



NATIONAL BANK OF ROMANIA

ANNUAL REPORT

2008

Note

Annual Report for 2008 was examined and approved by the National Bank of Romania Board on 25 June 2009 and was submitted to Parliament pursuant to Law No. 312/2004 on the Statute of the National Bank of Romania.

Some of the data for the period covered are provisional and will be updated as appropriate in the subsequent publications.

Sources of data are mentioned when institutions other than the National Bank of Romania supplied data.

The drafting, English version and technical coordination of the Annual Report for 2008 were carried out by the Economics Department.

Reproduction of the publication is forbidden. Data may be used only by indicating the source.

National Bank of Romania, 25 Lipscani Street, postal code 030031, Bucharest

Telephone: 4021/312 43 75; fax: 4021/314 97 52

www.bnro.ro

ROMANIA

- Overview -

- 1. Location**
 - In the Southeastern part of Central Europe, on either side of the Carpathians, on the lower course of the Danube (1,075 km), with exit to the Black Sea (coast line: 245 km);
 - Boundaries: 3,150 km;
 - Neighbouring countries: Bulgaria, Hungary, the Republic of Moldova, Serbia and Ukraine.
- 2. Area**
 - 238,391 sq. km (ranking 12th in Europe);
 - Land use: farmland 61.7 percent (of which 39.5 percent arable land), forest 28.4 percent, other 9.9 percent.
- 3. Population**
 - 21.5 million inhabitants as of 1 January 2009 (ranking 9th in Europe);
 - Density: 90 inhabitants/sq. km;
 - Urban: 55.1 percent;
 - Ethnic breakdown: Romanians 89.5 percent, Hungarians 6.6 percent, other 3.9 percent;
 - Administrative organisation: 42 counties, including Bucharest Municipality (enjoying county status); 320 towns (103 municipalities) and 2,856 communes;
 - Capital city: Bucharest (1.9 million inhabitants);
 - Official language: Romanian.
- 4. Government**
 - Republic;
 - Legislative body: Parliament (Senate and Chamber of Deputies);
 - Executive body: government headed by Prime-Minister (appointed by the President). The President is elected by universal vote for a five-year mandate.
- 5. Currency**
 - Romanian leu (RON); fractional coin: ban;
 - Full convertibility;
 - Exchange rate is set in the interbank forex market on a daily basis; reference currency: euro.

ABBREVIATIONS

BIS	Bank for International Settlements
BSE	Bucharest Stock Exchange
BSTDB	Black Sea Trade and Development Bank
CD	certificates of deposit
CPI	consumer price index
EBRD	European Bank for Reconstruction and Development
EC	European Commission
ECB	European Central Bank
ECOFIN	Council of Economics and Finance Ministers of the European Union
EFC	Economic and Financial Committee
EIB	European Investment Bank
EMU	Economic and Monetary Union
ERM II	Exchange Rate Mechanism II
ESA	European System of Accounts
ESCB	European System of Central Banks
Eurostat	Statistical Office of the European Communities
FDI	Foreign Direct Investment
IBEC	International Bank for Economic Cooperation
IBRD	International Bank for Reconstruction and Development
IFC	International Financial Corporation
IFI	International financial institutions
IFRS	International Financial Reporting Standards
IIB	International Investment Bank
ILO	International Labour Office
IMF	International Monetary Fund
ISC	Insurance Supervisory Commission
MEF	Ministry of Economy and Finance
MFA	Ministry of Foreign Affairs
MIGA	Multilateral Investment Guarantee Agency
NCFS	National Committee for Financial Stability
NRP	National Reform Plan
NSC	National Securities Commission
OECD	Organisation for Economic Cooperation and Development
RBA	Romanian Banking Association
ROBID	Romanian Interbank Bid Rate
ROBOR	Romanian Interbank Offered Rate

CONTENTS

Overview of the main economic and financial developments in 2008	11
1. Developments and policies in the field of nominal convergence	12
2. Developments and policies in the field of real convergence	14
3. Macroeconomic policy mix	16
4. Market functioning	19
5. EU integration and relations with international organisations	21
5.1. NBR contribution to drafting strategic documents	21
5.2. NBR participation in the European System of Central Banks and other European structures	21
5.3. Relations with international financial institutions	22
6. Banking system	23
6.1. Changes in the composition of the Romanian banking system	23
6.2. Developments in prudential indicators	24
6.3. Measures aimed at improving bank supervision	25
6.4. Measures aimed at strengthening financial stability	25
6.5. Regulatory measures	27
7. Financial statements of the National Bank of Romania as at 31 December 2008	28
Chapter 1. Monetary policy of the National Bank of Romania	29
1. Policy challenges	30
2. Policy implementation	33
3. Use of monetary policy instruments	39
4. Policy guidelines	42
Chapter 2. Financial stability, regulation and prudential supervision	45
1. Financial stability	45
1.1. Main assessments on financial stability	45
1.2. Instruments supportive of prudential supervision and financial stability	49
1.3. Contingency planning and financial crisis management	51
2. Licensing and regulation of financial institutions	54
2.1. Licensing and regulation of credit institutions	54
2.2. Regulation of lending activity performed by non-bank financial institutions	56
2.3. Regulation of activity performed by the Bank Deposit Guarantee Fund	57
2.4. Regulations in the field of prevention and control of money laundering and combating the financing of terrorism	57
2.5. Legal and accounting regulatory framework for credit institutions, non-bank financial institutions and the Bank Deposit Guarantee Fund	58
2.6. Key objectives for 2009	60

3. Prudential supervision of credit institutions	61
3.1. Structure of the banking system.....	61
3.2. Performance and outlook	64
3.3. Measures to improve prudential supervision of credit institutions	70
3.4. Banking risk assessment	72
3.5. International cooperation in the field of prudential supervision	73
3.6. Non-bank financial institutions.....	75
3.7. Prudential supervision and monitoring of non-bank financial institutions	77
Chapter 3. Currency issue	79
1. Developments in currency outside banks	79
2. NBR's cash payments and receipts in the relationship with credit institutions	81
3. Currency processing	83
4. Numismatic issues	83
5. Counterfeiting of the domestic currency and of the euro	85
Chapter 4. Payment and settlement systems.....	87
1. ReGIS	87
2. The payment system ensuring the paper-based clearing of payments via debit payment instruments (PCH)	91
3. SaFIR.....	91
4. National Bank of Romania's participation in the activities carried out within the European System of Central Banks	95
5. Regulation, licensing and monitoring of payment systems	95
Chapter 5. Management of international reserves	99
1. Developments in international official reserves in 2008	99
2. Strategic goals	99
2.1. Goals for the period April 2008-March 2009	99
2.2. Developments in the external economic environment	100
3. The manner to achieve strategic goals.....	101
Chapter 6. Balance of payments and international investment position.....	105
1. Current account	105
2. Financial and capital account	107
3. Romania's international investment position	108
Chapter 7. International activity	111
1. Romania as a EU Member State	111
2. Cooperation with international financial and economic institutions	124
Chapter 8. Preparation of the euro adoption process	129
1. Romania's progress towards convergence	129
2. Experience of countries that have recently joined the Economic and Monetary Union	132

Chapter 9. External communication of the National Bank of Romania	137
Chapter 10. Macroeconomic research activity	143
1. Macroeconomic modelling	143
2. Macroeconomic analyses and surveys.....	144
3. Financial stability	145
4. Conferences organised by the NBR.....	147
5. Guidelines and objectives of research activity in 2009	148
Chapter 11. Other activities of the National Bank of Romania.....	150
1. Human resources management.....	150
2. Statistical activity	152
3. Information technology	153
4. Internal audit.....	154
5. Legal activity	155
6. NBR Archives, Museum and Library	157
Chapter 12. Financial statements of the National Bank of Romania as at 31 December 2008.....	160
1. Overview	160
2. Recognition of monetary policy operations	161
3. Recognition of international reserve management operations.....	163
4. Effects of developments in the exchange rate of the domestic currency.....	164
5. Conclusions	164
Financial Statements of the National Bank of Romania as at 31 December 2008 (audited by Deloitte)	169
Report of the financial auditor	171
Balance sheet of the National Bank of Romania.....	173
Income statement of the National Bank of Romania.....	175
Notes to financial statements.....	176

ANNEXES

Organisation chart of the National Bank of Romania as of 31 December 2008	206
National Bank of Romania publications as of 31 December 2008.....	208
Main papers submitted to Parliament by the NBR in 2008.....	208

TABLES

Credit Institutions by Ownership.....	62
Market Share of Banks and Foreign Bank Branches.....	63
Banks and Foreign Bank Branches as a Share in Aggregate Capital.....	63
Foreign Participations in the Share Capital of Credit Institutions in Romania as at end-2008	64
Key Indicators.....	66
Net Assets and Own Funds as at 31 December 2008	69
Breakdown of non-bank financial institutions by activity as of 31 December 2008.....	75
Main Indicators of the NFI Sector as of 31 December 2008	76
Shares of Foreign Capital by Country of Origin	76
Coin and medal issues	84
Payments Traffic in ReGIS.....	88
Structure of Payments in ReGIS in 2008.....	90
Developments in Paper-based Cleared Payments.....	91
Current Account.....	105
Current Account Deficit Financing.....	108
Key External Indebtedness Indicators	110
Maastricht Criteria.....	129
Balance Sheet of the National Bank of Romania as at 31 December 2008.....	162
Results of Transactions Performed in 2008	163
Revaluation Differences as at 31 December 2008.....	164
Equity	165
Performance of Financial 2008.....	165
Profit/Loss for Financial 2007 and 2008	166

CHARTS

Inflation Rate	29
Policy Rate and Inflation Rate	34
Contribution of the Main Demand Components to GDP Growth	35
Exchange Rates (RON/EUR and RON/USD)	37
Credit to Private Sector.....	38
Credit to Households	38
Household Deposits.....	39
Interbank Money Market Rates	40
Denomination Composition in Total Value of Banknotes Outside Banks.....	80
Payment Composition by Denomination.....	82
Receipt Composition by Denomination.....	82
Number of Counterfeits of the New Denominations	86
Developments in Large-value and/or Urgent Payments in 2008.....	89
Developments in Large-value and/or Urgent Payments in 2008 versus 2007.....	89

Number and Value of Transactions	92
Structure of Transfers in 2008	93
Value of Collateral related to Ancillary Systems	93
International Reserves in 2008	99
Romania's Foreign Exchange Reserve Structure.....	102
Yield against Merrill Lynch Indexes.....	103
Romania's Foreign Exchange Reserve Composition.....	103
Outcomes of International Reserve Management.....	104
Development of GDP per Capita	131
Share of Economic Sectors in GDP	131
Economy Openness	131
Share of Trade with the EU in Total Foreign Trade.....	131
Developments in NBR's Costs with Banking Operations	160
Developments in NBR's Foreign Assets	163
NBR's Financial Result Structure during 2007-2008	165

Overview of the main economic and financial developments in 2008

The second year of Romania's participation in EU mechanisms saw a plethora of events at both international and local levels that rendered more difficult the authorities' task of ensuring macroeconomic stability. At international level, the subprime mortgage-related financial market turmoil that began in the summer of 2007 turned into the most serious global economic crisis since the Great Depression of 1929-33. The crisis intensified especially after the Lehman Brothers default and the selling-off of Merrill Lynch to Bank of America in September 2008. Paradoxically enough, emerging economies bore the brunt of the crisis following the liquidity crunch, against the background of investors' increased risk aversion. Romania counted among the countries with wide external imbalances, which were – to a larger extent – adversely affected by the turmoil. The only positive aspect of the global crisis was the sharp fall in prices of oil and other commodities, the evolution of which represented an important determinant of inflation in 2008 H1.

At domestic level, the economic picture was complicated by the Parliamentary elections held in November, which occasioned an unprecedented easing of income and fiscal policies. The government deficit increased to a 10-year high of 5.4 percent of GDP. Thus, the expansion of the public sector offset almost completely the external adjustment efforts undertaken by the private sector and contributed to the current account deficit remaining at a level deemed as overly high by foreign investors (12.3 percent of GDP). Moreover, the pro-cyclical nature of fiscal policy caused a reduction in the room for manoeuvre available to the incoming government for countering a possible recession in 2009. Excess demand stemming from loose wage and fiscal policies was boosted January through September by the overly fast dynamics in bank credit which came to an abrupt halt in the run-up to year-end 2008. In such intricate conditions, a favourable impact had only the good performance of the agricultural sector, which dampened food-driven inflationary pressures during 2008 H2.

In 2008, full capital account liberalisation produced both benefits and costs for Romania. While in the first three quarters of the year the relatively high external financing translated into an above-potential economic growth, the spill-over of the global financial crisis to the real sector and the worsening of foreign investors' sentiment depressed sizeably the annual rate of increase of GDP. The lesson to be learned by policymakers and the general public alike is the following: in view of the full freedom of capital movements, the authorities should pursue prudent, sustainable policies capable of giving foreign investors the comfort they need during both upturns and downturns of the economy so that they maintain their exposure to the host country.

1. Developments and policies in the field of nominal convergence

Euro adoption by Romania is conditional upon the fulfilment of both nominal criteria – referred to as the “Maastricht criteria” – and legal convergence criteria. As far as the euro adoption calendar is concerned, it is noteworthy that, assuming Romania starts participating in the European Exchange Rate Mechanism II (ERM II) in 2012, the position of the European Commission and that of the European Central Bank will be available no earlier than 2014 H1, since the minimum stay in this exchange rate arrangement covers 2 years. If these assessments lead to the conclusion that Romania fulfils all convergence criteria, the country will be able to introduce the euro on 1 January 2015.

As for the nominal convergence criteria, the year 2008 saw no progress. On the contrary, while in 2007 Romania fulfilled both components of the criterion on the sustainability of the government budgetary position (fiscal deficit and public debt as share of GDP), in 2008 the share of fiscal deficit in GDP exceeded by far the 3 percent reference value. Moreover, although the exchange rate criterion cannot accurately be assessed unless the leu participates in ERM II, central bank simulations point to the fact that over the past two years the RON/EUR exchange rate neared the lower bound of the ± 15 percent fluctuation band around a “reference level” (i.e. the average exchange rate in December 2006).

Inflation rate

In 2008, the annual inflation rate measured by the consumer price index (CPI) stood on average at 7.85 percent. According to the Harmonised Index of Consumer Prices (HICP) used by the European Commission and the European Central Bank, inflation rate equalled 7.9 percent compared to the reference value (i.e. 1.5 percentage points above the average of the three best performing EU Member States) of 4.0 percent.

In terms of end-of-period inflation, the performance of 2008 (6.30 percent, December/December) was marginally better than that of a year earlier (6.57 percent), yet an overshooting of the target of 3.8 percent ± 1 percentage point announced by the central bank could not be avoided.

The impact and magnitude of factors contributing to this outcome varied throughout the year. Thus, in January-July 2008, a major impact exerted the supply-side inflationary pressures generated by tensions on the agrifood market¹ (as a result of production decline in 2007, higher import prices of agricultural commodities and unprocessed products and an unfavourable base effect), on the one hand, and the effect of higher world oil prices on the prices for fuels and natural gas, on the other. The second half of 2008 saw the gradual alleviation of the impact exerted by these two factors, but also the persistence of demand-side pressures arising from: (i) the further loose wage policy throughout the year (which led to a wider negative gap between the dynamics of labour productivity and that of

¹ The annual growth rate of food prices accelerated in May-June to a 4-year high of 11.77 percent.

wages, with unfavourable effects on the pressures generated by unit labour costs) and (ii) the fiscal policy loosening, particularly in the context of elections in the final quarter of 2008. Another factor fuelling demand was lending, whose strong expansion in the first three quarters contributed to the rise in GDP at a pace above potential (9 percent, the resulting rate for 2008 as a whole standing at 7.1 percent). Exchange rate developments were uneven, the 9.9 percent² nominal depreciation of the domestic currency against the euro throughout 2008 entailing higher import prices, as well as more expensive products with prices expressed in euro (telephony, rents, motorcars). Moreover, the exchange rate volatility (through the depreciation episodes in Q1 and Q4), along with the impact of the other above-mentioned shocks, acted as a stimulus for inflation expectations, whose persistently high levels slackened the resumption of disinflation.

Long-term interest rates

The compliance with this criterion is closely linked to observing the inflation rate criterion. In 2008, average interest rates on long-term government securities stood at 7.7 percent per annum, exceeding the reference value of 6.2 percent (2 percentage points above the average interest rates of the three best performing EU Member States in terms of price stability). Given the scarce liquidity on the long-term government securities market in Romania, a conclusion on the compliance with this criterion is difficult to draw. Long-term government securities issues are seldom launched; for instance, there were nine issues of 5-year securities in 2008, but no issue of 10-year securities. In addition, liquidity is scarce on the secondary market for government securities too, which makes difficult the emergence of a fair price.

Government budgetary position

In 2001-07, Romania has strictly complied with the budget deficit criterion, maintaining it below the reference value of 3 percent of GDP. The expansionary budget and fiscal policies pursued in 2008, mainly due to elections, caused the significant excess of the reference value, the budget deficit measured in accordance with the European standards (SEC 1995) accounting for 5.4 percent of GDP. The pick-up in spending was partly incidental (compensation of refugees from Bessarabia, Bukovina and Southern Dobrudja, of the persons who had made down payments for purchasing Dacia motorcars) and will no longer have an impact on budget in the period ahead. However, there are structural budget commitments, the effects of which will propagate for several years, such as the decision to raise the pension point from 32 to 45 percent of the average wage. According to the World Bank's estimates, this decision requires annual transfers from the state budget to the social security budget in amount of roughly 1.6 percent of GDP (without taking into account the deterioration of demographic factors). On the other hand, in 2006-2008, budget spending for public authorities (agencies, mayoralities, prefectures) rose from 1.7 percent to 2.8 percent of GDP. It is obvious that bringing budget deficit below the 3 percent reference value and the ERM II entry according to the schedule (2012) require several urgent and belt-tightening measures aimed at correcting the above-mentioned structural imbalances. To this end, the adoption by

² December/December, monthly averages.

the Parliament of Romania of three key pieces of legislation (law on pension system reform; law on wage system reform; law on fiscal accountability) in 2009 will be of particular importance for observing the euro adoption calendar.

General government debt

As regards general government debt, the 13.6 percent debt-to-GDP ratio recorded at end-2008 is far below the 60 percent of GDP reference value laid down in the Maastricht Treaty.

Exchange rate fluctuations

As the domestic currency is not participating in ERM II for the time being, the central parity against the euro could not be defined, relative to which exchange rate movements may fluctuate within a ± 15 percent band. Assuming that the reference value is the average exchange rate in December 2006, the exchange rate of the domestic currency versus the euro stayed in a 9.7/-14.6 percent variation band by end-2008.

2. Developments and policies in the field of real convergence

The Maastricht Treaty does not explicitly set forth real convergence criteria. However, it is obvious that in order for the adoption of the euro to generate less costs and greater benefits, the prior achievement of a high real convergence with euro area members is required in terms of GDP per capita, labour productivity, economy structure, economy openness, foreign trade integration etc.

GDP and GDP per capita growth

Unlike other Central and Eastern European countries that benefited from significant foreign investment flows as early as the '90s, Romania was a late starter, being "discovered" by foreign investors only in recent years, after the occurrence of significant events such as the NATO accession (April 2004), full capital account liberalisation (September 2006) or joining the EU (January 2007). This is one of the major reasons for which GDP per capita (in terms of Purchasing Power Standards) increased rapidly in Romania during 2003-2008, i.e. by about 74 percent, as compared with 40 percent in Poland, 34 percent in the Czech Republic, 20 percent in Hungary. This swift rise was however accompanied by wider macroeconomic imbalances (general government deficit and current account deficit of the balance of payments), rendering the maintenance of the fast GDP growth unsustainable, particularly in an international context marked by uncertainty and caution. In 2008, Romania's GDP per capita (in terms of Purchasing Power Standards) stood at PPS 11,300, about 43.5 percent of the EU25 average, as against 40.7 percent in 2007.

Labour productivity

In 2000-06, a fundamental economic correlation was observed in Romania, i.e. productivity rose faster than wages. As a result, the domestic currency

strengthened versus the major currencies in real terms (and even in nominal terms in the last years of that period), entailing a wealth effect (an increase in the EUR-denominated value of fixed and non-fixed assets of companies and households).

However, starting with 2007, the pursuit of a loose wage policy caused the breakdown of the respective correlation. For instance, the annual growth rate of gross wage in industry stood at 22.2 percent in January-September 2008, while the annual dynamics of labour productivity ran at merely 9.8 percent in the same period. Even though the annual growth rate of wages slowed down to 18.8 percent in Q4, it continued to significantly exceed labour productivity dynamics that turned negative (-1.6 percent). These developments had adverse effects on both disinflation progress and external competitiveness of the Romanian products. Hence, the domestic currency depreciation in early 2009 was broadly corrective, being generated by the worsening economic fundamentals. If the mismatch between the growth rate of wages and that of productivity persisted, a new corrective depreciation would result, thereby entailing additional difficulties in inflation curbing and a further wealth loss (expressed in euro) in the case of companies and households.

Structure of the economy

Progress in achieving a sectoral structure of the economy similar to that of EU Member States has continued and is likely to become more visible by the time of euro adoption. Thus, the share of agriculture in gross value added economy-wide dropped to 7.2 percent in 2008 from 13 percent in 2003, compared to 1.8 percent³ in EU-25. Industry also posted a downtrend, from 27.8 percent in 2003 to 25.6 percent in 2008 (while in EU-25 industry accounted for 19.9 percent of GVA formation). Convergence was also manifest in the services sector, whose share increased from 52.8 percent in 2003 to 55.4 percent in 2008, still below the EU-25 average, i.e. 71.9 percent.

Openness of the economy

What makes Romania different from the other EU Member States (and illustrates the domestic absorption-based economic growth) is the relatively low openness of the economy (62.6 percent of GDP in 2008⁴, close to the previous year's reading). Therefore, Romania lags behind other EU Member States in the region, such as Bulgaria, the Czech Republic, Hungary, Poland and Slovakia, where openness ranged from 71 percent to 148 percent of GDP in the period under review. Adding to this is Romania's smaller contribution of exports to the openness of the economy (24.6 percent of GDP in 2008), whilst in the aforementioned countries the share of exports is much larger (ranging between 33 percent and 74 percent of GDP) and – except Bulgaria – the two components of the trade balance hold relatively similar weights. Incidentally, Romania's poor export-orientation will prove to the benefit of the domestic economy in 2009, given the contraction in major foreign markets.

³ Eurostat data for 2008.

⁴ Based on the ratio of imports + exports of goods to GDP. When determined by the ratio of imports + exports of goods and services to GDP, the openness of the economy stood at 74.8 percent in 2008.

Over the medium and long term, however, exports will have to play an increasingly important role as the driver of the economy, all the more so that growth based on domestic absorption has shown its limitations.

Foreign trade integration

The share of trade with the EU in total foreign trade remains elevated, despite witnessing a slight retrenchment in 2008. Thus, exports to EU countries accounted for 70.4 of total exports in the year under review, compared to 72 percent in 2007. The share of imports from other EU Member States reached 69.1 percent of total versus 71.3 percent a year earlier.

3. Macroeconomic policy mix

Romania needs to adjust its macroeconomic policies to the new context shaped by the international financial crisis. Ever since end-2007, the National Bank of Romania pointed to the Romanian economy's vulnerability to global financial turbulences, underlining the necessity to recalibrate the economic policy mix in order to cope with the ensuing challenges. The central bank emphasised that the relatively high restrictiveness of monetary policy, warranted by overheating of the Romanian economy, should be accompanied by a similar stance of fiscal policy, as well as by a prudent income policy and the continuation of structural reforms. Such a rebalancing of the macroeconomic policy mix was deemed necessary primarily for gradually narrowing the current account deficit, as the external imbalance has been the main source of vulnerability of the economy to the liquidity crunch and the deteriorating international financial market sentiment.

In the first half of 2008, the joint impact of supply- and demand-side factors caused a rise in the inflation rate to 9 percent in July, which called for monetary policy tightening. Consequently, the central bank revised the monetary policy rate upwards, in five consecutive stages, from 8.0 percent to 10.25 percent per annum (February through July), and firm management of money market liquidity via open-market operations was further pursued. Furthermore, in order to consolidate broad monetary conditions' restrictiveness, minimum reserve requirement ratios on leu- and foreign currency-denominated liabilities of credit institutions were left in the first three quarters at 20 percent and 40 percent respectively.

Although essentially intended for the fulfilment of the monetary policy objective, the various measures, adopted over the past five years to slow down credit dynamics (especially its foreign currency component), had also a prudential role, some of them providing banks with a liquidity buffer which proved particularly useful amid the deepening of the international financial crisis.

In order to increase the efficiency of money market liquidity management, the NBR decided to shorten the maturity of standard deposit-taking operations from 2 weeks to 1 week and to set up a symmetrical corridor of ± 4 percentage points around the policy rate delineated by interest rates on its standing facilities. Both changes were part of the gradual harmonisation process of the National Bank of Romania's operational framework with that of the European Central Bank.

The tightening of monetary policy, the alleviation of supply-side tensions and the change in the economic context were reflected by the drop in the 12-month inflation rate from 9 percent in July to 7.3 percent in September and 6.3 percent in December. Moreover, during 2008, the structural liquidity surplus narrowed gradually, causing commercial banks to shift to a net liquidity deficit position starting October and the central bank to move to a creditor position. In view of this structural change, in Q4, the minimum reserve requirement ratio on leu-denominated liabilities of credit institutions was cut from 20 percent to 18 percent, whereas management of liquidity was rendered more flexible.

