of information on macroprudential policy at national level. The *Report* aims to provide information in a clear and readily-understandable manner, with a message targeting a wide audience, to become in time an efficient and effective communication tool.

# Overview

The *Annual Report* of the National Committee for Macroprudential Oversight is prepared with contributions from the three NCMO member authorities, namely the National Bank of Romania, the Financial Supervisory Authority and the Government of Romania, via the Ministry of Public Finance, and describes the NCMO activity in the field of macroprudential policy during 2017. The main objective of the *Report* is to inform on the macroprudential measures taken by the NCMO with a view to safeguarding the stability of the national financial system. The first *Report* is structured into three chapters: (i) establishment of the National Committee for Macroprudential Oversight, (ii) measures implemented for achieving national macroprudential objectives, and (iii) communication in the macroprudential area.

The first chapter provides an in-depth analysis of the rationale behind the establishment of the National Committee for Macroprudential Oversight, describing the milestones in the field of macroprudential policy at international level, as well as the European institutional framework. In this context, the chapter presents the main objectives, tasks, and powers of the NCMO, as conferred upon it by Law No. 12/2017 on the macroprudential oversight of the national financial system, but also elements regarding its organisational structure and the mechanisms whereby the NCMO addresses recommendations or warnings to the sectoral competent authorities. The closing part of the chapter reviews the NCMO activity during 2017, with a focus on the topics discussed in the General Board meetings, regarding primarily the recalibration or implementation of macroprudential policy instruments.

The second chapter describes the measures implemented for achieving national macroprudential objectives and starts with a comparison of the macroprudential policy stance at European level in 2017. The analysis points out that most Member States which implemented or recalibrated macroprudential instruments took restrictive measures. A closer look shows the prevalent tightening of instruments addressed to the real estate sector, in line with the steep uptrend in property prices in several Member States, or the use of the structural systemic risk buffer, whose flexibility enables the coverage of a wide range of vulnerabilities.

As regards the recalibration of macroprudential instruments, during 2017, the NCMO made the following recommendations: (a) maintaining the countercyclical buffer (CCyB) rate at 0 percent, given that the analyses conducted in June and December 2017 did not provide signals on excessive credit growth at aggregate level, (b) applying a buffer for other systemically important institutions (O-SIIs), equal to 1 percent of the total risk exposure, in the case of nine identified institutions, starting 1 January 2018 and (c) implementing a systemic risk buffer (SRB) starting 30 June 2018. The decision on the systemic risk buffer was based on several considerations: (i) the need to address the issue of non-performing loans, which has become a concern on the agenda of the decision-making bodies in the

European Union and worldwide, (ii) the tensions surrounding domestic macroeconomic equilibria, (iii) the shaping of a legislative framework with potentially adverse effects on the management of risks in the banking sector, and (iv) lingering uncertainties about the regional and international context. The buffer rate will be 1 or 2 percent of the overall risk-weighted exposure (the maximum level between the systemic risk buffer and the buffer for systemically important institutions will apply), depending on the values of the indicators on the non-performing loan ratio and the coverage ratio, determined for each credit institution. The sections on each capital buffer include theoretical concepts regarding the instruments, comparative analyses with other EU Member States, the implementation methodology used at a national level, as well as empirical evidence on the impact of capital requirements on the real economy.

The following sections describe the macroprudential instruments addressed to borrowers, such as the debt service-to-income (DSTI) and the loan-to-value (LTV) requirements. Recent analyses on household indebtedness show the timeliness of conducting an in-depth assessment with regard to setting an explicit limit on the overall DSTI level and revising, from a social point of view, the conditions for accessing a loan under the “First Home” programme, given the latter’s importance in credit to households.

The closing part of the chapter presents other macroprudential instruments or measures as well, such as the reciprocation of measures implemented in other Member States, so as to render macroprudential policy more effective and limit regulatory arbitrage opportunities, or the assessment of the impact of credit institutions’ funding plans on the flow of credit to the real economy. Moreover, another initiative implemented by the National Bank of Romania in 2017 with a view to safeguarding financial stability was the revision of the regulatory framework applicable to non-bank financial institutions. The changes encompass new criteria for falling under the NBR’s prudential supervision (registration with the Special Register) and requirements for the build-up of additional own funds, accounting for two-thirds of the value of loans, by those NBFIs extending loans under low prudence conditions, at APRC rates exceeding those mentioned.

The third chapter on communication in the macroprudential field underlines how this policy area has gained importance in the wake of the global financial crisis. In this context, the chapter showcases the main communication tools and channels that the National Committee for Macroprudential Oversight uses in its activity, as well as the importance of communication – both at the national level and as part of the cooperation with European and international macroprudential authorities – in the effective implementation of macroprudential policy measures.

# 1. Establishment of the National Committee for Macroprudential Oversight

Financial stability is a precondition for the continuity of financial intermediation carried out by financial system operators, essentially contributing to sustainable economic growth, job creation and higher standards of living. According to the European Central Bank's definition, financial stability is a state whereby the build-up of systemic risk is prevented. Systemic risks carry the potential to impair the provision of financial services by the financial system to a point where economic growth and welfare may be materially affected.

Given the current interlinkages at the international level among financial institutions, markets and infrastructures, underpinned by the free movement of capital, financial stability is a global public good that can be safeguarded only through the concerted action of all responsible authorities nationally, regionally (European level) and worldwide.

At a national level, the National Bank of Romania, the Financial Supervisory Authority, and the Government have financial stability responsibilities according to the respective area of accountability defined through legal regulations. In particular, central bank responsibilities as regards financial stability are implicit and derive from its primary objective, which is to ensure and maintain price stability[1], as well as from the explicit tasks of supervising credit institutions and overseeing the smooth operation of payment systems. The FSA is tasked with ensuring the stability of the financial instruments markets and of the insurance activity, as well as protecting the interests of participants in the private pension systems[2].

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1 Art. 2 of Law No. 312/2004 on the Statute of the National Bank of Romania sets forth: (1) The primary objective of the National Bank of Romania shall be to ensure and maintain price stability. (2) The main tasks of the National Bank of Romania shall be: a) to define and implement the monetary policy and the exchange rate policy; b) to conduct the authorisation, regulation and prudential supervision of credit institutions and to promote and oversee the smooth operation of the payment systems with a view to ensuring financial stability; c) to issue banknotes and coins as legal tender on the territory of Romania; d) to set the foreign exchange regime and to supervise its observance; e) to manage the official foreign reserves of Romania. (3) Without prejudice to its primary objective of ensuring and maintaining price stability, the National Bank of Romania shall support the general economic policy of the State.

2 According to Art. 5 of Government Emergency Ordinance No. 93/2012 on the establishment, organisation and operation of the Financial Supervisory Authority, as subsequently amended and supplemented: In exercising the duties and prerogatives provided hereby, the FSA shall contribute to the consolidation of an integrated framework of operation and supervision of markets, participants and operations on such markets, having as objectives: a) to ensure the stability, competitiveness and proper functioning of financial markets, to promote trust in these markets and in investments in financial instruments, and to ensure the protection of operators and investors against unfair, abusive and fraudulent practices; b) to promote the stability of the insurance activity and to defend policyholders' rights; c) to ensure the efficient operation of the private pension system and to protect the interests of participants and beneficiaries.

As an officially-recognised deposit guarantee scheme in Romania, the objective of the FGDB[3] is to guarantee the deposits of and indemnify the guaranteed depositors up to a guarantee ceiling[4]. The Government has the role of ensuring the balanced functioning and the development of the national economic and social system, along with its connection to the global economic system while promoting national interests[5]; its mandate includes a set of functions (strategy, regulatory, administration, representation, state authority in the economic and social fields)[6].

The fragmentation of regulatory and supervisory responsibilities of national sectoral authorities is at odds with the integrating nature of the financial stability objective, which called for the need to establish a distinct entity, explicitly mandated and legally authorised to adopt measures for safeguarding financial stability at a national level. In Romania, this entity is the National Committee for Macroprudential Oversight, which was set up in 2017[7] as a cooperation platform among national authorities with financial stability responsibilities, namely the NBR, the FSA, the Government and the FGDB. This laid the groundwork for the macroprudential oversight framework in Romania, in line with institutional developments in Europe and worldwide.

## **1.1.** International context

The outbreak of the financial crisis proved that the microprudential supervisory framework could not avert the build-up of excessive risks in the financial system and lacked the tools to prevent negative developments at a macroprudential level. Hence, it became apparent that the mechanisms in place were insufficiently focused on macroprudential supervision and on the interlinkages between the macroeconomic environment and the financial system, with still fragmented responsibility for macroprudential analysis. This called for completing

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3 According to Art. 92 para. (1) of Law No. 311/2015 on deposit guarantee schemes and the Bank Deposit Guarantee Fund, "The main objective of the Fund, as the statutory deposit guarantee scheme officially recognised within Romania's territory, shall be to guarantee deposits, an activity performed according to the provisions of the present law".

4 The guarantee ceiling is currently the leu equivalent of EUR 100,000.

5 Art. 1 para. (2) of Law No. 90/2001 on the organisation and functioning of the Romanian Government and Ministries, as subsequently amended and supplemented.

6 Art. 1 para. (5) of Law No. 90/2001 on the organisation and functioning of the Romanian Government and Ministries, as subsequently amended and supplemented: (5) When carrying out its Governing Programme, the Government shall exercise the following functions: a) the strategy function, which ensures the preparation of the strategy to implement the Governing Programme; b) the regulatory function, which ensures the preparation of the legislative and institutional framework required for achieving strategic objectives; c) the state property administration function, which ensures the administration of public and private state property, as well as the management of services that the state is in charge of; d) the representation function, which ensures the representation of the Romanian State both domestically and abroad; e) the state authority function, which ensures the follow-up of the enforcement of and compliance with regulations in the areas of defence, public order and national security, as well as in the economic and social fields and the functioning of institutions and bodies reporting to the Government or operating under Government authority.

7 The National Committee for Macroprudential Oversight was established by Law No. 12/2017 on the macroprudential oversight of the national financial system.

the supervisory institutional architecture by adding the pillar consisting of macroprudential supervision, with the stated objective of preventing and mitigating systemic risk in the financial system.

Thus, April 2009 saw the establishment of the Financial Stability Board (FSB), which undertook a key role in promoting the reform of the global financial regulatory framework and of financial stability, by coordinating the activity of national financial authorities and international regulatory bodies, with a view to developing regulatory and supervisory policies. The FSB mandate consists of: (i) assessing vulnerabilities affecting the global financial system, as well as reviewing, on an ongoing basis from a macroprudential perspective, the regulatory and supervisory actions needed to address these vulnerabilities and their outcomes; (ii) promoting coordination and information exchange among authorities responsible for financial stability; (iii) monitoring and advising on market developments and their implications for regulatory policy; (iv) monitoring and advising with regard to best practice in meeting regulatory standards; (v) undertaking strategic reviews of the international standard-setting bodies, focused on priorities and policy coordination; (vi) setting guidelines for establishing and supporting supervisory colleges; (vii) supporting contingency planning for cross-border crisis management, particularly with regard to systemically important firms; (viii) collaborating with the International Monetary Fund to conduct early warning exercises; (ix) promoting member jurisdictions' implementation of agreed commitments, standards and policy recommendations, through monitoring of implementation, peer reviews included.

In the US, the Financial Stability Oversight Council (FSOC) was set up in 2010, with a mandate to: (i) identify risks to financial stability that could arise from the material financial distress or failure of interconnected bank holding companies or non-bank financial companies, or that could arise outside the financial services marketplace; (ii) promote market discipline, by discouraging moral hazard; (iii) respond to emerging threats to the stability of the country's financial system. The FSOC is the first entity with a clear statutory mandate that creates collective accountability for identifying risks and responding to emerging threats to financial stability. It is a collaborative body chaired by the Secretary of the Treasury that brings together the expertise of the federal financial regulators, an independent insurance expert appointed by the President, and state regulators.

As regards the EU, the European Commission tasked a High Level Group, chaired by Jacques de Larosière, to formulate recommendations on how European supervisory mechanisms could be strengthened in order to better protect taxpayers and rebuild trust in the financial system. The de Larosière report recommended, inter alia, that a Union-level body with a macroprudential supervisory mandate be established, tasked primarily with overseeing and preventing systemic risks identified across the financial system. Thus, microprudential supervision, responsible for preserving the financial soundness of individual institutions, is complemented by macroprudential supervision, whose main objective is to safeguard financial stability at EU level.

### The European regulatory framework

Regulation (EU) No. 1092/2010 of the European Parliament and of the Council of 24 November 2010 on European Union macroprudential oversight of the financial system and establishing a European Systemic Risk Board laid the groundwork for the macroprudential oversight framework in the European Union, by setting up the European Systemic Risk Board. Alongside the European Banking Authority[8], the European Insurance and Occupational Pensions Authority[9], the European Securities and Markets Authority[10], the Joint Committee of the European Supervisory Authorities (ESAs)[11], and the competent authorities or national supervisors in Member States[12], the European Systemic Risk Board is part of the European System of Financial Supervision (ESFS), whose task is to ensure financial supervision throughout the EU.

### About the European Systemic Risk Board (ESRB)

According to the provisions of the regulatory framework, the ESRB is responsible for the macroprudential oversight of the EU financial system in order to contribute to the prevention or mitigation of systemic risks to financial stability in the Union that arise from developments within the financial system and taking into account macroeconomic developments, so as to avoid periods of widespread financial distress. Moreover, through its activity, the ESRB supports the smooth functioning of the internal market and thereby ensures a sustainable contribution of the financial sector to economic growth.

### ESRB tasks

With a view to fulfilling its fundamental objective, the ESRB carries out the following tasks: (i) collecting and analysing all the relevant and necessary information, for the purposes of achieving the objective; (ii) identifying and prioritising systemic risks; (iii) issuing warnings where such systemic risks are deemed to be significant; (iv) issuing recommendations for remedial action in response to the risks identified; (v) monitoring the follow-up to warnings and recommendations; (vi) cooperating closely with all the other parties to the ESFS, inter alia by providing the ESAs with information on systemic risks and developing a common set of quantitative and qualitative indicators (risk dashboard) to identify and measure systemic risk; (vii) coordinating its actions with those of international financial organisations, as well as the relevant bodies in third countries on matters related to macroprudential oversight.

### ESRB organisation

From an organisational perspective, the ESRB has a General Board, a Steering Committee, a Secretariat, an Advisory Scientific Committee, and an Advisory Technical Committee.

8 The European Banking Authority (EBA) was set up via Regulation (EU) No. 1093/2010.

9 The European Insurance and Occupational Pensions Authority (EIOPA) was established via Regulation (EU) No. 1094/2010.

10 The European Securities and Markets Authority (ESMA) was set up through Regulation (EU) No. 1095/2010.

11 The Joint Committee of the European Supervisory Authorities is laid down under Art. 54 of Regulation (EU) No. 1093/2010, Regulation (EU) No. 1094/2010 and Regulation (EU) No. 1095/2010.

12 The competent or supervisory authorities in Member States as specified in the Union acts laid down under Art. 1 para. (2) of Regulation (EU) No. 1093/2010, Regulation (EU) No. 1094/2010 and Regulation (EU) No. 1095/2010.

The General Board[13] of the ESRB takes the decisions necessary to ensure that the ESRB is able to perform the tasks entrusted to it under the legal framework in force. The Steering Committee assists in the decision-making process of the ESRB by preparing the meetings of the General Board, reviewing the documents to be discussed and monitoring the progress of the ESRB's ongoing work. The Advisory Scientific Committee and the Advisory Technical Committee provide advice and assistance on issues relevant to the work of the ESRB. The rationale behind the establishment of the Advisory Scientific Committee was to ensure transparency of the ESRB's work, by also supplying independent assessments for neutral and balanced decisions by the General Board.

The General Board is empowered to establish the rules of procedure for the ESRB. The ordinary plenary meetings of the General Board take place at least four times a year, while extraordinary meetings may be convened at the initiative of the Chair of the ESRB or at the request of at least one-third of the members of the General Board with voting rights.

The President of the ECB chairs the ESRB for a five-year term. This choice took into account the need for a credible and high-profile leadership for the new institution. Given its key role and its international and internal credibility, the President of the ECB was appointed as Chair of the ESRB for a first term of five years, during which period the newly-established institution benefited from the ECB's expertise in the area of financial stability. The ESRB Regulation is currently undergoing a revision process, one of the proposals being that the ECB President serve as ESRB Chair on a permanent basis. The ESRB has a first Vice-Chair, elected from the members of the General Council of the ECB for a term of five years, with regard to the need for a balanced representation of Member States overall and between those whose currency is the euro and those whose currency is not the euro. The second Vice-Chair is the Chair of the Joint Committee of European Supervisory Authorities. The Chair represents the ESRB externally.

### The ESRB *Annual Report*

In terms of accountability and reporting obligations, the regulations set forth that the Chair and the Vice-Chairs of the ESRB present to the European Parliament, during a public hearing, how they intend to discharge their duties under Regulation (EU) No. 1092/2010. Moreover, the Chair of the ESRB is invited, at least once a year[14], to an annual hearing in the European Parliament, marking the publication of the ESRB's *Annual Report* to the European Parliament and the Council. The *Annual Report* is made available to the public.

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13 The General Board ensures a broad representation of European and national competent authorities, consisting of members with and without voting rights respectively (Art. 6 of Regulation (EU) No. 1092/2010). Members of the General Board with voting rights comprise: (a) the President and the Vice-President of the ECB; (b) the Governors of the national central banks; (c) one member of the European Commission; (d) the Chairperson of the European Banking Authority; (e) the Chairperson of the European Insurance and Occupational Pensions Authority; (f) the Chairperson of the European Securities and Markets Authority; (g) the Chair and the two Vice-Chairs of the Advisory Scientific Committee; (h) the Chair of the Advisory Technical Committee. Members of the General Board without voting rights include, among others: (a) one high-level representative per Member State of the competent national supervisory authorities (the high-level representatives shall rotate depending on the item discussed, unless the national supervisory authorities of a particular member State have agreed on a common representative); (b) the President of the Economic and Financial Committee (EFC).

14 And more frequently in the event of widespread financial distress, according to Art. 19 of Regulation (EU) No. 1092/2010.

### Impartiality requirement for ESRB members

Regulation (EU) No. 1092/2010 includes special provisions on the impartiality of ESRB members, stipulating that, when participating in the activities of the General Board and of the Steering Committee or when conducting any other activity relating to the ESRB, the members of the ESRB perform their duties impartially and solely in the interest of the Union. Furthermore, neither the Member States, the Union institutions nor any other public or private body shall seek to influence the members of the ESRB in the performance of the tasks[15].

### The requirement for central banks to play a leading role in national macroprudential oversight

At the same time, Regulation (EU) No. 1092/2010 stipulates that the ECB and the national central banks should have a leading role in macroprudential oversight because of their expertise and their existing responsibilities in the area of financial stability. The participation of microprudential supervisors in the work of the ESRB is also required to ensure that the assessment of macroprudential risk is based on complete and accurate information about developments in the financial system. These topics were taken into consideration when establishing the composition of the ESRB General Board.

### ESRB warnings and recommendations

The ESRB's specific method of operating is by issuing warnings and recommendations. In particular, when significant risks, to the achievement of the fundamental objective, are identified, the ESRB provides warnings and, where appropriate, issues recommendations for remedial action, including, where appropriate, for legislative initiatives[16]. Warnings or recommendations issued by the ESRB may be of either a general or a specific nature and are addressed in particular to the Union as a whole or to one or more Member States, or to one or more of the ESAs, or to one or more of the national supervisory authorities. Recommendations include a specified timeline for the policy response, and the ESRB[17]monitors their follow-up. The addressees of the recommendations shall communicate to the ESRB and to the Council the actions undertaken in response to the recommendation and provide adequate justification for any inaction. Where relevant, the ESRB shall, subject to strict rules of confidentiality, inform the ESAs without delay of the answers received. If the ESRB decides that its recommendation has not been followed or that the addressees have failed to provide adequate justification for their inaction, it shall, subject to strict rules of confidentiality, inform the addressees, the Council and, where relevant, the European Supervisory Authority concerned.

### The policy framework for establishing national macroprudential authorities

For a consistent and effective macroprudential framework, the establishment of the European Systemic Risk Board is complemented by the creation of national macroprudential authorities, since the responsibility for the adoption of measures necessary to maintain financial stability lies first within national frameworks in each EU Member State. ESRB Recommendation on the macroprudential mandate of national authorities (ESRB/2011/3) recommends that Member States designate in the national legislation an authority entrusted with the

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15 Art. 7 – Impartiality in Regulation (EU) No. 1092/2010.

16 Art. 16 – Warnings and recommendations in Regulation (EU) No. 1092/2010.

17 Art. 17 – Follow-up of the ESRB recommendations in Regulation (EU) No. 1092/2010.

conduct of macroprudential policy[18]. Where a board is designated as the macroprudential authority, the mechanisms for inter-institutional cooperation shall be without prejudice to the mandates of the member national authorities. Also as part of the institutional arrangements, the ESRB recommends Member States to ensure that the central bank plays a leading role in the macroprudential policy and that macroprudential policy does not undermine central bank independence in accordance with Art. 130 of the Treaty of the European Union. The national macroprudential authority must be mandated to cooperate and to exchange information also cross-border, in particular by informing the ESRB of the actions taken to address systemic risks at the national level.

In terms of the objective of national macroprudential authorities[19], Recommendation ESRB/2011/3 recommends Member States: 1) to specify that the ultimate objective of macroprudential policy is to contribute to the safeguard of the stability of the financial system as a whole, including by strengthening the resilience of the financial system and decreasing the build-up of systemic risks, thereby ensuring a sustainable contribution of the financial sector to economic growth; 2) to ensure that macroprudential policies can be pursued at national level upon the initiative of the national macroprudential authority, or as a follow-up to recommendations or warnings from the ESRB.

In terms of tasks, powers and instruments[20], Member States are recommended to: 1) entrust the macroprudential authority as a minimum with the tasks of identifying, monitoring and assessing risks to financial stability and of implementing policies to achieve its objective by preventing and mitigating those risks; 2) ensure that the macroprudential authority has the power to require and obtain in a timely fashion all national data and information relevant to the exercise of its tasks, and that the macroprudential authority share with microprudential supervisory authorities the data and information relevant for the exercise of the tasks of those authorities; 3) entrust the macroprudential authority with the power to designate and/or develop the surveillance approaches for identifying the financial institutions and structures that are systemically relevant for the respective Member State; 4) ensure that the macroprudential authority has control over appropriate instruments for achieving its objectives.

As regards transparency and accountability[21], Member States are recommended to: 1) ensure that macroprudential policy decisions and their motivations are made public in a timely manner, unless there are risks to financial stability in doing so, and that the macroprudential policy strategies are set out and published by the macroprudential authority; 2) entrust the macroprudential authority with the power to make public and private statements on systemic risk; 3) make the macroprudential authority ultimately accountable to the national parliament; 4) ensure legal protection for the macroprudential authority and its staff when they act in good faith.

18 Recommendation B – Institutional arrangements in Recommendation ESRB/2011/3 – The macroprudential authority may be either a single institution or a board composed of the authorities whose actions have a material impact on financial stability. The national legislation should specify the decision-making process of the governing body of the macroprudential authority.