This transition was not smooth at all, given that such a structural change overlapped with great woes on key financial market segments. October through November 2008, the interbank money market was temporarily afflicted by the fallout from the global crisis, namely banks' confidence crunch, the most likely downward adjustment in their exposure limits to one another, and the increase in non-residents' speculative demand for domestic currency. Consequently, interbank money market rates surged, whereas ROBOR quotations were subject to an even ampler adjustment, outrunning by far the actual interest rates on transactions. The central bank viewed this development as a market dysfunction and introduced the possibility to temporarily suspend the publication of indices calculated based on participating banks' quotations, should they exceed by more than one-fourth of the interest rate on the lending facility.

The slowdown in the dynamics of external financing in 2008 Q4 compelled most banks to rethink their strategies. Thus, the fast expansion of credit to the private sector in the first part of the year (about 66 percent year on year in March) lost momentum, its pace of increase reaching 33.7 percent in December. Nevertheless, the large share of foreign currency credit was still a reason for concern, given its pick-up (also as a result of domestic currency depreciation) to 57.8 percent in total credit to the private sector in December 2008.

In 2008, in the context of challenges posed by the international financial crisis, the stance of fiscal and wage policies was inadequate, enhancing the pro-cyclical character of economic developments. Thus, economic expansion (already above its potential level) was additionally fostered, exhausting the room for manoeuvre for the coming period, when growth was expected to be below potential.

The positive output gap, fuelled by loose fiscal and wage policies (combined also with the aggressive promotion of credit products by most commercial banks in the first half of the year), forced the National Bank of Romania to significantly tighten monetary policy, by raising the policy rate in several stages by 2.25 percentage points and by keeping minimum reserve requirement ratios at high levels. The result was a suboptimal mix, defined by loose fiscal and wage policies and a restrictive monetary policy.

Against the background of the international financial crisis becoming manifest in the final quarter of 2008, this mix amplified the challenges facing monetary policy.

During this period, the central bank had to cope, on the one hand, with the significant inflationary pressures exerted by a persistently high demand, including as a result of looser fiscal and income policies in the run-up to elections, and by the domestic currency depreciation. The weaker leu was likely to generate risks not only to disinflation, but also to financial stability, given the still wide current account deficit and the shortage of available financing sources worldwide. The significant widening of the budget deficit during the period countered the opposite influence from the external deficit adjustment caused by the private sector, slowing down the narrowing of the balance of payments overall disequilibrium to levels that would diminish pressures on the leu exchange rate. On the other hand, calibrating the monetary policy response was more difficult due to the growing uncertainties surrounding the outlook for world economy and their repercussions on the local economy against the backdrop of broadening and fast-deteriorating adverse effects exerted by the deepening of the global financial crisis on the real sector. Under the circumstances, the central bank adjusted monetary policy so as to strike a balance between the restrictiveness required by the achievement of medium-term inflation objective and the prudence needed for avoiding unwarranted costs in terms of economic growth.

Romania was sanctioned for its loose fiscal policy in the context of the global financial crisis: some rating agencies downgraded the country's ratings, and the credit default swap spread rose from less than 100 basis points at end-2007 to more than 700 basis points in 2009 Q1. The widening of the budget deficit by the equivalent of 3 percent of GDP in 2008 Q4 alone offset the external adjustment made by the private sector, causing the current account deficit to remain stuck at an overly high level, i.e. 12.3 percent of GDP. For this reason, Romania's response to the global crisis fallout in 2009 cannot resemble that of some European countries or of the United States (fiscal easing). Faced with a large and difficult to finance current account deficit, the Romanian authorities need to choose between an orderly adjustment and its disorderly correction by the market, with negative repercussions on the exchange rate, economic growth and financial stability. Another negative effect exerted by the expansionary fiscal policy was the government's massive resort to bank loans, in the final quarter of 2008 and the first months of 2009, possibly leading to a crowding-out of the private sector.

In light of the above, the macroeconomic policy mix needs to be recalibrated in 2009. Thus, the suboptimal mix in place over the last years should be replaced by a mix of (budget, wage and monetary) policies featuring similar restrictiveness that would ensure sustainable economic growth in the long run. The need to recalibrate the economic policy mix is also emphasised by the provisions of the loan agreement concluded by Romania with the IMF-EU-IFI. The completion of this agreement in the spring of 2009 – shortly after the investiture of the Government and before liquidity risks generated by the international financial crisis come close to materialising – was a first step towards regaining foreign investors' confidence in Romania's ability to successfully overcome financial turbulences.

4. Market functioning

Apart from complying with the nominal and real convergence criteria and improving the economic policy mix, Romania should also continue developing markets, by focusing on the freedom of movement of goods, services, capital and labour force.

Trade balance

The trade balance deficit (EUR 18,372 million, up 3.1 percent versus 2007) had a key influence on the balance of payments' current account. In year-on-year comparison, the dynamics of exports was 4 percentage points faster than that of imports, and the share of trade deficit in GDP edged down 1 percentage point to 13.4 percent.

Exports of goods amounted to EUR 33,628 million, up 13.8 percent year on year, owing mainly to the improved structure of exports and the real depreciation of the domestic currency versus the euro. The structure of exported goods shows an increase in the share of capital goods and commodities, concurrently with the drop in the share of intermediate and consumer goods.

Imports of goods reached EUR 52,000 million, up 9.8 percent year on year. Structural analysis shows a higher share of commodities and consumer goods (with the latter accounting for about 16 percent in total imports), concurrently with the decrease in the share of capital goods and the maintenance of intermediate goods at a level similar to that in the previous year (46.4 percent).

In 2009 Q1, the trade balance was subject to a considerable adjustment. Thus, the value of exports (expressed in euro) went down by 19.4 percent, while the value of imports (expressed in euro) diminished by 35.4 percent. Should these trends continue, Romania's current account deficit financing will no longer be a problem at end-2009.

Services balance

In 2008, the services balance surplus increased from EUR 477 million to EUR 845 million. The development was due, on the one hand, to the improvement in the transport balance (moving from EUR -505 million in 2007 to EUR +17 million). On the other hand, the significant surplus reported in 2008 as well by "other services" (EUR 946 million) cannot be overlooked – particularly advertising and marketing services, communication services, financial services, etc. Nevertheless, the positive trajectory was dampened by "tourism" (reporting a EUR 117 million deficit), which, alongside transport services, can make a high contribution to improving the current account.

Capital and financial account

In 2008, the positive balance of capital and financial account stood at EUR 18,331 million, up 6.1 percent versus the previous year. The international financial crisis notwithstanding, net direct investment rose by 31.6 percent from

2007, to reach EUR 9,272 million. Thus, in 2008, 58.4 percent of the current account deficit (EUR 16,897 million) were covered from direct investment and capital transfers.

In 2008, privatisation proceeds caused equity capital to rise by EUR 873 million. The year under review saw two important privatisation deals, namely the takeover by Ford Motor Company of 72.4 percent of S.C. Automobile Craiova S.A. share capital and the completion of the takeover by the Italian group ENEL of 64.4 percent of S.C. Electrica Muntenia Sud S.A. share capital.

Medium- and long-term external debt added 31 percent versus end-2007 to EUR 50.7 billion. The structure of the medium- and long-term external debt by creditor shows a persistent upward trend in the share of private sources (from 85.1 percent in December 2007 to 86.8 percent in December 2008), as a result of loans taken from foreign private banks, concurrently with the falling shares of multilateral undertakings to 12.6 percent and bilateral sources to 0.6 percent of total. During 2009, in the context of the loan agreement concluded by Romania with the IMF-EU-IFI, the share of multilateral undertakings is expected to rise significantly, offsetting a potential reduction in loans from foreign banks.

Portfolio investment posted a poor development in 2008, as illustrated by the trend reversal in its balance to EUR -834 million. The capital market witnessed the worst development over the last decade, with the main stock exchange indicators reverting to readings seen in 2004-2005. Thus, in spite of the increase in the number of companies admitted to trading (to 68, from 59 in 2007), stock exchange capitalisation plummeted by almost 47 percent, to RON 45,701 million, whereas the value of transactions performed plunged by more than 49 percent, to RON 6,832 million. This performance illustrates the very large share of foreign capital in stock exchange investment and also the shallow capital market.

Labour market

Despite the global financial crisis, manifest as early as mid-2008 in the main European immigration countries, the number of Romanians working abroad appears not to have declined, the same as their private transfers. Thus, net private transfers (most of which were remittances from abroad) rose to EUR 5,139 million compared to EUR 5,120 million in the prior year.

Net transfers of public administration also increased from EUR 207 million in 2007 to EUR 862 million in 2008, mainly on account of (pre- and post-accession) structural funds from the EU. In 2008, inflows from structural funds stood at EUR 2,166 million compared to EUR 929 million in 2007. However, the bulk of these inflows came from pre-accession funds (PHARE, ISPA, SAPARD) and only a small part derived from post-accession funds. According to an estimate of the Ministry of Economy and Finance, out of post-accession funds worth of EUR 1,854 million that the EU earmarked to Romania, the payments made in 2008 were tantamount to only EUR 231 million (at a 12.5 percent absorption rate). Nevertheless, due to the drawing of pre-accession funds, at 30 November 2008,

financial flows between Romania and the EU showed a net balance of EUR 1,167 million, corresponding to total amounts from the EU worth of EUR 2,275 million and to total amounts paid to the EU equalling EUR 1,108 million. For 2009 and the coming years, the challenge consists in improving markedly Romania's capacity to access European funds so as to offset the drop in private capital inflows.

5. EU integration and relations with international organisations

In light of Romania's full EU membership and amid the ongoing global financial crisis, the NBR worked, along with other Romanian authorities, for adjusting and integrating national policies into a European operational framework.

5.1. NBR contribution to drafting strategic documents

On 7 May 2008, the European Commission and the European Central Bank published simultaneously their Convergence Reports for the period 2006-2008, including, for the first time since EU accession, assessments on Romania and Bulgaria as Member States. The NBR was actively involved in analysing and approving the ECB's Convergence Report, by formulating opinions during the editorial working group meetings and through the participation of the NBR governor in the approval procedure. Upon enforcing the Lisbon Strategy, the NBR was consulted in the drafting of the National Reform Programme (NRP) according to its field of activity and legal tasks. Romania submitted the second report on the National Reform Programme to the European Commission in October 2008. Similarly to previous years, the NBR participated in the biannual macroeconomic forecast exercises of the European Commission and the ECB.

5.2. NBR participation in the European System of Central Banks and other European structures

As of 1 January 2007, when Romania joined the EU, the NBR became a full member of the ESCB. At present, the NBR governor and deputy governor in charge of European affairs take part in the quarterly meetings of the ESCB General Council, while NBR representatives participate – with equal rights and responsibilities as other Member States' representatives – in the meetings of the 12+1 ESCB committees and relevant substructures.

Furthermore, the central bank is actively integrated in several structures and substructures of the European Commission and of the EU Council, such as: the ECOFIN Council, the Economic and Financial Committee, the Financial Services Committee, the European Banking Committee, the Committee of European Banking Supervisors, etc. Within these structures, the NBR is involved in preparing, transposing, implementing and notifying Community legislation.

Technical co-operation with the European Central Bank has manifold facets. As a technical assistance provider, the NBR is involved in two projects co-ordinated by the ECB: (i) the technical assistance programme for the National Bank of Serbia, spanning a nine-month period, along with other 16 ESCB members, in preparation

for Serbia's accession to the European Union; (ii) the three-year co-operation programme with the Central Bank of Egypt, along with other six ESCB members, aimed at implementing the Basel II Accord. As a recipient of technical assistance, the NBR focused on strengthening co-operation with the ECB via short-term exchanges of experience on sundry issues, such as monetary policy, communication, etc. A major step in this sense is the NBR's affiliation – at the ECB's invitation – to the "Cultural Days" project. Romania will be the theme country of the seventh edition of this project, scheduled in Frankfurt during 21 October – 9 November 2009.

5.3. Relations with international financial institutions

In the year under review, Romania's relations with the International Monetary Fund consisted mainly in the yearly consultations laid down in Article IV of the IMF's Articles of Agreement. Thus, in April 2008, an IMF mission visited Bucharest in order to assess together with the Romanian authorities the economic developments of 2007. Also, a joint IMF-World Bank mission visited Bucharest in November 2008 for a follow-up on the financial system stability assessment under the Financial Sector Assessment Program (FSAP).

In early 2009, amid the deepening of the global financial crisis and the previous year's fiscal and wage policy slippages, Romania concluded a two-year stand-by arrangement with the IMF for a EUR 12.95 billion loan aimed at consolidating foreign exchange reserves. The arrangement also includes financing provided by the European Commission and other international financial institutions⁵ (worth EUR 5 billion and EUR 2 billion respectively) for project funding.

In 2008, the IBRD's financial assistance to Romania amounted to USD 133.1 million via two projects, while IFC financing targeted the banking sector, with a view to fostering lending to small- and medium-size enterprises (SMEs). Thus, Banca Transilvania and ATE Bank were granted loans totalling around EUR 40 million.

Over an 18-year period (1991-2008), the EBRD granted Romania assistance with a cumulated value of almost EUR 4 billion, of which funds amounting to EUR 2.9 billion were actually drawn. In 2008, the overall business volume stood at EUR 318 million, the most important being the EUR 100 million loan to Banca Transilvania for reviving SME lending.

The cumulative value of the financial assistance provided by the European Investment Bank (EIB) to Romania during 1991-2008 exceeded EUR 6 billion. In 2008 EIB-funded projects totalled EUR 1.1 billion and focused on industry, public utilities, transports, and SME lending.

The NBR has been a BIS shareholder ever since the latter's establishment in 1930. In 2008, the central bank received EUR 2.4 million in dividends for the

⁵ IBRD, EBRD.

2007-08 financial year in relation to the shares held in the BIS capital.

Amid the ongoing global financial crisis, two of the major rating agencies downgraded the sovereign rating for long-term debt in foreign currency to below “investment grade” (Standard&Poor’s from BBB- to BB+ in October and Fitch from BBB to BB+ in November), Romania being the only Member State in this situation. Such a classification is debatable, at least by comparison to other EU countries facing more difficult macroeconomic challenges. Moody’s and JCRA adopted a more balanced stance, by maintaining Romania’s rating at “investment grade” throughout 2008.

6. Banking system

Following our country’s EU accession and the liberalisation of the services market, some 190 foreign institutions notified their intention to provide banking services directly on the territory of Romania, of which 174 banking institutions, 3 non-bank financial institutions and 13 issuers of electronic currency. In spite of the global financial crisis and the recent years’ lending spree, overall, the domestic banking system may be deemed as stable, with capitalisation, solvency and liquidity levels in line with prudential requirements.

6.1. Changes in the composition of the Romanian banking system

The major changes occurring in the domestic banking system during the year under review were:

- the establishment of BCR Banca pentru Locuințe;
- the opening of a branch of Ireland-based Depfa Bank;
- takeover of Banca di Roma – Bucharest branch by UniCredit Țiriac Bank, following the European-wide merger of the two institutions’ shareholders (UniCredit Group and Capitalia);
- Sanpaolo IMI Bank Romania changed its name to Banca Comercială Intesa Sanpaolo Romania, following the merger between Intesa SpA and SanPaolo IMI SpA;
- C.E.C. changed its name to CEC Bank, while Egnatia Bank became MARFIN Bank;
- takeover of ABN Amro by Royal Bank of Scotland.

Hence, at end-2008, there were 43 credit institutions operating in Romania (42 banks and CREDITCOOP credit co-operative network). As for banking system composition by equity ownership, two banks (CEC Bank and Eximbank) were state-owned, three had majority domestic private capital, 27 had majority foreign capital, and 10 were branches of foreign banks. Fully or majority privately-held banks made up 94.8 percent of total assets in the Romanian banking system, the remaining

5.2 percent being accounted for by fully or majority state-owned banks. The share of assets of banks with foreign capital ran at 88.2 percent of total.

Although they hold more than half of banking system activity, the top-five banks (in terms of assets) saw a further decline in their share, to 54.3 percent in December 2008 against 56.3 percent in the same year-ago period, amid smaller banks' aggressive customer campaigns.

Capitalisation of the Romanian banking system continued to grow in 2008 as well, in both nominal and real terms (19.6 percent and 12.6 percent respectively), mainly on account of shareholders' cash contribution. As regards the country of origin of invested capital, the top-three countries were Greece (22.4 percent of total capital), Austria (18.4 percent), and the Netherlands (9.2 percent).

6.2. Developments in prudential indicators

In the context of the global financial crisis, namely of the stronger domestic competition, in 2008, Romania's banking system shifted from excess liquidity to liquidity shortage, i.e. from aggressive lending in 2008 Q1-Q3 to a considerable slowdown of credit growth rate and to promotions aimed at attracting deposits in Q4. Despite the deceleration in credit growth rates (33.7 percent in nominal terms or 25.8 percent in real terms in 2008 versus 60.4 percent in nominal terms or 50.5 percent in real terms in 2007), the worsening of loan portfolio could not be averted. Thus, the share of unadjusted exposure of loans and related interest under "doubtful" and "loss" categories rose from 3.76 percent in December 2007 to 5.95 percent at end-2008.

The solvency ratio of the banking system remained relatively unchanged (13.76 percent in December 2008 from 13.78 percent a year earlier), as the solvency ratio reported by all credit institutions was higher than the minimum required level of 8 percent.

At end-2008, the key profitability indicators were markedly higher than in December 2007 (ROA equalled 1.56 percent versus 1.01 percent; ROE stood at 17.04 percent from 9.43 percent). The major drivers of this development were the sale of the stakes held by four banks in the capital of an insurance company, on the one hand, and the expansion of net interest income, on the other.

The liquidity indicator for the overall banking system, i.e. effective liquidity/required liquidity, was higher than the minimum requirement (1) and the figure reported at end-2007 (2.13), reaching 2.47 in December 2008.

Given the global circumstances, the central bank's prudent regulation policy in recent years was a net advantage, which rendered Romania's banking system stronger than those of other countries. However, looking ahead, banks' financial performance is expected to be lower, given the contraction of lending and the larger provisioning requirements to cover credit risk.

6.3. Measures aimed at improving bank supervision

The transposition of EU standards and regulations into the documents prepared by the Committee of European Banking Supervisors (CEBS) was further a key objective of the National Bank of Romania. The features of 2008 required the strengthening of international co-operation by way of periodical consultations and meetings of the NBR representatives and those of foreign financial supervisory authorities.

Particular emphasis was laid on strengthening co-operation with the authorities in charge of supervising credit institutions that hold the largest market share in Romania, i.e. the Austrian Financial Market Authority (FMA) and the Bank of Greece. Apart from the ten memoranda of understanding on co-operation signed during 2001-2006, a memorandum of understanding was concluded with *Banco de Portugal*, which entered into force in March 2009. Moreover, a memorandum of understanding on co-operation with *Banco de España*, initiated at end-2008, is under negotiation.

The NBR participated in 12 general supervisory colleges, which are permanent and flexible co-operation bodies focusing on the exchange of information with a view to understanding the risk profile of the banking group under supervision, devising supervision plans to avoid the overlapping of supervisory activities, etc. Co-operation within these organisations implies the conclusion of multilateral memoranda of understanding on co-operation with each international group under supervision; so far, two such memoranda were concluded between supervisors (as regards *Crédit Agricole* and *Société Générale*).

Among the key events of 2008 also ranked the assessment of the implementation by the NBR of the 25 principles laid down by the Basel II Accord for an efficient supervision. In November 2008, a team of IMF and World Bank experts conducted such an exercise as part of the Financial Services Action Plan (FSAP). The outcome of the assessment was positive and the conclusion was that most principles had been successfully implemented and almost all the recommendations made by the previous mission had been put into practice.

Another key area for prudential supervision was the monitoring of activity carried out by NFIs, a growing sector, the assets of which accounted for 8.4 percent of GDP in 2008. Financial leasing held a very large share (78.7 percent) in total activities performed by NFIs, slightly down year on year. Monitoring the activity of NFIs included both off-site and on-site inspections, resulting in warnings and sanctions imposed by the NBR.

6.4. Measures aimed at strengthening financial stability

In terms of financial stability, the year 2008 witnessed uneven developments. Until September, the features were similar to those in the prior year: a sound financial system, yet facing increased vulnerability, in the context of a wider current account deficit and of the heavy indebtedness of both households and the corporate sector.

In the final quarter of the year, risks to financial stability increased amid the global financial crisis fallout. Overall, the vulnerability of the banking system rose in 2008, with exogenous factors making a larger contribution than endogenous factors.

The impact of the global crisis on Romania's financial system was also reflected in the temporary disruption of the interbank market to which unfounded rumours that a leading bank might face major strains were added. Against this background, in October 2008, depositors' confidence was shaken. The central bank acted as lender of last resort, in compliance with the provisions of the NBR Statute, granting the respective credit institution, whose solvency ratio stood at an adequate level, a special financing to overcome the temporary liquidity shortages. The loan was repaid according to contractual clauses. Subsequently, the bank in question managed to regain access to market financing, in a competitive environment. The NBR's intervention prevented depositors' nervousness to turn into a phenomenon that would have posed threats to the system.

The analysis of lending to households revealed the prevalence of long-term loans, foreign-currency loans and consumer loans. A key feature of year 2008 was that more than half of new loans were granted with a promotional interest rate, which implies that the impact of a higher debt service will be felt in the coming years. The central bank intervened with a view to moderating the said risks, by taking prudential measures to ensure a more efficient management of risks relative to lending to households.

Preparations for managing potential financial crises are a significant part of the NBR activity in the field of financial stability.

In 2008, the NBR gave particular attention to developing procedures and instruments for financial crisis management in compliance with its legal prerogatives. In this respect, the central bank participated in the organisation of a financial crisis dry-run, conducted half-yearly stress tests focusing on the extreme but plausible shocks that may affect the banking system and prepared a number of documents in the field of contingency planning.

Thus, on 6 February 2008, a financial crisis dry-run was conducted with the participation of representatives of the National Bank of Romania, the Ministry of Economy and Finance, the National Securities Commission, the Insurance Supervisory Commission, the Romanian Private Pension System Supervisory Commission and the Bank Deposit Guarantee Fund. The dry-run simulated a situation in which a bank, Romanian legal entity, would face liquidity shortage as a result of an internal fraud, which would have major negative consequences on Romania's financial system.

Towards the end of the year, the NBR experts participated, along with IMF and World Bank experts, in a stress test aimed at assessing the capacity of the

Romanian banking system to withstand exogenous shocks. The exercise showed that the aggregate solvency ratio might drop from 12.3 percent (before the shock) at end-2008, to 10.6 percent in 2009 and to 9.7 percent in 2010. This prompted the NBR to require some banks' shareholders to increase share capital in order to maintain a comfortable margin of the solvency ratio.

As part of the NBR's role to maintain financial stability, the dedicated departments in the central bank prepared, in 2008, a number of documents including principles and procedures for the management of financial crises, such as: "The contingency plan applicable to credit institutions" and "The list of issues to be addressed in case of contingencies".

A key role in the development of certain coordinated arrangements for managing financial crises in Romania is played by the National Committee for Financial Stability (NCFS), a body whose main objective is to ensure financial stability by promoting a permanent and efficient exchange of information between the authorities in charge of regulation and supervision of different sectors of Romania's financial system and the Ministry of Economy and Finance, as well as to assess, prevent and, where appropriate, manage financial crisis situations at the level of financial institutions, financial groups or the financial market as a whole. In 2008, NCFS focused particularly on the development of the methodological framework for the coordination of financial crisis management operations.

The support offered by the NCFS to the NBR also included the creation, in April 2009, of a financial crisis management department that will play a key role in the development and updating, on a permanent basis, of central bank's procedures in the field, as well as in the laying-out, at European level, of NBR's positions regarding such issues.

6.5. Regulatory measures

As far as credit institutions are concerned, NBR regulations focused primarily on the following issues:

- amending prudential provisions with a view to slowing down credit expansion (NBR Regulation No. 4/2008, NBR Regulation No. 11/2008, etc.);
- properly enforcing the Basel II framework (NBR Regulation No. 3/2008, NBR Regulation No. 5/2008);
- supplementing the access framework for banking activity (NBR Regulation No. 1/2008, NBR Regulation No. 2/2008).

As for the NFI sector, apart from NBR Regulations Nos. 4/2008 and 11/2008, central bank experts also drafted and submitted to Parliament for approval Law No. 93/2009 on non-bank financial institutions.

Regarding the coverage of bank deposits, the NBR has reviewed the legal framework governing deposit guarantee schemes and has initiated a draft law

aimed at transposing Directive 2009/14/EC into the national law by 30 June 2009. Mention should be made that the government has acted in a proactive manner, by raising the coverage level on household deposits to the equivalent in domestic currency of EUR 50,000/depositor even before the European directive was issued.

7. Financial statements of the National Bank of Romania as at 31 December 2008

According to the *acquis communautaire*, the NBR does not pursue the fulfilment of commercial purposes, such as profit maximisation, its actions concerning the implementation of a monetary policy aimed at securing the achievement of its primary objective, namely to ensure and maintain price stability. Thus, in 2001-2006, when inflation could not be curbed in the absence of massive liquidity-absorbing operations, the NBR assumed the costs associated with a tight monetary policy, ending the financial years with operating losses. The central bank's steady efforts to bring inflation down to levels consistent with the definition of price stability and maintaining financial stability, as acknowledged at European level, contributed to the progress of the domestic economic environment towards a full-fledged state, laying the groundwork for the central bank to revert to its creditor position vis-à-vis the banking system – a process accelerated by the sweeping change in international liquidity conditions. In this context, the NBR's financial results improved considerably in 2008, the end-of-year profit (RON 3,338.3 million) being seven times higher year on year. Adding to this was also the steady concern for keeping own operating expenses within the approved budget limits.

Pursuant to Law No. 312/2004 – The Statute of the National Bank of Romania, the distribution of the 2008 profit was entirely aimed at covering the previous years' losses. By also using the profit yielded in 2009 Q1, the NBR managed to cover the previous years' losses in whole, resuming its contribution to the rise in state budget revenues through profit distribution, with an 80 percent share of net revenues. The adjustments for financial year 2009 as concerns the 80 percent share of net revenues transferred to the state budget will be made according to the legal deadline for submitting the annual balance sheet. Thus, the progress of disinflation was warranted by the costs associated with curbing inflation, given that the annual growth rate of consumer prices slowed down from 9.3 percent in 2004 to 6.3 percent in 2008 (December/December).

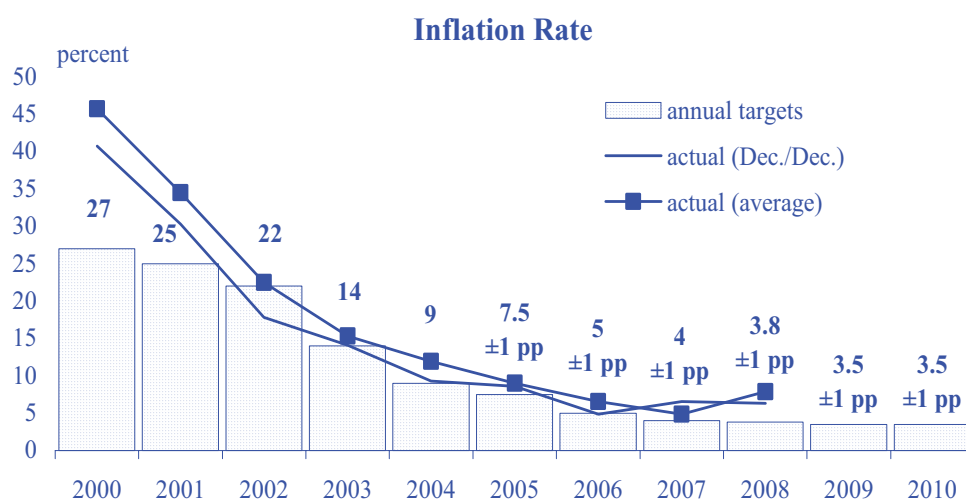
More precisely, the positive total result was induced by the operating profit from management of international reserves (RON 5,498.8 million), which was mitigated by operating losses from monetary policy operations and currency issue (RON 1,124.1 million) and other operations (RON 295.9 million), as well as by losses from revaluation of assets and liabilities (RON 740.5 million). The explanation for the losses from monetary policy operations lies with the central bank's net debtor position vis-à-vis the banking system for the most part of the year. Due to the NBR's shift to a creditor position vis-à-vis the banking system in late 2008, the related losses were about 13 percent lower than in 2007, while favourable conditions were created for their gradual elimination in the years ahead.

Chapter 1. Monetary policy of the National Bank of Romania

Policy objective

In accordance with its Statute¹, the primary objective of the National Bank of Romania is to ensure and maintain price stability; the main task of the central bank is to formulate and implement the monetary policy.

Given the specific conditions of 2008, the major objective of the central bank was to resume and continue the disinflation process in a manner consistent with the achievement of annual inflation targets and to create favourable conditions for curbing the annual inflation rate over the medium term to sustainable levels that are compatible with the definition of price stability. Such a monetary policy stance was in line with the commitments made by the Romanian authorities in terms of the programming documents prepared during the euro adoption process initiated by Romania on 1 January 2007 (the successive issues of the Convergence Programme). Therefore, it fulfilled the requirement of attaining, consistent with the timetable for euro adoption, an inflation rate compatible with the inflation criterion laid down in the Maastricht Treaty as well as with the ECB's quantitative definition of price stability. For the 2-year horizon relevant for monetary policy under the current inflation targeting strategy, the annual targets set by the National Bank of Romania and the Romanian Government for year-end 2008 and year-end 2009 were 3.8 percent ± 1 percentage point and 3.5 percent ± 1 percentage point respectively.



Source: NIS, NBR

¹ Law No. 312/2004

1. Policy challenges

Throughout the year under review, the objective of resuming disinflation and making the annual inflation rate return to a trajectory compatible with the achievement of inflation targets in the short and medium term was a genuine policy challenge. Over the first quarters of 2008, the difficulty of fulfilling this objective was due to the persistence and even strengthening of supply-side and cost-push inflationary shocks in the near run, as well as to the gradual heightening of demand-pull pressures amid the increase in the magnitude and duration of the positive output gap.

The main adverse exogenous shocks were the sharp rise in the dynamics of some volatile food prices and administered prices, along with the faster pace of increase of fuel prices in 2008 H1 and the quicker depreciation tempo of the domestic currency. Against this background, a major reason for the central bank's concern was the risk that the direct inflationary impact of supply-side shocks would translate into large second-round effects, particularly via the worsening of inflation expectations, as well as, implicitly, of the price- and wage-setting behaviour. The latter was aggravated by (i) still lax income policy arising also from the successive election run-ups, (ii) the ongoing demonstration effect of income policy in the public sector, and (iii) the maintenance of labour market tightening.

Another major risk to resuming disinflation was the heightening of demand-pull inflationary pressures given the very fast growth rate of the economy and the steady widening of the output gap. Acceleration of the annual GDP growth rate to 8.2 percent and 9.3² percent in 2008 Q1 and Q2 was almost solely attributable to the swifter rise in domestic absorption. Behind the brisk increase in this aggregate demand component stood the faster pace of increase of investment and final household consumption, propelled by the further quick dynamics of households' and companies' own incomes and of credit to the private sector, as well as by the substantial increase in public spending. Domestic demand dynamics gained momentum and remained very rapid, thus fuelling imports growth which, against the backdrop of further depreciation of the domestic currency, boosted contemporary inflationary pressures. In this context, the trade deficit continued to widen at a fast pace in the first months of 2008, despite the quicker annual dynamics of exports.

In addition, given the circumstances, the successive quarterly forecasting rounds for medium-term macroeconomic developments showed not only a deterioration of the inflation outlook over the monetary policy transmission horizon, but also a relative strengthening of upside risks to inflation under the forecast. The major risks were: (i) wage dynamics overtaking productivity gains, (ii) the likelihood of implementing looser-than-expected fiscal policy, and (iii) a possible continuation of the depreciation trend of the domestic currency. The risk of a weaker leu remained however an almost ongoing concern for the central bank, including from

² Statistical data available at the time of taking the policy decision; some of them were subsequently revised by the NIS.

the perspective of its detrimental impact on financial stability, the more so as the likelihood of this risk to materialise was higher as a result of the lingering tensions in the global financial environment and the delay in the emergence of signs of an improvement in domestic economic fundamentals, which could lift investor sentiment on the prospects of the Romanian economy.

The central bank's firm response to such circumstances consisted in the gradual tightening of interest rate policy (a trend that began in October 2007) meant to counter demand-pull inflationary pressures and re-anchor inflation expectations at levels compatible with the achievement of annual inflation targets in the medium term. Thus, during February-July 2008, the National Bank of Romania raised the policy rate five times, from 8 percent to 10.25 percent. At the same time, in order to enhance the efficiency of such measures, the central bank exerted firm control over money market liquidity and left unchanged the reserve ratios on RON-denominated liabilities (with residual maturity of up to 2 years) and foreign exchange-denominated liabilities of credit institutions at 20 percent and 40 percent respectively. However, as a direct result of fairly strong supply-side shocks, the annual inflation rate stayed on an upward path in 2008 Q1 (reaching as high as 8.63 percent in March), but thereafter remained virtually unchanged until July, when it crept up and stood above the upper bound of the variation band around the central target set for 2008. In August, the annual inflation rate reverted to a downward drift following the considerable slowdown in the growth rate of some volatile food prices – reflecting largely a base effect – and administered prices, as well as the resumption of the appreciation trend of the domestic currency.

The implementation context and, implicitly, the nature of policy challenges shifted significantly in September, when the resurgent turmoil on the world's financial markets turned into a full-scale global financial and economic crisis. On the one hand, during the final months of 2008, the central bank grappled with the risk of still high demand-pull inflationary pressures stemming from the persistence of a very fast GDP dynamics in Q3 and the likely easing of income and fiscal policies in the election run-up of Q4. Adding to this risk were the effects of renewed inflationary pressures from the exchange rate, which reverted to the upward trend and whose volatility augmented noticeably amid the higher risk aversion of foreign investors and the threat of an ensuing worsening of inflation expectations.

On the other hand, calibrating the monetary policy response was more difficult owing to the growing uncertainties surrounding the outlook for world economy and their repercussions on the local economy against the backdrop of broadening and fast deterioration of adverse effects exerted by the deepening of the global financial crisis on the real sector. Adding to this were the temporary strains on the local money market triggered by the global financial turmoil and later on the clear-cut signals of an economic slowdown, the magnitude of which was revealed by the statistical data released in 2009 Q1. The explanation for the turning point in the dynamics of domestic economic activity seen in 2008 Q4 lies with the increasingly pronounced pass-through of the fallout from the broadening and deepening of the global economic crisis via foreign trade and financial channels. As a result,

external demand for Romanian-made goods plummeted and local companies faced less readily available and costlier financing from both domestic and foreign sources. Nevertheless, the incipient stage of the global economic and financial crisis, along with the frequent downward revisions to economic activity forecasts in industrialised countries, complicated the attempts at projecting the pace and magnitude of the contagion effects on the Romanian economy.

Given the circumstances, the NBR Board decided to discontinue the upturn in the policy rate and keep the key rate unchanged at 10.25 percent per annum in 2008 Q4. The decisions taken in the run-up to year-end were meant to strike a balance between the tighter real broad monetary conditions accompanying the return of inflation to a downward path in order to attain disinflation objectives in the medium term and the caution required in view of the new threats to macro-stability. At the same time, the central bank tailored its monetary policy instruments to the newly-created context of an ongoing gradual reduction in excess liquidity of banks and their switch to a net debtor position since October 2008; the reserve requirements ratio on leu-denominated liabilities of credit institutions was lowered from 20 percent to 18 percent, and a more flexible liquidity management was pursued in a move aimed at ensuring smooth functioning of the interbank money market and, implicitly, adequate conditions for sustainable financing of the economy.

The sharp increase in the RON exchange rate in December 2008 and the risk of depreciation pressures to persist amid the still high current account deficit and the substantial widening of the fiscal deficit in an international environment fraught with growing risk aversion and stronger financial deleveraging were the major reasons for leaving unchanged the policy rate in January 2009 as well. Maintenance of a restrictive monetary policy stance was aimed at supporting an orderly unwinding of macroeconomic imbalances and achieving the medium-term inflation targets in a sustainable manner. The fast weakening of the leu towards the end of 2008 stymied disinflation considerably and the annual inflation rate stayed significantly above the upper bound of the variation band of ± 1 percentage point around the 3.8 percent central target. Nevertheless, in December 2008, inflation rate ran at 6.30 percent as against 6.57 percent in the year-earlier period.

Throughout the year, the National Bank of Romania enhanced its communication activity. The central bank steadily emphasised the risks to the inflation objective and to the confidence in the outlook for the Romanian economy stemming from a potential fiscal policy easing and from real wage dynamics further overtaking productivity gains. In this context, the central bank reaffirmed the fact that in order to ensure sustainable disinflation and anchor medium-term inflation expectations not only calls for retaining monetary policy restrictiveness through an appropriate dosage of its instruments, but also requires strong support from the other components of the macroeconomic policy mix, as well as from structural reforms. The need to tighten income and fiscal policies has become a must against the background of the escalating global financial and economic crisis and the beginning of external imbalance adjustment – this is essential for restoring foreign

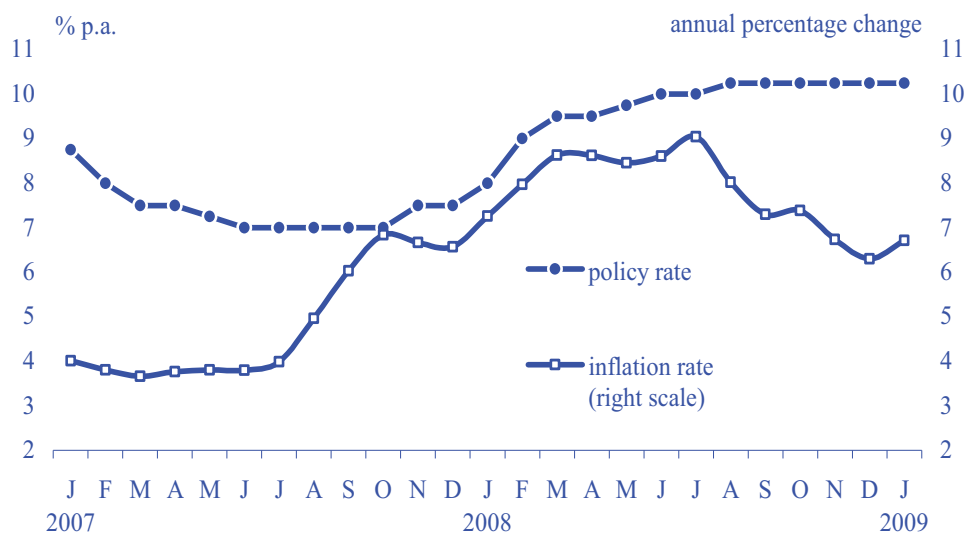
investors' confidence in the outlook for the Romanian economy and, implicitly, for minimising crisis-related economic and social costs at local level.

2. Policy implementation

The resurgence of inflation as a result of powerful economic and financial shocks on world markets and at domestic level, especially the brisk deterioration of medium- and short-term inflation outlook – due to the projected increase in excess demand and unfavourable effects of supply-side factors –, along with the heightening inflationary threats, prompted the National Bank of Romania Board to raise the policy rate in several successive moves during 2008 H1. The trend that had been initiated by the 0.5 percentage point-hikes of the key rate in October 2007 and January 2008 was followed by five consecutive increases totalling 2.25 percentage points; these moves were implemented in a descending order (between 1 percentage point and 0.25 percentage point) during February-July 2008, taking the policy rate to 10.25 percent. The rate-hiking campaign was subsequently discontinued and the policy rate was left unchanged until January 2009, as inflation reverted to the upward path and the uncertainties surrounding its outlook augmented amid the deepening and broadening of the global financial and economic crisis. In order to ensure restrictive broad monetary conditions, the central bank kept in place tight reserve requirements and pursued firm liquidity management on the money market. Moreover, the NBR took additional prudential measures in the financial sector, including higher provisioning for foreign currency-denominated loans extended by credit institutions to unhedged borrowers and broadening their scope to non-bank financial institutions.

The National Bank of Romania performed higher policy rate increases in February and March 2008 (by one percentage point and half of a percentage point respectively) largely as a result of the worsening of the projected annual inflation rate trajectory and its staying above the upper bound of the variation band around the central target. The upward revision of the inflation forecast was due basically to the larger-than-expected rise in consumer price dynamics at end-2007 and the projected increase in the magnitude and/or duration of inflationary effects arising from negative exogenous shocks, namely the severe 2007 drought, costlier food and fuels on world markets and higher administered prices. Other major determinants of the deteriorating inflation outlook were the relative increase in expectations on the RON/EUR exchange rate and the ongoing upward revision of the magnitude and duration of the forecasted output gap. The decision was based on the faster-than-expected economic growth in 2007 Q4, the protracted strong dynamics of both household income and credit to the private sector, as well as the significant rise in public spending at end-2007. The firm response of the central bank was also driven by the threat of a treacherous wage-price spiral taking shape and by the likelihood of: (i) second-round effects stemming from the impact of supply-side shocks; (ii) a relative fiscal policy easing in the run-up to the elections, and (iii) higher exchange rate volatility amid the persistent tensions on financial markets worldwide.

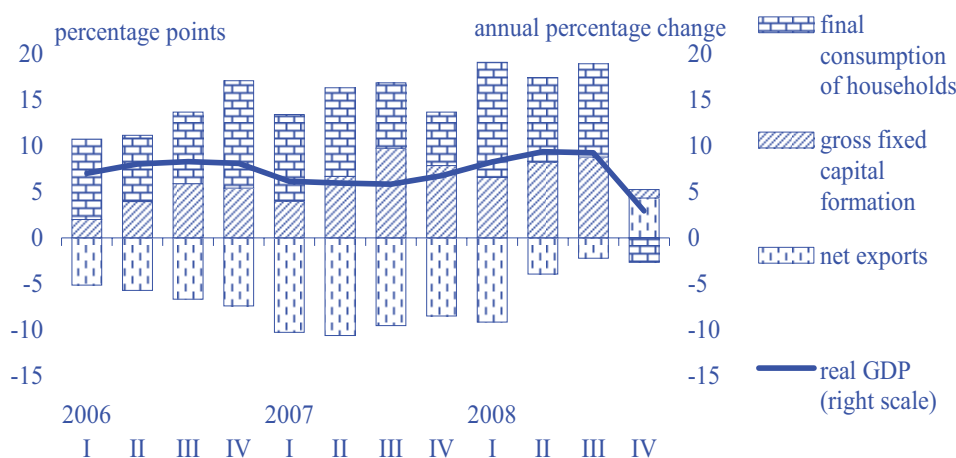
Policy Rate and Inflation Rate



Source: NIS, NBR

The further worsening of the inflation outlook and, implicitly, the repeated delays in the projected annual inflation rate falling back inside the variation band around the medium-term target led the NBR Board to raise again the policy rate in May, June and July 2008; the adjustment pace was contained to 25 basis points given that updated forecasts and assessments performed back then showed a relative slowdown in the upturn of the projected annual inflation rate trajectory. Inflation forecasts were updated again, due to the increase in the expected magnitude of administered price adjustments and fuel price dynamics, on the one hand, and the escalating size and duration of the projected positive output gap, on the other hand. The rise in the inflationary potential of demand was confirmed by the release of statistical data showing a much faster annual GDP expansion in 2008 Q1 (to 8.2 percent from 6.6 percent in 2007 Q4). This owed to the robust surge in domestic absorption (at an annual rate of increase of 15.9 percent) driven by the persistent upturn in investment dynamics, but especially by the renewed growth of actual final household consumption on the back of a strong increase in incomes (wages in particular) and loans to households. The accelerated advance in domestic absorption entailed not only a record increase in the dynamics of imports of goods and services which – together with the ongoing depreciation of the leu against the euro – boosted contemporary inflationary pressures, but also caused the trade deficit to widen at a faster pace in the first part of 2008. In addition, the inflationary potential of the then-existing macroeconomic environment was also fuelled by higher inflationary risks, especially those stemming from wage dynamics still overtaking productivity gains, the likely implementation of looser-than-expected fiscal policy, and an additional increase in inflation expectations.

Contribution of the Main Demand Components to GDP Growth



Source: NIS, NBR calculations

In September 2008, the NBR Board discontinued the series of successive policy rate hikes and kept the key rate at 10.25 percent per annum. The decision was substantiated by the disparity relative to the developments in key macroeconomic variables, i.e. the resumption of disinflation (the annual inflation rate dropped to 8.02 percent in August from 9.04 percent in July) and ongoing pick-up in economic growth in Q2, as well as by greater uncertainties surrounding the performance of such variables amid the renewed financial turmoil worldwide. Risks to disinflation remained prevalent, the most dangerous being a potentially higher deviation of the positive output gap and, implicitly, of demand-pull pressures, despite the positive supply-side effects following the considerable rise in farming output in the summertime. Such a risk was aggravated by the increased likelihood of an income and fiscal policy easing in the election run-ups and during the elections, which would have resulted in faster expansion of domestic consumption and worsening of inflation expectations. Therefore, the NBR Board's decision was aimed at further tightening broad monetary conditions – by expanding the real margin associated with interest rates – and anchor inflation expectations on consumer price developments in the medium term. Another reason to leave the policy rate unchanged was represented by the heightened uncertainties relating to short-term economic and financial developments in the context of the broadening of the global financial crisis; against this backdrop, the potentially contractionary effects on the local economy, as a result of the slowing growth in the USA and the euro area, are expected to feed through with a certain lag, mainly via higher costs and a likely reduction in the dynamics of external financing, especially bank financing.

The subsequent slowdown in actual and expected short-term disinflation, on the one hand, and the unprecedented increase in uncertainties surrounding the forecast of economic developments amid the still broadening global financial crisis, on the other hand, led the NBR Board to decide, in its October meeting, on a status quo as far as the policy rate was concerned. Apart from the persistence of demand-pull inflationary pressures in 2008 Q3, the central bank's serious concerns also

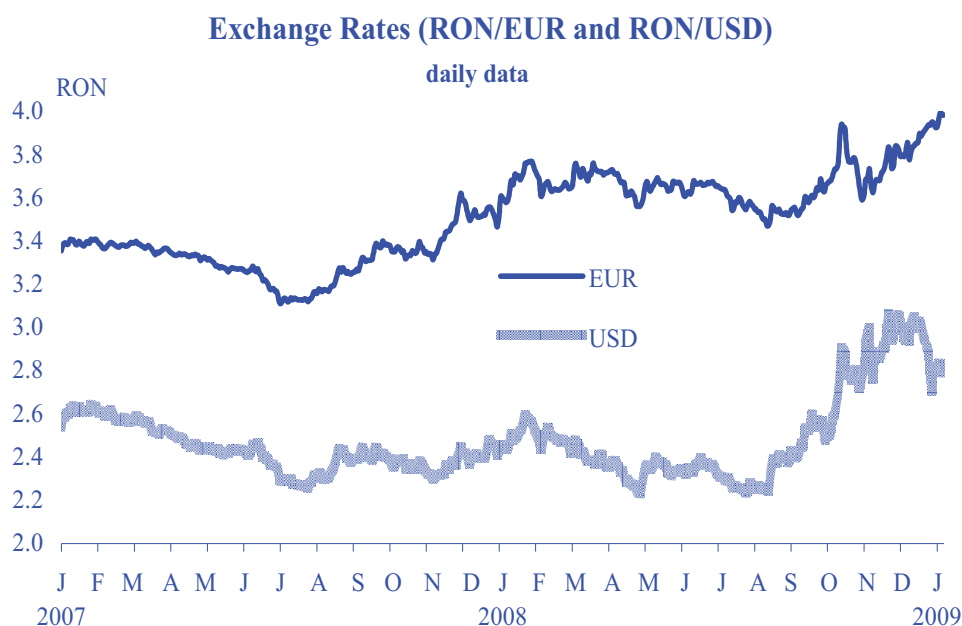
encompassed the envisaged larger adjustment of administered prices and the exchange rate resuming the upward trend in September, alongside its heightened volatility. At the same time though, given the anticipations of knock-on effects from the deepening of the global financial crisis on both international and local real sectors, the identified risks of inflation deviating upwards or downwards from the projected trend became relatively balanced. Thus, the risk that inflation could exceed the projected level due to the likelihood of wage increases overtaking productivity gains as well as to potentially stronger easing of fiscal policy was countered by the risk of faster deceleration in inflation against the background of a possibly slower-than-expected growth following the broadening of the global economic crisis. In October, the NBR Board also decided to lower by 2 percentage points the reserve requirements ratio on leu-denominated liabilities of credit institutions³, given that the net liquidity position of banks had shifted to a deficit.

In the Board meeting of 6 January 2009, the policy rate was left unchanged at 10.25 percent per annum. The chief driver behind this decision was the risk of persistence of inflationary pressures arising from the weaker domestic currency and the stronger exchange rate volatility against the background of broader, more protracted fallout from the global economic and financial crisis, and from the gradual adjustment of external and domestic imbalances of the Romanian economy. The softer leu in euro terms, broadly in line with the developments seen in the currencies of other emerging economies, was chiefly triggered by investors' renewed risk aversion and wariness that took shape at the end of 2008 Q3. The state-of-affairs on the financial markets in these economies was compounded over the period by the deteriorating picture in Iceland, which underscored the increased risk of massive capital outflows in the countries facing major macroeconomic imbalances. In this context, the reasons pertaining to the high magnitude of the balance-of-payment current account deficit and of budget deficit, combined with the banking system reliance on external financing, caused investors to place Romania and its regional peers into the group of economies with relatively higher vulnerability. The new worsening of investor sentiment, also confirmed by the downgrades in Romania's sovereign risk rating, put more downward pressure on the domestic currency. As a result, the annual inflation rate dropped at a slower pace in the run-up to year-end, reaching 6.30 percent in December, still above the upper bound of the variation band around the 3.8 percent central target.

By contrast, analyses for that period revealed a relative decline of risks to inflation due to the evolution of aggregate demand given that the positive output gap could have closed at a faster pace in 2008 Q4, though it had been running high in the previous quarter due to the still brisk acceleration of annual economic growth (9.2 percent). However, the magnitude of the expected GDP dynamics slowdown and especially the pace of decline of demand-pull inflationary potential were difficult to assess given the heterogeneity of recent developments in relevant indicators on aggregate demand, consumer demand in particular, and the uncertainties surrounding knock-on effects from the global economic crisis. Thus, the macroeconomic environment at the beginning of 2008 Q4 was characterised by

³ Starting with 24 November – 23 December 2008 maintenance period.

further strong dynamics of the real net average wage and, most notably, expectations of a wider-than-projected budget deficit, on the one hand, and the marked slowdown in the annual growth rate of retail trade turnover, the faster reduction in the year-on-year real dynamics of loans to households and the significant setback in annual dynamics of both household deposits with banks and key monetary aggregates, on the other hand.