19 Recommendation A – Objective in Recommendation ESRB/2011/3.

20 Recommendation C – Tasks, powers, instruments in Recommendation ESRB/2011/3.

21 Recommendation D – Transparency and accountability in Recommendation ESRB/2011/3.

In terms of independence[22], Recommendation ESRB/2011/3 recommends Member States to ensure that: 1) in the pursuit of its objective, the macroprudential authority is as a minimum operationally independent, in particular from political bodies and from the financial industry; 2) organisational and financial arrangements do not jeopardise the conduct of macroprudential policy.

### National macroprudential authorities in the EU

So far, 26 Member States have set up macroprudential authorities at national level, 12 of which assigned the macroprudential mandate to the central bank and another 12 opted for establishing a board comprising several national authorities with supervisory tasks of the domestic financial system. Two Member States decided to entrust the supervisory authority with the mandate of national macroprudential authority. Moreover, according to the requirements of Directive 2013/36/EU, Member States have to designate the authority tasked with setting the capital buffers. Table 1.1 shows a classification of Member States depending on institutional arrangements for setting the macroprudential authority and the designated authority. It is noteworthy that only three member countries (France, Romania and the UK) have opted for a Board as macroprudential authority and designated authority according to the CRD IV, whereas most states decided to entrust the central bank with the role of designated authority according to the CRD IV, the macroprudential instruments such as capital buffers being at the central banks' disposal.

**Table 1.1.** Classification of Member States depending on institutional arrangements for the implementation of the provisions of Recommendation ESRB/2011/3 regarding the macroprudential authority and the use of macroprudential instruments specified in the CRD IV/CRR by the designated authority

| Macroprudential authority \ Designated authority CRD IV | Board | Central bank | Supervisory authority | Government | No. |
|---|---|---|---|---|---|
| Board | FR, RO, UK | ES**, NL, HR, IT***, BG, SI | AT, DE, LU | DK, PL | 13 |
| Central bank | | BE, CZ, CY, EE, GR, HU, IE, LT, MT, PT, SK, UK* | LV | | 13 |
| Supervisory authority | | | FI, SE | | 2 |
| No. | 2 | 18 | 6 | 2 | X |

* In the UK, macroprudential supervisory tasks are shared between the central bank and the Financial Policy Committee; ** In Spain, the central bank is the designated authority, while the macroprudential authority has not been set up yet; *** In Italy, the central bank is the designated authority. In 2016, the Parliament tasked the Government to establish the Macroprudential Policy Committee.

Source: ESRB

The list of macroprudential authorities established in EU Member States is shown in Table A.1. in the Annexes.

[22] Recommendation E – Independence in Recommendation ESRB/2011/3.

## **1.2.** The national macroprudential policy framework

Recommendation ESRB/2011/3 on the macroprudential mandate of national authorities was implemented in Romania through Law No. 12/2017 on the macroprudential oversight of the national financial system. Pursuant to the provisions of this law, the National Committee for Macroprudential Oversight (NCMO) was established as an inter-institutional cooperation structure without legal personality, with the mission to ensure coordination in the field of macroprudential oversight of the national financial system by setting the macroprudential policy and the appropriate instruments for its implementation. The organisation and functioning of the NCMO follow those of the European Systemic Risk Board.

The NCMO is made up of the authorities that play a leading role in safeguarding financial stability in Romania, namely the National Bank of Romania, the Financial Supervisory Authority and the Government. Each authority has appointed, according to the legislation in force, three representatives with a voting right in the NCMO General Board. A representative of the Bank Deposit Guarantee Fund also participates in the NCMO meetings with an observer status. The Chair of the NCMO General Board, appointed by law, is the Governor of the National Bank of Romania.

**The fundamental objective of the NCMO** is to contribute to safeguarding financial stability, also by strengthening the resilience of the financial system and by containing the build-up of systemic risks, thereby ensuring a sustainable contribution of the financial sector to economic growth. In achieving the fundamental objective, the NCMO is operationally independent.

**NCMO tasks**

The main tasks of the NCMO are:

a) identifying, collecting and analysing the necessary information for the purpose of achieving the fundamental objective;
b) identifying, monitoring and assessing systemic risks;
c) identifying the systemically important financial institutions and financial system structures;
d) preparing the strategy on macroprudential policy for the purpose of achieving the fundamental objective;
e) issuing recommendations and warnings in order to prevent or mitigate systemic risks to the stability of the national financial system;
f) issuing recommendations and, where appropriate, warnings in order to ensure the implementation of ESRB recommendations or, where appropriate, issuing the necessary recommendations and warnings following the ESRB warnings, issued under the powers conferred upon it by Regulation (EU) No. 1092/2010;
g) monitoring the implementation of the recommendations issued by the NCMO and of the measures adopted at national level, following the recommendations and warnings issued by the NCMO;

h) setting, reassessing on a regular basis and monitoring the intermediate objectives of macroprudential policy;

i) setting and reassessing on a regular basis the macroprudential instruments at national level and recognising the macroprudential instruments set by the authorities of other Member States;

j) issuing advisory opinions in its remit, according to the legal provisions in force;

k) issuing recommendations for ensuring the implementation at national level of the regulations, decisions, recommendations, guidelines and guides in the field of macroprudential oversight, adopted at EU level.

The NCMO is also responsible for the coordination of financial crisis management, meaning that it will issue recommendations for establishing the necessary measures to mitigate the risk of contamination, when one or more participants in the financial system face difficulties that have a systemic impact, and will monitor their implementation.

In performing its tasks, the NCMO acts as: (i) macroprudential authority within the meaning of Recommendation ESRB/2011/3 on the macroprudential mandate of national authorities; (ii) designated authority within the meaning of provisions contained in Sections I and II, Chapter 4, Title VII of Directive 2013/36/EU of the European Parliament and of the Council of 26 June 2013 on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms, amending Directive 2002/87/EC and repealing Directives 2006/48/EC and 2006/49/EC (CRD IV), and (iii) designated authority within the meaning of Art. 458 of Regulation (EU) No. 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No. 648/2012 (CRR).

**NCMO recommendations and warnings**

In order to implement the measures necessary for preventing and mitigating systemic risks at national level, the NCMO is empowered to: (i) issue recommendations and warnings to the National Bank of Romania and the Financial Supervisory Authority, in their capacity of national financial supervisory authorities at a sectoral level; (ii) issue recommendations to the Government for the purpose of safeguarding financial stability; (iii) request the European Systemic Risk Board to issue a recommendation for the recognition by one or more Member States of the macroprudential instruments recommended by the NCMO.

The recipients of the NCMO recommendations or warnings may adopt the appropriate measures, including the issuance of regulations, in order to observe the recommendations or, where appropriate, may take action to mitigate the risks they were warned about. The recipients shall inform the NCMO of the measures adopted; in cases where the recipients have not taken such measures, they shall provide adequate justification for any inaction ("act or explain"). This mechanism for implementing the recommendations and warnings (soft law) issued by the NCMO is similar to that for the recommendations and warnings issued by the European Systemic Risk Board.

**The NCMO organisational structure** consists of:

a) the **General Board**, which is in charge of taking decisions to fulfil the fundamental objective and is composed of nine members, i.e. three representatives from each authority: a) from the NBR: the Governor, the First Deputy Governor and a Deputy Governor appointed by the Board of Directors of the National Bank of Romania; b) from the FSA: the President, the First Vice President and a Vice President appointed by the Board of the Financial Supervisory Authority; c) from the Government: three representatives appointed by the Prime Minister. The director of the Bank Deposit Guarantee Fund participates in the meetings of the General Board without having a voting right;

b) the **Technical Committee on systemic risk**, which supports the activity of the General Board by drawing up analyses to identify, assess and monitor systemic risk and by putting forward the measures necessary to fulfil the fundamental objective. It is made up of seven members, as follows: a) from the NBR: the director of the Financial Stability Department as coordinator, the director of the Supervision Department and the director of the Legal Department; b) from the FSA: the head of the Financial Stability and Market Analysis Department within the Strategy and Financial Stability Directorate and a financial analyst from the same Department; c) from the Government: the director general of the Treasury and Public Debt Directorate General and the director general of the International Financial Relations Directorate General in the Ministry of Public Finance;

c) the **Technical Committee on financial crisis management**, which supports the activity of the General Board by drawing up analyses concerning one or more participants in the financial system which are failing or are likely to fail, thereby having a systemic impact, and by putting forward the measures necessary to mitigate the risk of contagion of other financial institutions or markets, or the financial system as a whole. It is made up of seven members, as follows: a) from the NBR: the director of the Supervision Department as coordinator, the director of the Financial Stability Department and the director of the Bank Resolution Department; b) from the FSA: the head of the Supervision and Integrated Regulations Department within the Strategy and Financial Stability Directorate and a market analyst from the Financial Stability and Market Analysis Department within the same Directorate; c) from the Government: the director general of the Treasury and Public Debt Directorate General and the director general of the International Financial Relations Directorate General in the Ministry of Public Finance. The director of the NBR's Legal Department has a standing invitation to attend the meetings of the Technical Committee on financial crisis management;

d) the **Advisory Scientific Committee**, which will comprise representatives of the academia and whose composition will be established by the NCMO General Board;

e) the **Secretariat**, which is ensured by the National Bank of Romania and provides administrative and logistical support to the NCMO. The NBR has tasked its Financial Stability Department with coordinating the NCMO Secretariat.

### The secondary regulatory framework

The operationalisation of the NCMO took place on 11 April 2017, when the first NCMO meeting was held, which established the membership of the General Board.

During the subsequent meetings of 2017, the NCMO adopted two regulations that are part of the secondary regulatory framework for enforcing Law No. 12/2017:

- NCMO Regulation No. 1/2017 on the organisation and functioning of the National Committee for Macroprudential Oversight, which details inter alia the modalities for proxy voting in the General Board, the way to break a tie vote, the composition of the technical committees (Technical Committee on systemic risk and Technical Committee on financial crisis management) and of the Advisory Scientific Committee – defining the selection and attendance criteria for invitees/persons that are not NCMO members;

- NCMO Regulation No. 2/2017 on the methodology and procedures used for setting capital buffers and the scope of these instruments, replacing the provisions of NBR Regulation No. 5/2013 on prudential requirements for credit institutions as regards the setting of capital buffers, namely: (i) the countercyclical capital buffer, (ii) the systemically important institutions buffer, (iii) the systemic risk buffer, (iv) the capital conservation buffer. Until the operationalisation of the NCMO, the macroprudential measures consisting in capital buffers had been implemented by the NBR following the recommendations of the National Committee for Financial Stability, based on an agreement of cooperation between the National Bank of Romania, the Financial Supervisory Authority, the Ministry of Public Finance and the Bank Deposit Guarantee Fund.

In the period ahead, the NCMO will finalise the secondary regulatory framework by adopting a regulation on the confidentiality regime of documents and archival standards.

## 1.3. The NCMO's activity in 2017

### Organisation of NCMO meetings

The ordinary meetings of the NCMO take place at least four times a year, based on an agreed calendar. Extraordinary meetings of the General Board may be convened during the year at the request of any of its members. The ordinary or extraordinary meetings of the General Board are convened by the NCMO Chair and usually take place at the NBR headquarters.

The decisions of the General Board are adopted by a majority of the votes cast. The General Board validly deliberates in the presence of at least six members. Each General Board member or proxy has the right to one vote. The ballots for General Board decisions such as recommendations, warnings, advisory opinions, and decisions issued by the NCMO are signed during the meeting in which these decisions are taken by each member/proxy of a

General Board member next to the box representing the "for" or "against" personal voting option, by specifying – in the latter case – the underlying rationale for casting such vote.

At the beginning of each meeting, the General Board, on a proposal from the Chair of the NCMO, adopts the agenda. General Board meetings are audio recorded, with the members' approval. The Secretariat prepares the draft minutes of the proceedings of the General Board. The minutes include a record of the discussions, decisions adopted and/or of the conclusions reached by the General Board, as well as the list of attendees.

At the NCMO Chair's proposal, representatives of the Technical Committees (Technical Committee on systemic risk and Technical Committee on financial crisis management), of the Advisory Scientific Committee, as well as other persons carrying out activities directly related to NCMO tasks may be invited to participate in the General Board meetings.

The Technical Committee on systemic risk has the task to support the activity of the General Board by drawing up analyses to identify, assess and monitor systemic risk and by putting forward the measures necessary to fulfil the fundamental objective of the NCMO[23]. The committee is coordinated by the director of the NBR's Financial Stability Department, who also coordinates the NCMO Secretariat and, in this double capacity, presents during the NCMO meetings the analyses subject to the debates of the General Board members.

The year 2017 saw, besides the first meeting on the operationalisation of the NCMO within the 30-day deadline stipulated by law, held on 11 April, another three meetings of the NCMO General Board, on 14 June, 9 October, and 18 December respectively.

## Topics discussed during NCMO meetings

### A. Organisation and functioning of the NCMO

During the first meeting, the NCMO was operationalised by establishing the membership of the General Board and the organisational priorities for the period ahead were set, among which drafting the Regulation on the organisation and functioning of the NCMO, establishing the regulatory framework for enforcing the law and designing the NCMO website.

As regards the organisation of the NCMO activity, several important aspects were discussed, such as the fact that, according to the legislation in force: (i) the NCMO Secretariat is ensured by the NBR, which provides administrative and logistical support; (ii) the NCMO does not have its own staff; (iii) the NCMO does not have an allocated budget; (iv) NCMO members are not remunerated for their activity, as participation in the NCMO meetings may be assimilated to an additional task in the job description at the level of the authority they represent; (v) the documents discussed at the NCMO meetings shall be prepared either at the level of an authority (when the topic is within the respective authority's remit) or within the Technical Committees (when the topic falls under the scope of competence/interest of two or several authorities represented within the NCMO); (vi) the activity of the

[23] Art. 2 para. (1) of Law No. 12/2017 on the macroprudential oversight of the national financial system.

members of the Technical Committees is supported by staff from the relevant departments within the authorities they represent; (vii) the Technical Committees may set up expert-level working groups, either standing or temporary, to assist them in their activity with specific technical support.

Moreover, it was mentioned that the analyses prepared at the level of an authority and/or within the Technical Committees shall substantiate the issuance of: (a) the recommendations and warnings to the National Bank of Romania, in its capacity as sectoral financial supervisory authority; (b) the recommendations and warnings to the Financial Supervisory Authority, in its capacity as national authority for sectoral financial supervision; (c) the recommendations to the Government, for the purpose of safeguarding financial stability; (d) the requests submitted to the ESRB to issue recommendations for the recognition of NCMO-recommended macroprudential instruments by one or several Member States; (e) the advisory opinions within the NCMO remit.

The following NCMO meeting saw the adoption of two regulations, one regarding the methodology and procedure for setting capital buffers and the other the rules governing the organisation and functioning of the NCMO:

- Pursuant to Art. 3 para. (2) let. b) and para. (3) of Law No. 12/2017, the General Board adopted the Regulation on the methodology and procedure for setting capital buffers and the scope of these instruments. The regulation transposes the provisions of Directive 2013/36/EU of the European Parliament and of the Council on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms, amending Directive 2002/87/EC and repealing Directives 2006/48/EC and 2006/49/EC as regards the setting and scope of capital buffers, as well as the applicable provisions of ESRB recommendations and EBA guidelines respectively. It was published in *Monitorul Oficial al României*, Part One, No. 13 of 5 January 2018.

- Considering the provisions of Art. 5 para. (6) of Law No. 12/2017, the General Board adopted the Regulation on the organisation and functioning of the National Committee for Macroprudential Oversight. The regulation stipulates in detail the organising and functioning of the General Board, Technical Committee on systemic risk, Technical Committee on financial crisis management, Advisory Scientific Committee, as well as of the Secretariat. A distinct chapter addresses the rules governing the conditions in which the NCMO issues the warnings, recommendations and advisory opinions to the NBR, FSA and, if applicable, the Government.

**B. Assessing systemic risk and vulnerabilities**

Starting with the second NCMO meeting, the agenda included analyses on vulnerabilities identified in relation to the stability of the Romanian financial system: (i) the soundness of non-financial corporations in Romania and (ii) household indebtedness:

- As a result of identifying structural vulnerabilities concerning the financial soundness of non-financial corporations in Romania, which entail notable negative consequences on the stability of the Romanian financial system, i.e. persistence of negative financial results of many firms, poor quality of capital and the large number of firms either with owners' equity below the regulatory threshold or inactive, the NCMO adopted Recommendation No. R/6/2017. Specifically, the Government, by the agency of the Ministry of Public Finance, and the National Bank of Romania were recommended to set up a working group to conduct in-depth analyses of the firms' financial soundness and identify solutions so that businesses' budget constraints become tight in both public and private sectors.

- Another vulnerability to financial stability refers to the increase in household indebtedness, which may have notable negative effects on both the financial system and future economic growth. At present, indebtedness has risen substantially, with one-third of the debtors who took a loan in the past year reporting on average a level of indebtedness of more than 55 percent. For in-depth analyses supportive of substantiating the NCMO decisions on mitigating risks to financial stability as a result of higher household indebtedness, the NCMO recommended the set-up of a working group consisting of representatives from the Ministry of Public Finance and the National Bank of Romania.

**C. Activation and deactivation of macroprudential measures**

The NCMO meetings of 2017 discussed the findings of the latest analyses developed with a view to adopting macroprudential measures for the purpose of safeguarding financial stability, such as: (i) assessment of cross-border effects of macroprudential measures taken in EU Member States, (ii) regular analysis on the recalibration of the countercyclical capital buffer, (iii) assessment of the materiality of third countries for the banking sector in Romania, (iv) the need to improve the statistical information underlying real estate market analyses, (v) the manner of implementing the buffer for other systemically important institutions (the O-SII buffer) in 2018; (vi) the analysis on implementing a systemic risk buffer, and (vii) the analysis regarding the impact of credit institutions' funding plans on the flow of credit to the real economy. A comprehensive list of recommendations issued by the NCMO is available in Section 3.1.

# 2. Measures implemented for achieving national macroprudential objectives

Given the characteristics of the national financial system and the provisions of Recommendation ESRB/2013/1 (Recommendation A), the intermediate macroprudential policy objectives and the necessary instruments to achieve them are as follows:

**A. Mitigate and prevent excessive credit growth and leverage**

- Counter-cyclical capital buffer (CCB)
- Sectoral capital requirements (including intra-financial system)
- Macro-prudential leverage ratio
- Loan-to-value requirements
- Loan-to-income/debt (service)-to-income requirements

**B. Mitigate and prevent excessive maturity mismatch and market illiquidity**

- Macro-prudential adjustment to liquidity ratio (e.g. liquidity coverage ratio)
- Macro-prudential restrictions on funding sources (e.g. net stable funding ratio)
- Macro-prudential unweighted limit to less stable funding (e.g. loan-to-deposit ratio)
- Margin and haircut requirements

**C. Limit direct and indirect exposure concentration**

- Large exposure restrictions
- CCP clearing requirement

**D. Limit the systemic impact of misaligned incentives with a view to reducing moral hazard**

- Capital surcharges for systemically important financial institutions

**E. Strengthen the resilience of financial infrastructures**

- Margin and haircut requirements on CCP clearing
- Increased disclosure
- Structural systemic risk buffer

**F. Increase financial intermediation in a sustainable manner**

- Improved expertise of bank staff involved in lending
- Greater dissemination of statistical data
- Bringing into local banks’ loan portfolio the higher quality sold loans and the loans granted directly by non-resident banks to non-financial corporations in Romania

**G. Increase financial inclusion**

• Provision of payment services at prices adequate to both market conditions in Romania and the needs of consumers that do not benefit from financial services

• Greater dissemination of information

**H. Protect the insurance system against the consequences of the insolvency of some insurers**

• Prepare recovery plans by ailing insurance undertakings, including measures to re-establish the level of own funds or to change the risk profile

• Resolution mechanism (addressed to insurance undertakings with a significant share in the national insurance system)

• Insurance Guarantee Fund

**I. Mitigate the negative impact of operational risks generated by the use of ICT**

• Action plan on the remedial measures for vulnerabilities identified during the IT audit

Most Member States implemented tight macroprudential policy measures in 2017, designed primarily to address cyclical risks[24]. As regards the instruments used, worth mentioning is the introduction of positive rates of the countercyclical capital buffer in several Member States (for further details, see Section 3.1.1.1 on this instrument), alongside other measures in the residential real estate sector (instruments addressed to borrowers, such as DSTI or LTV caps) to contain potentially excessive credit growth. Moreover, some Member States chose to introduce instruments aimed at the macroprudential objective of mitigating and preventing excessive maturity mismatch and market illiquidity, using the liquidity coverage ratio or the loan-to-deposit ratio.

Among the Member States active in the field of macroprudential policy (Chart 2.1) were:

**Slovakia:** Národná banka Slovenska introduced binding DSTI and maturity limits for consumer loans, also to avoid circumvention of existing limits for mortgage loans.

**Czech Republic:** Česká národní banka made a number of changes to its non-binding recommendation on retail mortgage loans, especially as regards monitoring the DSTI ratio for high-risk loans.

**Iceland:** the central bank introduced a binding LTV limit of 85 percent for new mortgage loans from July 2017 onwards.

**Lithuania and Ireland** revised the regulatory framework governing mortgage loans, inter alia by recalibrating the thresholds for the LTV, LTI and DSTI ratios.

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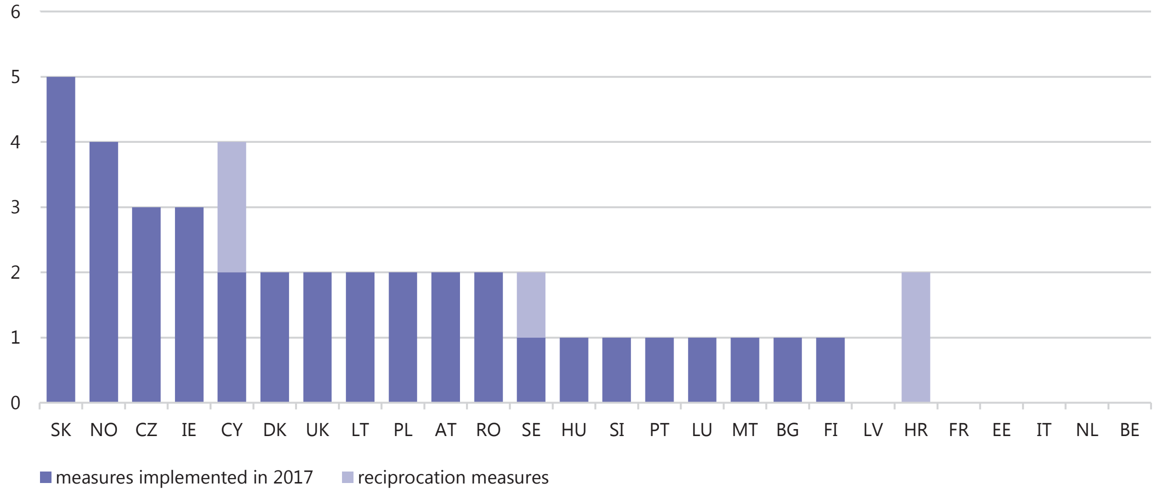
[24] European Systemic Risk Board, *A Review of Macroprudential Policy in the EU in 2017*, April 2018.