The slowdown in household credit growth⁴ became more pronounced in 2008 H2, after staying on an upward path in January-February and declining slightly in March-June (to 63.3 percent at mid-2008 as against 70.9 percent at end-2007). In 2008 H1, the developments in loans to households were ascribed to the combined effect of stimulative factors on both demand for and supply of loans (still strong bank competition and further rapid increase in household incomes) and to the emergence and/or enhancement of contractionary factors such as (i) higher lending rates for some of the new business, (ii) the likelihood of low-income households reaching a peak in their indebtedness ceiling, (iii) the coming into force of higher provisioning for foreign currency-denominated loans⁵, (iv) costlier financing resources provided by parent undertakings and (v) ongoing transfer of some loans abroad. Subsequently, the constraint on the loan supply became stronger following the less readily available external financing, amid the global crisis, and the dwindling excess liquidity across the banking system; adding to these was the impact of increased wariness of credit institutions, as reflected by the tightening of lending terms and standards (partly as a result of NBR Regulation No. 11/2008⁶

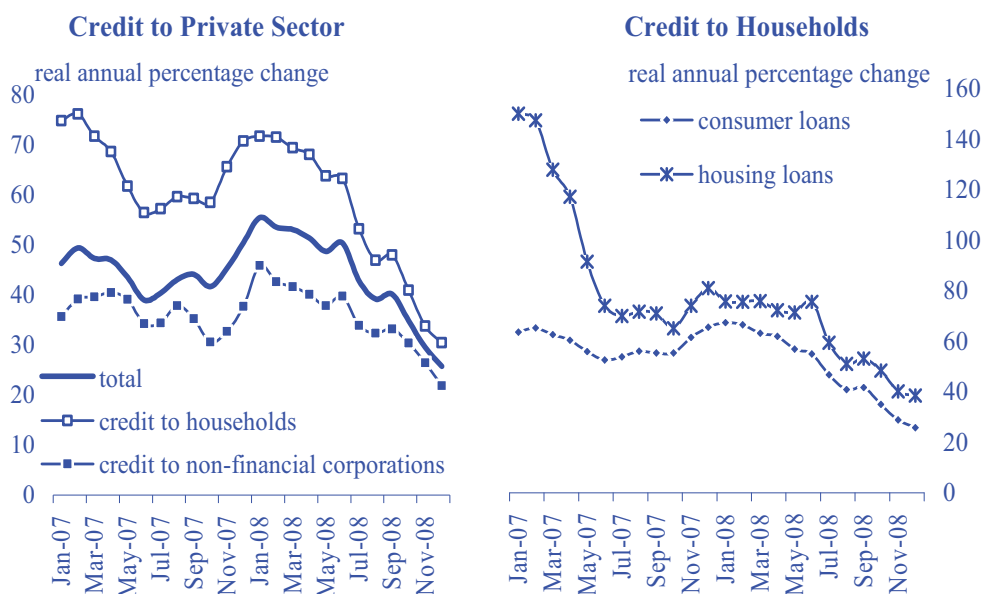
⁴ Unless otherwise indicated, the growth rates are annual percentage changes.

⁵ Regulation No. 4/2008 amending and supplementing Regulation No. 5/2002 on the classification of loans and placements as well as the setting-up, regularisation and use of specific provisions for credit risk and the methodological notes issued for its implementation.

⁶ Regulation No. 11/2008 amending and supplementing Regulation No. 3/2007 on containing credit risk attached to loans to households, effective October 2008.

taking effect), also in the context of heightening adverse selection risk, and the flight to safety, namely government bonds and, to some extent, foreign assets. In its turn, demand for loans was increasingly affected by the marked hike in lending rates on new business (unexpectedly high in some cases) and on the loans in progress, as well as by the softer leu and stronger uncertainties surrounding the future path of the exchange rate.

Against this background, the advance in loans to households slowed to a 7-year low of 30.5 percent in December 2008, at a rate faster than that of corporate loans (the annual growth rate of which shed 14.2 percentage points year on year to 21.3 percent). The bright spot in terms of the breakdown by purpose of loans to households was provided by the relatively faster decline in consumer credit dynamics (to 25.8 percent); consequently, at year-end 2008, consumer credit accounted for 74.3 percent of total loans to households, down 2.8 percentage points over the year before.

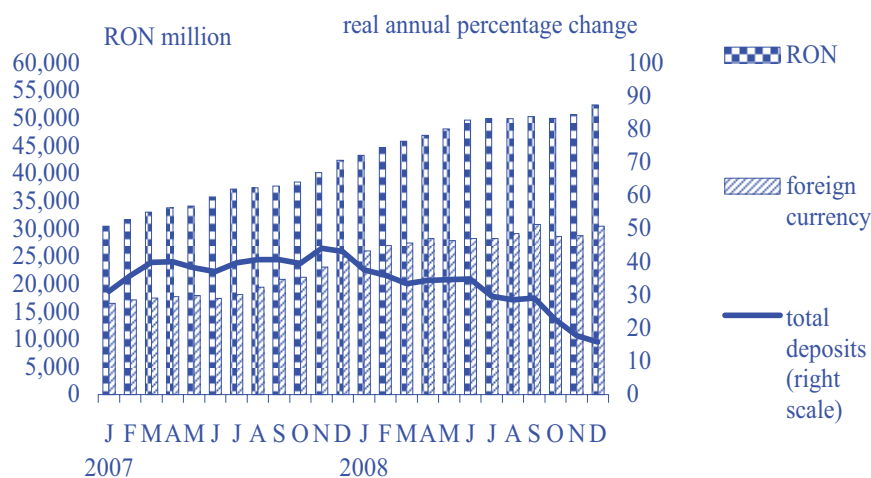


The successive policy rate increases coincided with the gradual decrease in the threat posed by the substitution of domestic currency-denominated loans with forex ones; starting February, the annual dynamics of foreign currency-denominated loans declined steadily to reach 39.1 percent in December 2008, more than three times slower than a year earlier. This development was also due to the sharp cut in the growth rate of loans denominated in Swiss francs (housing and consumer loans), as banks relinquished almost entirely to granting such loans towards year-end. Nevertheless, foreign currency-denominated loans saw their share in total household credit widening as a result of faster growth rates of such loans in comparison to leu-denominated ones and the statistical effect induced by the weaker domestic currency.

Policy rate decisions also took into account the need to counter the trend towards a weaker propensity to save, which had begun in 2007 H2 and became more

pronounced in early 2008, amid the still rapid dynamics of consumption and prices, as well as the heavier servicing of loans. Thus, the annual growth rate of households' time deposits in domestic currency with maturity of up to two years slowed faster and even entered negative territory in July (-0.6 percent from 8.7 percent at end-2007), despite the uptrend in deposit rates on new business. The dynamics of such deposits regained momentum, albeit unevenly, reaching 5.6 percent at end-2008 – this performance was partly in line with the significantly higher rates on deposits of credit institutions given the keener competition for resources. The latter occurred against the backdrop of a reduction in excess liquidity across the banking system and the less affordable external financing of credit institutions in particular. By contrast, the dynamics of households' overnight deposits in domestic currency slowed almost throughout the entire period under review, especially in the run-up to year-end (down to 30.2 percent in December 2008 from 117.2 percent in 2007). In turn, the year-on-year expansion of total household deposits in foreign currency was broadly stable only in the early months of 2008, but thereafter it decelerated considerably. As a result, the rate of increase of total household deposits witnessed a downward drift in the reported year, falling 27.3 percentage points year over year to 15.8 percent in December 2008.

Household Deposits

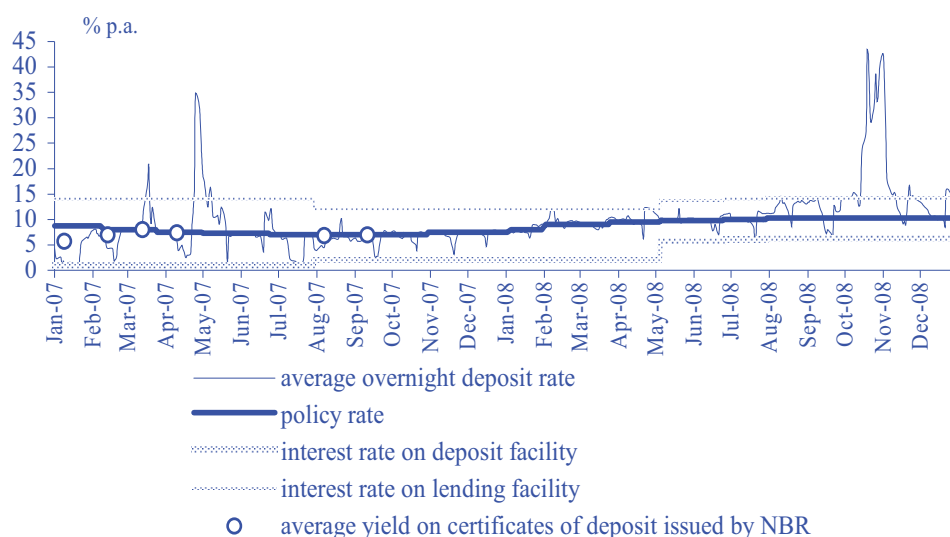


3. Use of monetary policy instruments

In 2008, the NBR's capability of making active and flexible use of the components of the monetary policy operational framework specific to inflation targeting was frequently resorted to. This occurred amid the faster unfolding of the gradual reduction in excess liquidity, as the central bank switched to a net creditor position vis-à-vis the banking system in Q4, concurrently with the pronounced intensification of the global financial turmoil since September.

However, the shift followed three quarters when the central bank was, over most of the period, a net debtor vis-à-vis the banking system; in January-September 2008, in order to enhance the efficacy of policy rate hikes, the NBR pursued firm money market liquidity management. The gradual reduction in excess liquidity and the short-lived wide fluctuations in autonomous liquidity factors prevented banks from purchasing certificates of deposit issued by the central bank⁷, so that absorption of excess reserves consisted usually in deposit-taking operations carried out via fixed rate tenders at which the NBR acted as rate taker. Adding to the regular deposit-taking operations were ad hoc operations with shorter maturities, especially earlier in the year, aimed at mopping up the Treasury's massive liquidity injections performed at end-2007.

Interbank Money Market Rates



Over the period, the monetary authority made several changes to its operational framework for monetary policy implementation. In order to increase the efficiency of money market liquidity management and implicitly steer short-term money market rates with the support of its monetary policy instruments, the central bank shortened the maturity of standard deposit-taking operations from 2 weeks to 1 week starting May 2008. At the same time, with a view to improving the transmission of monetary policy signals and reducing the scale of fluctuations in interbank market rates, a symmetrical corridor of no more than ± 4 percentage points⁸ around the policy rate for the interest rates on NBR's deposit and lending facilities was set up.

A more substantial adjustment, with a de facto nature, of the operational framework was implemented in 2008 Q4 when, amid the ongoing decline in excess

⁷ CD tenders were held until July 2008, but the NBR no longer issued such instruments throughout the year (the last CD issue was launched in September 2007).

⁸ In May, the interest rate on the deposit facility was raised to 5.75 percent from 2 percent and the interest rate on the lending facility was lifted to 13.75 percent against 12 percent, whereas the policy rate stood at 9.75 percent.

liquidity across the banking system, credit institutions' net liquidity⁹ turned negative. Against this background, for the first time over the last decade, cash injections came to the forefront, being most frequently resorted to in managing liquidity and steering money market rates. Hence, the NBR resumed the net creditor position vis-à-vis the banking system starting October.

This transition was not smooth at all, given that such a structural change – likely to fuel banks' uncertainties surrounding current liquidity conditions and their prospects in the near run – overlapped with sizeable woes on some financial market segments. During October – November 2008, the interbank money market was temporarily afflicted by the fallout from the global crisis such as banks' confidence crunch, the most likely downward adjustment of their exposure limits, and the increase in non-residents' speculative demand for domestic currency. As a result, in early October, interbank rates shifted to the upper half of the corridor set by interest rates on lending and deposit facilities and subsequently rose abruptly and remained at very high levels until early November. The short-lived market dysfunctions also affected ROBOR, which surged to unexpectedly high levels and outran by far the actual interest rates on transactions. The risk of these rises feeding through into lending rates – which had started to materialise – made the central bank amend the rules for determining such rates by introducing the possibility to temporarily suspend the publication of those indices calculated based on participants' quotations if they exceed by more than 25 percent the interest rate on the lending facility¹⁰. Yet another uncertainty source for market tensions was the highly unpredictable behaviour of the general account of the Treasury in the run-up to year-end, against the background of the unprecedented rise in the public authority's resort to deposit-taking operations on the money market in order to finance the considerable increase in government expenditures, thereby making the future evolution of liquidity conditions even less certain.

The NBR sought to ensure adequate functioning of the interbank money market in such an intricate context. Consequently, it tailored the liquidity management process by providing funds via the lending facility, foreign exchange swaps and repo transactions. At end-October, the NBR lowered the minimum reserve requirement ratio on leu-denominated liabilities of credit institutions to 18 percent, from 20 percent previously, starting with the 24 November – 23 December 2008 maintenance period. Against this backdrop, market tensions eased gradually, with short-term interest rates reverting to levels closer to the policy rate. In order to reinforce the favourable trends, the NBR decided in January 2009 to make active recourse to open market operations for managing liquidity. This measure was meant to ensure smooth functioning of the interbank money market and implicitly foster the ongoing financial intermediation.

The central bank's switch to the net creditor position vis-à-vis the domestic banking system could not rule out the emergence of sporadic excess liquidity

⁹ Credit institutions' net liquidity = excess liquidity – credit institutions' required reserves.

¹⁰ In this case, ROBID/ROBOR rates across the entire maturity spectrum are set at the level of interest rates on the deposit/lending facility.

which was soaked up via resorting to either the deposit facility or deposit-taking operations. The liquidity thus absorbed was relatively small in volume, far below the level of cash injections.

The gradual retrenchment in excess liquidity and the ensuing switch in central bank's position vis-à-vis the banking system weighed on the developments in the volume of the monetary authority's operations, i.e. open market operations and banks' resort to the standing facilities. The daily balance of sterilisation operations January through September fell on average by 65 percent over the year before. As a result, the costs associated with the National Bank of Romania's liquidity management decreased to 0.04 percent of GDP from 0.16 percent of GDP in 2007.

4. Policy guidelines

The monetary policy pursued by the National Bank of Romania will further be implemented under the inflation targeting framework. It will be geared towards consolidating disinflation and ensuring the decline in medium-term inflation rate to levels in line with the ECB's definition of price stability. The annual inflation targets over the monetary policy transmission horizon were set at 3.5 percent ± 1 percentage point for both 2009 and 2010.

The necessary steps for laying-down and setting the inflation target for 2010 were initiated by the NBR Board during the period prior to drafting the May 2009 Inflation Report. Following the assessment of various projection scenarios and of the uncertainties surrounding the updated forecast of macroeconomic indicators, policymakers opted for keeping the 2010 inflation target at 3.5 percent ± 1 percentage point, thus confirming the working assumption announced previously.

The major reason underlying this option was the pressing need to attain the inflation target in 2010. This is instrumental for preserving central bank credibility and, implicitly, for firmly anchoring inflation expectations given the overshooting of the annual targets over the past two years due to a string of powerful exogenous shocks occurring successively or concurrently. In addition, to attain a more ambitious target in a sustainable manner in 2010 is difficult in view of the outlook for persistently adverse effects of external imbalance adjustment and the substantial uncertainties surrounding the duration and magnitude of the economic downturn. The National Bank of Romania's cautious approach to setting the 2010 inflation target was also substantiated by the predictable persistence, over the next years, of direct inflationary effects from factors outside the central bank's sphere of influence, of which the following deserve mention: (i) adjustment of administered prices and indirect taxes, (ii) resumption of convergence of the Romanian economy, including price level convergence after a period marked by a synchronised economic downturn, and (iii) the lingering asymmetric nominal rigidities. At the same time, the current level of the inflation target is regarded as further fulfilling the requirement to consolidate disinflation in a sustainable manner and achieve, consistent with the timetable for euro adoption, an inflation rate in

line with the inflation criterion laid down in the Maastricht Treaty and the ECB's quantitative definition of price stability.

Consolidation of disinflation at a pace compatible with the aim of achieving end-year inflation targets further poses a challenge to monetary policy. In view of the particular features of 2009, the threat arises basically from the need of an ongoing orderly adjustment of macroeconomic imbalances and the requirement of preserving financial stability in an environment hit by the severe global financial and economic crisis. Thus, ensuring sustainable disinflation, while avoiding the undermining of the growth potential in the medium term, is conditional upon rebalancing and enhancing coherence and credibility of the macroeconomic policy mix as well as upon speeding up the implementation of structural reforms. This calls for the significant tightening of income and fiscal policies so as to allow a gradual removal of the overburdening of monetary policy and a conduct fitting the developments in both real and financial sectors of the local economy, which have been increasingly affected by the fallout from the global crisis in early 2009.

Under these conditions, the ever clearer outlining of a downturn in the Romanian economy and the ensuing deceleration in inflation at a pace that is expected to be consistent with attaining the inflation target in the medium term led the central bank to initiate a cautious easing of monetary policy in February 2009. Against this background, the policy rate saw a marginal lowering of a quarter of a percentage point to 10 percent per annum. The fading bout of inflation that occurred in 2009 Q1 as a result of the weaker leu and the frontloaded implementation of the hike in excise duties on tobacco products allowed the consolidation of this easing in May, when the policy rate was reduced by half of a percentage point and the minimum reserve ratio on foreign currency-denominated liabilities with residual maturity of over two years¹¹ was cut down to zero. The major reasons underlying these decisions taken by the NBR Board, thereby creating favourable conditions for disinflation to proceed in a sustainable manner, consisted in the faster adjustment of the external imbalance in early 2009, followed by the shaping of a relative exchange rate stabilisation and the potential implementation of tighter fiscal and income policies, according to the commitments assumed by the authorities under the multilateral financing arrangement concluded with the IMF and the EU. Furthermore, the balance of risks associated with the inflation outlook, while largely remaining in equilibrium, implies a moderately higher likelihood of inflation deviating downwards, rather than upwards, from the forecast coordinates, in spite of the still high uncertainties surrounding the future macroeconomic developments.

From this standpoint, and considering the broader perspective of an ongoing adjustment in broad monetary conditions, the reduction in key monetary policy rates is expected to proceed gradually. This decline will be in line with the fading inflationary pressures from aggregate demand arising from the widening of the

¹¹ The measure was decided in the NBR Board meeting of 31 March 2009 and came into force in the 24 May - 23 June 2009 maintenance period.

negative output gap in the near run and the sharper trend of the relative stabilisation of the exchange rate of the leu, as well as an improvement in inflation expectations.

The substantial increase in the economy's financial depth seen in the past few years and most notably the likely reduction of domestic credit denominated in foreign currency at a relatively quicker pace – following still tight access of banks to external financing, along with the unfavourable general sentiment regarding such loans – are anticipated to act as a catalyst in helping the interest rate play a greater role within the monetary policy transmission mechanism. In the period ahead, this will be underpinned by the continued tailoring of the monetary policy tools available to the NBR in order to capitalise upon their efficacy and strengthen central bank's creditor position vis-à-vis the domestic banking system. An essential role within the monetary policy operational framework will play open market operations aimed at providing liquidity, with the support of enhanced functions traditionally performed by minimum reserve requirements in domestic currency. The central bank has committed to adequately managing liquidity in the banking system so as to ensure smooth functioning of the interbank money market, together with a relative stabilisation of interbank rates around the policy rate, and implicitly the necessary conditions for a sustainable reinvigoration of financial intermediation.

Chapter 2. Financial stability, regulation and prudential supervision

1. Financial stability

1.1. Main assessments on financial stability

In terms of financial stability, year 2008 witnessed uneven developments. Until September, the features were similar to those seen in the prior year: a sound financial system, yet facing increased vulnerability, in the context of a wider current account deficit and a heavy indebtedness of both household and the corporate sectors. In 2008 Q4, financial stability worsened against the deepening of the global financial crisis. Overall, the financial system vulnerability moved up in 2008, due to exogenous factors rather than endogenous ones. In this context, a corrective response from monetary and prudential policies was imperative.

Internationally, year 2008 marked the deepening of the crisis unleashed a year earlier. At an early stage, the financial crisis affected mainly the developed economies. Following the bankruptcy of Lehman Brothers Investment Bank, risk aversion translated swiftly towards emerging economies, spreading to Central and Eastern European countries. Market sentiment increasingly impacted spreads on foreign borrowings and the exchange rates in the Central and Eastern European countries. The widespread contagion and this region lying in a high risk area had adverse effects on Romania as well. Under these conditions, the restoration of public confidence in the light of favourable prospects for this region is vital.

In 2008 H2, external financing conditions deteriorated markedly in term of ready availability and costs. Moreover, some rating agencies contributed to the worsening of investor sentiment regarding Romania's sovereign risk (below investment grade¹, which entailed the rise in financing costs for domestic debtors.

The impact of the global financial turmoil on Romania's financial system was also manifest in the emergence of interbank market disruptions. The situation worsened at the rumours that a leading bank might face major strains. Against this background, in October 2008, depositors' confidence was shaken, which led to a run on some banks in October. The phenomenon affected all the banks in the system, irrespective of size and legal status (branch/subsidiary) of the banks. The type of ownership appears to have influenced depositors' sentiment. With a view to helping restore public confidence, the central bank acted as lender of last resort, in compliance with the provisions of the NBR Statute, granting the respective credit institution, whose solvency ratio stood at an adequate level, a special financing to

¹ The perception regarding Romania is mixed: two rating agencies (Standard&Poor's – quotation BB+ and the negative outlook of October 2008, and Fitch – quotation BB+ and the negative outlook of November 2008) assess Romania's country risk as higher (below *investment grade*); two other agencies (Moody's – quotation Baa3 and the stable outlook of October 2006, and JCRA – quotation BBB- of December 2008) assess Romania's country risk to be similar to the *investment grade*.

overcome the temporary liquidity shortage. The loan was repaid according to contractual clauses. Subsequently, the bank in question managed to regain access to market financing, in a competitive environment. The NBR's intervention prevented depositors' nervousness from turning into a phenomenon that would have posed threats to the system.

The domestic macroeconomic environment was generally favourable to financial stability. Nevertheless, the lax income policy and the wide fiscal deficit in the final part of 2008 weighed heavily on the financial system's capacity to absorb shocks.

In 2008 H1, the NFC sector enjoyed a sound financial position, with financial indicators showing comfortable levels and an adequate loan repayment behaviour. However, towards the year-end, the capacity to pay the debt service deteriorated in the context of: (i) the global economic crisis with adverse effects on domestic and external demand, which depressed companies' cash inflows and (ii) tighter lending standards, which entailed the emergence of risks associated with refinancing of matured debt. As a result, banks' overdue loan ratio for the corporate sector stepped up.

The risk premium for Romanian companies increased in the final months of 2008. This development was attributable to the worsening of overall economic conditions rather than idiosyncratic factors, as the difference between the risk premium associated with the Romanian companies and that associated with the European companies remained unchanged (except November, when investor sentiment regarding emerging economies deteriorated).

The household sector was also affected by financial stability-related tensions. The net debtor position to the banking sector widened, with currency risks posting the highest levels. The growth rate of loans to households slowed down and their volume exceeded that of corporate loans (without however taking into account the effect of loan outsourcing). Foreign currency-denominated consumer loans with long maturity prevailed. A key feature of 2008 was that more than half of new businesses were loans with promotional interest rates, which implies that the impact of a higher debt service will be felt in the coming years. The overdue loan ratio saw a twofold increase, with foreign currency-denominated overdue loans showing the fastest dynamics. The default behaviour is more frequent relative to small value uncollateralised consumer loans. The mounting currency, interest rate or income risks might have a heavy impact on the capacity to service debt. The central bank intervened with a view to moderating the said risks, by taking prudential measures to ensure a more efficient management of risks associated with loans to households.

The household and corporate sectors diversified their financing sources in 2008. Domestic banks were still the main resource providers (66 percent of total), and the external and NFI sectors strengthened their positions. Thus, foreign creditors accounted for roughly 21 percent, with the corporate sector benefiting almost exclusively of this type of financing, while NFIs provided 13 percent of total

financial indebtedness of the household and corporate sectors, the bulk of resources being channelled towards companies (77 percent). At end-2008, overall indebtedness of the household and corporate sectors totalled about RON 300 billion, accounting for around 60 percent of GDP. Structural analysis shows that foreign borrowings remained in the lead (70 percent), avoidance of abrupt swings in the exchange rate being essential for maintaining financial stability. In terms of maturity profile, medium- and long-term debt held 78 percent of total. This situation is detrimental to the households that took consumer loans given that their wealth was negatively affected as the value of the assets acquired depreciates (wear and tear as well as obsolescence) at a much faster pace than that of loan repayment. To this adds the large drop in asset prices over the previous period.

The banking sector, the main component of Romania's financial system, posted a relatively unchanged structure in 2008. The concentration degree was moderate, as illustrated by the Herfindahl-Hirschmann² index and further followed a downtrend amid alleviation of the aggressive behaviour of the top five market players. The tendency to expand the territorial network and the staff numbers slowed down due to the global crisis.

Recent developments on international markets continued to generate significant changes in the balance sheet of credit institutions, with a heavy impact on the volume and structure of resources as well as the investment policy. Deposits taken from companies and households, slightly on the wane, remained the main financing source of Romanian banks, while foreign liabilities followed an upward path until November 2008, subsequently declining. Deposits taken from the interbank market and the government sector further held small shares in balance sheet liabilities and at end-2008 the interbank money market started to cool. Bank placements were mainly oriented towards the domestic market, preponderantly in the form of non-government credit (about 50 percent was destined to households), the dynamics of which slowed down markedly in 2008 Q4, in favour of government securities.

The Romanian banking system remained adequately capitalised, but the fallout from the global financial crisis was felt towards end-2008, in particular as regards the external liquidity channel and the worsening of the macroeconomic conditions. Nonetheless, in 2008 as a whole, all credit institutions reported solvency levels higher than the minimum solvency ratio according to the regulations in force. A positive development is the deceleration of the downward trend in the solvency ratio compared to the previous years, against capital increases by the shareholders of credit institutions and the slowdown in non-government loans. The results of stress tests for end-2008 conducted by the central bank and the IMF with a view to assessing the capacity of the Romanian banking system to withstand exogenous shocks showed the drop in the aggregate solvency ratio to 10.6 percent in 2009³

² The index Herfindahl-Hirschmann is a measure of market concentration. It is calculated as the sum of the squares of market shares relative to each company and may take values between 0 and 10,000. Empirically, it is considered that the market shows a high concentration level when the value of the indicator exceeds the 1,800 mark.

³ From 12.3 percent (before the shock) at end-2008

and to 9.7 percent in 2010 respectively. At end-2008 and in early 2009, the shareholders of certain banks raise their equity stakes in order to maintain a comfortable margin of the solvency ratio. Moreover, it is noteworthy the commitment of parent banks, which own the top nine banks in Romania (accounting for 70 percent of total bank assets), to extend the existing credit lines in favour of their subsidiaries and to recapitalise them where appropriate.

The adverse effect of the economic slowdown, the rise in inflation and a weaker domestic currency entailed the lower demand for loans and the poor quality of claims portfolios held by banks on non-banks. The growth rate of credit to the private sector moderated significantly in the final quarter, so that at end-2008 it was barely half the level of the year-earlier growth rate. Credit quality still remained at a manageable level but the brisk pace of quality deterioration became a matter for concern. Nevertheless, credit risk expanded due to local currency depreciation which negatively affected debtors exposed to currency risk and to the uncertainties associated with the fallout from the global economic crisis. The stress test analysis conducted for end-2008, which included the assessment of credit risk to which credit institutions are exposed, calculated based on the indirect impact of shocks considered in the multi-factor macroeconomic scenario, revealed a potential erosion by 16.6 percent of own funds reported by banks, Romanian legal entities.

Although liquidity in the banking system was in excess until the autumn of 2008, it further stuck to the downtrend amid a higher degree of financial intermediation, which lowered towards the year-end, and the global financial turmoil. Tighter conditions associated with external liquidity eroded banks' confidence, a phenomenon that became manifest in late October. However, at end-2008, the performance of interbank market improved. The impact of lower liquidities worldwide translated into higher financing costs and higher risks relative to short maturities. In this context, the central bank maintained a flexible management of interbank liquidity, the reserves inflows hinging mainly on the lending facility as well as on foreign exchange swaps; occasionally, liquidity was also managed by way of the deposit facility and deposit-taking operations. With a view to improving liquidity conditions in the system, the central bank reduced the reserve ratio on RON-denominated liabilities from 20 percent to 18 percent as from 24 November 2008 and starting with the 24 May – 23 June 2009 maintenance period the reserve ratio on foreign currency-denominated liabilities with residual maturity longer than two years was reduced from 40 percent to zero percent.

The safe financial result reported by the Romanian banking system in 2008 was achieved in an environment marked by the end of a favourable economic cycle (also fuelled by financial and banking activities which posted historical highs of growth rate of operations) and by the outset of a strenuous period characterised by global economic and financial turbulences as well as by the uncertainties surrounding the future macroeconomic developments. The resilience of the Romanian banking system to shocks was enhanced to a great extent by the good financial results and the high capitalisation degree. The prolonged period of turmoil and uncertainties negatively affected the level of profitability indicators by way of

high financing and provisioning costs; in the first months of 2009, some banks reported negative financial results.

The insurance market was also impacted by the global financial crisis and the domestic economic downturn, which led mainly to the depreciation of investment portfolio assets and the heightening of credit risk. However, the convergence process with the European market continued in 2008 as well. Capital inflows offset the worsening of profitability ratios, chiefly as a result of mounting damages on the motor car insurance segment, so that solvency indicators of insurances companies stayed at optimum levels. With a view to bolstering the insurance sector stability, legislative changes were also made, such as: quality improvement and dispersion of assets eligible for covering gross technical reserves and the taking into account of the market value for financial placements in the calculation of prudential indicators.

The capital market featured high volatility, liquidity shrinkage and lower values of stock indices, amid instability of the international financial markets and mounting uncertainties regarding global economic prospects. A global reassessment of risks was made and stock markets were depressed. The effects of the global financial market were felt in Romania too, the stock market following closely the downtrend of foreign markets at the time the financial crisis was unleashed. Net assets held by open-end investment funds remained relatively unchanged, but the share of low risk placements stepped up (bonds, Treasury bills, bank deposits) due to investors' higher risk aversion and higher interest rates on such instruments. The listing of government securities on the Bucharest Stock Exchange eased investors' access to low risk assets but the volume of trades was modest.

Year 2008 saw the launch of private pension funds followed by the contribution accumulation and investment stage. The volume of assets is low but the fast expansion pace will cause this segment of the financial sector to gain ground. The development of private pension funds will have a positive impact on local financial markets due to their participation in the stock market. The long-term investment horizon and the low risk appetite of these funds imply an active participation on the fixed income instrument market and the allocation of resources towards economic sectors featuring long-term development potential. Moreover, pension funds represent a factor facilitating the financial education of the population by developing a saving-investment type of behaviour and by improving the capacity to assess the relationship between investment risks and return.

1.2. Instruments supportive of prudential supervision and financial stability

Central Credit Register (CCR)

In 2008, lending activity expanded steadily, yet towards the year-end its dynamics slowed down, which was also reflected in the smaller number of CCR database queries. Accordingly, in 2008, credit institutions sent 9 million queries (versus 11.5 million in 2007), of which 99.3 percent with the consent of potential debtors. The queries concerned data on global risk, loans and overdue loans. The share of new

debtors for which authorised queries were made dropped to 73.1 percent at end-2008 from 88.8 percent a year earlier.

The number of debtors in the CCR database after nine years in operation rose 75 times, the number of loans surged 62 times and the total amounts due soared by more than 41 times. At end-2008, the CCR database included 17.2 percent of the total number of debtors in the banking system and 19.8 percent of the total number of loans granted. These figures indicate that consumer loans still held a significant share in the loan stock. At end-2008, given that the reporting threshold was left unchanged at RON 20,000, the CCR database comprised 88.4 percent of Romanian banks loans value, compared to 85.1 percent at end-2007.

In this context, it is worth noting that the number of debtors, natural entities, rose considerably in 2008 as well. While at end-2007 the number of natural entities whose exposure exceeded the CCR database reporting threshold amounted to 724,658, the number reached 920,668 (up 27 percent) at end-2008. The value of loans granted to households rose to RON 76.7 million at end-2008 (up 54.6 percent) from RON 49.6 million at end-2007. Households accounted for 89.6 percent of total debtors in the CCR database at end-2008, compared to 88.4 percent a year earlier; the value of loans to households held 33.9 percent of the loan stock at end-2008 versus 29.5 percent a year earlier. At end-2008, out of total loans to households, EUR-denominated loans accounted for 57.7 percent, RON-denominated loans for 26.5 percent, and loans in Swiss francs for 15.3 and loans in US dollars for only 0.5 percent.

In addition, at end-2008, 167,326 debtor groups were recorded in the CCR database. In 2008, credit institutions reported to the CCR database card frauds perpetrated by 48 debtors, compared to 52 in 2007, the value of the fraud totalling RON 22,008 (compared to RON 19,081 a year earlier).

In compliance with provisions of Government Ordinance No. 27/2002 on the petition approach procedures and Law No. 677/2001 on the protection of persons concerning the processing of personal data and the free circulation of such data, in 2008, the Financial Stability Department provided 1,518 responses to 1,463 individuals and 55 legal entities that had requested information on the entries in the CCR database on their name, compared to 2,249 petitioners (2,199 individuals and 50 legal entities) in 2007.

Payment Incident Bureau (PIB)

The analysis of PIB database for 2008 shows that, especially in the final two months of the year, the main indicators used in monitoring this activity posted notable increases: the number of payment incidents, the number of accountholders that generated payment incidents and the amounts rejected form payment. These indicators moved up due to the unfavourable economic environment at end-2008.

Compared to the prior year, in 2008, the number of accountholders in the PIB database that had generated payment incidents stepped up markedly (59.1 percent

versus 32.3 percent). In addition, the number of rejected payment instruments rose by 73.4 percent (against 8.9 percent in 2007), and the value of rejected amounts increased by 141 percent (versus 1.8 percent in 2007). In 2008, the larger number of accountholders was due to both the larger number of payment incidents and the registration in the PIB database of a larger number of accountholders natural entities; thus, while in 2007 the number of natural entities that had generated payment incidents involving particularly promissory notes stood at 3.288, it grew to 5.342 (up 62.5 percent) in 2008.

In 2008, 82 percent of the total number of rejected payment instruments and 80 percent of the total value of the rejected amount were reported by nine banks, the same as in 2007. Furthermore, it is noteworthy that the most frequent reason for rejection (56 percent of total reasons for rejection) was the “total or partial lack of cash”.

In 2008, banks made 4.5 million queries into the PIB database, compared to 3.6 million a year earlier, in their own name or in the customers’ name. The queries were meant to check whether payment incidents had been recorded in the name of accountholders.

In compliance with provisions of NBR Regulation No. 1/2001 on the organisation and operation of the PIB with the National Bank of Romania, as subsequently amended and supplemented, the Financial Stability Department answers the queries from public authorities regarding the entering of accountholders into the PIB database. Thus, in 2008, the Financial Stability Department dealt with 2,039 queries from public authorities, compared to 1.840 in 2007.

Pursuant to provisions of Government Ordinance No. 27/2002 on the petition approach procedures and Law No. 677/2001 on the protection of persons concerning the processing of personal data and the free circulation of such data, in 2008, the Financial Stability Department dealt with 68 queries (from 8 individuals and 60 legal entities) concerning the data entered into the CCR database on their name, compared to 54 queries (from 3 individuals and 51 legal entities) in 2007.

1.3. Contingency planning and financial crisis management

The preparation in advance for the management of potential financial crises is an important part of the NBR activity in the field of financial stability. Financial disturbances with systemic effects may emerge suddenly and spread throughout the entire financial system rapidly. In this context, the central bank’s involvement in contingency planning will enable this institution to identify the adequate measures to address a specific financial crisis. Thus, crisis situations will be managed more quickly with lower financial costs and lower costs at real economy level.

The NBR activity in the field of financial crises management is conducted both domestically and at EU level.

At EU level, a specific framework for financial crises management was created over time; it includes authorities in charge of ensuring financial stability (central banks, financial supervisory authorities and finance ministries) as well as procedures and various instruments such as: legislative provisions, voluntary cooperation arrangements between authorities, monetary policy instruments specific to central banks, cooperation within dedicated EU commissions. The framework was strengthened in the past years to keep up with the accelerated process of integration of markets and financial infrastructures in the EU and with the emergence of an increasing number of cross-border financial institutions.

In the context of efforts meant to consolidate the EU memoranda on financial stability, on 1 June 2008, a new multilateral memorandum on cooperation in financial crisis situations came into force; it had been signed by financial supervisory authorities, central banks and finance ministries in the EU. The new memorandum, which supersedes the prior memorandum of 2005, promotes cross-border cooperation between the said authorities both in normal situations, by way of strengthening their preparation for managing potential crises and during financial crisis situations. The memorandum presents several novelties: a set of common principles on the management of cross-border financial crises, a common analytical framework to assess the systemic effects of potential financial crises and common practical guidelines for the management of cross-border financial crises which should reflect a common understanding of the stages and procedures to be followed in such situations. The NBR signed a multilateral memorandum on 4 April 2008, on the occasion of the ECOFIN Council meeting. As a result, in a cross-border crisis situation, the exchange of information and the consultations between the NBR and the supervisory authorities, central banks and finance ministries in the EU countries will be conducted in compliance with the stages and procedures laid down in the multilateral arrangement.

At national level, the central bank's preparations in the field of financial crisis management situations are based on the legislative framework in place and the memoranda in force on cooperation and the exchange of information between the public authorities in charge of ensuring financial stability and crisis management.

In 2008, the NBR attached particular attention to developing procedures and instruments for financial crisis management in compliance with its legal prerogatives. In this respect, the central bank participated in a financial crisis dry-run, conducted half-yearly stress tests focusing on the extreme but plausible shocks that may affect the banking system and prepared a number of documents in the field of contingency planning.

On 6 February 2008, a financial crisis dry-run was conducted with the participation of representatives from the National Bank of Romania, the Ministry of Economy and Finance, the National Securities Commission, the Insurance Supervisory Commission, the Romanian Private Pension System Supervisory Commission and the Bank Deposit Guarantee Fund. The dry-run simulated a situation in which a bank, Romanian legal entity, would have faced liquidity shortage as a result of an

internal fraud, which would have major negative consequences on Romania's financial system.

As part of the NBR's role to maintain financial stability, in 2008, the dedicated departments in the central bank prepared a number of documents including principles and procedures for the management of financial crises, such as: "The contingency plan applicable to credit institutions" and "The list of issues to be addressed in case of contingencies". Moreover, the NBR compiled lists of the contacts from the supervisory authorities in the Romanian financial system and other relevant EU authorities; the list is updated on a regular basis.

With a view to strengthening the capacity of the Romanian banking system to perform its duties in an adequate manner in an unfavourable macroeconomic environment, the provided measures were supplemented by half-yearly stress tests. All this enabled the quantification of capital reserves that credit institutions should build up in order to maintain an adequate level of solvency during periods of macroeconomic turbulences. The tests were based on multiple risk factor scenarios and the results were communicated to the Ministry of Economy and Finance.

A key role in the development of certain coordinated memoranda for crisis management situations in Romania is played by the National Committee for Financial Stability (NCFS), which was established based on a Memorandum of Understanding between the central bank, the other financial supervisory authorities and the Ministry of Economy and Finance, signed on 31 July 2007. The NCFS includes the following members: the minister of economy and finance, the NBR governor, the chairmen of the National Securities Commission, the Insurance Supervisory Commission and of the Romanian Private Pension System.

In 2008, the NCFS was chaired by the NBR governor and his tenure was renewed for another year on 16 February 2009.

The main objective of the NCFS is to ensure financial stability by promoting a permanent and efficient exchange of information between the authorities in charge of regulation and supervision of different sectors of Romania's financial system and the Ministry of Economy and Finance, as well as to assess, prevent and, where appropriate, manage financial crisis situations at the level of individual financial institutions, financial groups or the financial market as a whole.

In 2008, NCFS attached particular attention to the development of the methodological framework for the coordination of financial crisis management operations. In this context, the NCFS focused on the implementation in Romania of an analytical framework for the assessment of systemic implications of a financial crisis, laid down in the multilateral cooperation arrangement concluded in 2008 by financial supervisory authorities, central banks and finance ministries. During the same period and in the following months of 2009, the Committee closely monitored the global financial turbulences and their implications on the financial institutions, markets and infrastructures in Romania and abroad. In this assessment

process, the NBR provided its valuable experience in the field of prudential supervision at both macro and micro levels.

The involvement of the institutions represented in the NCFS in the preparation of the methodological framework and crisis management should not be viewed as an exception from the following principles: (1) primary financial responsibility of shareholders/owners and managers of financial institutions; (2) the need for creditors to keep vigil; (3) identifying particularly the market-related solutions capable of managing the crisis situations affecting individual institutions.

In April 2009, a financial crisis management department was established within the NBR, by taking over and integrating the already existing tasks of this nature from other departments in the NBR. The department will play a key role in the development and regular updating of the financial crisis management procedures of the central bank and in formulating this institution's opinions in the field at EU level. Moreover, the new department has responsibilities enabling it to assist the other institutions in the NCFS with a view to implementing measures aimed at strengthening their capacity to manage financial crisis situations, by securing the secretariat of this body.

2. Licensing and regulation of financial institutions

2.1. Licensing and regulation of credit institutions

2.1.1. Licensing of credit institutions

In 2008, the licensing of credit institutions by the NBR was further aimed at consolidating the banking system by attracting powerful investors capable of efficiently supporting banks' management in performing its activity.

In July 2008, in virtue of provisions of Government Emergency Ordinance No. 99/2006 on credit institutions and capital adequacy, as subsequently amended and supplemented, the NBR authorised the incorporation of BCR Banca pentru Locuințe joint-stock company. The founding members of the savings and loan bank for housing are legal entities belonging to the financial group Erste, Banca Comercială Română joint-stock company and Bausparkasse der österreichischen Sparkassen AG respectively.

Notification of non-bank financial institutions

In 2008, the notification and registration of the newly established non-bank financial institutions continued. In virtue of provisions of Government Emergency Ordinance No. 28/2006, as subsequently amended and supplemented by Law No. 266/2006, 30 non-bank financial institutions were entered into the General Register (out of which 16 were also entered into the Special Register), and 285 non-bank financial institutions were registered with the Entry Register.

2.1.2. Legal and regulatory framework for credit institutions

In the field of prudential regulation, 2008 witnessed strong advances consisting in the adoption of new regulations aimed at the following:

- a) completion of the regulatory framework for taking-up and pursuit of banking business with provisions on the conversion of financial institutions into credit institutions (NBR Regulation No. 1/2008 on the conversion of financial institutions into credit institutions) and the assessment of the supervision framework in third countries (NBR Regulation No. 2/2008 on the assessment of the adequacy of the supervisory framework in a third country and the checking of the matching of the supervision exercised by competent authorities in third countries with that governed by the principles stipulated in Government Emergency Ordinance No. 99/2006 on credit institutions and capital adequacy);
- b) harmonisation of the regulatory framework regarding the changes in the situation of credit institutions with provisions of Government Emergency Ordinance No. 99/2006 (NBR Regulation No. 6/2008 on the changes in the situation of credit institutions, Romanian legal entities and of branches of Romanian credit institutions in third countries);
- c) further issuing of regulations for the adequate enforcement of Basel II regulatory framework, on the requirements on the recognition of external credit assessment institutions (NBR Regulation No. 3/2008) and on approving the use of the alternative standardised approach for operational risk (NBR Regulation No. 5/2008);
- d) amendment of prudential regulations in the context of efforts made in 2008 to contain credit growth: the elimination of the interim profit from the calculation of credit institutions' own funds and the integration of the respective amendments in the reporting forms (Regulation No. 10/8/2008 issued by the NBR and the NSC on amending and supplementing Regulation No. 18/23/2006 issued by the NBR and the NSC on own funds of credit institutions and investment firms; NBR Order No. 9/2008 on amending NBR Order No. 12/2007 on the reporting of minimum capital requirements for credit institutions); increasing specific provisions for credit risk relative to foreign currency-denominated loans granted to households exposed to currency risk (NBR Regulation No. 4/2008 on amending and supplementing NBR Regulation No. 5/2002 on the classification of loans and placements, as well as the setting-up, adjustment and use of specific provisions for credit risk, as subsequently amended and supplemented, and NBR Methodological Norms No. 12/2002 on the enforcement of NBR Regulation No. 5/2002); the introduction of additional requirements regarding alternate plans for liquidity risk management in financial crisis situations (NBR Norms No. 2/2008 on amending and supplementing NBR Norms No. 1/2001 on bank liquidity); the introduction of additional provisions aimed at improving the management of risks relative to loans to households by raising the degree of sensitivity of the lending decision to interest rate risk and currency risk and as well as bank lending practices by requiring documents certifying the income source in an

adequate manner (NBR Regulation No. 11/2008 on amending and supplementing NBR Regulation No. 3/2007 on containing credit risk associated with loans to households);

- e) completion of the reporting framework for prudential indicators with reporting requirements for large exposures of credit institutions (NBR Order No. 2/2008 on the reporting of large exposures by credit institutions).

After Romania's becoming an EU Member State, the NBR has taken an active part, via opinions formulated by its representatives in the EU structures, both in establishing EU level strategies in the field of prudential regulation and in preparing new directives.

2.2. Regulation of lending activity performed by non-bank financial institutions

The measures applied to the banking system with a view to containing the expansion of non-government credit and especially the foreign currency-denominated credit were also applied to non-bank financial institutions. In this respect, in 2008, the following regulations were issued:

- NBR Regulation No. 4/2008 on amending and supplementing NBR Regulation No. 5/2002 on the classification of loans and placements, as well as the setting-up, adjustment and use of specific provisions for credit risk and NBR Methodological Norms No. 12/2002 on the enforcement of NBR Regulation No. 5/2002), which provided for a new methodology for including the loans taken by households exposed to currency risk in the classification categories and the distinct disclosure of the impact of currency risk as an additional risk, by applying, for such exposures, certain higher provisioning coefficients.
- NBR Norms No. 9/2008 on amending NBR Norms No. 16/2006 on own funds of non-bank financial institutions, which eliminated the possibility that non-bank financial institutions entered into the Special Register should include interim profit in the calculation of own funds;
- NBR Regulation No. 11/2008 on amending and supplementing NBR Regulation No. 3/2007 on containing credit risk associated with loans to households which was aimed at improving credit risk management and the introduction of sound lending practices.

In 2008 as well, the NBR contributed, in its capacity as regulatory authority, to identifying the issues that need further clarification or the potential amendments to the regulations applicable to non-bank financial institutions. Thus, talks were held with the concerned entities in order to achieve a more efficient exchange of information and to find adequate solutions with a view to ensuring the expected impact of the central bank's policies in this field.

The active steps taken by the central bank included supporting the interests of this segment of the lenders' market in the formulation of a law which should also provide an advantage from their perspective; these steps materialised in debates in the dedicated commissions of the Parliament in the process of passing the Draft law on non-bank financial institutions.

These steps led to the adoption of Law No. 93/2009 on non-bank financial institutions, which is aimed at harmonising the regulatory framework applicable to non-bank financial institutions with the corporate governance principles regulated by the general law (Law No. 31/1990 on commercial companies, as republished, amended and supplemented subsequently) and at the adequate adjustment of amendments to the regulatory framework governing the activity of credit institutions.

2.3. Regulation of activity performed by the Bank Deposit Guarantee Fund

In 2008, the NBR took an active part in the formulation of Directive 2009/14/EC on amending Directive 94/19/EC on deposit-guarantee schemes as regards the coverage level and the payout delay; the central bank formulated opinions in different stages of the preparation of the draft directive. In addition, with a view to implementing the new requirements of the said Directive nationwide, the NBR conducted an assessment of the legal framework in the deposit guarantee field (Government Ordinance No. 39/1996 on the establishment and operation of the Bank Deposit Guarantee Fund) and initiated a draft law for the transposition of the Directive by 30 June 2009.

During the transposition of Directive 2009/14/EC, the NBR will pay particular attention to the cooperation with the other authorities involved in the enforcement of requirements in the deposit guarantee field (Bank Deposit Guarantee Fund and Romanian Banking Association).

2.4. Regulations in the field of prevention and control of money laundering and combating the financing of terrorism

Following the amendments to the *acquis communautaire* in the field of prevention and control of money laundering and combating the financing of terrorism, a nationwide revision of the related framework was performed.

In 2008, two pieces of legislations were issued regarding, on the one hand, the transposition into the national legislation of Directive 2005/60/EC on the prevention of the use of the financial system for the purpose of money laundering and terrorist financing and of Directive 2006/70/EC laying down implementing measures for Directive 2005/60/EC, and on the other hand, the establishment of competent authorities and the sanctions for breaching of EC Regulation No. 1781/2006 on information on the payer accompanying the transfer of funds:

- Government Emergency Ordinance No. 53/2008, on amending and supplementing Law No. 656/2002 on the prevention and sanctioning of money laundering as well as for enforcing measures to prevent and combat the financing of terrorism, as amended and supplemented;
- Government Decision on approving the Regulation in performance of Law No. 656/2002 on the prevention and sanctioning of money laundering as well as for enforcing measures to prevent and combat the financing of terrorism, as amended and supplemented;

These pieces of legislation were formulated by a national working group, composed of representatives of all interested parties, with the NBR playing an active part in the areas that have an impact on its prerogatives.

The revision of the regulatory framework at principle level required the change of secondary legislation in the field prepared by the NBR by issuing Regulation No. 9/2008 on “know-your-customer” standards with a view to preventing money laundering and combating the financing of terrorism which meets the new requirements instituted by the shift to the risk-based approach, i.e. setting as regulations of only two principles and focusing on the final result, thus passing on to the regulated entities the responsibility of managing risk by identifying the adequate solutions.

Moreover, it is worth noting Romania’s participation in the third round of assessment from the perspective of the rules set in the field of prevention and control of money laundering and combating the financing of terrorism, performed by Moneyval – the European Council based on the criteria and recommendations of the Financial Action Task Force and the taking into account of the conclusions of the assessment process when formulating the final version of the said regulation.

2.5. Legal and accounting regulatory framework for credit institutions, non-bank financial institutions and the Bank Deposit Guarantee Fund

One of the permanent concerns of the NBR, in its capacity as accounting regulatory authority for credit institutions, non-bank financial institutions and the Bank Deposit Guarantee Fund is the harmonisation of the regulatory framework with the requirements of the European directives and the International Financial Reporting Standards (IFRS).

The accounting regulations issued by the NBR in force in the 2008 financial exercise, approved by NBR Order No. 5/2005 (henceforth called Accounting regulations) stipulate that the compilation of financial statements at individual level should comply with the EU directives, and the compilation of consolidated financial statements should comply with IFRS.

Accounting regulations were updated by NBR Order No. 7/2008, having regard to the following: (i) ensuring a unitary accounting method for the operations of non-

bank financial institutions especially those relative to claims and RON-denominated debts, the settlement of which is made in relation to a foreign currency, (ii) the regulation of the annual financial statement forms applicable to the Bank Deposit Guarantee Fund and (iii) ensuring compliance with the requirements of the Ministry of Economy and Finance.