Chart 2.1. Number of macroprudential measures implemented by Member States in 2017 (including reciprocation measures)




Source: ESRB

As regards Romania, the macroprudential measures adopted in 2017 and other potential measures analysed during the year under review are detailed in the sections below.

## 2.1. Macroprudential instruments

The main instruments under the macroprudential policy framework are the capital buffers covering structural risks (the O-SII/G-SII buffer for systemically important institutions or the SRB systemic risk buffer) or cyclical risks (the countercyclical capital buffer), measures related to demand for loans and addressed to borrowers (DSTI/LTV ratios) or regarding liquidity, concentration, exposures, etc. Given that several types of instruments may be used to achieve a single intermediate macroprudential policy objective (e.g., DSTI/LTV ratios and the countercyclical capital buffer have the role of containing excessive credit growth), macroprudential authorities need to analyse carefully the structural features of the banking sector in order to assess and decide on the most effective macroprudential instrument.

Table 2.1 summarises the effects that macroprudential instruments have on credit institutions or borrowers, as applicable.

Also in this context, macroprudential authorities can implement other specific measures as well (such as introducing new regulations) to manage the risks and vulnerabilities in the financial systems they oversee.

**Table 2.1.** Mapping of macroprudential objectives and instruments

| Objective | Instrument | Effects |
|---|---|---|
| Excessive credit growth and leverage | Countercyclical capital buffer | Capital surcharges during periods of significant growth in lending to be released in times of credit decline (downswing of the financial cycle) |
| | DSTI limits | Diminish excessive leverage of borrowers, ensure the sustainable provision of credit |
| | LTV limits | Diminish excessive leverage of borrowers, ensure the sustainable provision of credit |
| Market illiquidity | Liquidity coverage ratio (LCR) and net stable funding ratio (NSFR) | Ensure adequate liquidity for the institution over the short and long term |
| Concentration | Exposure limits | Ensure diversification of financial institutions' portfolios |
| Systemically important institutions | Capital buffer for systemically important institutions | Capital surcharges covering the risks related to the size of the institution and reduce the likelihood and severity of financial crises |
| Strengthen the resilience of financial infrastructures | Systemic risk buffer | Cover any other vulnerabilities with a systemic potential that may have a negative impact on the real economy |

Source: NBR, ESRB

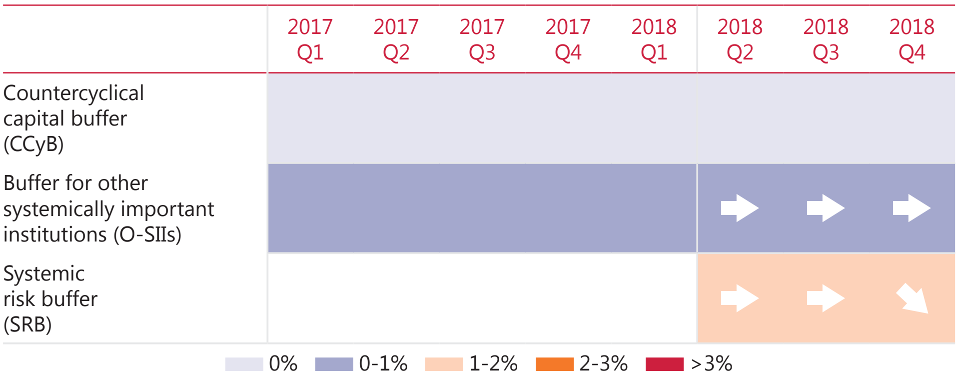
In order to safeguard the stability and integrity of the financial system, according to EU and national laws, the FSA may decide to cap the leverage that can be used by Alternative Investment Fund Managers (AIFMs) or may impose other restrictions to limit the extent to which the use of leverage contributes to the build-up of systemic risks in the financial system or the risk of disorderly markets (Art. 24 para. (3) – Law No. 74/2015 on Alternative Investment Fund Managers). Prior to implementing such a measure, the FSA needs to notify the ESRB and ESMA. The assessments conducted during 2017 showed that the level of leverage employed by alternative investment funds whose managers had registered with the FSA was very low; hence the Authority did not consider it necessary to impose such restrictions.

### 2.1.1. Capital buffers

Capital buffers are macroprudential instruments recommended by the NCMO and implemented by the sectoral supervisory authorities – the NBR and the FSA.

In 2017, the National Committee for Macroprudential Oversight assessed the need to recalibrate or implement the macroprudential instruments at its disposal and issued six recommendations to the National Bank of Romania regarding the capital buffers. Table 2.2 shows the evolution of buffers during 2017 and the expectations for 2018.

**Table 2.2.** The implementation of capital buffers in 2017 and expectations* for 2018




Note: the colour depicts the level of the buffer (see legend), while the arrow points to expectations on the number of identified institutions (O-SIIs) or the number of institutions in each category (1 or 2 percent), in the case of the systemic risk buffer.

* Expectations are based on the expert opinions of the NBR's Financial Stability Department.

Source: NBR

**As regards the countercyclical capital buffer (CCyB)**, the analyses conducted in June and December 2017 did not point to signals on excessive credit growth at an aggregate level (for further details, see Section 3.1.1.1).

**Regarding the buffer for other systemically important institutions (O-SIIs)**, nine systemically important institutions were identified, which were applied a buffer equal to 1 percent of the total risk exposure amount starting 1 January 2018 (for further details, see Section 3.1.2).

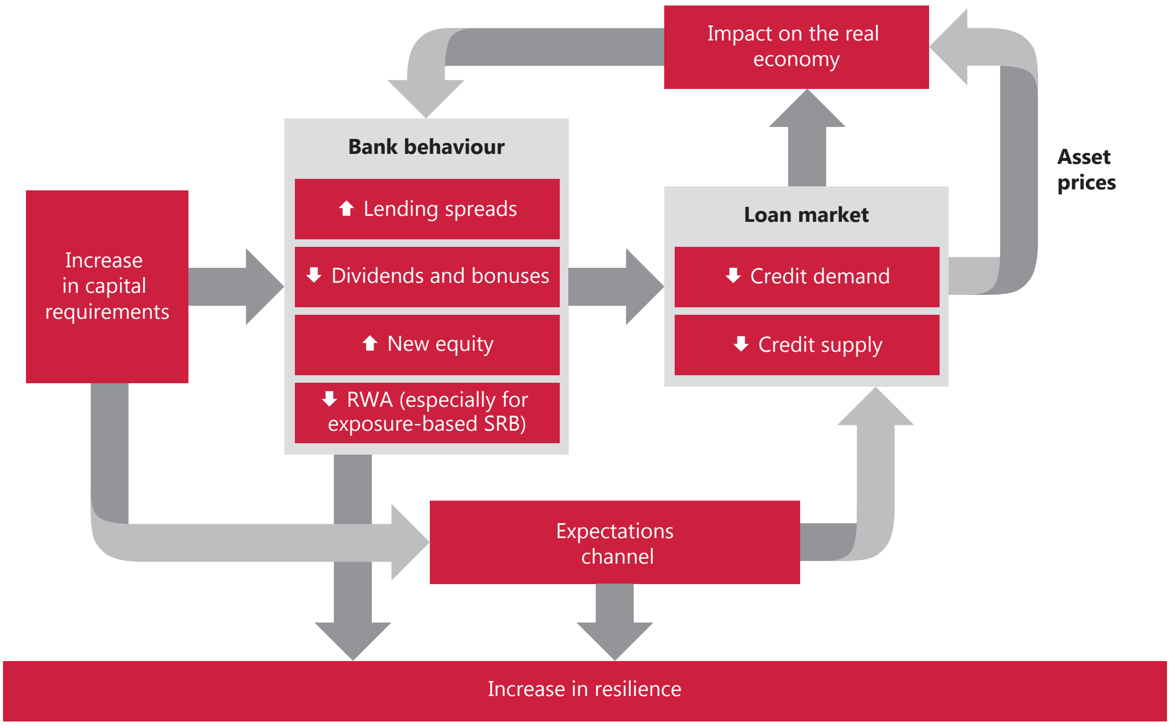
The NCMO recommended the implementation of a **systemic risk buffer (SRB)** starting 30 June 2018, based on several considerations: (i) the need to address the issue of non-performing loans, which has become a concern on the agenda of the decision-making bodies in the European Union and worldwide, (ii) the tensions surrounding domestic macroeconomic equilibria, (iii) the shaping of a legislative framework with potentially adverse effects on the management of risks in the banking sector, and (iv) lingering uncertainties about the regional and international context. The buffer rate will be 1 or 2 percent of the overall risk-weighted exposure (therefore, the maximum level between the systemic risk buffer and the buffer for systemically important institutions will apply), depending on the values of the indicators on the non-performing loan ratio and the coverage ratio, determined for each credit institution.

Macroprudential capital buffers were introduced to accomplish different macroprudential policy objectives, defined after setting up the EU-wide framework in response to the recent financial crisis. However, although the rationale or the timing of implementing these instruments may differ, the transmission mechanism of higher capital requirements within the financial system and eventually in the real economy is similar. Box 2.1. describes the impact of capital requirements on the economy, with references from academic literature worldwide.

**Box 2.1. Impact of capital requirements on the real economy**

In the wake of the financial crisis of 2007-2009, international policymakers in the field of financial supervision focused their attention on macroprudential oversight. Financial sector vulnerabilities stemming mostly from large financial institutions and cross-border interconnections underlined the need for more resilient banking sectors.

Figure 2.1. Transmission mechanism of capital requirements in the economy




Source: ESRB

The economic crisis highlighted that some of the credit institutions were undercapitalised to cushion the shocks of the crisis. The increase in capital requirements and liquidity standards has positive indirect effects on economic growth, by reducing the probability of banking crises and by lowering the volatility of GDP fluctuations. At the same time, capital constraints on banks may lead to higher funding costs and might entail a restriction in credit conditions for both households and companies, which might negatively affect economic growth in the short run. Figure 2.1 provides a graphical representation of transmission channels via which capital requirements may affect the financial system and the real economy; it illustrates the changes both in credit institutions' individual behaviour and in terms of asset prices, as well as of expectations on banking sector resilience.

Thus, from the perspective of macroprudential policy stance, there is a consensus across academic literature between the short-term costs and long-term benefits of higher capital requirements. The intermediate and long-term benefits, as well as the transitional costs of an increase in capital requirements, have been inferred in the assessments performed by the LEI Group (Long-Term Economic Impact, BCBS, 2010) and the Macroeconomic Assessment Group (MAG, 2010a, b).

The LEI Group (2010) assessed the long-term economic impact in terms of economic benefits and costs of stronger capital and liquidity regulations. The study was aimed at quantifying net benefits, measured as GDP deviation from its dynamics in the absence of changes in capital requirements. Assuming that banks have already attained the new levels of the capital requirement, the analysis points to net benefits of increased capital requirements across banks for a broad range of capital ratios (8 percent – 16 percent). The expected net gain is also associated with a reduction in the frequency and severity of banking crises. The conclusions of the paper underline that the Tier 1 capital for which the net benefits are at a maximum is between 14 percent and 15 percent of risk-weighted assets, based on the assumption that bank crises have a moderate permanent effect[25]. Using an average representative bank from 13 developed countries, the same paper shows that a 1 percentage point rise in the level of capital ratios leads to an increase of 9-19 basis points in lending rates.

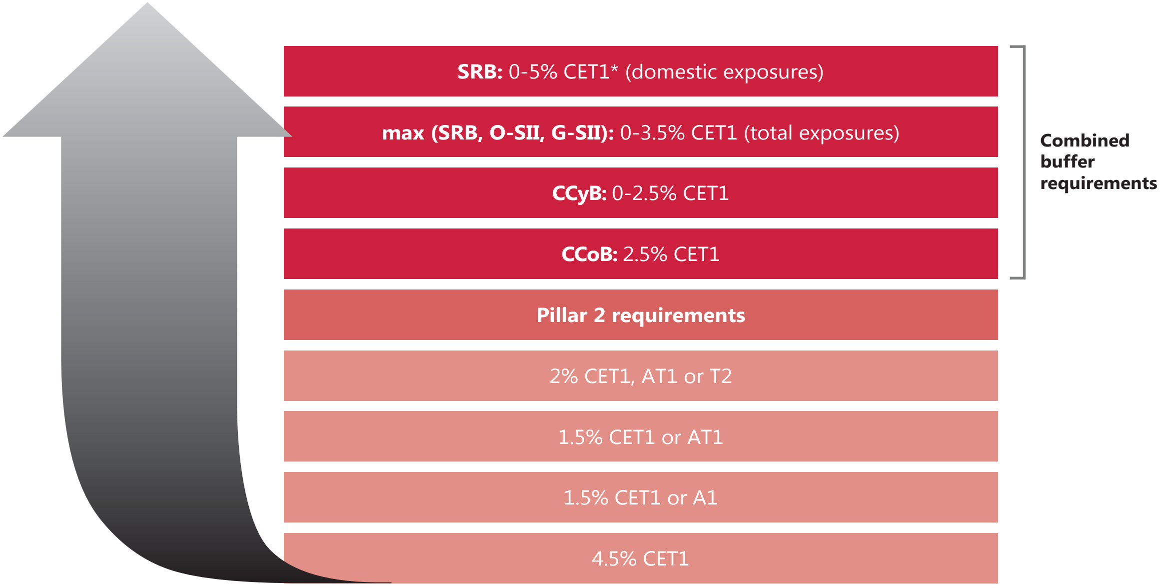
The MAG (2010a) quantifies the short-term transitional costs associated with the increase in capital requirements. Within the interim report, following the estimation of 89 models (semi-structural and DSGE models used for policy analysis), the findings indicate that a 1 percentage point rise in capital ratios leads to negative and transitory deviations of GDP from its baseline of 0.1 percent to 0.26 percent and may generate an increase of 15-17 basis points in lending spreads. The findings of the final report of the MAG (2010b) are similar. Under the assumption that credit institutions act so as to adjust within eight years (i) the global common equity to a level meeting the agreed minimum and (ii) the capital conservation buffer requirement, the study estimates that weighted median GDP is projected to fall by 0.15-0.26 percentage points below the forecasted baseline before returning to positive territory.

Capital buffers are set up as additional capital instruments to those pertaining to Pillar 1 or 2 and are aggregated to calculate the combined buffer requirement. Member States forbid any institution that meets the combined buffer requirement to make a distribution on Common Equity Tier 1 to an extent that would reduce its Common Equity Tier 1 to a level at which the combined buffer requirement would no longer be met (Art. 291 para. (1) of NBR Regulation No. 5/2013 on prudential requirements for credit institutions). Figure 2.2 shows the theoretical structure of a credit institution's capital according to European regulations.

Given the obligation to activate the capital conservation buffer and the countercyclical capital buffer starting 1 January 2016, as well as NCFS Recommendation No. 2/18.12.2015, the FSA, in its capacity as competent authority, activated and applied to financial investment companies similar levels of these buffers as those applied by the NBR to credit institutions.

[25] Findings have been updated. See Fender and Lewrick (2016) and Brooke *et al.* (2015).

Figure 2.2. Breakdown of capital requirements in line with European regulations




Source: adapted from the ESRB

In particular, the capital conservation buffer for financial investment companies was phased in between 2016 and 2018 in equal increments of 0.625 percent per annum, as follows:

| | | |
|---|---|---|
| As of 1 January 2016 – 0.625% | As of 1 January 2017 – 1.25% | As of 1 January 2018 – 1.875% |

According to the same legal provisions mentioned above, the capital conservation buffer for financial investment companies will be 2.5 percent starting 1 January 2019. At the same time, the FSA has set the countercyclical capital buffer at 0 percent, pursuant to NCFS/NCMO recommendations applicable during 2017.

The assessments conducted by the FSA during 2017 did not identify any financial investment companies meeting the systemic importance criteria, hence the Authority did not apply the capital buffer for systemically important institutions to any of the financial investment services companies under supervision.

#### 2.1.1.1. The countercyclical capital buffer

**The implementation framework of the macroprudential instrument**

The main objective of the countercyclical capital buffer is to increase the resilience of the banking sector against potential losses induced by excessive credit growth. The buffer mitigates financial sector pro-cyclicality, by constraining credit supply during the upswing and releasing the capital surplus during the downturn, helping diminish lending contraction.

EU Member States implement the countercyclical capital buffer in line with the provisions of Recommendation ESRB/2014/1 on guidance for setting countercyclical buffer rates, according to which the deviation of the ratio of credit-to-GDP from its long-term trend should serve as a common starting point in guiding decisions on countercyclical buffer rates, most notably in the build-up phase. However, designated authorities should also take into account other quantitative and qualitative information, reflecting national specificities as well, when assessing cyclical system-wide risk and setting the appropriate countercyclical buffer rate.

**Box 2.2. The Basel indicator and the smoothing parameter in the Hodrick-Prescott filter**

The Basel indicator, recommended by the BCBS and the ESRB to calibrate the countercyclical capital buffer, is defined as the deviation from long-term trend of the ratio of credit to GDP (hereinafter referred to as deviation) determined based on the Hodrick-Prescott filter, using a recursive (unilateral) method and a smoothing parameter (*lambda*) of 400,000.

**The Hodrick-Prescott (HP) filter** is a standard statistical instrument statistic used in macroeconomics to establish the trend of a variable across business cycles.

A time series can be defined as follows:

$$yt = \tau_t + c_t,$$

where $\tau_t$ is the trend and $c_t$ is the cyclical component.

The trend is estimated by minimising the following function:

$$\sum_{1}^{T}(y_t - \tau_t)^2 + \lambda \sum_{2}^{T-1}[(\tau_{t+1} - \tau_t) - (\tau_t - \tau_{t-1})]^2,$$

where $t$ is the point in time when the estimate is made for a time series where data are available for the period from 1 to $T$ and $\lambda$ is the smoothing parameter.

The value of the smoothing parameter, determined by Hodrick and Prescott (1980)[26] to estimate the trend of the business cycle (lasting between 1 to 8 years), for quarterly data series, is 1,600.

The smoothing parameter is defined as follows:

$$\lambda = \frac{\sigma^2(c_t)}{\sigma^2(\Delta^2\tau_t)}$$

As concerns the financial cycle, the empirical evidence shows that the duration of financial cycles is even four times longer than the duration of the business cycle, particularly based on developed country data (Drehmann *et al.*, 2010[27]). In this context, estimating the long-term trend of a financial cycle implies the adjustment of the smoothing parameter.

[26] Hodrick, R. & Prescott, E. – "Postwar U.S. Business Cycles: An Empirical Investigation", Reprinted in *Journal of Money, Credit, and Banking*, 29, 1981, pp. 1-16.

[27] Drehmann, M., Borio, C. E., Gambacorta, L., Jimenez, G. & Trucharte, C. – "Countercyclical Capital Buffers: Exploring Options", BIS Working Papers No. 317, July 2010.

In 1997[28] and 2002[29], Ravn and Uhlig proposed the following relation to adjust the smoothing parameter for the frequency of data (quarterly, yearly, monthly) or the cycle duration (2, 3, 4 times the business cycle length):

$$\lambda_s = s^n \lambda,$$

where $\lambda$ is the standard value of the business cycle parameter, i.e. 1,600, s is an indicator of frequency (expressed as the ratio of time units within a quarter) or cycle duration (calculated as the ratio of cycle duration to a standard business cycle duration) and n was set by Ravn and Uhlig at 4 in 1997.

The values calculated by Drehmann *et al.* in 2010 for the financial cycle are:

| Duration of the financial cycle relative to the business cycle (s) | Value of the smoothing parameter ($\lambda$) |
|---|---|
| 1 | 1,600 |
| 2 | 25,000 |
| 3 | 125,000 |
| 4 | 400,000 |

The HP filter can be estimated in two ways, i.e. recursively (unilaterally) or bilaterally. The difference between these two methods consists in the data set used to determine the long-term trend. Specifically, the recursive method uses only the information available at any point in time, while the bilateral filter uses the entire data set.

The strength of using the unilateral filter is that the results can be used to make a real-time analysis of the predictive capacity of the deviation from the long-term trend for the time series under review (in this case, total indebtedness).

Using the HP filter to identify cycles is prone to limitations, such as (i) the results are sensitive to the length and quality of the data used and may be problematic for short time series and (ii) the estimates at the beginning of the period have a high error rate, which requires a trade-off between the minimum number of observations necessary to calculate the trend for the early period of the series and the maintenance of a number of observations large enough to calculate the deviation.

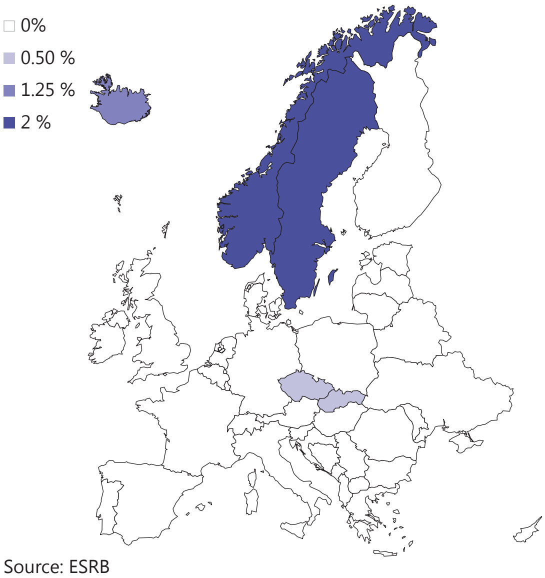
### The experience of implementing the countercyclical capital buffer in the EU

In some EU Member States, the measure to calibrate the countercyclical capital buffer at a rate higher than 0 percent is relatively recent and starts in 2016 (Chart 2.2). In all other EU countries, the buffer rate remains unchanged at 0 percent.

[28] Ravn, M. O. & Uhlig, H. – "On Adjusting the HP-Filter for the Frequency of Observations" (No. 50), CentER Discussion Paper, 1997.

[29] Ravn, M. & Uhlig, H. – "On Adjusting the HP-Filter for the Frequency of Observations", *Review of Economics and Statistics*, Vol. 84 (2), 2002, pp. 371-376.

Chart 2.2. Implementation of the countercyclical capital buffer in the EU




| Country | CCB rate (percent) | Application date |
|---|---|---|
| Czech Republic | 0.50 | 1 January 2017 |
| Sweden | 2.00 | 19 March 2017 |
| Slovakia | 0.50 | 1 August 2017 |
| Iceland | 1.25 | 1 November 2017 |
| Norway | 2.00 | 31 December 2017 |

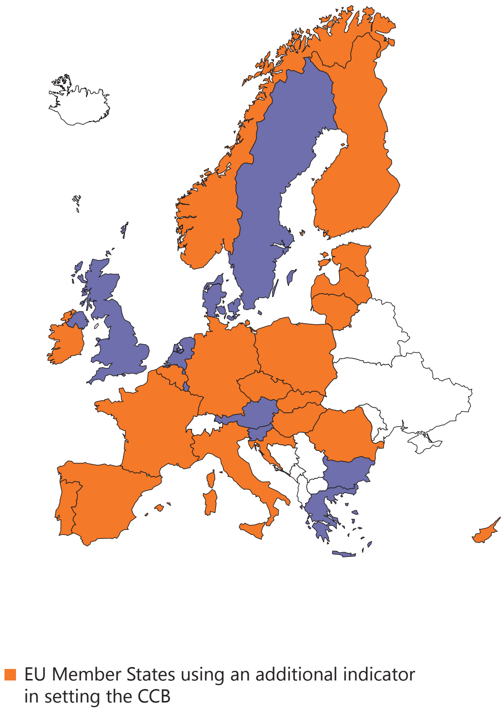
Source: ESRB

Thus, the countercyclical macroprudential measures are relatively heterogeneous, being based on the evolution of financial cycles in EU Member States, as well as on the diversity of indicators and specific alternative methodologies implemented in some EU countries.

According to Recommendation ESRB/2014/1, where designated authorities deem that a measurement and calculation of the credit-to-GDP gap different from the methodology presented in Box 2.2 would better reflect the specificities of the national economy, they are recommended to measure and calculate quarterly an additional credit-to-GDP gap further to the standardised gap.

As a result, most EU Member States chose to calculate an additional indicator for setting the optimal countercyclical buffer rate (Chart 2.3).

Chart 2.3. Setting countercyclical buffer rates by EU Member States




Source: ESRB

### Implementation of the countercyclical capital buffer in Romania

The recalibration of the countercyclical capital buffer is analysed during the meetings of the National Committee for Macroprudential Oversight (NCMO), in its capacity as macroprudential authority. In order to implement this measure, the NCMO issues a recommendation addressed to the National Bank of Romania.

In the period from 2016 to 2017, the countercyclical buffer rate applicable in Romania was set at 0 percent,

Chart 2.4. Analysis of the countercyclical capital buffer in Romania in the assumption of a short financial cycle (alternative indicator)

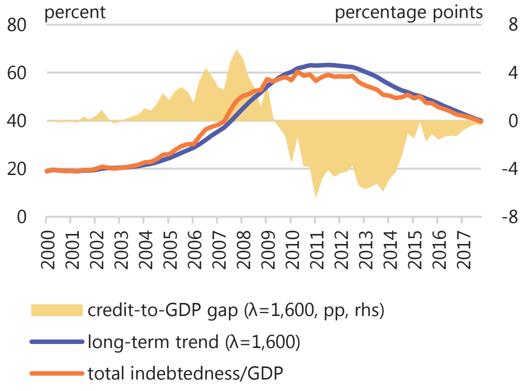
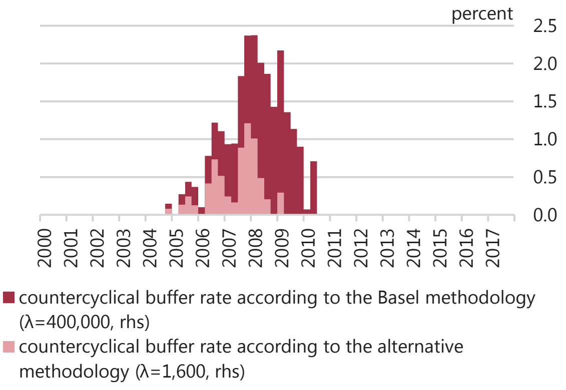



Chart 2.5. The countercyclical buffer rate




Note: The 1,600 value of the smoothing parameter λ is used for cycles having lengths similar to those of business cycles, referred to in the literature as short cycles of up to eight years.

Source: NBR, NIS, NBR calculations

as the results of the analysis on total indebtedness showed no signals of an excessive rise in aggregate indebtedness. Conversely, developments in lending to households point to a potential excessive increase, which made the NCMO recommend a closer monitoring of this component.

The methodology implemented to set the countercyclical buffer rate is compliant with the reference techniques recommended by the Basel Committee, being adapted, however, to reflect the specificities of the national banking sector. Specifically, the Basel indicator and the alternative indicator of the credit-to-GDP gap are used, both indicators being taken from the EU-recommended methodology. Additional indicators (private sector indebtedness, households' total indebtedness, non-financial corporations' total indebtedness) and structural indicators (real estate market, financial standing of the banking sector and credit standards, macroeconomic framework), which reflect the characteristics of lending at national level, are also used.

The results of the latest reassessment of the countercyclical capital buffer, based on the data available at 31 December 2017, showed that the deviation of total indebtedness from its long-term trend remained in negative territory, i.e. down 0.37 percentage points in December 2017, yet it had been narrowing over the past quarters (Chart 2.4). Under the circumstances, the indicator is further below the 1 percentage point alert threshold and the 2 percentage point signalling threshold and, thus, setting a positive countercyclical buffer rate is not necessary (Chart 2.5).

The analysis relied on the assumption of a short financial cycle[30], with a length similar to that of business cycles, which was deemed adequate for small open economies with

[30] A recent study made by Altăr, Kubinschi and Bârnea confirms the assumption of short financial cycles in CEE countries as compared with those in Western Europe – Altăr, M., Kubinschi, M., and Bârnea, D. – "Measuring Financial Cycle Length and Assessing Synchronization using Wavelets", *Romanian Journal of Economic Forecasting*, Institute for Economic Forecasting, Vol. 0 (3), 2017, pp. 18-36.

developing financial systems. In the assumption of a long financial cycle, the deviation from the long-term trend is further well below the potential level, i.e. -8.01 percent in December 2017.

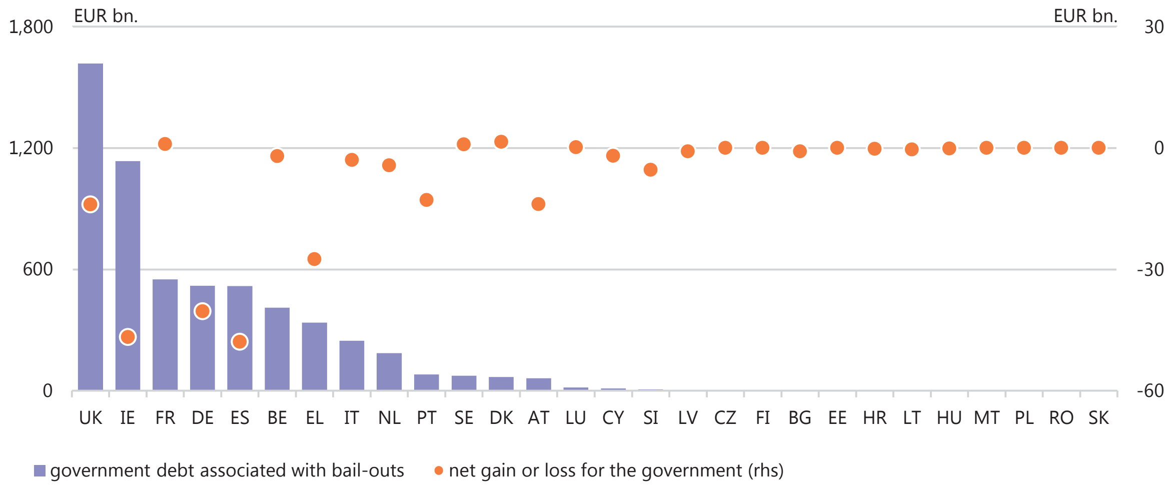
At a sectoral level, there are further signals relative to the existence of vulnerabilities associated with household lending: the deviation from the long-term trend remained in positive territory at 0.14 percentage points in December 2017. Moreover, residential property prices continued to increase at a fast pace, their annual growth rate coming in at 8.68 percent in nominal terms in September 2017[31] (6.79 percent in real terms over the same period), standing above the 6 percent alert threshold recommended by the European Commission, yet further below the 10 percent signalling threshold.

### 2.1.1.2. The capital buffer for systemically important institutions

#### The implementation framework of the macroprudential instrument

Pursuant to Recommendation ESRB/2013/1 (Recommendation A – Definition of intermediate objectives and Recommendation B – Selection of macroprudential instruments of the European Systemic Risk Board's Recommendation on intermediate objectives and instruments of macroprudential policy), in order to achieve the intermediate objective of "limiting the systemic impact of misaligned incentives with a view to reducing moral hazard", the national macroprudential authorities should use, as a dedicated macroprudential instrument, the additional capital requirements for systemically important institutions[32].

Chart 2.6. Government intervention in supporting financial institutions in EU Member States over the period from 2007 to 2015




Source: Voinea, L. – "Romania in the Euro Zone: When and How", 2017

31 However, this piece of information should be interpreted with caution, taking account of the changes made by the NIS in the calculation methodology of residential property prices.

32 Table 1 – Indicative list of macroprudential instruments in Recommendation B – Selection of macroprudential instruments specified in the ESRB Recommendation on intermediate objectives and instruments of macroprudential policy (ESRB/2013/1).

The surcharges for systemically important institutions were implemented pursuant to Directive 2013/36/EU, being a macroprudential instrument applicable to institutions that may pose a systemic risk due to their being perceived as too big to fail[33]. Chart 2.6 presents the EU-wide public spending to bail out financial institutions after the global financial crisis, pointing to the fact that a small number of Member States, Romania included, did not resort to public funds for bank recapitalisations.

Similarly to the other instruments consisting in surcharges, the objective of the capital buffer for systemically important institutions is to enhance the institution's resilience to the idiosyncratic or common shocks of the financial sector, by increasing the loss-absorption capacity. Strengthening the soundness of individual financial institutions, particularly of those that are systemically important, has a favourable impact on the stability of the financial system as a whole. The importance of building a sound financial system was highlighted by the latest international financial crisis, which was caused not only by markets' exuberance, the excessive risk-taking, and the more flexible regulatory framework but also by the undercapitalisation of numerous financial institutions.

The macroprudential instrument consisting in the "additional capital requirements for systemically important institutions" refers to the structural dimension of systemic risk, namely that concerning the distribution of risks across the financial system – in the case of large institutions, the systemic risk is generated by asset size, varying marginally throughout the business cycle.

Member States identify systemically important institutions based on a methodology developed by the European Banking Authority (EBA). Pursuant to Art. 131(3) of Directive 2013/36/EU, EBA is mandated to issue guidelines on the criteria to determine the conditions of application of the provisions in relation to the assessment of other systemically important institutions (O-SIIs)[34]. On 16 December 2014, EBA published the final version of the Guidelines on the criteria to determine the conditions of application of Art. 131(3) of Directive 2013/36/EU (CRD) in relation to the assessment of other systemically important institutions (O-SIIs)[35] (EBA/GL/2014/10). The Guidelines were issued based on Art. 16 of EU Regulation No. 1093/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Banking Authority). Pursuant to Art. 16(3) of the EBA Regulation, the competent national authorities shall make every effort to comply with those guidelines and recommendations issued by the European Banking Authority, by implementing their provisions into their supervision practices. EBA Guidelines reflect the appropriate supervisory practices within the European System of Financial Supervisors.

33 *The ESRB Handbook on Operationalising Macroprudential Policy in the Banking Sector.*

34 O-SII – Other Systemically Important Institutions (O-SIIs).

35 EBA Guidelines were published on the European Banking Authority's website (http://www.eba.europa.eu/documents/10180/930752/EBA-GL-2014-10+%28Guidelines+on+O-SIIs+Assessment%29.pdf).

Specifically, in compliance with EBA Guidelines, systemically important institutions are assessed yearly, based on a two-step procedure:

I. In the first step, a score is calculated based on the mandatory indicators set forth in EBA Guidelines at the highest consolidation level for the entities that fall under the jurisdiction of the national competent authority. The mandatory criteria used to assess systemic importance are presented in Table 2.3.

**Table 2.3.** Mandatory criteria and indicators set forth in EBA Guidelines for the assessment of other systemically important institutions

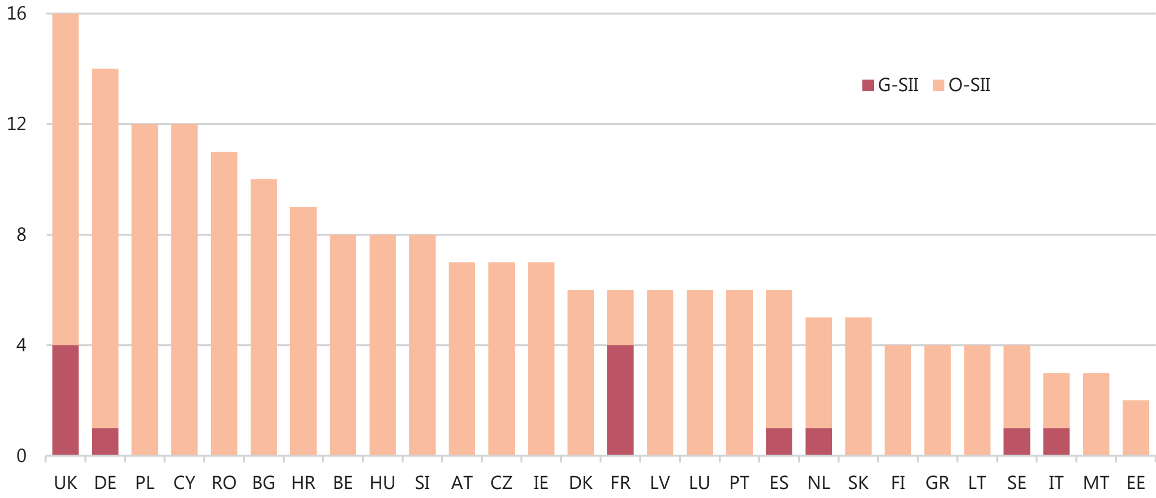
| Criterion | Indicator | Share (percent) |
|---|---|---|
| Size | Total assets | 25.00 |
| Importance (including substitutability/financial system infrastructure) | Value of domestic payment transactions | 8.33 |
| | Private sector deposits from depositors in the EU | 8.33 |
| | Private sector loans to recipients in the EU | 8.33 |
| Complexity/ cross-border activity | Value of OTC derivatives | 8.33 |
| | Cross-jurisdictional liabilities | 8.33 |
| | Cross-jurisdictional claims | 8.33 |
| Interconnectedness | Intra financial system liabilities | 8.33 |
| | Intra financial system assets | 8.33 |
| | Debt securities outstanding | 8.33 |

Source: EBA

All criteria should be weighted equally at 25 percent. The indicators of each criterion must be weighted equally relative to the other indicators specified by that criterion. This step ensures the comparability and transparency of the assessment of systemically important institutions across the EU and must be completed by all Member States. Harmonised definitions are used to calculate mandatory indicators, which are based on the financial reporting submitted on the basis of implementing technical standards of the EU-wide common reporting framework for supervisory purposes.

II. In the second step, additional indicators chosen by the competent national authority from the list of optional indicators specified in EBA Guidelines are used; they reflect the specificities of the national financial sector in order to identify all systemically important institutions, including the small-sized ones, which were not automatically deemed as having systemic importance in the first assessment stage (the indicators for Romania are presented in Table A.2. in the Annexes). This step is necessary due to the large differences across Member States in terms of size and structure of national financial systems. In this step, the criteria analysing the detailed connections between financial market intermediaries as well as the relations with the real economy are used, thus contributing to the thorough analysis on systemically important institutions.

Chart 2.7. Number of systemically important institutions identified in the EU in 2017




Source: ESRB

**The experience of implementing the buffer for other systemically important institutions in the EU**

So far, all 28 EU Member States notified to the ESRB the identification of systemic institutions at national level, of which 20 countries implemented the O-SII buffer and 6 countries chose to use the systemic risk buffer to mitigate the risks that systemic entities may generate in the context of the national banking sector either as a single macroprudential instrument or for supplementing the O-SII buffer. The Member States that used this strategy due to the constraints imposed by the European regulatory framework on limiting the maximum O-SII buffer rate at 2 percent of the total risk exposure amount, as well as on the possibility of implementing the O-SII buffer no earlier than 1 January 2016.

A recent ESRB report on the implementation of structural capital buffers shows that, in 2016, 199 systemically important institutions were identified across the EU, of which 13 were global systemically important institutions (G-SII). There is high heterogeneity with regard to the number of identified institutions (Chart 2.7), which partly reflects the degree of concentration of national banking sectors.

These institutions have a different importance from one economy to another, accounting for approximately 75 percent of the European banking sector at an aggregate level and a total asset-to-GDP ratio of about 200 percent. The heterogeneity is evident in this case as well, as there are banking sectors where systemically important institutions make up for nearly 100 percent of this sector (Greece, Denmark) as compared with a share below 60 percent in countries such as Germany or Italy.

As for the buffer rate calibration, there are notable differences between the methodology for mapping the scores determined based on EBA Guidelines and the final rates applied to institutions. Member States mainly opted for a calibration based on score ranges (determined by way of cluster analyses in countries such as Germany, Greece, Italy or Hungary) or a proportional approach (as is the case with Luxembourg). Another frequently used methodology is the equally expected impact, in which case the base assumption is that the bankruptcy of these institutions must have the same impact as the bankruptcy of institutions other than those having systemic importance.

### Implementation of the buffer for other systemically important institutions in Romania

At the national level, the provisions of the legal framework in force stipulate that the tasks of the National Committee for Macroprudential Oversight (NCMO) also include the identification of systemically important institutions[36], based on a methodology harmonised with EBA Guidelines[37].

The list of mandatory indicators and optional indicators used to assess the Romanian banking system in terms of the systemic importance of institutions is presented under the section entitled References, list of tables, list of charts in this *Report*. Data on credit institutions are provided by the National Bank of Romania, in its capacity as sectoral supervisory authority. The threshold set for the automatic designation of systemically important institutions in the step of determining the EBA-recommended mandatory indicators is 275 basis points.

In the second step of credit institutions' assessment, the following additional criteria are used: a) the credit institution's contribution to real sector financing, calculated based on the volume of loans to non-financial corporations and the degree of substitution of such loans; b) the credit institution's contribution to financial intermediation, determined based on the volume of deposits raised from households and non-financial corporations; c) the credit institution's presence on the interbank market and the quantification of the contagion effect; d) the identification of systemically important institutions in the ReGIS payment system; e) the vulnerability to contagion as regards the relationship between parent undertakings and their affiliates via the common lender channel (country of origin of capital). In the step of calculating additional indicators, no systemically important institutions were identified in the case of credit institutions, other than those automatically designated as having systemic importance in the step of determining the EBA-recommended mandatory indicators. The result coherence is ensured by using the 2.75 percent threshold for additional indicators, which is the equivalent of 275 basis points set for the first stage of analysis.

In order to implement the additional capital requirements for systemically important financial institutions, to prevent or mitigate systemic risks, the NCMO is empowered to issue recommendations and warnings to the National Bank of Romania and the Financial Supervisory Authority, in their capacity as national sectoral financial supervisory authorities[38].

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[36] Art. 3 para. (1) let. c) of Law No. 12/2017.

[37] Art. 22 para. (1) of NCMO Regulation No. 2/2017 on the methodology and procedures used for setting capital buffers and the scope of these instruments: (1) With a view to identifying the O-SIIs, the Committee shall use a methodology in accordance with EBA Guidelines GL/2014/10 on the criteria to determine the conditions of application of Art. 131(3) of Directive 2013/36/EU in relation to the assessment of other systemically important institutions (O-SIIs) [...].

[38] Art. 4 para. (1) of Law No. 12/2017.

The method of implementing the capital buffer for other systemically important institutions (O-SII buffer) is set forth in NCMO Regulation No. 2/2017 on the methodology and procedures used for setting capital buffers and the scope of these instruments, which stipulates that the Committee may recommend the national sectoral financial supervisory authorities to require O-SIIs to maintain an O-SII buffer of up to 2 percent of the total risk exposure amount. In line with the provisions of applicable EU regulations, the O-SII buffer rate that may be imposed on a national systemically important institution that is a subsidiary of either a G-SII or an O-SII which is an EU parent institution and subject to an O-SII/G-SII buffer on a consolidated basis in the country of origin cannot exceed the higher value of a) 1 percent of the total risk exposure amount and b) the G-SII or O-SII buffer rate applicable to the group at consolidated level[39].

In the case of systemically important credit institutions, the O-SII buffer is implemented based on an order issued by the National Bank of Romania, at the recommendation of the National Committee for Macroprudential Oversight[40]. The O-SII buffer should consist of top quality own funds items with a high loss-absorption capacity as well as of Common Equity Tier 1 capital. Credit institutions are required to maintain own funds in order to meet the O-SII buffer capital requirement in addition to those used for meeting other capital requirements laid down in the legislation in force.

In 2017, in order to achieve the intermediate objective of "limiting the systemic impact of misaligned incentives with a view to reducing moral hazard", the NCMO issued Recommendation No. R/5/2017 on the capital buffer for other systemically important institutions in Romania[41] whereby the National Bank of Romania is recommended to require, starting 1 January 2018, a capital buffer for other systemically important institutions (O-SII buffer), on an individual or consolidated basis, as applicable[42], equal to 1 percent of the total risk exposure amount for all the credit institutions identified as having a systemic nature in accordance with the methodology harmonised with the provisions of EBA Guidelines on the criteria to determine the conditions of application of Art. 131(3) of Directive 2013/36/EU (CRD) in relation to the assessment of O-SIIs, based on the data reported as at 31 March 2017: Banca Comercială Română S.A. (consolidated level), BRD – Groupe Société Générale S.A. (consolidated level), UniCredit Bank S.A. (consolidated level), Raiffeisen Bank S.A. (consolidated level), Alpha Bank România S.A. (individual level), Bancpost S.A. (individual level), Banca Transilvania S.A. (consolidated level), CEC Bank S.A. (individual level) and Garanti Bank S.A. (individual level). The NCMO Recommendation took account of the fact that the O-SII buffer is a capital reserve set to mitigate the systemic risk posed by the size of credit institutions, by strengthening institutions' resilience to potential endogenous and exogenous shocks as well as by reducing their negative impact on the financial system in cases of financial market turmoil.

39 Art. 23 para. (1) of NCMO Regulation No. 2/2017.

40 Art. 269 para. (1) of Regulation No. 5/2013, as subsequently amended and supplemented.

41 NCMO Recommendation No. R/5/2017 is published on the NCMO website, under Macroprudential Policy/Recommendations (http://www.cnsmro.ro/en/politica-macroprudentiala/lista-recomandarilor/).

42 In accordance with the provisions of Art. 5 of the EBA Guidelines, competent authorities should calculate a score for each relevant entity at the highest consolidation level of the part of the group that falls under its jurisdiction, including subsidiaries in other Member States and third countries.

Systemically important credit institutions play a decisive role in the financial intermediation at the national level. According to the data available at 31 March 2017, (i) they held 76.1 percent of bank assets; (ii) they provide a significant part of financial services to the real economy, i.e. 75.5 percent of loans in stock, 77.5 percent of deposits taken, and 61.2 percent of payments made; (iii) in terms of complexity, they conduct 89.6 percent of transactions in OTC derivatives, they place 84.1 percent of cross-border assets and raise 77.2 percent of foreign liabilities, while (iv) in terms of interconnectedness with the other undertakings conducting financial activities, they provide 59 percent of intra-financial assets, they use 74.6 percent of intra-financial liabilities and hold 98.6 percent of bonds issued.

The buffer rate recommended by the NCMO took into account that, out of the nine banks identified as having systemic importance, seven are subsidiaries of foreign banks in other Member States (AT – BCR, Raiffeisen; IT – UniCredit; GR – Alpha Bank, Bancpost; FR – BRD; ES – Garanti Bank S.A.), falling under the scope of the European regulatory framework for limiting the O-SII buffer applicable in the host country at the maximum rate between 1 percent and the O-SII buffer rate applicable to the parent bank at consolidated level. One bank in the group of systemically important institutions, i.e. CEC Bank, has Romanian capital, whereas Banca Transilvania has mixed capital that cannot be, however, allocated to a single country and, as a result, the bank is not a foreign bank subsidiary. The G-SII/O-SII buffer capital requirements applicable to parent banks having subsidiaries in Romania are presented in the section entitled References, list of tables, list of charts in this *Report*.