During 2006-2008, Accounting regulations were amended and supplemented by several normative acts due mainly to the extension of the NBR's prerogatives in the field of issuing accounting norms and regulations governing the non-bank financial institutions entered into the General Register and governing the Bank Deposit Guarantee Fund. In this context, new accounting regulations in compliance with the EU Directives needed to be formulated, applicable to credit institutions, non-bank financial institutions and the Bank Deposit Guarantee Fund, approved by NBR Order No. 13/2008, which shall include all accounting rules and principles with a view to a better understanding and enforcement; the new Accounting regulations, applicable starting with the 2009 financial exercise, complete the text of the basic normative act (NBR Order No. 5/2005, which had been repealed); in the context of the national strategy adopted by the Accounting and Financial Reporting Council, based on the sectoral strategies adopted by each accounting regulatory authority, the time will be set when IFRS will be implemented by credit institutions and at the level of individual financial statements.

With a view to ensuring a unitary reporting system economy-wide, i.e. the observance of reporting requirements set by the Ministry of Economy and Finance, and to eliminate the difficulties related to monitoring and enforcement of the prior regulation (Order No. 999/3/2003 issued by the MEF and the NBR, to which four successive amendments had been made before its abrogation, i.e. before Order No. 2448/2008 issued by the MEF and the NBR was issued) a new half-yearly accounting reporting framework for credit institutions and non-bank financial institutions was prepared, as laid down in NBR Order No. 8/2008.

Furthermore, the new regulations included the Bank Deposit Guarantee Fund into the applicability scope of the half-yearly accounting reporting framework for credit institutions and non-bank financial institutions.

In order to transpose into national legislation the standardised reporting framework on a consolidated basis (FINREP) developed by CEBS and to include in the methodological norms the responses formulated by CEBS to the questions regarding the implementation of the FINREP reporting framework, approved and posted on CEBS website, the NBR issued Order No. 5/2008 on amending and supplementing the methodological norms and models regarding the consolidated financial statements consistent with IFRS that credit institutions are requested to adopt for prudential purposes.

In addition, the NBR issued Order No. 12/2008 with a view to harmonising the FINREP reporting framework at individual level with the new FINREP reporting framework at consolidated level and to introduce additional specifications regarding the filling-in of some financial statement positions for an adequate enforcement of the regulation.

With a view to ensuring the continuity of information reported to the NBR by the branches in Romania of credit institutions in other EU Member States, in the context of their failing to apply the FINREP reporting framework at individual level, regular reporting models were prepared, applicable to the respective entities, comprising financial and accounting statistical data and methodological norms on their compilation and use (NBR Order No. 14/2008).

2.6. Key objectives for 2009

I. Objectives in the field of prudential regulation

- Completion of the draft law ensuring the transposition into the national legislation of Directive 2007/44/EC on financial sector purchases, as well as of the related regulation framework;
- Continuation of the transposition into the NBR regulations of the guidelines issued by CEBS, concurrent with the completion of regulation projects in the final stage at end-2008, namely: regulation on business management internal framework, the internal process of assessing capital adequacy to risks and outsourcing of the business of credit institutions; regulation on the implementation, validation and assessment of internal ratings-based approach for credit institutions; regulation on the implementation, use, validation and assessment of advanced measurement approach for the determination of capital requirements for operational risk and the approval of this approach to be used by credit institutions;
- Revision of the legislative and prudential regulation framework relevant in the context of domestic and global financial market developments. In this environment, the special regulations to be considered refer to the classification of loans and provisions, calculation of own funds, liquidity supervision;
- Change/completion of the prudential regulation framework based on the developments in the *acquis communautaire*.

II. Objectives in the field of foreign currency and accounting regulation

- Designing the strategy on the implementation of IFRS by the banking system, with a view to compiling financial statements at individual level and as accounting basis, which, along with the sectoral strategies formulated by the other accounting regulatory authorities, will help elaborate the national strategy to be adopted by the MEF and the Accounting and Financial Reporting Council;

- Preparation of a project on the regulatory framework adequate for the implementation of IFRS at individual level and as accounting basis by credit institutions;
- Participation in elaborating accounting/tax reconciliation guides in the context of enforcing IFRS as an accounting basis;
- Updating of the FINREP reporting framework (developed by CEBS) at both individual and consolidated levels;
- Updating of regulations on the currency regime based on the developments in the national and European regulatory framework and the objectives pursued by the NBR as well as of accounting regulations based on their stage of harmonization with EU Directives and IFRS.

III. Objectives in the field of regulation of non-bank financial institutions

- Revision of the secondary regulatory framework applicable to non-bank financial institutions in view of adjusting to the new legislation;
- Preparation of the primary and secondary frameworks necessary for ensuring the transposition of provisions on licensing and prudential supervision of payment institutions provided for in Directive 2007/64/EC of the European Parliament and of the Council on payment services in the internal market amending Directives 97/7/EC, 2002/65/EC 2005/60/EC and 2006/48/EC and repealing Directive 97/5/EC;
- Preparation of the legislation for transposition of Directive 2009/14/EC of the European Parliament and of the Council amending Directive 94/19/EC on deposit-guarantee schemes as regards the coverage level and the payout delay.
- Active participation in the completion of the Draft directive relating to the taking-up, pursuit and prudential supervision of the business of electronic money institutions, amending Directives 2005/60/EC and 2006/48/EC and repealing Directive 2000/46/EC.

3. Prudential supervision of credit institutions

3.1. Structure of the banking system

According to the latest developments, the Romanian banking system may be assessed as stable in its entirety, enjoying capitalisation, solvency and liquidity levels in line with prudential requirements, despite the fast-paced lending reported over the past several years and the deepening of the global financial crisis. Overall, the levels of prudential indicators did not raise major concerns, yet their tendency needs to be closely monitored given the uncertainties surrounding the prospects for global economic growth.

In 2008, the Romanian banking system underwent the following structural changes:

- the establishment of BCR Banca pentru Locuințe;
- the opening of a branch of the Ireland-based Depfa Bank;
- the take-over of the business of Banca di Roma – Bucharest branch by UniCredit Țiriac Bank following the merger of UniCredit Group and Capitalia;
- the take-over of ABN Amro by Royal Bank of Scotland;
- changes to the names of C.E.C. and Bank Egnatia, which were rebranded as CEC Bank and MARFIN Bank respectively;
- change to the name of Sanpaolo IMI Bank Romania which was rebranded as Banca Comercială Intesa Sanpaolo Romania, following the merger in Italy of Intesa SpA and SanPaolo IMI SpA.

As a result, the number of foreign bank branches at end-2008 remained unchanged from a year earlier (10 entities), while the number of domestic banks rose from 32 to 33 entities⁴. By ownership, at end-2008, the structure of the banking system was as follows: 2 banks with fully or majority state-owned capital (CEC Bank and Eximbank), 3 banks with majority domestic private capital (Banca Transilvania, Banca Comercială Carpatica and Libra Bank), 27 banks with majority foreign capital and 10 foreign bank branches. Furthermore, the Romanian banking system also included an authorised credit cooperative organisation, i.e. Central Cooperatist Bank CREDITCOOP with a network including 19 agencies and 124 cooperatives.

Table 1. Credit Institutions by Ownership

	<i>number of banks, end of period</i>	
	2007	2008
Banks, Romanian legal entities, of which:	31	32
Fully or majority state-owned capital, of which:	2	2
- fully state-owned capital	1	1
- majority state-owned capital	1	1
Majority private capital, of which:	29	30
- majority domestic capital	3	3
- majority foreign capital	26	27
Foreign bank branches	10	10
Total banks and foreign bank branches	41	42
CREDITCOOP	1	1
TOTAL CREDIT INSTITUTIONS	42	43

Once Romania joined the EU and services were liberalised, 190 foreign institutions (of which 174 banks, 3 NFIs and 13 electronic money institutions) expressed, by end-May 2009, their intention to perform direct banking activities on the territory of Romania.

⁴ Including the Central Cooperatist Bank CREDITCOOP

Given all these changes, the share of assets held by banks with private capital or majority private capital in total assets of the Romanian banking system was 94.8 percent at end-2008 (while the share of assets held by banks with foreign capital or majority foreign capital, including foreign bank branches, accounted for 88.2 percent). Banks with fully or majority state-owned capital held only 5.2 percent.

Table 2. Market Share of Banks and Foreign Bank Branches

	<i>end of period</i>			
	Net assets			
	2007		2008	
	RON mill.	%	RON mill.	%
Banks with domestic capital, of which	30,330.5	12.1	36,448.6	11.6
- with majority state-owned capital	13,535.8	5.4	16,452.6	5.2
- with majority private capital	16,794.7	6.7	19,996.0	6.4
Banks with majority foreign capital	207,906.7	82.7	259,633.1	82.6
I. Total commercial banks	238,237.2	94.8	296,081.7	94.2
II. Foreign bank branches	12,545.6	5.0	17,663.7	5.6
Banks with majority private capital including foreign bank branches	237,247.0	94.4	297,292.8	94.6
Banks with majority foreign capital including foreign bank branches	220,452.3	87.7	277,296.8	88.2
Total banks and foreign bank branches (I+II)	250,782.8	99.8	313,745.4	99.8
CREDITCOOP	643.0	0.2	696.1	0.2
TOTAL CREDIT INSTITUTIONS	251,425.8	100.0	314,441.5	100.0

In terms of bank capitalisation, share/endowment capital of Romanian banks at end-2008 was higher from a year earlier, in both nominal and real terms, by 19.6 percent and 12.6 percent due mainly to shareholders' cash contributions.

Table 3. Banks and Foreign Bank Branches as a Share in Aggregate Capital

	<i>end of period</i>			
	Share/Endowment capital			
	2007		2008	
	RON mill.	%	RON mill.	%
Banks with domestic capital, of which:	2,273.8	20.4	2,913.3	21.9
- with majority state-owned capital	1,408.5	12.7	1,520.0	11.4
- with majority private capital	865.3	7.7	1,393.3	10.5
Banks with majority foreign capital	8,060.4	72.5	9,477.6	71.2
I. Total commercial banks	10,334.2	92.9	12,390.9	93.1
II. Foreign bank branches	681.6	6.1	799.5	6.0
Banks with majority private capital, including foreign bank branches	9,607.3	86.3	11,670.4	87.7
Banks with majority foreign capital, including foreign bank branches	8,742.0	78.6	10,277.1	77.2
Total banks and foreign bank branches (I+II)	11,015.8	99.0	13,190.4	99.1
CREDITCOOP	108.5	1.0	119.4	0.9
TOTAL CREDIT INSTITUTIONS	11,124.3	100.0	13,309.8	100.0

As regards the country of origin of the capital invested in domestic banks and foreign bank branches operating in Romania at end-2008, the top three countries were Greece (22.4 percent), Austria (18.4 percent) and the Netherlands (7.7 percent). The most relevant move on the domestic market was made by Greece which, starting with 2008, came in first among the countries holding equity stakes in the capital of banks in Romania, its quota rising from 21.5 percent at end-2007 to 22.4 percent at end-2008.

Table 4. Foreign Participations in the Share Capital of Credit Institutions in Romania as at end-2008

	RON mill.	%
Greece	2,980.0	22.4
Austria	2,448.3	18.4
The Netherlands	1,229.0	9.2
Italy	637.5	4.8
Hungary	573.8	4.3
France	562.1	4.2
EBRD + IFC	295.9	2.2
Cyprus	274.1	2.1
Israel	247.8	1.9
Portugal	241.1	1.8
USA	189.6	1.4
Germany	172.6	1.3
United Kingdom	130.9	1.0
Other	60.3	0.5
Aggregate foreign capital of the banking system	10,043.0	75.5
Total capital of the banking system	13,309.8	100.0

Although they held more than half of bank asset volume, the top five banks in terms of asset size further witnessed the drop in their asset share in aggregate assets, from 56.3 percent at end-2007 to 54.3 percent at end-2008. This drop in the market share in favour of small-sized banks was attributable to the higher profitability and diversity of banking products as well as to the aggressive policy of expanding their client portfolios.

3.2. Performance and outlook

With a view to achieving harmonization with the best international practices and the modernisation of prudential supervision, starting with 2008, the financial reporting framework was brought in line with the standardised framework recommended by CEBS for ensuring a single financial reporting recognised at EU level for supervision purposes (FINREP) and prudential purposes (COREP). In addition, these reportings were outlined and integrated into the electronic reporting system of the NBR.

With financial intermediation still running low, according to the share of bank assets in GDP as compared to other EU countries, the Romanian market potential remained high. Thus, over the past several years, banking business and competitiveness moved up, the share of bank assets rising to 50.1 percent of GDP at end-2006, 60.9 percent in 2007 and 62.4 percent in 2008.

Credit institutions' permanent effort to diversify their range of products and services resulted in a substantial rise in bank assets. Thus, the net aggregate balance sheet of the banking system totalled RON 314.4 billion at end-2008, i.e. a 25.1 percent increase in nominal terms versus end-2007, a 17.7 percent growth in real terms and a 13.3 percent rise of EUR-denominated assets.

Capital adequacy

The slight downtrend in the solvency ratio in 2008 (12.99 percent at end-March 2008, 12.78 percent at end-June 2008 and 11.85 percent at end-September 2008) was stimulated by the fast-paced lending growth, the worsening of loan portfolio and by the introduction of an additional requirement for operational risk and market risk. The higher solvency ratio at end-2008 (13.76 percent) compared to September 2008 was largely attributable to the rise in own funds following the inclusion of the profit achieved during the 2008 financial exercise. In this context, all the banks posted a solvency level higher than the minimum solvency ratio (8 percent), while 20 banks exceeded the average of this indicator for the banking system.

The leverage effect also illustrates an upward trend, from 7.32 percent at end-2007 to 8.13 percent at end-2008, chiefly on account of Tier 1 capital rising at a much faster pace than assets.

Asset quality

In recent years, lending was the most aggressive segment, with banks focusing mainly on increasing their market share by expanding the range of products and territorial networks. In a new competition-driven environment, in 2008, the Romanian banking system switched from excess liquidity to liquidity shortfall, from aggressive lending in 2008 Q1-Q3 (up 11.1 percent in Q1, 8.2 percent in Q2, 9.0 percent in Q3, compared to 2.0 percent in Q4 2008), to promotions aimed at attracting deposits in 2008 Q4.

At end-2008, banking system-wide indicator illustrating the share of loans to customers in total gross assets stood at 62.50 percent, up 3.4 percentage points from the prior year's figure.

According to monetary balance sheet data of credit institutions, in 2008, the dynamics of non-government credit slowed down versus the previous year (by 33.7 percent in nominal terms or 25.8 percent in real terms, compared to 60.4 percent in

nominal terms or 50.5 percent in real terms), as well as the change in the lei/foreign currency structure of loans in favour of foreign currency-denominated loans (their share in total non-government credit stepped up to 57.8 percent in 2008 from 54.3 percent a year earlier).

Table 5. Key Indicators

Indicator	percent	
	2007	2008
Capital adequacy		
Solvency ratio	13.78	13.76
Leverage ratio (Tier 1 capital/Total assets (average))	7.32	8.13
Asset quality		
Loans to customers (gross)/Total assets (gross)	59.09	62.50
Interbank loans and placements (gross) /Total assets (gross)	29.98	26.01
Doubtful and overdue loans to customers/Total loan portfolio relative to customers (net)	0.22	0.32
Doubtful and overdue loans to customers/Total loan portfolio relative to customers (gross)	0.77	1.37
Doubtful and past-due claims/Total assets (net)	0.17	0.29
Doubtful and past-due claims (net)/Total debt	0.19	0.32
Doubtful and past-due claims (net)/Total equity	1.63	3.19
Unadjusted exposure from loans and related interest under "doubtful" and "loss"/Total classified loans and related interest including off-balance-sheet items (*)	3.76	5.95
Profitability		
ROA (Net income/Total assets - average)	1.01	1.56
ROE (Net income/Total equity - average)	9.43	17.04
Liquidity		
Immediate liquidity	38.70	34.43
Liquidity indicator (effective liquidity/required liquidity)	2.13	2.47
Loans to customers (gross)/Deposits taken from customers	108.72	122.03

(*) Indicator based on loan classification reporting (in compliance with Regulation No. 5/2002, as subsequently amended and supplemented). Exposures from loans are classified by banks based on debt service, debtor's financial performance and the downgrading by contamination principle.

Loans to households⁵ remained the fastest growing segment; at end-2008, the NFC sector posted a 38.7 percent rate of increase versus 29.7 percent year on year. Moreover, it is noteworthy the larger share of foreign currency-denominated loans to households, up 53.6 percent, while RON-denominated loans rose by merely 22 percent in 2008. Against this background, the NBR moved to improve the loan classification framework in order to contain currency risk and the worsening of the loan portfolio quality, imposing credit institutions additional provisioning requirements for loans granted in a currency other than the income currency (NBR Regulation No. 4/2008 on amending and supplementing NBR Regulation No. 5/2002 on the classification of loans and placements, as well as the setting-up, adjustment and use of specific provisions for credit risk and NBR Methodological

⁵ According to monetary balance sheet data

Norms No. 12/2002 on the enforcement of NBR Regulation No. 5/2002, which came into force in March 2008).

As expected, on the retail credit segment, housing loans destined to the purchase of houses or building materials recorded, in 2008, a growth rate (47.2 percent) faster than that of consumer loans (33.7 percent). Nevertheless, in absolute terms, consumer loans held the largest share in 2008.

In terms of loan currency, foreign currency-denominated credit consolidated its position at end-2008, holding a share of about 57.8 percent in total non-government credit. The steadfast dynamics of foreign currency-denominated loans (a 42.2 percent increase in nominal terms or a 33.8 percent rise in real terms; 28.8 percent for EUR-denominated loans) was possible amid higher demand for this type of loans, as a result of lower interest rate applied by credit institutions.

After a period during which lending was banks' main option for increasing their market share, signs appeared of a gradual deterioration of the indicators measuring the loan portfolio quality, manifest especially in 2008 H2. Accordingly, although below par, it is noteworthy the steady rise in the share of doubtful and overdue loans⁶ in the portfolio of loans to customers (net) from 0.22 percent at end-2007 to 0.32 percent at end-2008. Moreover, the same indicator (gross) saw a faster rise during the said interval, from 0.77 percent to 1.37 percent. The share of doubtful and past-due claims in total bank assets moved up 0.12 of a percentage point in 2008 (from 0.17 percent to 0.29 percent).

Concurrently, the high volatility of domestic currency and the worsening of macroeconomic conditions caused the deterioration of the main indicators quantifying credit risk⁷, which pushed up the share of unadjusted exposure associated with loans and interests under "doubtful" and "loss" in total loans and interests, from 3.76 percent at end-2007 to 5.95 percent at end-2008.

Liquidity

The liquidity indicator was slightly higher than both the minimum requirement (1) and the level at end-2007, to reach 2.47 percent at end-2008 from 2.13 a year earlier.

Expansion of lending was also affected by the rise in the ratio of loans to customers to deposits taken⁸, from 108.72 percent at end-2007 to 122.03 percent at end-2008, which illustrates a much faster growth of loans (33.6 percent) compared to that of deposits (19 percent). Against this background, the main types of funds raised with a view to financing the growth of assets and loans were: (i) larger deposits from

⁶ Based on FINREP reportings

⁷ Based on loan classification reporting

⁸ Based on balance sheet data

customers, (ii) increasing interbank sources and subordinated loans (especially from parent banks) and (iii) higher equity stakes.

Therefore, banks needed to take measures to improve resource management with a view to reducing the vulnerability of volatile funds, diversifying financing sources, bolstering the trend and the stability of deposits taken. In addition, the diversification of the financing base in terms of both resources and the classification by maturity may contribute to maintaining an adequate liquidity level.

Profitability

At end-2008, the key profitability indicators (ROA – return on assets and ROE – return on equity) showed a significantly higher level (1.56 percent and 17.04 percent) compared to that reported at end-2007 (1.01 percent and 9.43 percent). This development was due mainly to the sale of participating interests held by four banks in the equity capital of an insurance company, on the one hand, and to the higher net interest income, on the other.

Given the international context, the cautious policy pursued by the NBR in the regulatory field represented a net advantage, which increased the soundness of the Romanian banking system compared to other countries. Nevertheless, looking ahead, banks performance is expected to diminish amid the contraction of lending and the pick-up in provisioning requirements.

Table 6. Net Assets and Own Funds as at 31 December 2008

	Net assets		Own funds*	
	RON mill.	%	RON mill.	%
1. Banks with majority domestic capital, of which:	36,448.6	11.6	4,583.4	15.8
1.1 State-owned banks, of which:	16,452.6	5.2	2,589.0	8.9
1.1.1 Banks with fully state-owned capital:	13,536.3	4.3	1,664.2	5.7
1. CEC Bank	13,536.3	4.3	1,664.2	5.7
1.1.2 Banks with majority state-owned capital:	2,916.3	0.9	924.8	3.2
1. Banca de Export-Import a României - Eximbank	2,916.3	0.9	924.8	3.2
1.2 Banks with majority private capital, of which:	19,996.0	6.4	1,994.4	6.9
1. Banca Transilvania	17,014.3	5.4	1,705.3	5.9
2. Banca Comercială Carpatica	2,287.7	0.8	209.2	0.7
3. Libra Bank	694.0	0.2	79.9	0.3
2. Banks with majority foreign capital, of which:	259,633.1	82.6	23,265.7	79.9
1. Banca Comercială Română	63,919.7	20.3	5,169.4	17.8
2. BRD Groupe Société Générale	49,239.6	15.7	4,324.7	14.8
3. Volksbank România	21,359.0	6.8	1,673.3	5.7
4. Raiffeisen Bank	18,879.9	6.0	1,794.0	6.2
5. Alpha Bank	17,441.6	5.5	1,309.1	4.5
6. UniCredit Ţiriac	17,373.7	5.5	2,007.0	6.9
7. Bancpost	14,989.3	4.8	1,029.2	3.5
8. Piraeus Bank	9,265.9	3.0	972.9	3.3
9. Banca Românească Grupul National Bank of Greece	9,164.1	2.9	1,085.7	3.7
10. RBS Bank	9,145.6	2.9	603.1	2.1
11. Credit Europe Bank	6,085.9	1.9	496.4	1.7
12. Citibank România	4,222.4	1.3	474.7	1.6
13. OTP Bank România	3,450.2	1.1	380.4	1.3
14. MKB ROMEXTERRA Bank	2,922.4	0.9	181.2	0.6
15. Intesa Sanpaolo România	2,774.8	0.9	512.9	1.8
16. MARFIN Bank	2,345.3	0.8	165.9	0.6
17. Bank Leumi	1,352.4	0.4	257.4	0.9
18. Millennium Bank	1,188.9	0.4	64.1	0.2
19. ProCredit Bank	1,187.2	0.4	131.5	0.4
20. ATE Bank	993.5	0.3	231.6	0.8
21. Emporiki Bank - România	743.3	0.2	160.9	0.6
22. Banca C.R. Firenze România	490.0	0.2	60.2	0.2
23. Romanian International Bank	472.6	0.2	48.4	0.2
24. Raiffeisen Banca pentru Locuințe	276.3	0.1	28.4	0.1
25. Porsche Bank România	232.4	0.1	45.4	0.2
26. BCR Banca pentru Locuințe	63.7	0.0	32.2	0.1
27. HVB Banca pentru Locuințe	53.4	0.0	25.7	0.1
I. Total commercial banks	296,081.7	94.2	27,849.1	95.7
II. Foreign bank branches, of which:	17,663.7	5.6	1,038.7	3.6
1. ING Bank N.V.	10,909.5	3.5	179.1	0.6
2. Banca Italo-Romena	3,329.7	1.0	455.3	1.6
3. Garanti Bank International	1,821.0	0.6	95.2	0.3
4. Anglo Romanian Bank	598.1	0.2	144.2	0.5
5. La CAIXA	321.7	0.1	-13.3	-0.1
6. BLOM Bank France	316.5	0.1	148.7	0.5
7. Bank of Cyprus	252.9	0.1	6.0	0.0
8. Fortis Bank	102.2	0.0	11.8	0.1
9. FINICREDITO	11.3	0.0	10.9	0.1
10. DEPFA Bank	0.8	0.0	0.8	0.0
Total banks and foreign bank branches (I+II)	313,745.4	99.8	28,887.8	99.3
CREDITCOOP	696.1	0.2	213.7	0.7
Total credit institutions	314,441.5	100.0	29,101.5	100.0

*equity (for foreign bank branches)

3.3. Measures to improve prudential supervision of credit institutions

In 2008, although the direct impact of the international crisis on the domestic market could not yet be foreseen, the Romanian supervisory authority paid particular attention to countering the potential effects of the crisis and made further efforts to improve the regulatory and supervisory framework for credit institutions, in line with the EU requirements in the field. The implementation of EU standards and regulations for credit institutions set forth in the documents issued by CEBS was still one of the key objectives of the NBR. The features of 2008 required enhanced international cooperation via regular consultations and meetings of the NBR representatives with foreign supervisory authorities, in order to coordinate the measures taken with a view to maintaining the soundness of institutions performing cross-border operations and the European structures. Moreover, the dialog with the domestic banking community via the Romanian Banking Association and the participation in different events aimed at raising public awareness focused on ensuring the transparency of NBR's activities regarding the issue of new regulations, amendment or implementation of existing regulations, as well as of the challenges and risks the Romanian banking system had to deal with.

The assessment of the manner in which the 25 principles of the Basel Accord on efficient supervision were implemented by the NBR was one of the major events of 2008. During 3-14 November 2008, a joint team of IMF and World Bank experts assessed the Romanian banking system, the supervisory authority's ability and the efficiency of its activity. The mission was part of the Financial Sector Assessment Programme in Romania – FSAP 2008 and was similar to that carried out by the two international institutions in 2003. The objectives of the mission consisted in assessing the laws, regulations, policies and practices at NBR level based on: (i) the self-assessment and a questionnaire to be filled in by the NBR; (ii) in-depth interviews with the NBR staff; (iii) analysis of pieces of legislation, regulations and other documents on which supervision is based, as well as of information on the structure and development of Romania's financial sector; (iv) meetings with other authorities and independent bodies, such as the Ministry of Economy and Finance and the Ministry of Justice; (v) various meetings with banks and the Romanian Banking Association.