The NCMO Secretariat notified the European Systemic Risk Board, the European Commission, the European Banking Authority, the European Central Bank and the national competent, and designated authorities in the home countries of parent banks having subsidiaries in Romania of its intention to implement the O-SII buffer in the Romanian banking system, in compliance with the provisions of the European regulatory framework[43]. The European Systemic Risk Board currently provides a thorough platform for informing the national authorities with macroprudential supervision tasks about the measures adopted by Member States to contribute to the coordination of measures implemented EU-wide. Considering that, within the 30-day time frame set for the prior notification, the European authorities had no observations to make, the National Bank of Romania, in its capacity as sectoral supervisory authority, implemented the measure recommended by the NCMO, by issuing NBR Order No. 12/2017 on the buffer for credit institutions authorised in Romania and identified by the National Bank of Romania as other systemically important institutions (O-SIIs)[44].

43 Art. 131(7) of Directive 2013/36/EU on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms stipulates that, before setting or resetting an O-SII buffer, the competent authority or the designated authority shall notify the Commission, the ESRB, EBA, and the competent and designated authorities of the Member States concerned one month before the publication of the decision.

44 NBR Order No. 12/2017 on the buffer for credit institutions authorised in Romania and identified by the National Bank of Romania as other systemically important institutions (O-SIIs) was published in *Monitorul Oficial al României*, Part I. No. 1009/20 December 2017.

### 2.1.1.3. The structural systemic risk buffer

**Framework for the implementation of the macroprudential instrument**

The structural systemic risk buffer is designed to cover the losses arising from the materialisation of some risks, except for excessive lending risks that may affect the financial stability sector-wide. The instrument may be used to achieve the intermediate objective of "strengthening the resilience of financial infrastructures" as a macroprudential tool to prevent and mitigate long-term non-cyclical systemic or macroprudential risks that do not fall under the scope of Regulation (EU) No. 575/2013[45], which may disrupt the financial system and the real economy of a certain Member State.

The macroprudential instrument consisting in imposing the systemic risk buffer aims the structural dimension of systemic risk, namely that relative to risk distribution across the financial system. The buffer is designed as a flexible instrument available for competent authorities, which may be applied to high-risk exposures (exposures located in Romania, in other Member States or in third countries) of institutions, groups of institutions or the banking sector as a whole, on a consolidated, sub-consolidated or individual basis, as applicable. The buffer level may vary among institutions, depending on each institution's contribution to the risk build-up. The CRD IV/CRR legislative package does not specify the criteria for applying the systemic risk buffer. These criteria will be established by the national competent authorities that need to calibrate the indicators used for the activation/deactivation of the buffer based on the specificities of the national financial system. The only condition imposed by the regulations applicable at EU level is that the use of this instrument should not entail disproportionate adverse effects on the financial systems of other Member States or of the Union as a whole.

Pursuant to Art. 133(1) of Directive 2013/36/EU[46], the structural systemic risk buffer refers to long-term non-cyclical systemic or macroprudential risks not covered by Regulation (EU) No. 575/2013. In this context, significant adverse effects may be manifest in the financial sector as a whole, following the emergence of strong exogenous shocks or small shocks the impact of which is enhanced by the transmission mechanism system-wide.

The ESRB Handbook on Operationalising Macroprudential Policy in the Banking Sector[47] recommends the following three main categories of risks that can be mitigated by using a systemic risk buffer:

1. **Propagation and amplification of shocks across the financial system:** financial crises may have dimensions of systemic importance due to the mechanisms of propagating and amplifying initial shocks. Contagion channels are established by way of direct or indirect

[45] Regulation (EU) No. 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No. 648/2012.

[46] Directive 2013/36/EU of the European Parliament and of the Council of 26 June 2013 on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms, amending Directive 2002/87/EC and repealing Directives 2006/48/EC and 2006/49/EC.

[47] *The ESRB Handbook on Operationalising Macroprudential Policy in the Banking Sector.*

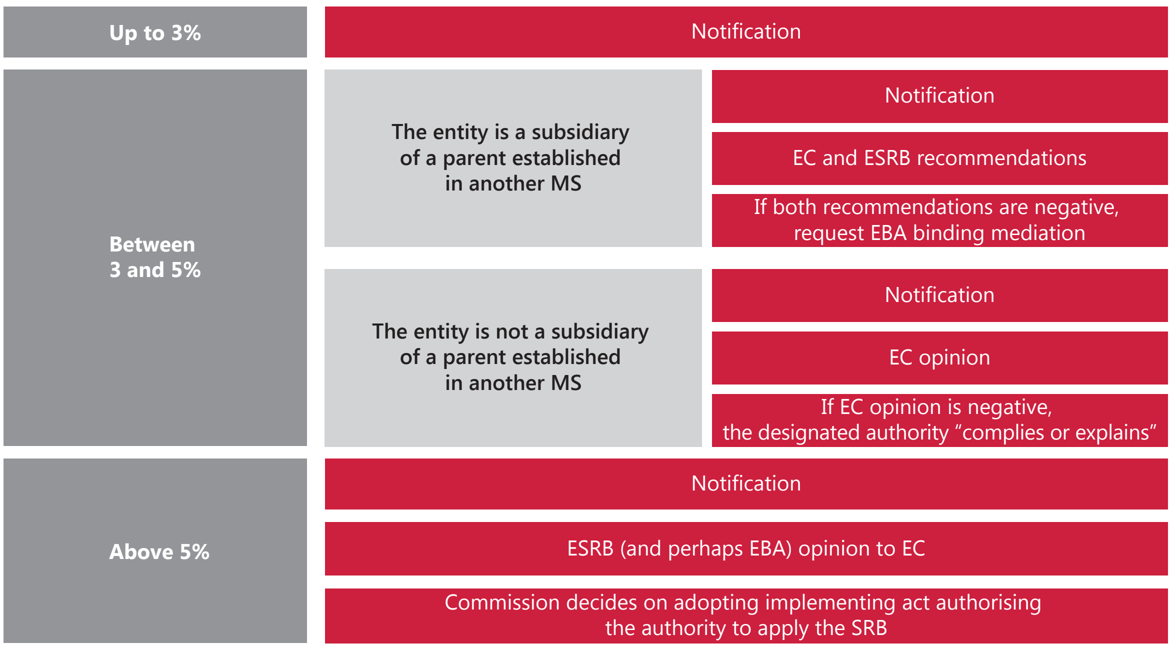
interconnectedness among individual financial institutions, as a result of common exposures or similar business models.

2. **Structural characteristics of the banking system:** certain specific characteristics of the banking sector are not likely to cause direct losses, but can amplify losses in the event of a financial crisis. These structural aspects may be linked to both the specificities of the financial system and the institutional framework.

3. **Risks to the banking sector from the real economy:** are visible particularly in small open economies, where shocks from the real economy can trigger significant losses for the banking sector. Conversely, financial system losses may affect lending to the real economy, amplifying the initial adverse effects. The shocks may arise from specific sectors of the national economy, as well as from the cross-border effects manifest regionally or even globally.

Romania transposed the provisions of the European CRD IV package into the national legislation, which refer, inter alia, to the implementation of the structural systemic risk buffer. Specifically, pursuant to Art. 281 of NBR Regulation No. 5/2013 on macroprudential requirements for credit institutions, for the purpose of preventing and mitigating long-term non-cyclical systemic or macroprudential risks not covered by Regulation (EU) No. 575/2013, in the sense of a deterioration in the financial system, with the potential to have serious negative consequences to the financial system and the real economy, the NBR may set this buffer for the financial sector as a whole or one or several subsets of financial institutions, following the recommendation of the coordination structure.

Figure 2.3. Mechanism of notifying the SRB implementation, according to EU regulations




Source: Final report on the use of structural macroprudential instruments in the EU, December 2017

Credit institutions must apply the systemic risk buffer to exposures located in Romania, in third countries, and in other Member States, in accordance with the conditions set out in the Regulation. The National Bank of Romania may require the systemic risk buffer to be applied in gradual or accelerated steps of adjustment of 0.5 percent. The central bank may also require that different systemic risk buffer rates should apply to different subsets of financial institutions. The systemic risk buffer must be of at least 1 percent Common Equity Tier 1 capital based on the relevant exposures. As for the notification of implementing a systemic risk buffer, the competent authority notifies the European institutions when the buffer level is below 3 percent. By contrast, when the buffer level is above 3 percent, the additional steps presented in Figure 2.3 are necessary.

### The experience of implementing the systemic risk buffer in the EU

Most EU Member States transposed the systemic risk buffer provisions into the national legislation. Starting with 2016, nine Member States, most of which are small open economies and, therefore, vulnerable to external shocks, have implemented a systemic risk buffer. In 2017, two more Member States announced their intention to implement this buffer, the flexibility of this instrument being revealed by the wide range of risks addressed.

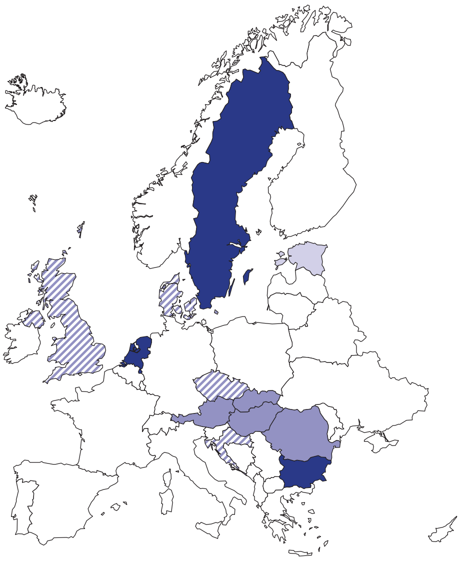
The most frequently used categories of risks are: (i) the vulnerabilities posed by systemically important institutions, identified in eight Member States; (ii) the impact of external shocks, quality of cross-border exposures and contagion mentioned in four Member States and (iii) the real estate specific risks addressed by macroprudential authorities in Croatia and Hungary. Additionally, there are cases where the buffer implementation was decided based on more of the aforementioned risk categories.

The indicators used point to a high heterogeneity among countries, based on the risks identified. In 2017, The ESRB Handbook on Operationalising Macroprudential Policy in the Banking Sector was updated by including a taxonomy of risks and potential indicators that may be monitored when assessing the implementation of a structural risk buffer. The buffer rate ranges from 1 percent to 3 percent, being calibrated on the basis of qualitative or quantitative factors, as well as of stress test results (Chart 2.8). Moreover, some authorities decided to apply the same buffer rate to all institutions, whereas the authorities that identified risks generated by systemically important institutions calibrated the instrument on an individual basis, in line with the conceptual implementation of the buffer for systemically important institutions (Chart 2.9).

**Bulgaria** uses this instrument, i.e. the systemic risk buffer, to limit the decline in the banking sector capitalisation by transposing the CRD IV/CRR requirements as well as through its economic specificities and the need to preserve a budget surplus amid the constraints induced by the currency board arrangement. As a result, the macroprudential authority in Bulgaria has decided to apply a systemic risk buffer of 3 percent to all credit institutions, at the highest consolidation level, starting with 2014.

**Austria** has implemented a systemic risk buffer on a consolidated basis, its level ranging between 1 percent and 2 percent, for the risk pertaining to systemically important institutions

Chart 2.8. Implementation of the systemic risk buffer in the EU (SRB level)

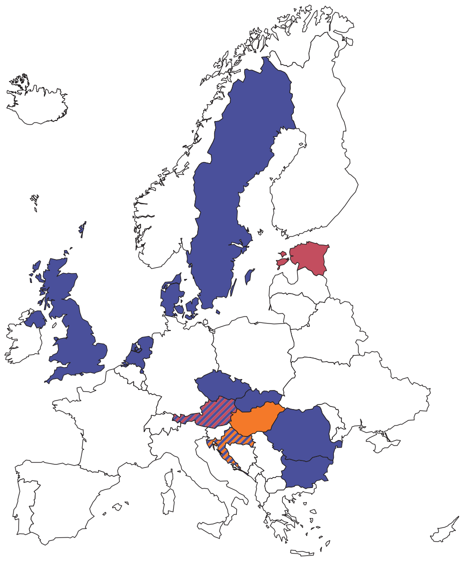


0-1% 1-2% 2-3% 1-3% 3%

Note:
In Croatia, the buffer was applied in two steps of 1.5 percent or 3 percent.
In the United Kingdom, the buffer is set to be implemented as of 2019.

Source: ESRB

Chart 2.9. Implementation of the systemic risk buffer in the EU based on the risk type



- macroeconomic risks (incl. contagion risk and cross-border exposures)
- banking sector risks (incl. systemic importance)
- sectoral risks (incl. real estate market)

Note:
The countries marked in two colours have identified both categories of risks.
Croatia is the only country that identified all three categories of risks.

Source: ESRB

and for the significant exposure of credit institutions in Austria to the emerging markets in Central, Eastern and Southeastern Europe (CESEE). The indicators used to determine the buffer rate are the share of deposits and assets of individual institutions in total deposits and assets of this sector as well as the share of exposures to the CESEE region and the associated risk, quantified by way of CDS quotes.

**Croatia** states that the systemic risk buffer covers a set of identified risks to financial stability, among which: (i) risks posed by systemically important institutions, (ii) macroeconomic imbalances, (iii) illiquid real estate market and (iv) banking sector concentration. The instrument covers all exposures and credit institutions, on an individual or sub-consolidated basis, being applied in two steps of 1.5 percent and 3 percent respectively, based on the institution's market share. The buffer threshold was set at 5 percent.

### Implementation of the systemic risk buffer in Romania

In Romania, applying a systemic risk buffer is a current issue, considering the general framework characterised by: (i) the need to solve the problem of non-performing loans in the EU and worldwide, (ii) the further tensions surrounding domestic macroeconomic equilibria and (iii) the lingering uncertainty about the regional and international context. In particular, the new monetary conditions and the recent real economy developments required the adoption of such a measure in order to reduce the probability of escalating vulnerabilities in the Romanian financial sector.

Thus, in its meeting of 18 December 2017, the NCMO issued a recommendation to the NBR to implement a systemic risk buffer. The Recommendation was issued in the context of structural vulnerabilities that were identified, are currently noticed or possibly emerging in the future, which may lead to a larger stock of non-performing loans, concurrently with a narrower room for manoeuvre of (monetary, fiscal and macroprudential) policies and credit institutions' potentially lower capacity to clean up their balance sheets. The macroprudential instrument is to be applied to all exposures, starting 30 June 2018, with the aim of supporting the adequate management of credit risk and enhancing banking sector resilience to unanticipated shocks, amid unfavourable structural circumstances.

The buffer level was calibrated at 0 percent, 1 percent or 2 percent, depending on past 12-month averages of the indicators on the non-performing loan ratio and coverage ratio, according to the methodology presented in Table 2.4. The indicators and thresholds used in the calibration of the systemic risk buffer will be reassessed with a half-yearly frequency to monitor in real time the progress in resolving non-performing loans.

**Table 2.4.** Calculation methodology of the systemic risk buffer[48]

| NPL ratio | Coverage ratio | SRB level (% of Tier 1 capital ratio) |
|---|---|---|
| < 5% | > 55% | 0% |
| > 5% | > 55% | 1% |
| < 5% | < 55% | 1% |
| > 5% | < 55% | 2% |

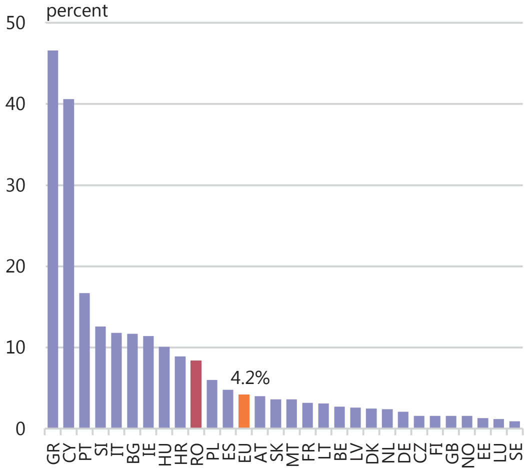
Source: NBR

Considering that the systemic risk buffer is applied to all exposures, the capital requirement for structural buffers is determined as the maximum level of the other systemically important institutions (O-SII) buffer and the systemic risk buffer (SRB). Therefore, in the case of systemically important credit institutions, the maximum additional requirement introduced by this measure is 1 percent (the difference between the maximum 2 percent SRB and the current 1 percent O-SII buffer).

The non-performing loan ratio in the national banking sector currently stands at a relatively low level (Chart 2.10), yet it stays above the EU average of 4.2 percent (2017 Q3). In addition, the coverage ratio is the highest in the EU (Chart 2.11). On the other hand, given that Romania is currently witnessing a swift economic expansion and that the NPL ratios are unevenly distributed by sector of exposure, with still high NPL ratios for loans to certain economic sectors or in certain currencies, concerns are emerging over credit risk in the period ahead.

48 The values established by the European Banking Authority in the Risk Dashboard, published on a quarterly basis, were used to set the thresholds to determine the buffer rate.

Chart 2.10. NPL ratio – comparisons at EU level (2017 Q3)




Source: EBA

Chart 2.11. Coverage ratio – comparisons at EU level (2017 Q3)

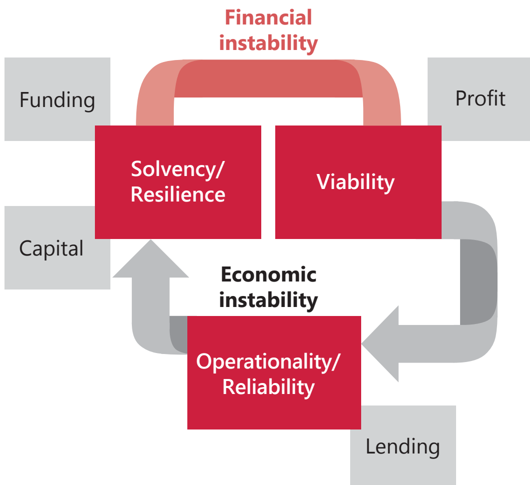

Source: EBA

In order to understand the importance of the non-performing loan issue, it is necessary to consider the way in which the four activity channels of credit institutions affected by this phenomenon intervene in the interaction between the business cycle and the financial cycle (Figure 2.4). The four main channels are capital, lending, funding, and profitability. Furthermore, there are interactions between them, which means that the effects on a business area of credit institutions also translate into other areas. In this respect, the risks to and vulnerabilities of institutions should also be viewed from the perspective of their potential to enhance the effects produced by the increasing incidence of non-performance events.

Specifically, due to its flexible nature, the systemic risk buffer is the most appropriate instrument for managing the above-mentioned constraints and the identified vulnerabilities, which have the potential of producing systemic effects. Moreover, there is no overlapping between this macroprudential measure and the potential microprudential measures, i.e. additional requirements via Pillar II, given that the vulnerability refers to the future NPL developments affected by changes in the macro-financial environment, this measure being forward-looking and not just a static vision applied to each credit institution.

This is the second implementation of the systemic risk buffer in Romania. The National Committee for Financial Stability had previously recommended that the NBR should apply a systemic risk buffer rate of 1 percent to all the exposures of credit institutions that have their parent bank registered in a country where bonds issued by the central government are not rated as investment-grade, starting in 31 March 2016. The decision was made considering that the unfavourable rating developments in the

Figure 2.4. Relation between economic instability and financial instability




Source: ESRB, EC

country of origin of the parent bank may have contagion effects on its subsidiaries in Romania via the channel of increased funding costs and therefore may affect own funds. On 9 May 2016, the NCFS recommended the NBR to cease the application of the systemic risk buffer on credit institutions over the period necessary for conducting the study on the impact of legislative developments on the financial and prudential situation of the banking system, at least until 31 December 2016. Subsequently, given the favourable macroeconomic and financial conditions, as well as the mitigation of external contagion risks, the NCFS recommended the NBR, in its meeting of 13 December 2016, to deactivate the systemic risk buffer starting with 1 March 2017.

## 2.1.2. Other macroprudential instruments or measures

### 2.1.2.1. Instruments that target borrowers

At the international level, the most frequently resorted to macroprudential instruments that target borrowers include indebtedness requirements (DSTI) and requirements for the down-payment on loans (LTV). In Romania's case, these instruments are implemented via NBR regulations.

**Indebtedness requirements (DSTI)**

The indebtedness level (measured as the debt service-to-income ratio, DSTI) is an indicator with a good capacity of signalling excessive leverage, on the one hand, and a macroprudential instrument designed to ensure debtors' resilience in the event of adverse financial developments, on the other.

The DSTI implementation and calibration rely on the assessments of systemic risks associated with indebtedness, as well as of costs and benefits of implementing measures. The increase in household indebtedness may have negative effects on the financial system given the vulnerabilities related to debtors with high levels of indebtedness. In addition, macroeconomic imbalances may lead to adverse developments in interest rates, exchange rate, and household income, which, in turn, have a direct impact on indebtedness.

Romania has a relatively long history of using this instrument, the first macroprudential regulations of this kind implemented by the NBR aiming particularly household lending. The first DSTI regulation was enforced in 2003 by way of Norms No. 15 of December 2003[49] on limiting credit risk to consumer loans. The regulation set indebtedness ceilings of 30 percent for consumer loans and 35 percent for housing loans, which applied to both lei- and foreign currency-denominated loans. In 2005, the regulation on the level of indebtedness was amended for the first time, the cap for a debtor's total level of indebtedness being set at 40 percent. The period from 2007 to 2011 saw the shift to a self-regulatory system, as

49 Norms No. 15 of 18 December 2003 on limiting credit risk to consumer loans.

creditors (banks and non-bank financial institutions enlisted in the Special Register) were required to establish through internal regulations the maximum level of indebtedness based on the debtors' risk profile.

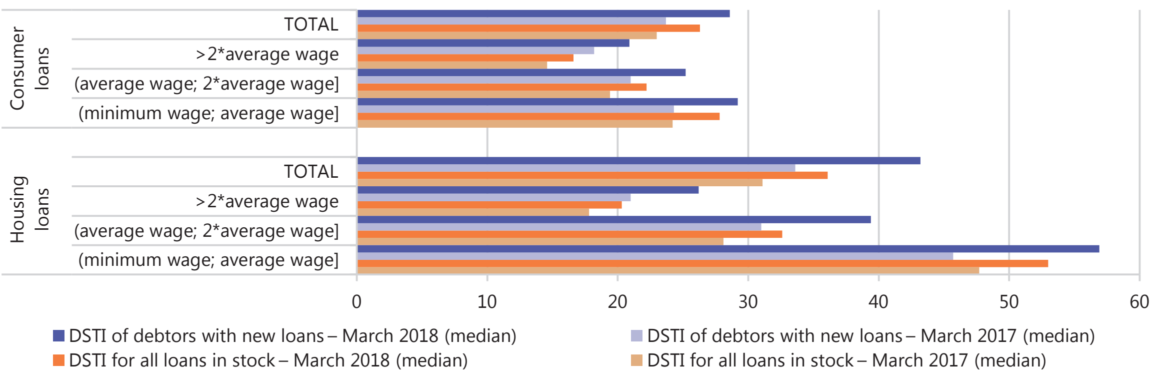
The regulations that are currently in force were implemented in October 2011 by NBR Regulation No. 17/2012 on certain lending conditions, and set forth that credit institutions and non-bank financial institutions enlisted in the Special Register shall determine the maximum level of indebtedness based on a stress scenario reflecting the currency risk, the interest rate risk and the income risk. Specifically, the regulation stipulates that the following shocks shall be applied to calculate the maximum DSTI ratio: (i) depreciation of the local currency by 35.5 percent versus the EUR, by 52.6 percent versus the CHF and by 40.9 percent versus the USD, (ii) a 0.6 percentage point shock on the interest rate and (iii) a 6 percent shock on the monthly income.

The recent NCMO analyses aimed to assess to what extent the current regulatory framework is sufficient to ensure a sustainable level of household indebtedness. They also assessed the impact of some proposals to recalibrate the level of indebtedness and impose an explicit maximum level of indebtedness.

### Recent developments in household indebtedness and household lending

In 2017, total household indebtedness was on the rise, picking up 8.1 percent year on year, amid the further swift-paced growth of bank lending, i.e. up 7.5 percent. The main determinant of the positive dynamics of bank credit was the sizeable increase in the median of a loan, irrespective of its purpose, whereas the number of loans taken was smaller in 2017 than in 2016. The median of a housing loan and that of consumer credit rose by 12 percent and 15 percent respectively in 2017 than in the previous year.

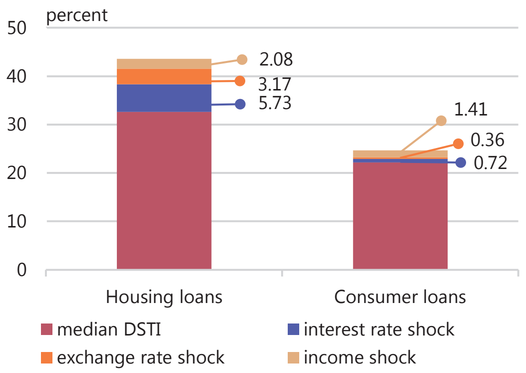
Chart 2.12. Level of indebtedness (DSTI) by loan type and income group




Note: DSTI (debt service-to-income) for new loans takes into account, for housing loans, all debtors with at least one new housing loan regardless of other types of credit they may have, while, for consumer credit, only debtors with this type of loans. Cards and overdrafts are not included in the consumer credit category. DSTI represents the weight of the bank debt service in the monthly net wage of the debtor, without taking into account the co-debtors. Wage earnings refer to December 2016. The median for total loans also covers debtors with income below the minimum wage.

Source: NBR, CB, MPF

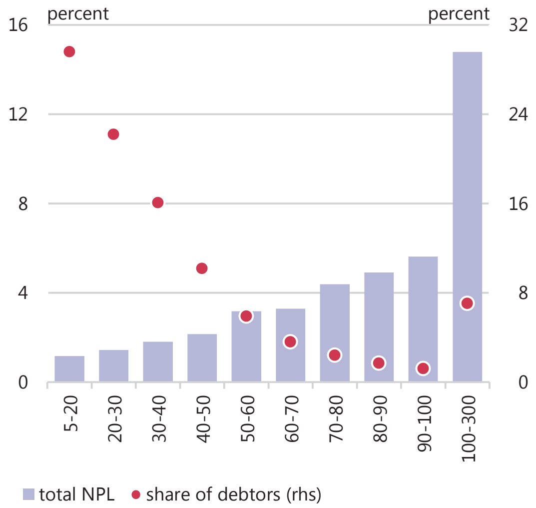
Chart 2.13. DSTI dynamics in the context of economic shocks, March 2018




Note: The values in the chart stand for the differences betweeen DSTIs before and after shocks, expressed in percentage points. The following were considered: interest rate shock of 2 percentage points, income shock of 6 percent and exchange rate shock of 35 percent.

Source: NBR, CB, MPF

Chart 2.14. DSTI ratio and NPL ratio, March 2018




Source: NBR

Individuals' level of indebtedness measured by debt service-to-income ratio (DSTI) was of approximately 28 percent for outstanding loans in March 2018, while it stood marginally higher, i.e. at 31 percent, for debtors who took new loans in the past 12 months. The breakdown paints a similar picture. The DSTI ratios for debtors with new housing loans and consumer loans rose by 7 percentage points and 2 percentage points respectively as compared with that for outstanding loans. An important vulnerability remains the indebtedness asymmetry by income, as the DSTI ratio for debtors earning minimum to average wage economy-wide is significantly higher than that for high-income earners. The gap is more pronounced for borrowers with housing loans, the individuals earning income below the economy-wide average recording a DSTI ratio of 57 percent as compared with 26 percent for debtors earning double the average wage economy-wide (Chart 2.12). A potential shock on income could push indebtedness well above the sustainable level in the case of more vulnerable debtors.

The level of indebtedness is strongly sensitive to interest rate shocks, as it would witness the highest increase (compared with the materialisation of exchange rate or income shocks). In the case of a 2 percentage point interest rate hike, the DSTI ratio for debtors with housing loans and consumer credit would see rises of about 6 percentage points and 1 percentage point respectively. A 6 percent drop in debtors' wage could push the DSTI ratio higher by approximately 2 percentage points and 1.5 percentage points respectively for debtors with housing loans and consumer credit. At the same time, a substantial domestic currency depreciation[50] would have a moderate effect on debtors with housing loans (about 3 percentage point rise in the DSTI ratio), on the back of the contraction in the stock of foreign currency-denominated loans (Chart 2.13).

The running of models estimating households' probability of default shows that borrowers' level of indebtedness is one of the main explanatory factors. Where the DSTI ratio increases by 10 percentage points, the probability of default goes up by 6 percent for housing loans

[50] A 35 percent depreciation of the leu against the euro was taken into consideration.

and by 3 percent for consumer credit. Moreover, on account of historical developments, a high DSTI ratio tends to be associated with larger volumes of non-performing loans. The NPL ratio for the loan portfolio featuring DSTI ratios of over 60 percent is 10 percent, standing two times higher than the ratio for the entire portfolio of household exposures (Chart 2.14).

Therefore, the economic or financial shocks that can affect the level of indebtedness would have a direct impact on debtors' non-performing loans. In particular, the effect of an interest rate hike by about 2 percentage points on the DSTI ratio would translate into increases in the probability of default on a one-year horizon by around 6 percent for housing loans and approximately 0.7 percent for consumer credit. The cumulative impact on the DSTI ratio of shocks on the interest rate (2 percentage points), income (-6 percent) and exchange rate (35 percent) would enhance the probability of default by 20 percent for debtors with housing loans and 2 percent for debtors with consumer credit.

**Requirements for the down-payment on loans (LTV)**

Another major instrument used to contain excessive household indebtedness aims to limit credit value to a share of the associated collateral, the down-payment representing the difference between the collateral value and the loan value. The LTV cap is a macroprudential instrument that can also contribute to trimming down excessive credit growth. Setting an LTV cap is aimed at enhancing the capacity of both debtors and creditors to cope with possible adverse economic developments (particularly those related to the real estate market). An LTV cap has both a direct and indirect impact on debtors, i.e. by reducing their potential indebtedness and by lowering the probability of default. For creditors, a lower LTV entails a lower LGD (loss-given-default). The LTV cap can mitigate excessive credit growth, thus reducing the magnitude of the financial cycle[51].

Romania has an over decade-long experience in using this macroprudential instrument. The NBR implemented the first regulation on the maximum threshold of the loan-to-value ratio in 2003, the LTV ratio being set at 75 percent for both consumer credit and housing loans. The measure was removed at the beginning of 2007 (following Romania's joining the EU), together with other measures relative to lending to households. Neagu *et al.* (2015)[52] show that banks behaved in a pro-cyclical manner at the time, as they granted loans with high LTV ratios, which supported the unsustainable growth of loans and fuelled pressures on the real estate market.

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51 The literature assesses the capacity of this instrument in terms of its impact on real estate prices, yet the results are mixed. No significant connection was evidenced in Romania's case (Neagu, F., Tatarici, L., Mihai, I. – "Implementing Loan-to-Value and Debt Service-to-Income Measures: A Decade of Romanian Experience", *NBR Occasional Papers* No. 15/2015).

52 Neagu, F., Tatarici, L., Mihai, I. – "Implementing Loan-to-Value and Debt Service-to-Income Measures: A Decade of Romanian Experience", *NBR Occasional Papers* No. 15/2015.

Chart 2.15. Distribution of housing exposures* and the NPL ratio by LTV range** (March 2018)

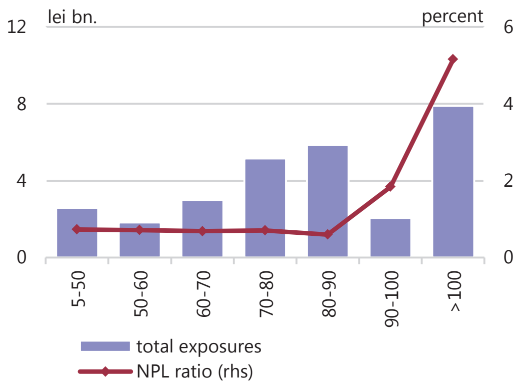
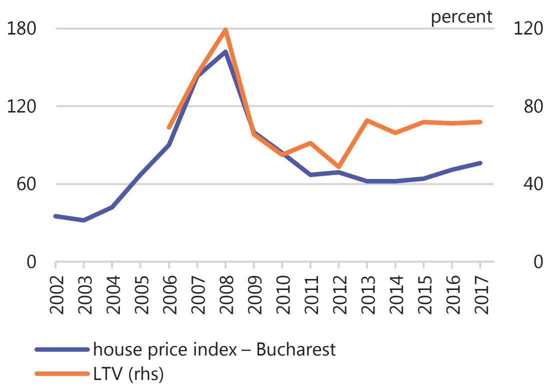



Chart 2.16. Developments in property prices[55] and median LTV** by loan origination year




*except for "First Home" loans

** In order to calculate LTV, only housing loans secured by a residential building as the primary type of collateral were taken into account.

Source: NBR

Source: NIS, UNNPR, EPS, NBR calculations

In 2011, the NBR proposed a distinct approach[53], in the context of the recommendation of the European Systemic Risk Board on lending in foreign currencies[54] and the systemic risks identified in the banking sector. Caps on LTV were set based on the type of debtor (hedged or unhedged borrowers) and the loan currency: (i) 85 percent for leu-denominated housing loans, (ii) 80 percent for foreign currency-denominated housing loans granted to hedged borrowers, (iii) 75 percent for EUR-denominated housing loans granted to unhedged borrowers and (iv) 60 percent for other foreign currency-denominated loans granted to unhedged borrowers.

Empirical evidence has pointed to a direct relation between the level of collateralisation and borrowers' debt servicing capacity. This evidence calls for maintaining prudential levels of these indicators in lending. Thus, the NPL ratio for standard housing loans with above-one LTV ratio stands at 5 percent, whereas the average NPL ratio for housing loans with LTV ratio in the maximum range established between 60 percent and 85 percent is 0.7 percent (Chart 2.15).

Additionally, in the period from 2004 to 2007, house prices saw a substantial rise, exceeding the reference values. Debtors who took loans during an upturn report an above-one median LTV ratio, amid the correction of house prices after 2008 (Chart 2.16). Moreover, these loans currently record the highest NPL ratio, i.e. 11 percent as compared with an aggregate level of 3.2 percent (March 2018), and account for approximately 45 percent of the total NPL volume. Thus, setting a maximum threshold of the LTV would contribute to enhancing debtors' capacity to absorb future shocks on the real estate market.

[53] ESRB Recommendation of 21 September 2011 on lending in foreign currencies.

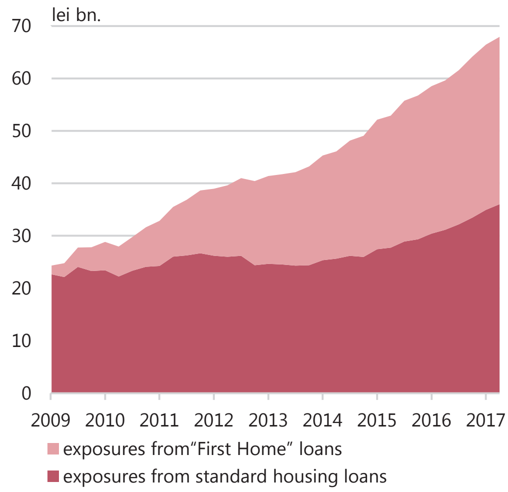
[54] NBR Regulation No. 17/2012 on certain lending conditions.

[55] The price index for a standard property in Bucharest was constructed for the period prior to the start of the NIS index (2009) based on data reported by the UNNPR (the National Union of Notaries Public in Romania) for a standard flat in Bucharest (three rooms, built after 1976, middle floor) and adjusted based on expert assessments. NIS data on flats in Bucharest are used from 2009 onwards, in order to ensure a comfortable level of continuity in the time series.

The LTV cap imposed by NBR Regulation No. 17/2012 was applied to new housing loans, except "First Home" loans, in which case the LTV ratio can be of 95 percent at most.

At present, the volume of "First Home" loans gained systemic importance (Chart 2.17), as regards both the loan stock (lei 31.9 billion, accounting for 26 percent of total loans to households, March 2018) and the flow of housing loans (amounting to 64 percent and 58 percent of loans extended in 2016 and 2017 respectively).

Chart 2.17. Exposures from standard housing loans and "First Home" loans




Source: NBR

Given the significant hike in real estate prices and the robust growth of loans to households (for further details on lending, see Section 3.1.2.1), "First Home" loans with an LTV ratio of up to 95 percent, considering the systemic nature of this portfolio, may give rise to vulnerabilities in the event of future adjustments. Furthermore, the programme has become pro-cyclical over the past years, fostering lending on a market segment that currently posts significant dynamics. The systemic nature of the programme may create problems for financial stability, mainly through: (i) the overstimulation of housing demand, as there are already signs of concern regarding the recent movements in house prices; (ii) the rise in the government exposure to the banking sector as opposed to the EU trends in prudential regulation (the collateral value currently stands at approximately lei 21.5 billion); (iii) the overindebtedness of borrowers, as the indebtedness level of individuals who took "First Home" loans is high even in the context of low interest rates and higher income, and these loans are highly sensitive to interest rate changes.

In this context, it is necessary to target the "First Home" programme better from a social perspective by reviewing the terms and conditions for lending while also preserving a sustainable level of indebtedness.

### 2.1.2.2. Other macroprudential instruments

The instruments described below are generally implemented by the NBR following the NCMO's recommendation and they target the banking sector.

**Reciprocity for macroprudential measures**

In order to enhance the efficiency of macroprudential policy and to limit opportunities for regulatory arbitrage, the NCMO may recognise the macroprudential measures adopted by other Member States. Macroprudential measures generally apply only to resident banks and the subsidiaries of foreign banks. Reciprocity ensures the same prudential treatment for similar risk exposures in a Member State by extending the applicability of macroprudential measures also to direct exposures or through the branches of foreign banks in the given Member State. According to the reciprocity principle laid down in the EU regulatory framework, the NCMO may recognise the measures adopted by other Member States with respect to the systemic risk buffer (SRB), as well as those adopted under Art. 458 of CRR.

The ESRB promotes voluntary reciprocity for macroprudential measures via Recommendation ESRB/2015/2 on the assessment of cross-border effects of and voluntary reciprocity for macroprudential policy measures. Pursuant to this Recommendation, the national authorities tasked with the activation of macroprudential policy measures assess the cross-border effects of the application of these measures and may submit to the ESRB a request for reciprocation by the other Member States of the macroprudential policy measures implemented in Romania which are not voluntarily recognised by the macroprudential authorities in the Member States whose banks have exposures located in Romania. As a follow-up to such a request, the ESRB may issue a recommendation for the reciprocation of the said measures by the other Member States or, where this is not possible, the adoption of equivalent measures. Member States may exempt certain individual institutions from applying the reciprocity principle if the latter have non-material exposures to the Member State requesting reciprocation (*de minimis* principle).

In 2017, the ESRB amended its reciprocity framework by introducing provisions on the application of the *de minimis* principle. Specifically, each Member State requesting reciprocation for a macroprudential measure should also set an institution-level materiality threshold for exposures, based on which the other Member States may exempt the institutions from applying the said measure. The ESRB considers appropriate a materiality threshold of 1 percent of the institution's total risk exposure as an initial orientation value. If the material exposure stems from several banks with small exposures or in order to safeguard financial stability, Member States may choose thresholds below 1 percent. The proposed threshold is validated by the ESRB and should be considered a maximum threshold. The other Member States will be able to set a lower threshold or no threshold at all if they acknowledge reciprocity as a matter of principle.

By 31 March 2018, the ESRB had issued three recommendations on the reciprocity of measures adopted by Member States:

(i) Recommendation ESRB/2016/3 ➡ whereby the Member States' relevant authorities are recommended to reciprocate the macroprudential measure adopted by the National Bank of Belgium, i.e. the 5-percentage-point risk-weight add-on applied under Art. 458(2)(d)(vi) of Regulation (EU) No. 575/2013 (CRR) to Belgian mortgage loan exposures of credit institutions using the internal ratings-based approach (IRB).

(ii) Recommendation ESRB/2016/4 ➡ whereby the Member States' relevant authorities are recommended to reciprocate the 1-percent systemic risk buffer rate established by the Bank of Estonia.

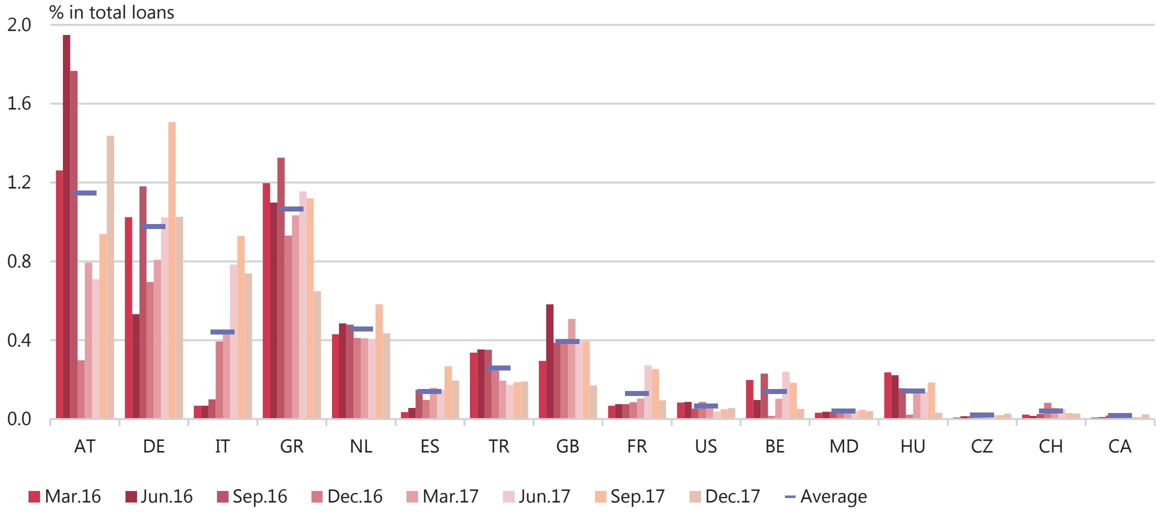
(iii) Recommendation ESRB/2018/1 ➡ whereby the Member States' relevant authorities are recommended to reciprocate the macroprudential measure adopted by Finland, i.e. the 15-percent floor for the average risk-weight (RW) on residential mortgage loans secured by a mortgage on housing units in Finland applicable to credit institutions using the internal ratings-based (IRB) approach for credit risk. The materiality threshold proposed by the Finnish authorities stands at EUR 1 billion exposure to the residential mortgage lending market in Finland.

On 14 June 2017, the NCMO discussed the voluntary reciprocity for the macroprudential measures adopted by Belgium and Estonia and decided: (i) not to reciprocate the macroprudential measure adopted by Belgium, in light of the fact that credit institutions in Romania have non-material eligible exposures to this jurisdiction and (ii) to maintain the prior decision of the National Committee for Financial Stability (NCFS) not to reciprocate the macroprudential measure taken by Estonia, as the exposures of credit institutions to this jurisdiction continue to be very low.

As far as the macroprudential measure adopted by Finland is concerned, the NCMO shall decide on its reciprocation in the period ahead. According to preliminary assessments, the loans granted in Finland by the credit institutions based in Romania are at an insignificant level. At the same time, no credit institutions based in Romania have branches located in Finland.

The NCMO recommended the NBR to monitor, on a regular basis, the cross-border exposures of credit institutions, before the NCMO adopts the necessary measures should these exposures become material. At the level of the Romanian banking sector, external loans amounted to lei 15 billion, accounting for approximately 5.3 percent of total loans as at 31 December 2017 (Chart 2.18). The most important external exposures are in Austria (lei 4.1 billion), Germany (lei 2.9 billion) and Italy (lei 2.1 billion).

Chart 2.18. External loans granted by the Romanian banking sector




Source: NBR

Every two years, the NCMO shall inform the ESRB of the manner of implementation of Recommendation ESRB/2015/2 on the assessment of cross-border effects of and voluntary reciprocity for macroprudential policy measures. The first *Report* was submitted in June 2017.

**Identification of material third countries for the Romanian banking sector in terms of recognising and setting countercyclical buffer rates**

Apart from the use of the countercyclical capital buffer set by each Member State as a macroprudential instrument likely to protect banking sectors against risks arising from excessive credit growth at national level, based on domestic exposures, the European regulatory framework includes provisions on the cyclical dimension of the systemic risk and for cross-border exposures, namely the exposures localised in other Member States or in third countries (outside the EU). The purpose of these provisions is to ensure the uniform treatment of the country-specific countercyclical capital buffer for the calculation of total own funds requirements.

According to Art. 139 of Directive 2013/36/EU (CRD IV), designated authorities may, in certain circumstances, set a countercyclical buffer rate for exposures to a third country that domestically authorised institutions have to apply for the calculation of their institution-specific countercyclical capital buffer. The designated authority can act in situations where a countercyclical buffer rate has not been set and published by the relevant third-country authority for that third country, or if it considers that the countercyclical buffer rate set by the relevant third-country authority for that third country is not sufficient to protect the Member States' domestic banking sectors from potential losses associated with excessive credit growth in the third country in question. Moreover, pursuant to Art. 138 of the aforementioned Directive, the European Systemic Risk Board may recommend the implementation of a certain countercyclical buffer rate for exposures to third countries. Thus, at EU level, the identification and monitoring of material third countries[56] are built on three pillars: the ESRB focuses on the third countries to which the European banking sector as a whole has material exposures, whereas Member States and the ECB concentrate on the third countries to which the national banking sector and credit institutions participating in the Single Supervisory Mechanism have material exposures.

In order to standardise the decisions of Member States at EU level, the ESRB published, in December 2015, Recommendation ESRB/2015/1 on recognising and setting countercyclical buffer rates for exposures to third countries. This Recommendation stipulates that national designated authorities identify, on an annual basis, the third countries to which the banking sectors have material exposures and monitor the risks arising from excessive credit growth to these countries.