The 25 principles subject to assessment were: (1) objectives, independence, ability, transparency and cooperation of the supervisory authority; (2) allowed activities; (3) licensing criteria; (4) transfer of ownership; (5) major acquisitions; (6) capital adequacy; (7) risk management; (8) credit risk; (9) impaired assets, provisions and reserves; (10) large exposures; (11) exposures to persons in a special relationship with the bank; (12) country and transfer risks; (13) market risk; (14) liquidity risk; (15) operational risk; (16) interest rate risk; (17) audit and internal control; (18) abuse of financial services; (19) supervision process; (20) supervision techniques; (21) reporting to the supervisory authority; (22) bank accounting; (23) supervisors' ability to correct and remedy deficiencies; (24) consolidated supervision; (25) relationship between the supervisory authorities in the country of

origin and those in the host country. The assessment was favourable, given that most of the principles had been successfully implemented and that almost all of the recommendations made by previous missions were transposed into practice.

With a view to avoiding, as much as possible, the fallout from the financial turmoil, the NBR acted steadily against the higher banking risks generated mainly by the non-government credit surge, by taking measures aimed at dampening lending and especially foreign currency-denominated loans. Thus, amendments to the norms on loan classification provided the basis for both containing currency risk exposure in the case of loans to households in a currency other than the income currency and, at the same time, pushed up the cost of this type of loans, and implicitly caused their dynamics to slow down. Moreover, the NBR in its capacity as supervisory authority took several measures to closer monitor liquidity and solvency issues at bank level, both under normal circumstances and during crisis situations. These measures comprised: (i) enhanced monitoring of interbank market developments; (ii) optimisation of liquidity shortfall management at bank level so as to allow access to specific facilities provided by the central bank (marginal lending facility, foreign exchange swap); (iii) setting up a standardised reporting format for banks to be used for reporting external sources and placements; (iv) organising meetings with the management of credit institutions in order to assess the risks identified by the latter, the strategies adopted with a view to countering the effects of the crisis, the alternate programmes concerning liquidity and capital requirements, as well the results of stress tests on their prudential stance; (v) contacting supervisory authorities, in certain situations, with a view to increasing majority shareholders' contribution to improve liquidity and implicitly solvency.

In the package of measures aimed at ensuring stability and restore households' confidence in the domestic financial system, and apart from the measures adopted at NBR level, the government decided to increase the deposit guarantee ceiling from the RON equivalent of EUR 20,000 to the RON equivalent of EUR 50,000 starting with 15 October 2008.

With regard to the changes in the supervisory process, they were made in line with the latest developments in the regulatory framework and in the requirements for identifying and containing the risks to which credit institutions are exposed, especially amid the deepening global crisis.

Off-site supervision

Besides the aspects specific to off-site supervision (assessment of banks' financial standing and of the risks they assume in the pursuit of their business, monitoring on a continuous basis of the observance of prudential limits and regulations), in 2008, particular importance was attached to liquidity monitoring. In this context, most of the notifications sent to credit institutions referred to the need of bringing banks' liquidity strategy in line with the legal provisions in the field (NBR Norms No. 17/2003 and NBR Norms No. 1/2001 on bank liquidity, as amended and supplemented). The notifications also referred to the putting in place of alternate

plans that stipulate the conclusion of alternate financing agreements (NBR Norms No. 2/2008 supplementing and amending NBR Norms No. 1/2001 on bank liquidity), as well as to the slow-down of credit growth rate and the worsening of loan portfolio quality. Once the regulation on loan classification and the norms on containing credit risk associated with loans to households were amended, the validation of internal norms on bank lending became necessary, in case they underwent changes.

On-site supervision

In 2008, a number of 54 on-site inspections were performed at 31 banks including head offices and branches, as well as at the Central Cooperatist Bank CREDITCOOP and within its network. Sanctions were imposed on 8 credit institutions, consisting mainly of written warnings imposed on 9 administrators, 4 managers and 3 banks, as well as of fines in the case of the management of 2 banks. Remedial measures were ordered in 41 cases where deficiencies were recorded and deadlines for fulfilling remedial measures were set. Sanctions were imposed for violation of internal control procedures and for failing to implement recommendations or for non-observance of prudential limits for certain indicators. The imposed measures were aimed at improving the risk management framework, the formulation, supplementation and revision of norms, policies and internal procedures, the changes in IT systems, the preparation and revision of alternate plans, the improvement of instruments for assessing operational risk exposure, the discontinuation of granting certain types of loans, the putting on hold of the extension of territorial networks and the elaboration of alternate plans for crisis management situations.

3.4. Banking risk assessment

After a period when the main concern was to moderate fast-paced lending growth and to prevent credit risk from mounting, concurrently with the constraints induced by the global turmoil, a new concern emerged regarding the maintenance of a liquidity balance. Against this backdrop, monitoring of liquidity risk was strengthened by requiring alternate plans for ensuring liquidity including alternate financing agreements, the processing on a daily basis of data on the exposure of each bank on the domestic interbank market with a view to identifying possible imbalances, the monitoring on a daily basis of developments of sources taken from external markets and, in some cases, the conduct of inspections aimed at assessing the risk management framework and liquidity management.

In order to monitor credit risk, the NBR focused especially on the loan portfolio quality by monitoring and containing credit growth and its poor performance, as well as on the loan portfolio concentration, with a view to assessing and limiting banks' exposure to certain economic sectors or categories of customers. Moreover, given the large weight of lending in bank portfolios, inspections focused especially on several areas, such as the manner in which lending activity is conducted, the credit risk management system, i.e. management strategies, policies and methods, as well as the monitoring of credit risk and the techniques for its mitigation.

According to banks' reportings, at end-2008, credit risk accounted for 90.3 percent of capital requirements, whereas operational risk and market risk held 8.9 percent and 0.8 percent respectively.

3.5. International cooperation in the field of prudential supervision

Cooperation within supervisory colleges

Participation and cooperation within supervisory colleges is increasingly important for the NBR in terms of analysis and assessment of risks at individual and consolidated level, i.e. on-site inspections and validation of risk assessment models. By definition, supervisory colleges are standing, flexible coordination structures ensuring cooperation between the authorities responsible for overseeing the different components of cross-border bank groups. The purpose of establishing supervisory colleges is to facilitate the exchange of information, opinions and assessments between supervisory authorities for a more efficient individual and consolidated supervision; to ensure a common understanding of the group's risk profile; to coordinate the analysis and assessment of risks by formulating supervision plans, assigning responsibilities and inspections, thereby avoiding the overlapping and overloading of both supervisors' and supervised credit institutions' activity. As for the organisation of colleges, which have different degrees of association, according to the position of the supervised bank in the group, namely the general college, it implies multilateral meetings and an exchange of information on general issues (general discussions on supervision policy or projects of interest for a large number of authorities) and the basic college, which implies multilateral meetings attended by a small number of authorities, intended to a more structured co-operation that concerns only a limited number of authorities.

So far, the NBR participated in 12 general colleges belonging to the following institutions: the group Crédit Agricole (France), Unicredit (Italy), Intesa Sanpaolo (Italy), Erste Bank (Austria), Raifeisen Zentralbank (Austria), Volksbank (Austria), National Bank of Greece (Greece), Société Générale (France), ING Bank (the Netherlands), BayernLB (Germany), Banco Comercial Portugues (Portugal), OTP (Hungary). The information shared within the general colleges referred to developments of the respective groups and their main international components in 2008, the coordination of supervision among authorities and the set-up of on-site inspection plans, the overview of the group's risk profile, as well as to specific aspects concerning the methodology used to evaluate pillar II indicators.

Cooperation within these colleges implies the conclusion of memoranda of understanding on multilateral cooperation at the level of each active cross-border group. Two such memoranda were concluded (Crédit Agricole, Société Générale). The content of these memoranda is structured according to CEBS recommendation and they will be signed by the authorities in charge of supervising different entities of the group by end-2009. The main sections of the memoranda concern the objectives and principles of cooperation between parties, the ensurance of confidentiality, the assignment of tasks between supervisors, cooperation in crisis

situations, as well as the description of the model validation process and the assessment and analysis of supervision activities.

Cooperation with the supervisors signatories to the regional memorandum between countries in South-Eastern Europe

The memorandum, whose overall goal is the consolidation of stability in South-Eastern Europe and the improved efficiency of supervisory measures, focused particularly on the coordination of supervisors' activity carried out in the region in order to consolidate the supervision of credit institutions at individual and consolidated level and on the identification and correction of some issues relative to contagion and spread of the fallout from the global turmoil. The exchange of information referred to the position of the financial systems in the region and of the bank groups carrying out activities in the seven countries signatories to the memorandum, as well as to the internal control system and the internal organisation of bank groups.

Cooperation with partner supervisory authorities abroad

Amid the difficulties generated by the worsening international and domestic environment, cooperation with foreign supervisory authorities played a significant role in achieving the goals of supervision. In 2008, the bilateral meetings focused mainly on presenting and analysing the developments of institutions performing cross-border activities and on finding solutions to mitigate the impact of the global crisis on the entities established in Romania.

Thus, in the case of entities posting a poor performance of asset portfolio, solvency or liquidity, the authorities involved debated on supporting these entities by an increase in contributed capital or on taking other measures aimed at improving their financial situation. Special emphasis was put on cooperation with the authorities supervising the banks that held the largest market share in Romania, i.e. the Financial Market Authority (Austria) and Bank of Greece. Moreover, on 29 March 2009, nine large international banks signed a memorandum to support their subsidiaries in Romania in order to: (i) confirm that these affiliates' good financial standing will be preserved throughout the period of market turbulences and economic slowdown; (ii) demonstrate the long-term commitment to the development of the Romanian economy; and (iii) signal their readiness to contribute to the efforts of the international community to put in place comprehensive and well-coordinated measures to counter the effects of the financial crisis.

To the 10 memoranda on cooperation signed during 2001-2006 added a memorandum with the central bank of Portugal (Banco de Portugal) in force as of 11 March 2009. Moreover, negotiations were being held on a memorandum on cooperation with the supervisory authority in Spain (Banco de España).

3.6. Non-bank financial institutions

At end-2008, some 238 non-bank financial institutions were registered with the General Register, 20 more from the previous year, as a result of the registration of 30 new companies and the easement of 10 institutions. In the same period, the number of non-bank financial institutions registered with the Special Register increased from 38 to 53, following the fulfilment by some non-bank financial institutions of the criteria set forth in NBR Norms No. 6/2006.

**Table 7. Breakdown of non-bank financial institutions by activity
as of 31 December 2008**

Activity	Special Register		General Register*		General Register	
	No.	%	No.	%	No.	%
Multiple lending activities	30	56.60	97	52.43	127	53.36
Financial leasing	20	37.73	68	36.76	88	36.97
Consumer loans	1	1.89	7	3.78	8	3.36
Issuing of guarantees and assuming commitments, including credit guarantee	1	1.89	5	2.70	6	2.52
Micro-crediting	0	0.00	6	3.24	6	2.52
Mortgage and/or real-estate loans	1	1.89	0	0.00	1	0.42
Financing of commercial transactions	0	0.00	1	0.54	1	0.42
Factoring	0	0.00	1	0.54	1	0.42
Discount	0	0.00	0	0.00	0	0.00
Forfeiting	0	0.00	0	0.00	0	0.00
Other financing means in the form of credit	0	0.00	0	0.00	0	0.00
Total	53	100	185	100	238	100

* Excluding non-bank financial institutions in the Special Register

Similar to 2007, the great majority of non-bank financial institutions, i.e. 53.36 percent, were involved in multiple lending activities and 36.97 percent in financial leasing. No non-bank financial institution was registered with three sections of the General Register (discount, forfeiting and other forms of non-bank financing). Moreover, there are only a few non-bank financial institutions dealing mainly with financing of commercial transactions, factoring or granting of mortgage loans and/or housing loans, only one such institution being registered with each of these sections of the General Register.

Overall, in 2008, the weight in the Romanian economy of the NFI sector, a component of the financial and banking sector, moved up. Thus, at end-2008, total assets held by non-bank financial institutions accounted for 8.4 percent of GDP⁹, up from the level recorded at end-2007. At end-2008, total assets of this sector amounted to RON 42,565.2 million, up 43 percent from the previous year. This substantial rise was due mainly to the increases in share capital, borrowings and the establishment of new non-bank financial institutions during 2008.

⁹ Estimated at RON 503.958 billion by the NIS

Table 8. Main Indicators of the NFI Sector as of 31 December 2008

Indicator	RON million		
	Special Register	General Register*	General Register
Share capital	1,646.4	667.1	2,313.5
Total assets	39,578.6	2,986.6	42,565.2
Loans granted (net), of which:	32,833.5	1,987.2	34,820.7
- financial leasing	26,417.9	1,297.3	27,715.2
- other types of loans	6,415.6	689.9	7,105.5
Doubtful and overdue loans	1,705.6	34.9	1,740.5
Provisions (for doubtful and past-due claims)	914.3	234.1	1,148.4
Balance of overdue loans	3,641.3	398.7	4,040.0
Profit/loss	-378.4	-134.9	-513.3

* Excluding NFIs in the Special Register

The structure of activities carried out by non-bank financial institutions shows that financial leasing held a large share in total loans (79.6 percent for the entire sector) and 80.5 percent in the Special Register, slightly down from the levels recorded in prior year (81.7 percent and 85.9 percent respectively).

At end-2008, non-bank financial institutions witnessed an aggregate loss of RON 513.3 million. Nevertheless, 26 out of 53 non-bank financial institutions registered with the Special Register, i.e. 101 out of 185 non-bank financial institutions registered only with the General Register, reported gains. The main factor behind these unfavourable developments was the deterioration of debtors' repayment behaviour, especially in 2008 H2, as a direct effect of the economic crisis.

The table below shows the distribution of non-bank financial institutions' share capital by country of origin for the 53 companies registered with the Special Register at end-2008.

Table 9. Shares of Foreign Capital by Country of Origin

Country of origin	Participations of foreign capital (%)	
	in total foreign capital	in total capital
The Netherlands	47.31	27.56
France	12.87	7.50
Italy	8.90	5.18
Sweden	7.57	4.41
Cyprus	6.43	3.74
Austria	5.01	2.92
Belgium	4.11	2.39
Greece	3.74	2.18
USA	3.14	1.83
Germany	0.37	0.22
Hungary	0.36	0.21
The United Kingdom	0.10	0.06
Switzerland	0.06	0.04
Ireland	0.03	0.02

In 2008, foreign capital came from 14 countries, of which 6 (Belgium, the USA, Hungary, the United Kingdom, Switzerland and Ireland) are new entries, compared to 2007. This shows an increase in the number of countries providing foreign capital, concurrently with a decrease in foreign capital concentration. Thus, the first three countries mentioned in the table provided 69.08 percent of total foreign capital, compared to 82.8 percent in 2007. Mention should be made that most of the countries are EU Member States, which points to a high degree of integration of the NFI sector in the European financial and banking industry.

Furthermore, it is to be noted that the weight of domestic capital in total share capital of non-bank financial institutions dropped slightly from 45.6 percent in 2007 to 41.74 percent at end-2008.

3.7. Prudential supervision and monitoring of non-bank financial institutions

In 2008, prudential supervision and monitoring actions of non-bank financial institutions were conducted having in view the observance of the provisions of Government Ordinance No. 28/2006 on some tax and financial measures, as amended and supplemented, as well as of the secondary regulations in this field issued by the central bank.

Thus, following the quarterly assessment of the compliance with the provisions in force concerning the reporting on a regular basis by non-bank financial institutions, a number of 70 off-site supervision reports were prepared. In 43 cases, sanctions stipulated by the aforementioned ordinance were imposed, as follows: 8 written warnings, 31 fines and 4 suspensions from performing lending activities.

As regards on-site inspections, during June-July 2008, inspectors within the NBR branches performed checks at the headquarters of 180 institutions registered with the General Register that had not been inspected in 2007. Following the inaccuracies found, a number of 142 non-bank financial institutions were sanctioned as follows: lending activity was prohibited in 15 cases and written warnings were sent to 127 institutions. The institutions were notified to draw up and submit to the Supervision Department plans for correcting the respective inaccuracies. Moreover, in October 2008, inspectors within the NBR Bucharest branch conducted on-site inspections in 18 non-bank financial institutions, in order to check the manner in which previously found inaccuracies were corrected. Following these inspections, a number of 6 entities were warned and other 11 entities received notification letters.

In 2008, monitoring the observance of provisions of NBR Regulation No. 3/2007 on containing credit risk associated with loans to households, as amended and supplemented, was part of supervision activity as well. This aspect was checked during on-site inspections, as well as within the validation process of internal norms on loans to households submitted to the Supervision Department for this

purpose. By end-2008, the validation of internal norms on loans to households was granted to 5 non-bank financial institutions registered with the Special Register.

Moreover, following the notifications sent by non-bank financial institutions in 2008, the following changes were operated in the registers kept by the NBR:

- the shift of certain NFIs from one section of the General Register to another, following the change of their scope of activity;
- the recording of certain NFIs in the Special Register, following the fulfilment of the indicators level set by NBR Norms No. 6/2006;
- the erasure from the General Register of 10 NFIs, out of which 6 at the request of the respective institutions, 2 following mergers with other entities, while in 2 cases the erasure was imposed as a sanction.

Changes in the registers concerned headquarters or name changes as well.

Chapter 3. Currency issue

In 2008, the National Bank of Romania fulfilled its tasks as an issuing bank by providing the currency necessary to ensure smooth money circulation in terms of quantity, quality and denomination composition. The new amounts of notes and coins issued according to the Programme for Printing Notes and Minting Coins were meant to replace worn-out or deteriorated banknotes and coins, as well as to cover the annual increase in the value of currency outside banks.

The central bank put into circulation starting 1 December 2008 a new, redesigned note with face value of *lei* 10 which circulates in parallel with the *lei* 10 banknotes issued in 2005.

1. Developments in currency outside banks

In 2008, currency outside banks showed a moderation in growth to reach *lei* 26,960 million¹ at year-end, up 17 percent from 2007. This was the lowest increase in the post-communist era, which saw annual growth rates between 25 percent (1998) and 155 percent (1993). In the period under review, the annual percentage changes were about three times slower than a year earlier.

Monthly developments in currency outside banks point out three periods at the end of which more significant growth rates than at the end of the prior periods were recorded (as much as 2.4 percentage points from the monthly average). Thus, at end-April 2008, the value of currency outside banks increased by *lei* 942 million (up 4.1 percent) month on month, at end-June it rose by *lei* 768 million against end-May (up 3.2 percent) and posted the sharpest expansion by *lei* 1,116 million in October (up 4.5 percent) versus the prior month.

October was atypical in terms of both cash payments and currency in circulation as compared to previous developments in this month as well as to any other month of the year when payments and currency outside banks usually reach peaks. Payments carried out by the NBR in October ran at *lei* 3,418 million, about twice as much than in September and 63 percent above the estimated value. On 13 October, cash withdrawals of credit institutions totalled *lei* 694.5 million, an all-time high of payments performed by the NBR in one day.

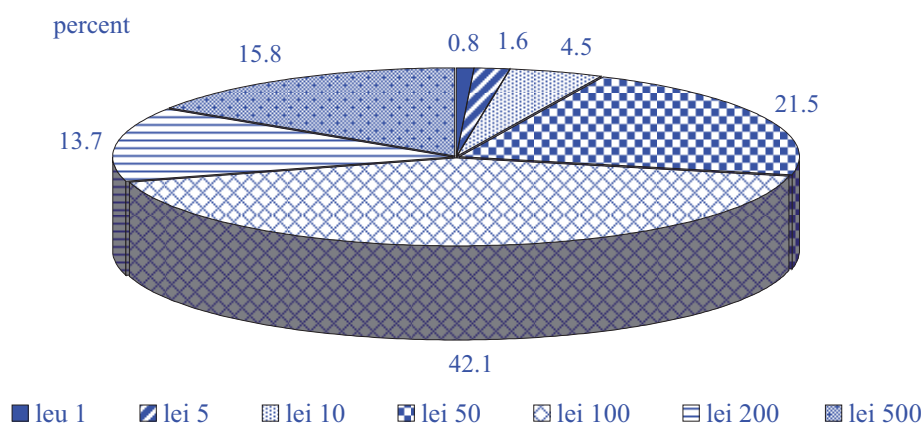
Two months later, on 19 December 2008, currency outside banks reached its peak for 2008 in terms of value, i.e. *lei* 28,777 million, up 18 percent from the high of December 2007.

¹ RON 25,314 million, excluding the cash in automatic teller machines, automatic exchange teller machines and money market funds' vault cash.

Payments performed in December worth *lei* 3,490 million were about 7 percent lower against the same year-ago period and 14 percent below the level estimated at the beginning of December 2008. Nevertheless, the payment peak of the month (*lei* 590 million) recorded on 12 December was 30 percent higher than in the same year-ago period.

At end-2008, the number of banknotes in circulation dropped by 4 percent year on year, while in terms of value, banknotes in circulation witnessed a 17 percent increase. The increase in the value of banknotes in circulation along with to their decline in volume was the result of the 2 percentage point pick-up in the shares of *lei* 50, *lei* 100 and *lei* 200 banknotes and the drop in those of *leu* 1 and *lei* 5 banknotes by 4 percentage points and 3 percentage points respectively, in total currency used by the NBR for payments to credit institutions. Nevertheless, the share held by *lei* 50 banknotes in the total value of banknotes in circulation shrank 5 percentage points versus the previous year to approximately 21 percent. At end-2008, *lei* 100 banknotes held 42 percent of the total value of banknotes in circulation, accounting for roughly 47 percent of their rise in value. The *lei* 200 banknote also posted a significant increase in the total value of banknotes in circulation; at end-December it accounted for 14 percent of total value of banknotes in circulation, up approximately 10 percentage points from the same year-earlier period. At end-December 2008, *lei* 500 banknotes took nearly 16 percent of the total value of banknotes in circulation, i.e. about 2 percentage points lower than at end-2007.

**Denomination Composition in Total Value
of Banknotes Outside Banks**



At end-2008, the number of coins outside banks stood 48 percent higher than at end-2007. This rise was in line with the tendency to maintain the high interest in resorting largely to metal coins for payments and in particular to middle-value denominations. For example, the *bani* 10 coin accounted for approximately 40 percent of total number of coins outstanding with households and companies, followed by the *bani* 5 coin with a share of about 30 percent of the total figure.

Coins in circulation posted a 43 percent increase in value, down 5 percentage points below the growth in number of coins. This development was due mainly to the 5 percentage point rise in the share of *bani* 5 coins in total coins in circulation.

At end-2008, out of the total number of notes and coins in circulation, the number of notes and coins per inhabitant amounted to 34 and 51 respectively.

Average value of a banknote in circulation was *lei* 39.2, up *lei* 8 versus that recorded at end-2007. The increase was due to the 4 percentage point rise in the share of *lei* 100 banknotes in currency in circulation, a denomination in high demand by credit institutions for the frontloading of automatic teller machines (ATM), as well as to the 3.2 times expansion in the number of *lei* 200 banknotes. Although not yet used in frontloading of ATMs, the *lei* 200 banknote fitted into money circulation starting with 2008, being increasingly requested by credit institutions. 2008 was the first year when the last denomination in the newly-issued series witnessed a normal circuit, with 60 percent out of the 22.8 million banknotes introduced by the NBR through payments remaining in circulation.

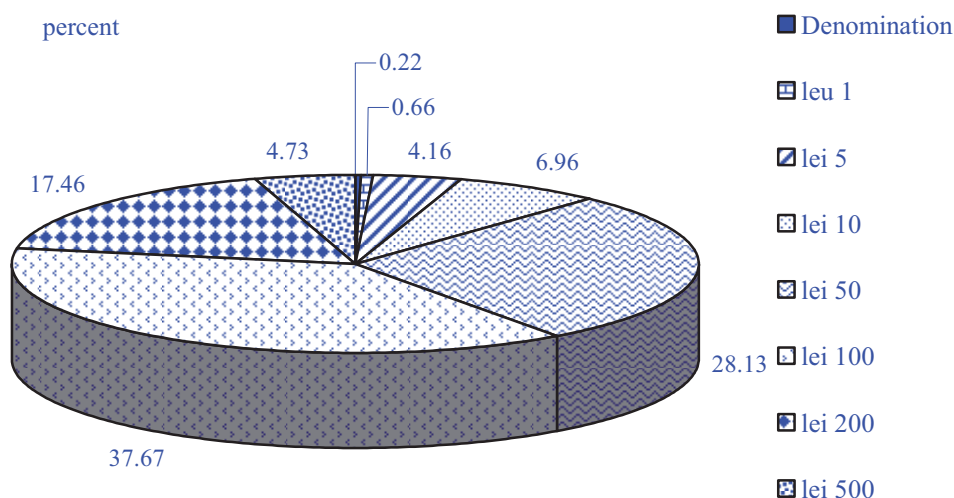
2. NBR's cash payments and receipts in the relationship with credit institutions

During 2008, some 842 million banknotes and 368 million coins, in amount of *lei* 26,112 million, about 30 percent higher than in 2007 were put into circulation via payments to credit institutions. Together, *lei* 1 and *lei* 5 banknotes held roughly 40 percent of total banknotes used for payments while *lei* 50, *lei* 100 and *lei* 200 banknotes took nearly 84 percent of the total value of banknotes put into circulation in 2008. Roughly 269 million coins with face value *bani* 5 and *bani* 10 accounted for around 73 percent of total coins in circulation. In year-on-year comparison, three times more *bani* 5 coins, some 20 percent more *bani* 10 coins and about 25 percent more *bani* 50 coins were put in circulation, following the growing demand of credit institutions, as these coins were required by an increasing number of cash user categories.