In addition, in December 2015 as well, the ESRB published Decision ESRB/2015/3 on the assessment of materiality of third countries for the Union's banking system in relation to the recognition and setting of countercyclical buffer rates, which lays down the methodology

[56] In view of the large number of third countries, the focus is on material third countries, to which exposures exceed certain thresholds.

used by the Board to identify material third countries. Even though Member States may establish their own approach, most of them have adopted the ESRB methodology, to which some have made certain amendments or added supplements.

At a national level, the procedures for the identification of material third countries, the recognition and setting of countercyclical buffer rates and the communication of relevant decisions were established in compliance with Recommendation ESRB/2015/1 and the methodology on the assessment of materiality of third countries for the Romanian banking system in relation to the recognition and setting of countercyclical buffer rates is harmonised with that of the ESRB. For further details on the matter, see the May 2017 Financial Stability Report released by the NBR. Furthermore, with a view to ensuring the robustness of results, the ESRB methodology is supplemented with the analysis of other available information on external exposures. The indicators employed are listed in Table 2.5. This is not a comprehensive list, as other indicators relevant to the purposes of the analysis may also be included.

**Table 2.5.** Indicators used to identify material third countries for the Romanian banking sector

| ESRB indicators | National indicators |
|---|---|
| Risk-weighted assets (COREP reports) | loans granted in third countries (monetary balance sheet reports) |
| Original exposure (COREP reports) | ratio of original exposures, other than domestic ones, to total original exposures, prior to applying risk weights (COREP reports) |
| Defaulted exposures (COREP reports) | own funds requirements for exposures relevant to the calculation of the institution-specific countercyclical capital buffer (breakdown by country) |

In its meeting of June 2017, the NCMO assessed the materiality of third countries for the Romanian banking sector in terms of setting countercyclical buffer rates, concluding that the exposures of the Romanian banking sector to third countries continued to be low and identifying no material third countries.

The analysis conducted as part of annual monitoring exercises showed that the exposures of the Romanian banking sector are mainly related to the domestic economy, whereas non-domestic exposures are of marginal importance. Thus, according to data as of 31 December 2016, domestic loans extended by credit institutions held the prevailing share in the latter's loan portfolio (94 percent), loans granted to borrowers in other Member States accounted for 5.4 percent and those extended in third countries made up 0.61 percent of the total loans granted by credit institutions based in Romania. The subsequent developments in lending did not indicate any notable changes in the exposures of the Romanian banking sector to third countries (Chart 2.18).

Against this background, the NCMO recommended the NBR to assess, on a regular basis, material third countries for the banking sector in Romania in terms of recognising and setting countercyclical buffer rates, before proposing the necessary measures should these exposures become material[57]. As a follow-up to the Recommendation, in line with the EU requirements, the NCMO submitted to the ESRB the reporting template concerning the list of material third countries.

### Assessment of the impact of credit institutions' funding plans on the flow of credit to the real economy

Sub-recommendation A3 of Recommendation of the European Systemic Risk Board of 20 December 2012 on funding of credit institutions (ESRB/2012/2) recommends national supervisory authorities and other authorities with a macroprudential mandate "to assess the impact of credit institutions' funding plans on the flow of credit to the real economy".

Recommendation ESRB/2012/2 aims to ensure adequate funding risk management by banks and sustainability of funding plans. This Recommendation focuses on the following: (1) funding and funding risks (Recommendation A), (2) asset encumbrance (Recommendations B, C, D) and (3) covered bonds (Recommendation E). According to Recommendation A – Monitoring and assessment of funding risks and funding risk management by supervisors, national supervisory authorities with responsibility for banking supervision are recommended to intensify their assessments of the funding and liquidity risks incurred by credit institutions, as well as their funding risk management, within the broader balance sheet structure.

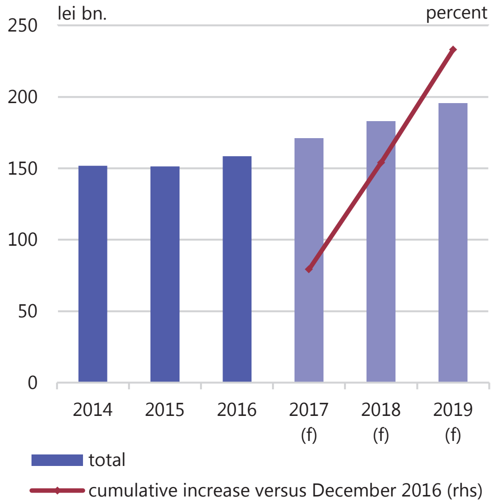
In order to facilitate the reporting of credit institutions' funding plans, in compliance with the recommendations included in Recommendation A (also subparagraph 3), and to establish consistent, efficient, and effective supervisory practices by harmonising templates and definitions for funding plans, the European Banking Authority prepared EBA Guidelines on harmonised definitions and templates for funding plans of credit institutions under Recommendation A4 of ESRB/2012/2, which was incorporated by the National Bank of Romania in the domestic regulatory framework.

In its meeting of 18 December 2017, the NCMO took note of the assessment conducted by the National Bank of Romania based on the funding plans of credit institutions and issued a recommendation to the latter to assess, on a regular basis, the impact of credit institutions' funding plans on the flow of credit to the real economy[58].

57 NCMO Recommendation No. 2 of 14 June 2017 on material third countries for the Romanian banking sector in terms of recognising and setting countercyclical buffer rates.

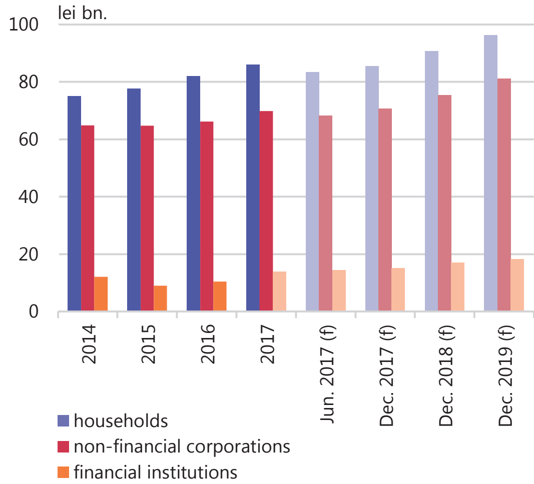
58 NCMO Recommendation No. 10 of 18 Dec 2017 on the impact of credit institutions' funding plans on the flow of credit to the real economy.

Chart 2.19. Lending forecast




Source: NBR, reports of credit institutions on funding plans

Chart 2.20. Breakdown of credit developments by component




Source: NBR, reports of credit institutions on funding plans

According to the funding plans submitted by credit institutions[59], having a reference date of 31 December 2016, banking will make a positive contribution to lending to the real economy December 2016 through December 2019 across all types of loans under analysis (the cumulative expected increase in loans to non-financial customers over the next three years stands at 19.7 percent, Chart 2.19). The rise will characterise loans to both households and non-financial corporations (Chart 2.20).

Banks aim to cover the rise in loans to the private sector amounting to approximately lei 37 billion first by using: (i) available funds as a result of a reduction in cash and balances with central banks, ahead of an increase in (ii) household deposits; (iii) the deposits of non-financial corporations and (iv) equity.

Based on the funding plans of the eight selected credit institutions and extrapolating their forecasts to the whole banking system, the NCMO may broadly substantiate the appropriateness of using macroprudential instruments in the period ahead.

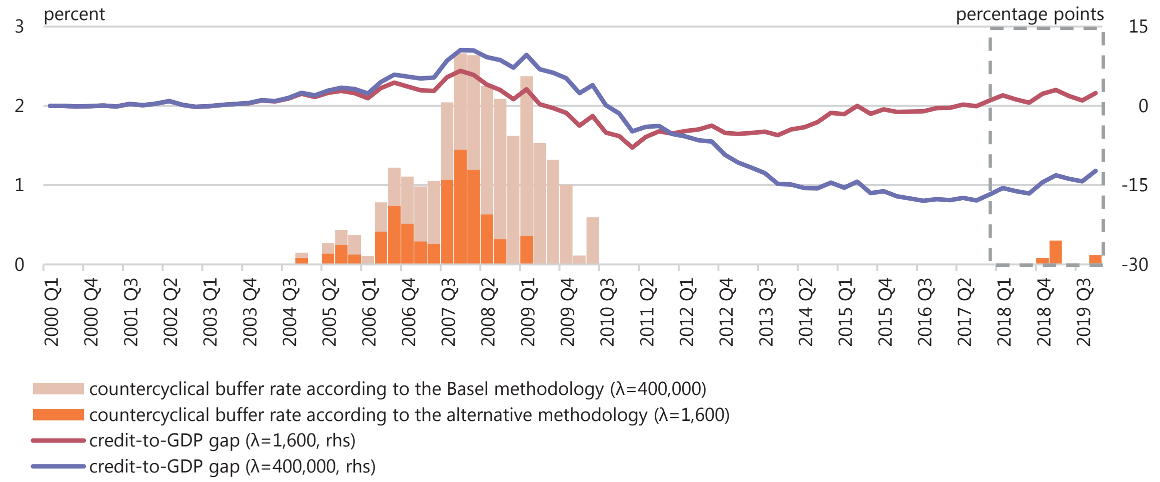
As far as the intermediate objectives of macroprudential policy are concerned, the reports on funding plans may prove useful chiefly to achieve the following objectives: (i) to mitigate and prevent excessive credit growth and leverage (countercyclical capital buffer); (ii) to mitigate and prevent excessive maturity mismatch and market illiquidity (LCR, NSFR, LTD) and (iii) to strengthen the resilience of financial infrastructures (systemic risk buffer).

The key findings of the analysis concerning macroprudential policy show that:

- the dynamics of credit to the real economy further run lower than the values projected for GDP growth, but the differential is expected to narrow over the coming years;

[59] The obligation to submit, on a regular basis, reports on funding plans was imposed on the eight largest banks in the Romanian banking system.

Chart 2.21. Implementation of the countercyclical capital buffer, according to the funding plans of credit institutions over the following years




Source: NBR, NIS, NCSP, NBR calculations

- financial intermediation, measured as a ratio of total indebtedness of the private sector to GDP, is expected to decrease slightly over the next years, to approximately 39 percent;
- with regard to the currency of denomination of loans, according to the reports on funding plans, banks prefer to extend domestic currency loans to the detriment of foreign currency ones;
- forecast data indicate the possibility of introducing a 0.25 percent countercyclical capital buffer as of 2019 (Chart 2.21);
- forecast dynamics of the liability structure point to an improved funding and liquidity profile of credit institutions by their shifting to more stable funding sources, with a longer maturity.

## 2.2. Other initiatives adopted to preserve financial stability

In order to maintain financial stability, the sectoral competent authorities monitor a broad range of potentially systemic vulnerabilities that may adversely affect the financial system and the real economy. Therefore, measures that do not refer directly to the macroprudential policy framework at the European level may be implemented, given their necessity to manage the specific risks identified. A case in point is the amendment to the regulatory framework applicable to non-bank financial institutions (NBFIs) implemented by the National Bank of Romania.

The need for strengthening the regulatory and supervisory framework applicable to NBFIs has arisen following the late developments in this sector. Specifically, NBFI lending gained momentum and there is notable growth potential, especially for household lending. Moreover, there was a rise in short-term, relatively low-value loans with high costs, mainly contracted by household segments that already had difficulties in managing their current payment obligations. Given that heightened uncertainty surrounds future macroeconomic developments and the monetary policy stance might change, highly indebted borrowers may face serious difficulties in servicing their debt.

Against this background, the NBR has revised the regulatory framework applicable to NBFIs via NBR Regulation No. 1/2017 amending and supplementing NBR Regulation No. 20/2009 on non-bank financial institutions, in order to better capture the specifics of this business model, to reduce regulatory arbitrage and to address the issue of potential systemic effects that may stem from the NBFI sector. The changes aim at introducing two new criteria for NBFIs to fall under NBR prudential supervision (enlisting in the Special Register) depending on: (i) the volume of new loans (exceeding lei 75 million over the past three quarters), so as to capture lending by creditors focused on short- and very short-term loans, and (ii) the average interest rates applied, which reveal the potential for a build-up of excessive risks at NBFI level. As far as the second criterion is concerned, an NBFI falls under NBR supervision if it exceeds the levels in Table 2.6.

**Table 2.6.** Criteria on APRC level for falling under NBR supervision

| Maturity | APRC level for leu-denominated loans | APRC level for foreign currency-denominated loans |
|---|---|---|
| up to 15 days | >200% | >133% |
| 16-90 days | >100% | >67% |
| more than 90 days | >10 x NBR's Lombard rate | >6.7 x NBR's Lombard rate |

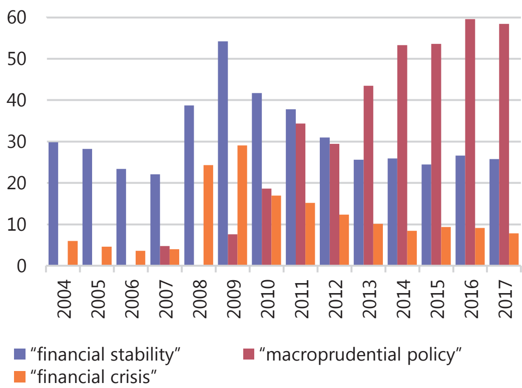
Source: NBR

In addition, for NBFIs granting less prudent loans at APRC levels above those specified in Table 2.7, requirements for building up additional capital were introduced at two thirds of the loan amount. The new requirements are only applicable to loans granted as of 1 October 2017.

# 3. Communication in the macroprudential field

In accordance with its mandate and with the principles of transparency and institutional accountability, the NCMO started its communication activity as early as its first meeting by publishing a press release which announced that the National Committee for Macroprudential Oversight had been set up and become operational.

Chart 3.1. Number of internet searches for terms related to the field of "financial stability"




Note: The indicators for each term are relative as compared with the top level in the period under analysis (comparisons of interest in different key words cannot be made).

Source: Google Trends

The general public's interest in the notions of financial stability and macroprudential policy has increased markedly after the global financial crisis (Chart 3.1), as proven by the number of internet searches for these keywords. Consequently, throughout 2017, the communication activity of the NCMO was aimed at correctly and promptly informing the general public, experts, other institutions and the media of the measures and policies adopted in pursuit of its tasks, as set out in Law No. 12/2017[60].

To this end and approaching the transparency-enhancing process in line with the legal provisions[61], the public interest and European practice, the NCMO published on its website, after each meeting, press releases on the macroprudential policy decisions and the reasons for making them, as well as other information in the macroprudential field relevant to the public and related to the topics on the agenda of its meetings. Press releases were discussed and agreed on by the members of the General Board of the NCMO at its meetings. The creation of a contact group consisting of experts from the authorities included in the NCMO, i.e. the NBR, the FSA, and the MPF, fostered the necessary informal cooperation, contributing to the consistency of the communication processes. The NCMO Secretariat ensures that the external communication is in line with the decisions taken. The websites of the NBR, FSA and Romanian government/MPF provide links to the NCMO's website and press releases. Should no consensus be found with respect to accountability, each of the three aforementioned authorities may resort to explaining the reasons behind the differences in opinions or inaction.

60 Art. 3 of Law No. 12/2017.

61 Art. 10 of Law No. 12/2017.

According to the law, the NCMO may publish the issued recommendations and warnings unless it considers there are risks to financial stability in doing so. So far, the NCMO General Board has approved the publication of the issued recommendations on its website. These recommendations referred to capital buffers – the countercyclical capital buffer, the capital buffer for systemically important institutions and the systemic risk buffer, the macroprudential measures adopted by other Member States that should be applied in compliance with the reciprocity principle[62] or those applicable to exposures in third countries (non-EU countries). Moreover, the NCMO issued recommendations related to: (i) household overindebtedness, (ii) firms' financial soundness and (iii) enhancing statistical information required for the analyses on the real estate market.

The NCMO published the said recommendations to draw the attention of the public and particularly of financial institutions to potential vulnerabilities in the financial system so that the latter should be warned about the potential systemic risks that were identified. A better understanding of risks and macroprudential policy objectives by financial institutions contributes to their higher risk awareness and thus encourages them to act accordingly.

At the same time, the NCMO's macroprudential policy decisions are communicated by the NCMO Secretariat, which is owned by the NBR, according to the law, to both credit institutions and the competent authorities (the European Commission, the European Systemic Risk Board, the European Banking Authority, the supervisory authorities of credit institutions in other Member States) to which they apply and are relevant. As regards capital buffers, which are CRD IV/CRR instruments, notification differs depending on the buffer, the NCMO observing the requirements included in EU directives and regulations, as well as in the guidelines issued for their application.

In 2017, a top priority of the NCMO's communication activity was to create and develop the NCMO's website, aiming at fostering a high level of understanding among the general public of: (i) the notions of financial stability and macroprudential oversight; (ii) the role of the European Systemic Risk Board in the EU's macroprudential policy; (iii) the NCMO's mission, tasks and organisation; (iv) the macroprudential policy decisions, as measures meant to safeguard financial stability, in a challenging domestic and external environment marked by heightened uncertainty. The information on the website is provided in both Romanian and English, thus being accessible to a more significant number of users: financial and banking institutions in the country and abroad, researchers, students, the media, and the general public. Even though the NCMO's website is the main communication tool of the national macroprudential authority, contributing equally to increasing transparency, strengthening the NCMO's prestige and educating the interested audience, the NCMO's *Annual Report* may become, in time, a consistent and coherent communication tool that will help build and strengthen the NCMO's reputation.

The NCMO's *Annual Report* is prepared through the contribution of the three authorities comprised in the NCMO, namely the National Bank of Romania, the Financial Supervisory

[62] Measure applied based on an ESRB Recommendation.

Authority and the Government via the Ministry of Public Finance. The first issue of this *Report* shall be submitted to Parliament in June 2018, pursuant to the legislation in force[63]. The NCMO *Report* presents the macroprudential instruments applied by the competent authorities (the NBR and the FSA) and the measures adopted by the Government with a view to preventing and mitigating the systemic risks identified and communicated by the said authorities through their own *Reports* (the NBR *Financial Stability Report* and the FSA *Report*), as well as their objectives and the potential impact on the financial market. Thus, the NCMO *Report* aims to inform of the macroprudential measures adopted by this committee over a year in order to maintain the stability of the national financial system.

This communication tool ensures the NCMO's accountability to the Parliament as regards the macroprudential policy decisions taken. The structure of this *Report* may vary from one year to another, depending on the actual economic conditions and the macroprudential measures adopted. Thus, the *Annual Report* will have a flexible structure that might constitute an unbiased source of information on macroprudential policy at national level. Irrespective of its structure, the *Report* will contain information delivered in a clear and readily-understandable manner, with a message targeting a wide audience, to become an efficient and effective communication tool.

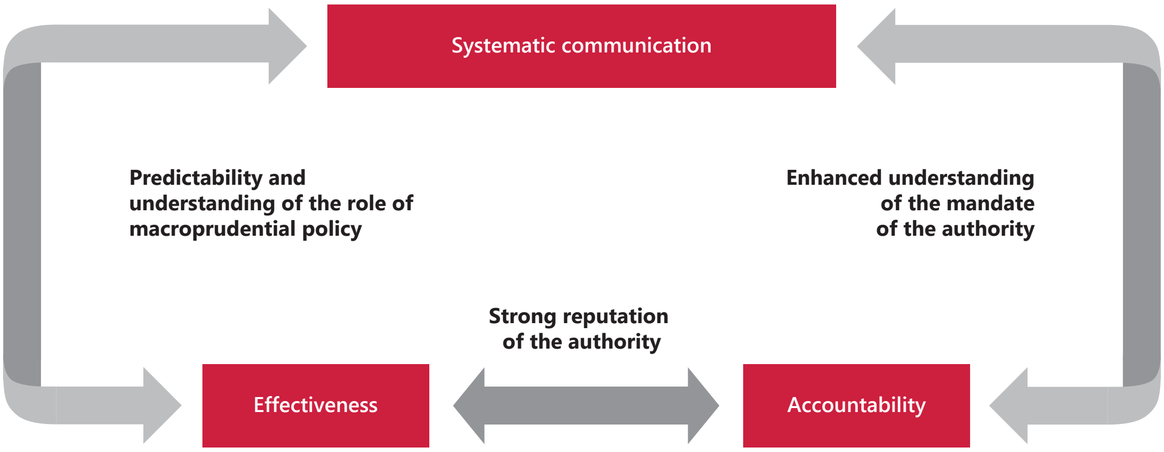
The communication policy is an important part of the macroprudential framework. To this end, a communication strategy, component of the strategy on macroprudential policy and macroprudential instruments, will be developed and prepared in accordance with the macroprudential responsibilities of the NCMO in its capacity as national macroprudential authority, which will subsequently present in detail the sectoral responsibilities of each authority composing it (the NBR, the FSA and the Government). This strategy will set the communication elements of macroprudential policy and the appropriate instruments (tailored to the typology of audiences and communication objectives), the aim being to render communication effective in order to ensure a transparent and predictable environment for the implementation of macroprudential measures. The strategy will be aligned with the general principles and best practices of communication on macroprudential policy recommended by the ESRB[64].

An efficient macroprudential policy calls for both a clearly-defined regulatory and institutional framework and a strategy prepared in line with the macroprudential responsibilities of the NCMO in its capacity as national macroprudential authority which should set the macroprudential policy elements and the appropriate instruments for their implementation, as well as the communication policy (Figure 3.1).

63 Pursuant to the legislation in force (Art. 11 of Law No. 12/2017), the chairperson of the NCMO General Board is to submit the first *NCMO Report* to the Parliament of Romania by 30 June 2018.

64 *The ESRB Handbook on Operationalising Macroprudential Policy in the Banking Sector*, 2014.

Figure 3.1. Role of communication policy in implementing the framework for operationalising macroprudential policy




Source: Adaptation from the BIS

The strategy on macroprudential policy aims to explain to the public the primary objective of macroprudential policy and its intermediate objectives, tools and institutional set-up at a national level. The macroprudential strategy is a comprehensive document that contains: (i) the objective of macroprudential policy, (ii) the institutions involved in macroprudential policy and their powers and instruments, together with the legal background; (iii) macroprudential instruments, (iv) the decision-making process. At the time being, the strategy on macroprudential policy is being drafted, before being discussed and approved at the meetings of the NCMO General Board.

## 3.1. Recommendations, warnings and advisory opinions

According to Law No. 12/2017[65], in order to implement the measures necessary for preventing or mitigating systemic risks at national level, the NCMO is empowered to: (i) issue recommendations and warnings to the National Bank of Romania and the Financial Supervisory Authority, in their capacity as national financial supervisory authorities at a sectoral level, (ii) issue recommendations to the Government for the purpose of safeguarding financial stability, and (iii) request the European Systemic Risk Board (ESRB) to issue a recommendation for the recognition by one or more Member States of the macroprudential instruments recommended by the NCMO.

The issuance of recommendations and warnings ("soft law") to the NBR or the FSA, in their capacity as national financial supervisory authorities at a sectoral level, relies on a "comply or explain" mechanism. The recipients of the NCMO's recommendations or warnings may adopt the appropriate measures, including the issuance of regulations, in order to observe the recommendations or, where appropriate, may take action to mitigate

65 Art. 4 of Law No. 12/2017.

the risks they were warned about. The recipients inform the NCMO of the measures adopted or, in cases where they have not taken such measures, they provide adequate justification for any inaction.

Since its establishment, the NCMO has issued 10 recommendations to the NBR, the FSA and/or the Government (the MPF), as applicable. These were mostly macroprudential measures in the form of additional capital requirements, whose objective was to strengthen institutions' resilience to endogenous and exogenous shocks, thus helping to mitigate cyclical or structural risks. Capital buffers[66] to which the NCMO's recommendations referred were: the countercyclical capital buffer, the buffer for systemically important institutions and the systemic risk buffer. The additional requirements consisting of capital buffers add to the minimum own funds requirements and apply solely to credit institutions, Romanian legal entities. Table A.4 in the Annexes shows a list of all the recommendations that have been issued so far.

The NCMO did not issue any warnings or advisory opinions in 2017.

## 3.2. Communication with other international and European macroprudential authorities

In compliance with the legal provisions[67] applicable at a national level, the NCMO ensures the cooperation and the exchange of information with the European Commission, the European Banking Authority, and the European Systemic Risk Board, as well as with its peers in other Member States. In addition, the NCMO is responsible for informing the European Systemic Risk Board of the actions taken for preventing and mitigating systemic risks at a national level, by observing, where appropriate, the deadlines set forth in ESRB recommendations or any other relevant acts issued at EU level.

The CRD IV/CRR regulatory framework specifies that all macroprudential measures adopted by Member States should be notified to the European Systemic Risk Board and other interested European institutions. Such measures may refer to: (a) the implementation, in advance, of the capital conservation buffer and the countercyclical capital buffer[68]; (b) the implementation of the O-SII buffer[69]; (c) the implementation of the systemic risk buffer[70];

66 In compliance with the CRD IV/CRR regulatory framework at EU level, the capital conservation buffer also ranks among the capital buffers that may be imposed on credit institutions. The manner of implementing the capital conservation buffer in the Romanian banking sector was established by the National Committee for Financial Stability, which was entrusted with macroprudential tasks prior to the setting-up of the NCMO, via NCFS Recommendation No. 1/26.11.2015 on the implementation of capital buffers in Romania.

67 Art. 3 para. (8) and para. (9) of Law No. 12/2017.

68 Art. 160 para. (6) of Directive 2013/36/EU.

69 Art. 131 – Global and other systemically important institutions of Directive 2013/36/EU.

70 Art. 133 of Directive 2013/36/EU.

(d) the assignment of risk weights for exposures secured by mortgages on immovable property[71]; (e) the determination of exposure weighted average LGD values for exposures secured by property located on their territory[72]; (f) the adoption of stricter measures at national level in the event of identifying changes in the intensity of macroprudential or systemic risk in the financial system with the potential to have serious negative consequences for the financial system and the real economy[73] (these measures may concern: (i) higher own funds requirements, (ii) stricter requirements for large exposures, (iii) higher public disclosure requirements, (iv) higher level of the capital conservation buffer, (v) larger liquidity requirements, (vi) greater risk weights for targeting asset bubbles in the residential and commercial property sector, (vii) reduction of intra financial sector exposures). The implementation of some of the aforementioned measures at national level requires prior approval by European institutions (the European Commission, the European Council, the European Banking Authority, the European Systemic Risk Board, etc.), given that an integrated financial system such as the EU Single Market needs strong political coordination in order to ensure the effectiveness of the national macroprudential policy.

Macroprudential authorities justify national measures by the identification of cyclical and structural risks in the domestic financial system. Nevertheless, one issue that should be taken into account is that these measures can have spillovers to other countries (contagion effect) or can sometimes be circumvented by foreign bank branches that are located in the host country[74] or by cross-border lending. In light of its mandate, the ESRB plays an important coordination role in assessing measures, discussing cross-border effects and recommending mitigating measures, including the voluntary reciprocity for macroprudential measures.

There are several channels of propagation through which the measures adopted in a Member State can affect other countries: (i) cross-border risk adjustments, (ii) network formation and potential for contagion, (iii) regulatory arbitrage, (iv) altering monetary transmission, and (v) trade effects[75].

The ESRB has contributed to the creation of a framework for voluntary cross-border reciprocity. Under the EU law currently in force, mandatory recognition is limited to a few cases, an arrangement for voluntary reciprocity for most macroprudential measures being in operation. Where macroprudential measures target risk exposures in a country, they should ideally be reciprocated. To ensure this, the ESRB issued Recommendation ESRB/2015/2 on the assessment of cross-border effects of and voluntary reciprocity for macroprudential

71 Art. 124 – Exposures secured by mortgages on immovable property of Regulation (EU) No. 575/2013.

72 Art. 164 – Loss Given Default (LGD) of Regulation (EU) No. 575/2013.

73 Art. 458 – Macroprudential or systemic risk identified at the level of a Member State of Regulation (EU) No. 575/2013.

74 For instance, the branches of foreign banks are not bound to meet the minimum capital requirements in the host country, as they are solely applicable to the parent bank at a consolidated level.

75 The European Systemic Risk Board (ESRB) – *The ESRB Handbook on Operationalising Macroprudential Policy in the Banking Sector* (https://www.esrb.europa.eu/mppa/framework/html/index.en.html).

policy measures[76] and Decision ESRB/2015/4 on a coordination framework regarding the notification of national macroprudential policy measures by relevant authorities. The aforementioned regulations define the process for the notification of macroprudential measures, the decision on reciprocity, communication and implementation monitoring.

So far, the NCMO Secretariat has notified the European institutions of the measures recommended by the NCMO General Board concerning the implementation of the buffer for systemically important institutions (O-SII buffer), the systemic risk buffer and the macroprudential measures adopted for non-bank financial institutions, as well as of the regular assessments of the countercyclical capital buffer, in compliance with the regulatory framework at national and EU levels. In view of the need for EU coordination of the macroprudential measures adopted by Member States, the national legislation specifies that, in cases where the issuance of recommendations is conditional on the prior notification or approval by European agencies and institutions, the NCMO shall communicate its recommendations to the interested parties after receiving an answer from the European agencies and institutions or from the expiry of the response deadline[77].

During 2017, the NBR and the FSA monitored both the macroprudential policy measures published by the European and international macroprudential authorities and those adopted by the national authorities in the relevant jurisdictions for the local non-bank financial market. At the same time, the NBR and the FSA contributed directly, via the experts appointed to the working groups set up within the ESRB, the FSB, the ESMA, the EIOPA and the European Commission, to the identification, assessment and monitoring of systemic risks at European level, having thus access to information of EU and global relevance that is useful for the macroprudential oversight of local markets. Moreover, at the request of the European macroprudential authorities, the two authorities provided information and risk assessments on a regular basis.

[76] Recommendation ESRB/2015/2 on the assessment of cross-border effects of and voluntary reciprocity for macroprudential policy measures is published on the ESRB website.

[77] Art. 10 para. (1) and para. (2) of Law No. 12/2017.

# Annexes

**Table A.1.** List of national macroprudential authorities and national designated authorities in EU Member States

| Country | Macroprudential authority[78] / Designated authority[79] | |
|---|---|---|
| | EU Member States with a single institution | |
| Belgium | Nationale Bank van België/Banque Nationale de Belgique | |
| Czech Republic | Česká národní banka | |
| Estonia | Eesti Pank | |
| Ireland | Central Bank of Ireland | |
| Greece | Τράπεζα της Ελλάδος (Bank of Greece) | |
| France | Haut Conseil de Stabilité Financière (High Council for Financial Stability) | |
| Cyprus | Κεντρική Τράπεζα της Κύπρου (Central Bank of Cyprus) | |
| Lithuania | Lietuvos bankas | |
| Hungary | Magyar Nemzeti Bank | |
| Malta | Central Bank of Malta | |
| Portugal | Banco de Portugal | |
| Romania | The National Committee for Macroprudential Oversight | |
| Slovakia | Národná banka Slovenska | |
| Finland | Finanssivalvonta (Finnish Financial Supervisory Authority) | |
| Sweden | Finansinspektionen (Financial Supervisory Authority) | |
| United Kingdom | Bank of England/Financial Policy Committee | |
| | EU Member States with several institutions | |
| | Macroprudential authority | Designated authority |
| Bulgaria | Financial Stability Advisory Council | Българската народна банка (Bulgarian National Bank) |
| Denmark | Det Systemiske Risikoråd (Systemic Risk Council) | Erhvervsministeren (Minister for Industry, Business and Financial Affairs) |
| Germany | Ausschuss für Finanzstabilität (Financial Stability Committee) | Bundesanstalt für Finanzdienstleistungsaufsicht (Financial Supervisory Authority) |
| Spain | * | Banco de España |
| Croatia | Vijeće za financijsku stabilnost (Financial Stability Council) | Hrvatska narodna banka |
| Italy | ** | EU Member States with several institutions |
| Latvia | Latvijas Banka | Finanšu un kapitāla tirgus komisija (Financial and Capital Market Commission) |
| Luxembourg | Comité du risque systémique (Systemic Risk Committee) | Commission de Surveillance du Secteur Financier (Financial Supervisory Authority) |
| Netherlands | Financieel Stabiliteitscomité (Financial Stability Committee) | De Nederlandsche Bank |
| Austria | Finanzmarktstabilitätsgremium (Financial Market Stability Board) | Finanzmarktaufsichtsbehörde (Austrian Financial Market Authority) |
| Poland | Komitet Stabilności Finansowej (Financial Stability Committee) | Minister Finansów (Minister of Finance) |
| Slovenia | Odbor za finančno stabilnost (Financial Stability Board) | Banka Slovenije |

* In Spain, the macroprudential authority has not yet been officially established; ** In Italy, in 2016 the Government was given powers by the Parliament to establish the Macroprudential Policy Committee.

Source: ESRB

[78] Macroprudential authority established in accordance with Recommendation ESRB/2011/3.

[79] Designated authority established in accordance with Art. 136 of Directive 2013/36/EU (CRD IV).

**Table A.2.** Optional criteria/indicators used in the second O-SII assessment stage and the minimum threshold at which institutions are designated as systemic

| Criterion | Indicators for assessing the criterion | Threshold at which institutions are designated as O-SIIs (percent) |
|---|---|---|
| Contribution made by the credit institution to financing real economy, calculated based on the volume of loans granted to non-financial corporations and the substitutability of non-financial corporations' lending activity | The average weight of loans granted to non-financial corporations by the credit institution in total credit granted to non-financial corporations by the banking sector related to: (i) the market share of the credit institution in the financing of non-financial corporations, overall and by main sector group*; (ii) the role in the economy of loan-taking companies as illustrated by: types of loans granted (simple arithmetic average of cash flow loans and equipment loans), the gross value added, the number of employees, net exports, net imports. | 2.75 |
| Contribution made by the credit institution to financial intermediation, calculated based on the volume of deposits taken from households and non-financial corporations | The arithmetic mean of the weights of deposits by non-financial corporations and households with the credit institution in total deposits by non-financial corporations and households in the banking sector. | 2.75 |
| Presence of the credit institution on the interbank market and the assessment of the contagion effect | Asset market shares of credit institutions whose total capital ratio would fall below 8 percent, upon simulating the pass-through of the shock, by considering the direct exposures via the interbank market. | 2.75 |
| Designating systemically important institutions in the ReGIS payment system | Volume and share of transactions carried out by each credit institution in the ReGIS payment system in total transactions. | 2.75 |
| Vulnerability to contagion in the parent bank-subsidiary relationship from the common lender standpoint (the origin country of the capital) | The assessment is conducted based on the following three indicators: (i) the bank's importance in sending a shock to the bank group by the origin country of the capital; (ii) the vulnerability of the other banks that are part of the same group to the shock sent by the failing bank (shock-transmitter); (iii) the importance of the common lender (the origin country of the capital) the failing bank is part of. | 2.75 |

* The classification by the mentioned economic sectors is based on NACE (National Classification of Economic Activities) Rev. 2: a. Agriculture, forestry and fishing (NACE code A); b. Mining and quarrying and manufacturing (NACE codes B and C); c. Electricity, gas, steam and air conditioning supply; Water supply; sewerage, waste management and remediation activities; Transportation and storage; Accommodation and food service activities; Information and communication; Professional, scientific and technical activities; Administrative and support service activities; Public administration and defence; compulsory social security; Education; Human health and social work activities; Arts, entertainment and recreation; Other service activities; Activities of households as employers; undifferentiated goods- and services-producing activities of households for own use; Activities of extraterritorial organisations and bodies (NACE codes D, E, H, I, J, M, N, O, P, Q, R, S, T and U); d. Real estate activities; Construction (NACE codes L and F); e. Wholesale and retail trade; repair of motor vehicles and motorcycles (NACE code G).

**Table A.3.** Measures adopted by the competent authorities for systemically important parent banks in their home country that have subsidiaries in Romania

In compliance with the data published on the ESRB website, the home country authorities required parent banks that are within their supervisory scope and which have subsidiaries in Romania to meet the following additional capital requirements:

| Home country | Credit institution to which the measure applies (parent bank) | Macroprudential instrument employed / Applicable level / Timeline of the instrument |
| --- | --- | --- |
| Austria | Erste Group Bank (owns BCR)<br><br>Raiffeisen Bank International AG (owns Raiffeisen Bank) | Both institutions should meet the capital requirements listed below:<br>a) the systemic risk buffer (SRB) applicable to all exposures, which is implemented in four equal increments between 1 January 2016 and 1 January 2019, as follows: 0.25% on 1 January 2016; 0.5% on 1 January 2017; 1% on 1 January 2018; 2% on 1 January 2019;<br>b) the O-SII buffer, set at 2%, which is implemented in four equal increments between 1 June 2016 and 1 January 2019, as follows: 0.25% on 1 June 2016; 0.5% on 1 January 2017; 1% on 1 January 2018; 2% on 1 January 2019.<br>In compliance with the provisions of the CRD IV/CRR regulatory framework, where the systemic risk buffer is implemented for all exposures, the institutions should apply the higher buffer between the systemic risk buffer and the O-SII buffer. According to the notification of the Austrian Financial Market Authority, the systemic risk buffer is applicable to the aforementioned banks. |
| Greece | Alpha Bank (owns Alpha Bank Romania)<br><br>Eurobank Ergasias (owns Bancpost) | The two credit institutions should meet the requirement on the O-SII buffer, set at 1% and phased in over seven years (1 January 2016 – 1 January 2022), as follows: 0% on 1 January 2016; 0% on 1 January 2017; 0% on 1 January 2018; 0.25% on 1 January 2019; 0.5% on 1 January 2020; 0.75% on 1 January 2021; 1% on 1 January 2022. |
| Italy | UniCredit SpA (owns UniCredit Bank Romania) | Unicredit Group SpA was identified as a global systemically important institution, being subject to a G-SII buffer of 1%. In addition, Unicredit Group SpA was identified as a domestic systemically important institution, the level of the O-SII buffer being however set at 0%. |
| France | Groupe Société Générale (owns BRD) | The banking group should meet the capital requirements listed below:<br>a) the G-SII buffer, set at 1% and implemented in four equal increments from 2016 to 2019, as follows: 0.25% on 1 January 2016; 0.5% on 1 January 2017; 0.75% on 1 January 2018; 1% on 1 January 2019;<br>b) the O-SII buffer, set at 1% and implemented in four equal increments from 2016 to 2019, as follows: 0.25% on 1 January 2016; 0.5% on 1 January 2017; 0.75% on 1 January 2018; 1% on 1 January 2019.<br>The two buffers overlap in terms of level and phase-in period; according to the CRD IV provisions, a single buffer applies to the aforementioned group. |
| Spain | G. Netherlands B.V. (owns Garanti Bank) | G. Netherlands B.V., based in the Netherlands, holds approximately 99.9% of Garanti Bank S.A., the former being 100% owned by Garanti Holding BV. De Nederlandsche Bank did not identify Garanti Holding B.V. as a systemically important institution, therefore it is not subject to an O-SII buffer. Moreover, De Nederlandsche Bank did not notify the implementation of the SRB for Garanti Holding B.V. In its turn, Garanti Holding B.V. is part of TGB (Turkiye Garanti Bankasi), a Turkish group which is registered in a third country (that does not apply CRD IV), but is however consolidated, through global consolidation, by BBVA (according to the notification submitted by Banco de España, this group is subject to a G-SII buffer of 1%). Under the circumstances, Garanti Bank S.A. comes under the provisions of Art. 269 para. (4) of NBR Regulation No. 5/2013 on prudential requirements for credit institutions. |

**Table A.4.** List of Recommendations issued by the NCMO since its establishment

| NCMO Recommendations issued in 2017 | Recipient | Recommendation |
|---|---|---|
| NCMO Recommendation No. 10 of 18 Dec 2017 on the impact of credit institutions' funding plans on the flow of credit to the real economy | NBR | The National Bank of Romania is recommended to assess on a regular basis the impact of credit institutions' funding plans on the flow of credit to the real economy. |
| NCMO Recommendation No. 9 of 18 Dec 2017 on the systemic risk buffer in Romania | NBR | The National Bank of Romania is recommended to implement a systemic risk buffer applicable to all exposures, starting 30 June 2018, with the aim of supporting the adequate management of credit risk and enhancing banking sector resilience to unanticipated shocks, amid unfavourable structural circumstances.<br><br>Moreover, it is recommended that the buffer level be calibrated at 0 percent, 1 percent or 2 percent, depending on the average values over the past 12 months (September 2016 – August 2017) of the indicators on the non-performing loan ratio and coverage ratio. The National Committee for Macroprudential Oversight recommends the National Bank of Romania to reassess the indicators and thresholds in the calibration of the systemic risk buffer with a half-yearly frequency, so as to monitor in real time the progress in resolving non-performing loans. |
| NCMO Recommendation No. 8 of 18 Dec 2017 on the countercyclical capital buffer in Romania | NBR | The National Bank of Romania is recommended to maintain the countercyclical buffer rate at 0 percent and to monitor developments in household indebtedness. |
| NCMO Recommendation No. 7 of 9 Oct 2017 on setting up a working group on household overindebtedness | Government (MPF), NBR | The Government, by the agency of the Ministry of Public Finance (MPF), and the National Bank of Romania (NBR) are recommended to set up a working group that should make in-depth analyses on household indebtedness, using the data to be made available to this working group by the MPF via the National Agency for Fiscal Administration, while complying with the confidentiality rules. The new data to be examined should at least refer to the reports on individuals' monthly wage earnings, their income from other sources than wages (Form 112), and income from the transfer of real estate from the personal patrimony (Form 208). |
| NCMO Recommendation No. 6 of 9 Oct 2017 on setting up a working group on the firms' financial soundness | Government (MPF), NBR | The Government, by the agency of the Ministry of Public Finance, and the National Bank of Romania are recommended to set up a working group that should make in-depth analyses of the firms' financial soundness, using the data to be made available to this working group by the Ministry of Public Finance via the National Agency for Fiscal Administration, while complying with the confidentiality rules. The new data to be examined should at least refer to the reports on the deliveries/supplies and acquisitions of goods made within the national territory (Form 394) and the reports on intra-Community deliveries/supplies and acquisitions (Form 390), for every firm for which there are full historical data sets. Following the analyses made by the said working group, solutions will be identified so that businesses' budget constraints become tight in both public and private sectors. |

– continued –

| NCMO Recommendations issued in 2017 | Recipient | Recommendation |
|---|---|---|
| NCMO Recommendation No. 5 of 9 Oct 2017 on the capital buffer for other systemically important institutions in Romania | NBR | The National Bank of Romania is recommended to require, starting 1 January 2018, a capital buffer for other systemically important institutions (O-SII buffer), on an individual or consolidated basis, as applicable, equal to 1 percent of the total risk exposure amount for all the credit institutions identified as having a systemic nature in accordance with the methodology harmonised with the provisions of the EBA Guidelines on the criteria to determine the conditions of application of Art. 131(3) of Directive 2013/36/EU (CRD) in relation to the assessment of O-SIIs, based on the data reported as at 31 March 2017. |
| NCMO Recommendation No. 4 of 9 Oct 2017 on the countercyclical capital buffer in Romania | NBR | Having regard to the fact that total indebtedness currently remains below the alert threshold and setting a countercyclical buffer rate above 0 percent is, thus, not necessary, the National Bank of Romania is recommended to maintain the countercyclical buffer rate at 0 percent and monitor developments in household indebtedness. |
| NCMO Recommendation No. 3 of 14 June 2017 on enhancing statistical information required for the analyses on the real estate market | NBR | Considering that the real estate sector has an important role in the economy, with empirical analyses showing a close interplay between excessive developments in property prices and the breakout of financial crises, while real estate market developments may amplify the financial crises, the National Bank of Romania and the Financial Supervisory Authority are recommended to take the necessary steps with a view to implementing Recommendation ESRB/2016/14 on closing real estate data gaps, as follows:<br>1. The NCMO takes note of the NBR's concern to broaden the scope of information originating in the residential real estate sector;<br>2. The National Bank of Romania and the Financial Supervisory Authority shall circulate a questionnaire (Annex) to the main investors on the commercial real estate market and financial institutions (credit institutions, insurance companies, pension funds, investment funds, etc.) in order to cover data gaps for the physical market (developments in prices, yields, rents, vacancy rates), as well as for the volume of investment in and financing of real estate. |
| NCMO Recommendation No. 2 of 14 June 2017 on material third countries for the Romanian banking sector in terms of recognising and setting countercyclical buffer rates | NBR | Considering that the exposures to third countries of the banking sector in Romania are further low, the assessments carried out have not found any material third country in terms of recognising and setting countercyclical buffer rates for the banking sector in Romania. |
| NCMO Recommendation No. 1 of 14 June 2017 on the countercyclical capital buffer in Romania | NBR | Considering that, at present, total indebtedness has increased further, yet remains below the indicative threshold, it is estimated that there is no need to set a countercyclical capital buffer rate of over 0 (zero) percent. |

# Abbreviations

| | |
|---|---|
| APRC | Annual percentage rate of charge |
| BIS | Bank of International Settlements |
| CB | Credit Bureau |
| CCoB | Capital conservation buffer |
| CCyB | Countercyclical capital buffer |
| CDS | credit default swaps |
| CET | Common Equity Tier |
| CRD IV | Capital Requirements Directive IV |
| CRR | Capital Requirements Regulation |
| DSTI | debt service-to-income |
| EBA | European Banking Authority |
| EC | European Commission |
| ECB | European Central Bank |
| EIOPA | European Insurance and Occupational Pensions Authority |
| EPS | Eurobank Property Services |
| ESMA | European Securities and Markets Authority |
| ESRB | European Systemic Risk Board |
| EU | European Union |
| Eurostat | Statistical Office of the European Communities |
| LCR | liquidity coverage ratio |
| LTV | loan-to-value |
| NBFIs | Non-bank financial institutions |
| NCFS | National Committee for Financial Stability |
| NCMO | National Committee for Macroprudential Oversight |
| NCSP | National Commission for Strategy and Prognosis |
| NIS | National Institute of Statistics |
| NPL | non-performing loans |
| NSFR | net stable funding ratio |
| O-SIIs | Other Systemically Important Institutions |
| ReGIS | Romanian Electronic Gross Interbank Settlement |
| ROBOR | Romanian interbank offer rate |
| SRB | Systemic Risk Buffer |
| UNNPR | National Union of Notaries Public in Romania |

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