Compared to the previous year, in 2008, composition by denomination and the share of each denomination in total coins used for payments shifted along the entire scale of face values. Thus, the shares of *bani* 1, *bani* 10 and *bani* 50 coins narrowed by 3 percentage points, 9 percentage points and 5 percentage points respectively, while that of *bani* 5 coins picked up 17 percentage points.

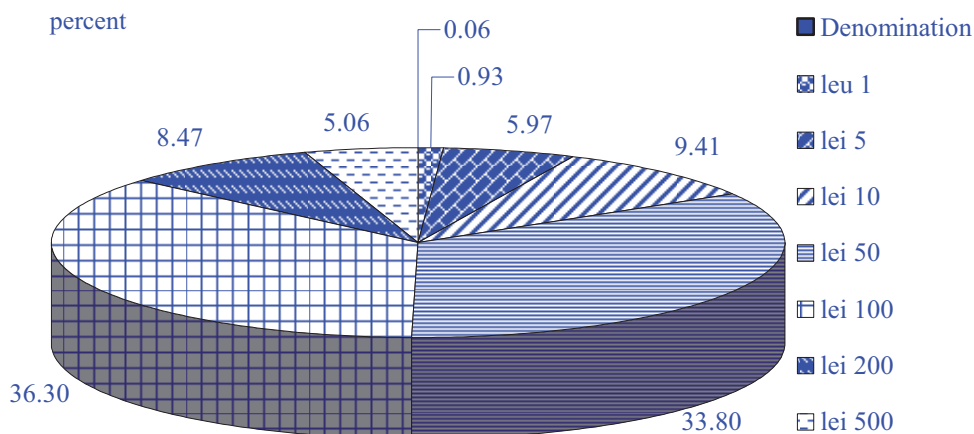
The NBR succeeded in constantly ensuring the strong demand for coins in the years following the redenomination of the domestic currency, especially for the two denominations in the middle of the face value scale. In this context, 2008 marked a significant step in meeting the requirements of all market segments.

Payment Composition by Denomination



Some 936 million banknotes, 11 percent more than those put in circulation throughout 2008 and 28 million coins, accounting for 7.6 percent of the number of coins resulting from payments, returned to the National Bank of Romania via collections from credit institutions. NBR's collections from credit institutions' deposits amounted to *lei* 22,511 million, i.e. 90 percent higher than in 2007. *Leu* 1 and *lei* 5 banknotes took 50 percent of the total number of banknotes collected by the NBR from credit institutions, while *lei* 50 and *lei* 100 banknotes accounted for 70 percent of the total value of banknotes collected. Similar to the previous years, once put into circulation the coins stayed outside the banking system, the only denominations which returned to the central bank being the *ban* 1 coin (to a proportion of 11 percent) and the *bani* 50 coin (to a proportion of 33 percent). The *bani* 50 coin held 89 percent of total quantity of coins collected and 99.5 percent of their value.

Receipt Composition by Denomination



3. Currency processing

The NBR has been seeking to ensure the authenticity, integrity and a homogenous quality of banknotes in circulation. Hence it withdrew and destroyed unfit notes and coins returned to the central bank via credit institutions' deposits or those submitted by individuals for exchange. At the same time, the central bank ensured the withdrawal from circulation of unfit banknotes and their replacement by new or circulated but adequate notes and coins.

In 2008, roughly 859 million banknotes (up 33 percent versus the previous year) were processed by using the high- and medium-speed automated equipment located in the four processing centres of the NBR.

Out of 983 million banknotes destined for processing, i.e. 936 million banknotes from credit institutions' deposits in 2008, along with the 47 million unprocessed banknotes on stock at end-2007, some 87 percent were processed.

Out of the banknotes processed in 2008, some 30 million banknotes were sorted as unfit for money circulation (worn out or deteriorated), resulting in an unfit banknote rate of 3.5 percent, i.e. almost 4.8 times lower than that in the euro area. The quality and durability of polymer-based Romanian banknotes translate into larger service life than that of paper-based notes.

Over the year under review, 169.7 million banknotes which were unfit for circulation were destroyed on-line by using the automated processing equipment and off-line by using the banknote shredding machines located in the processing centre of the NBR's Bucharest Branch. Of the aforementioned quantity of banknotes, some 162.1 million, accounting for 96 percent, belonged to the old issue. Out of the 7.6 million banknotes of the new issue unfit for circulation which were destroyed (less than one banknote destroyed per 3 inhabitants), small-value banknotes (*leu 1* and *lei 5*) held a share of 65 percent.

Out of the total quantity of 36 million coins, i.e. 28 million coins from credit institutions' deposits throughout 2008, along with the 8 million unprocessed coins on stock at end-2007, some 32 million coins (making up 89 percent) have been processed by using the automated authentication, counting, qualitative sorting and packaging equipment located in the four NBR branches performing cash operations.

Some 5.1 million coins, all part of the old issue, were destroyed in 2008.

4. Numismatic issues

In 2008, the National Bank of Romania further launched numismatic issues destined to coin collectors. These issues, meant to promote Romanian values both domestically and abroad, were dedicated to cultural, historical and political events as well as to outstanding cultural, historical and scientific figures. Moreover, it continued to launch the annual series of sets of coins including coins in circulation, accompanied by a silver medal dedicated to the event celebrated by the respective

set. Last but not least, the series “Monuments of Feudal Christian Art” and “History of Gold” continued, and in the series of historical replica coins, a replica of the *lei* 20 coin in the 1922 issue was minted.

In 2008, the National Bank of Romania issued 16 coins, of which 4 of gold, 10 of silver and 2 of coppered tombac. The issues consisted of 4,000 gold coins, 5,000 silver coins and 2,000 coppered tombac coins. In addition, 1,000 minting sets and 500 replica coins were issued.

The following table presents an overview of the 2008 numismatic issues, including data on the metal the coins are made of, as well as their face value.

Coin/medal issue	Metal and face value
Publius Ovidius Naso	gold coin with face value of <i>lei</i> 100, silver coin with face value of <i>lei</i> 5 and coppered tombac coin with face value of <i>lei</i> 1
NATO Summit organised in Bucharest during 2-4 April 2008	gold coin with face value of <i>lei</i> 100, silver coin with face value of <i>lei</i> 5 and coppered tombac coin with face value of <i>lei</i> 1
The 150th anniversary of the issue of the first Romanian postage stamps referred to as “Bull’s Head”	silver coin with face value of <i>lei</i> 10
The 100th anniversary of the birth of the economist Costin Kirişescu	silver coin with face value of <i>lei</i> 10
The 500th anniversary of the first printings manufactured on the Romanian territory, at Dealu Monastery	silver coin with face value of <i>lei</i> 10
The bicentennial anniversary of the birth of Simion Bărnuţiu	silver coin with face value of <i>lei</i> 10
The centennial anniversary of the building of “Grigore Antipa” Natural History Museum	mint set comprising a silver medal and the Romanian coins in circulation with face values of <i>ban</i> 1, <i>bani</i> 5, <i>bani</i> 10 and <i>bani</i> 50
“Monuments of Feudal Christian Art” – Cozia, Voroneţ and Brâncoveanu monasteries	coin issue comprising three silver coins with face value of <i>lei</i> 10
The 80th anniversary of the establishment of the Romanian Radio Broadcasting Company	silver coin with face value of <i>lei</i> 10
Replica of the <i>lei</i> 20 coin of 1922	gold replica
The 90th anniversary of the Grand Union of 1 December 1918	gold coin with face value of <i>lei</i> 500
“The History of Gold” - Hinova hoard	gold coin with face value of <i>lei</i> 10

5. Counterfeiting of the domestic currency and of the euro

In 2008, the National Bank of Romania continued to prevent counterfeiting of domestic currency by both ensuring an adequate quality of currency in circulation and cooperating with institutions involved in combating counterfeit currency.

According to the regulations in force and upon the request of the units within the Ministry of Administration and Interior specialised in combating and preventing counterfeit, banknotes and coins (RON and EUR) suspected to be counterfeit were subject to tests by analysing their specific security features.

The further use of polymer, which features a higher security against counterfeiting than paper, contributed to the low number of counterfeits in 2008 (2.87 counterfeit banknotes in 1 million banknotes in circulation).

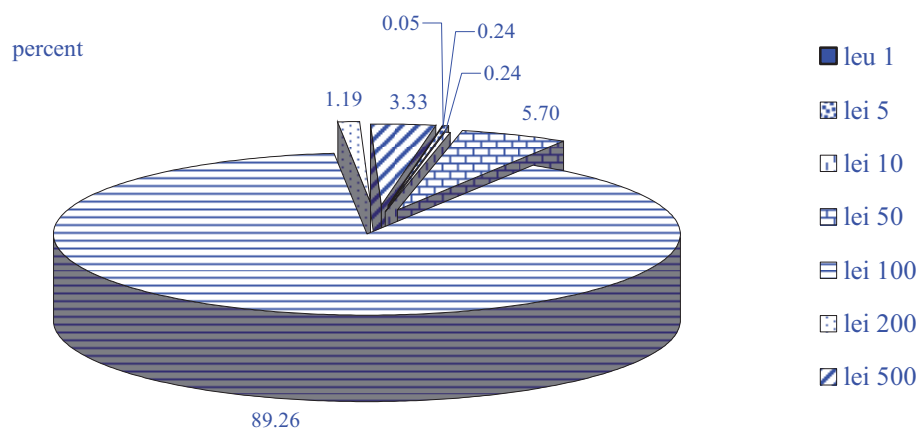
Thus, in the period under review 2,104 counterfeit Romanian banknotes were detected, up 16.8 percent from the previous year. The following table sets out the quarterly distribution of counterfeits:

2008			
Q1	Q2	Q3	Q4
84	156	468	1,396

The following table shows the distribution of counterfeits by denomination:

Denomination	Number of counterfeits
leu 1	1
lei 5	5
lei 10	5
lei 50	120
lei 100	1,878
lei 200	25
lei 500	70

Number of Counterfeits of the New Denominations



The *lei* 100 denomination recorded the highest number of counterfeits, i.e. 1,878 banknotes, of which 72 were made of plastic trying to imitate polymer. The *lei* 50 denomination came in second, totalling 120 counterfeits, of which 27 of plastic.

The technique used in most of the counterfeits on paper or plastic was poor, namely photocopying or scanning, and lacked security features of the banknotes in circulation, thus being easily detected by users. The only security element of the counterfeits was the transparent window which however lacked several features of an authentic banknote.

In 2008, the number of counterfeit euro banknotes detected in Romania stood at 2,701, up 8.5 percent versus 2007.

In spite of the slight increase in counterfeits both of national and euro banknotes versus the previous year, due to the launch of more sophisticated reproduction means, the confidence of general public in the two currencies remains high. Thanks to their specific security features, the public can easily distinguish authentic notes from counterfeits.

In 2008, the NBR continued to increase public awareness in order to recognize counterfeit RON or EUR banknotes by providing credit institutions with leaflets describing the banknotes' security features.

Chapter 4. Payment and settlement systems

In 2008, the smooth functioning of payment systems continued to be one of the major interests of the National Bank of Romania, which thus fulfilled one of the tasks provided by Law No. 312/2004 on the Statute of the National Bank of Romania.

The National Bank of Romania operates a real-time gross settlement payment system for large-value and urgent payments in domestic currency (ReGIS), and a central depository and securities settlement system for government securities and certificates of deposits issued by the National Bank of Romania (SaFIR). The central bank manages both systems, whereas services related to technical operation of the system were outsourced to TRANSFOND (as technical provider)¹.

Apart from the above-mentioned systems, the National Bank of Romania operates a payment system which ensures the paper-based clearing of payments made via debit payment instruments (cheques, bills of exchange and promissory notes). October 2008 saw the launch of SENT, which allows the electronic processing of debit payment instruments, with the system ensuring the paper-based clearing of payments via debit payment instruments (PCH – payment clearing house) – managed by the National Bank of Romania – being due for closure on 4 May 2009. Therefore, during October 2008 – May 2009, paper-based payment instruments may be cleared via both systems (SENT and PCH).

1. ReGIS

General aspects

ReGIS ensures the real-time gross settlement of large-value or urgent payments in domestic currency made by credit institutions, on its own behalf and account or on customers' account, as well as of payments in domestic currency arising directly from, or made for the settlement of net positions initiated by the net settlement systems and the settlement of the cash lag of operations performed with financial instruments.

In 2008, ReGIS contributed further to the smooth operation of money market and forex market, still playing a major role in the successful implementation of the National Bank of Romania's monetary policy, in view of the fact that monetary policy operations performed by the central bank are processed solely through this system.

ReGIS continued to run smoothly in 2008 as well, the volume of large-value and urgent payments settled through it posting a steady increase which contributed to the achievement of the National Bank of Romania's policy objective, i.e. promoting the settlement in the central bank money, as the sole means of payment.

¹ TRANSFOND is a joint-stock company, having as shareholders the National Bank of Romania (33.33 percent) and 23 credit institutions (66.67 percent).

Participation in the system

The number of participants in ReGIS continued to increase in 2008. At year-end, among the participants were 42 credit institutions, the National Bank of Romania, the State Treasury and 5 ancillary systems (SENT, SaFIR, RoClear, VISA Europe and MasterCard International).

Pricing policy

In view of the National Bank of Romania's objective to provide means of making payments efficient for the economy² and to adjust fees to the level of similar fees applied in the other EU Member States, the National Bank of Romania continued in 2008 as well to pursue the same policy aimed at reducing fees related to ReGIS. Thus, on 1 August 2008, the National Bank of Romania cut down the fee per transaction by 10 percent (from RON 8.03 to RON 7.23).

Payments in ReGIS

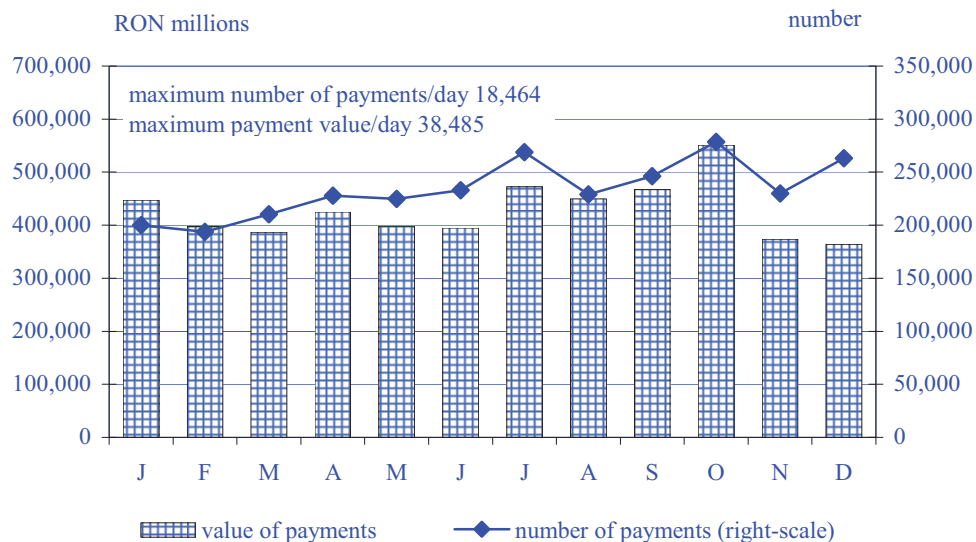
In 2008, both the average daily volume and the average daily value of payments via ReGIS posted increases versus the previous year (by 33 percent and 45 percent respectively). Table 1 shows a general picture of the payments traffic in ReGIS in 2007 and 2008.

Table 1. Payments Traffic in ReGIS

	Volume (no. of transactions)		Value (RON mill.)		Average value per transaction (RON mill.)
	Total	Daily average	Total	Daily average	
2007	2,097,829	8,259	3,530,015	13,898	1.68
2008	2,804,864	10,999	5,126,374	20,104	1.83
Change (±%)	+33	+33	+45	+45	+9

² This objective subscribes to the fundamental principles set forth by the Committee on Payment and Settlement System of the G-10 Group, which were adopted also by the Governing Council of the European Central Bank as minimum standards for supervision by the Eurosystem of large-value payment systems operating in euro (implicitly of national real-time gross settlement systems).

Developments in Large-value and/or Urgent Payments in 2008



The volume of payments settled throughout 2008 by ReGIS was nearly 2.8 million transactions; in January, the daily average stood at 9,520 transactions, whereas in December, it came in at 13,152 transactions. The peak of the daily volume of payments settled through ReGIS was recorded in October 2008 (18,464 transactions/day).

Developments in Large-value and/or Urgent Payments in 2008 versus 2007

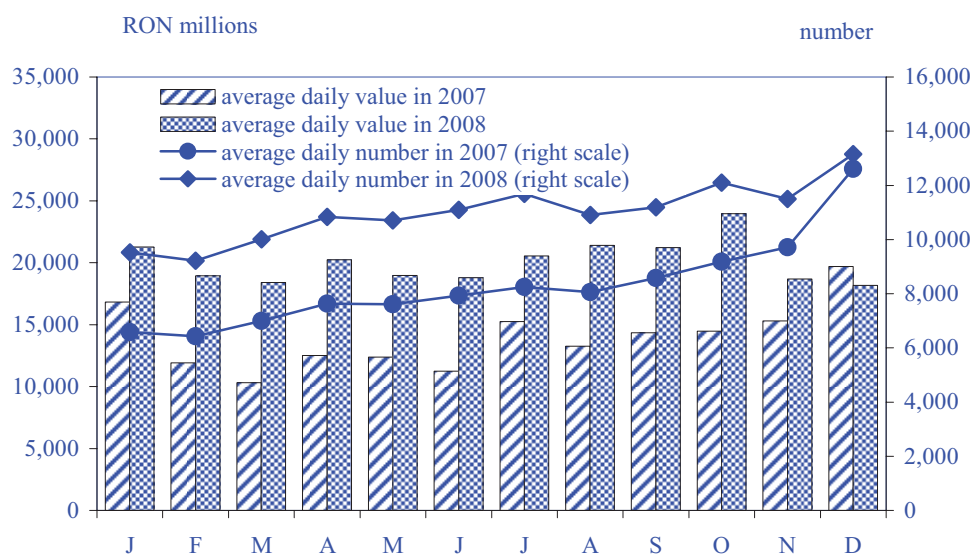


Table 2 shows the structure of payments via ReGIS in 2008 by type of message which indicates that payment transactions carried out by financial institutions on

their behalf, but on customers' account (SWIFT MT103 messages-customer payments) prevailed, holding 88.63 percent of the total volume of transactions in the system); however, their total value was relatively low, accounting for only 14.14 percent of the total value of transactions in the system). However, the volume of payment transactions carried out by financial institutions on their behalf and account (SWIFT MT202 messages) was relatively low, while their value was significant.

Table 2. Structure of Payments in ReGIS in 2008

Payments	MT103	MT202	<i>percent</i>
			Direct transfer
Total volume	88.63	9.27	2.10
Total value	14.14	76.90	8.96

The volume of payment transactions involving direct debiting/crediting of participants' settlement accounts stood at a low level given the low frequency of these operations (the collection of fees by the National Bank of Romania, operations in relation with the central bank, operations carried out by the National Bank of Romania on participants' behalf, in contingency situations, when they are not able to connect to the system and perform the operations etc).

As concerns the volume of payments made through ReGIS, market concentration is comparable to that in the previous year, the top five credit institutions accounting for about 55 percent of the market (against 56 percent in 2007). By contrast, in terms of value of payments via ReGIS, the concentration degree increased, the top five credit institutions holding nearly 60 percent of the market (compared with 42 percent in the preceding year).

A very high operating level in terms of ReGIS availability represents another major objective of the National Bank of Romania, taking into account the importance of the ReGIS system to the banking and financial system and the national economy. In 2008, the average availability of ReGIS, namely the extent to which participants could use the system without encountering difficulties during operations, was 99.99 percent, falling within the range of tolerances established by the National Bank of Romania according to the service level agreement.

In its capacity as system administrator, the National Bank of Romania continued to monitor steadily the settlement and activity of participants in the ReGIS system in 2008. The participants' behaviour was adequate, in accordance with the system rules and procedures, without their being subject to any penalties or sanctions. No gridlock situations occurred due to the lack of funds in one or more participants' settlement account/s. In 2008, participants succeeded in adequately and efficiently managing their liquidities, the number of payment instructions in the queue being relatively small and lasting for a short time only.

2. The payment system ensuring the paper-based clearing of payments via debit payment instruments (PCH)

This system ensures the paper-based clearing of payments via cheques, bills of exchange and promissory notes, being the last component of the former national paper-based payment system. The system is managed by the National Bank of Romania and operated by TRANSFOND, in its capacity as agent of the central bank.

In 2008, the traffic of cleared payments made by debit instruments (cheques, bills of exchange and promissory notes) increased significantly compared with 2007 in terms of both volume and value (9.1 percent and 35.4 percent respectively). The changes in payment flow of cleared payments through this system are shown in Table 3.

Table 3. Developments in Paper-based Cleared Payments

Payments	2007	2008	Change (±%)
Volume (mill. instruments)	7.7	8.4	+9.1
Value (RON mill.)	52,022	70,458	+35.4
Average daily value (RON mill.)	204.81	276.31	+34.9

In 2008, this system ensured the clearing of roughly 8.4 million payment instruments with a total value of RON 70,458 million; the daily average value of payments was nearly RON 276.31 million.

October 2008 saw the completion and implementation of the project for replacing this system by an automated component. The migration to the electronic processing of debit payment instruments via SENT will be gradual; in early May 2009, these payment instruments are expected to be processed mainly via this system, whereas the instruments that cannot be processed electronically due to reasons pertaining to the impossible use of the truncation procedure (such as the existence of some factors affecting the visibility of mentions attached to these instruments) are anticipated to be subject to interbank processing based on bilateral agreements between the concerned credit institutions.

3. SaFIR

General aspects

Central depositories and securities settlement systems are essential components of financial market infrastructure. For the central bank, the importance of the central depository and securities settlement system (SaFIR) consists in the interaction of this system with the other payment systems, as well as in the role played by these financial instruments in the settlement of monetary policy operations.

Face value of outstanding issues

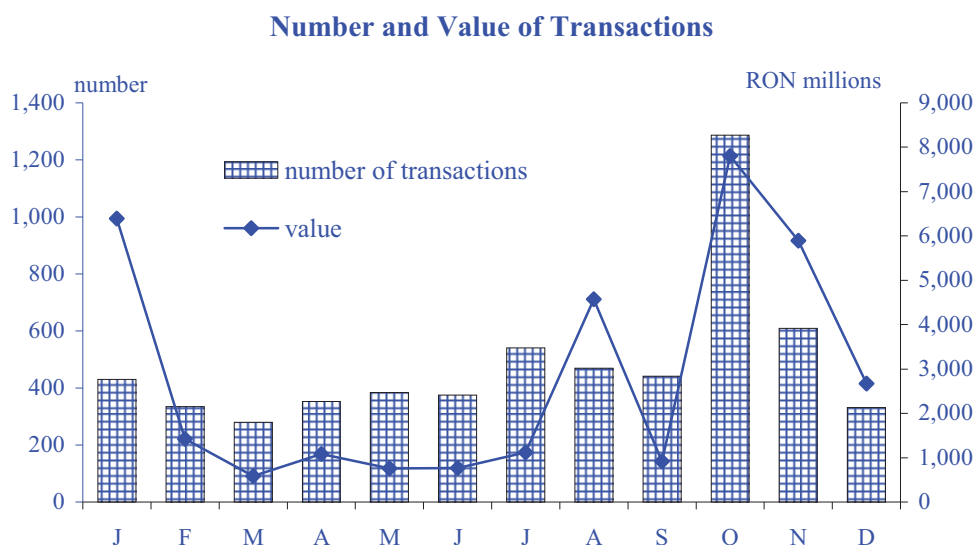
In 2008, the overall face value of issues of lei-denominated securities registered with SaFIR increased versus end-2007, following the turnaround in the primary market for government securities, the placement of new benchmark issues, and also the re-opening of outstanding benchmark issues.

The face value of outstanding government securities amounted to RON 17,570.48 million at end-2008, up significantly from that seen at end-2007.

Operations settled via SaFIR

SaFIR settles operations performed by participants in relation to the issuer (settlement of primary market results, interest and/or coupon payments, partial/optional/total redemption) and operations carried out by participants on the secondary market (sale/purchase transactions, financial collateral arrangements, repo transactions, portfolio transfers).

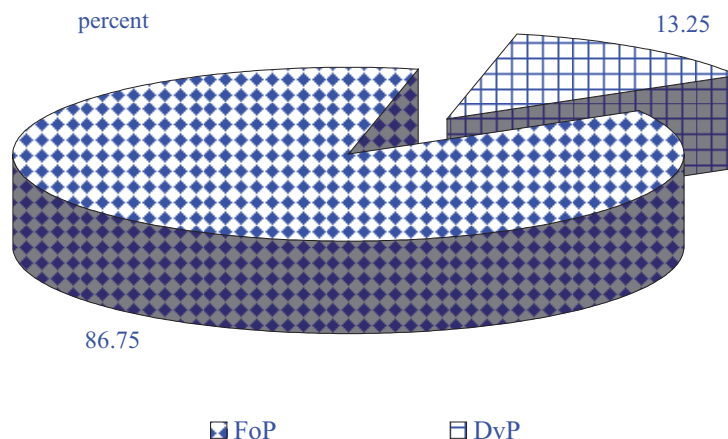
The following chart shows the number and value of sale/purchase transactions, including also repo transactions.



The structure of the transfers of financial instruments reveals the main feature of the secondary market for government securities. Out of the total number of transfers made in 2008, 86.75 percent were free-of-payment transfers (FoP), representing trades between credit institutions and their own customers.

In 2008, the number of delivery-versus-payment transfers (DvP) expanded by about 73 percent versus the previous year due to the step-up in the interbank activity on the secondary market for government securities.

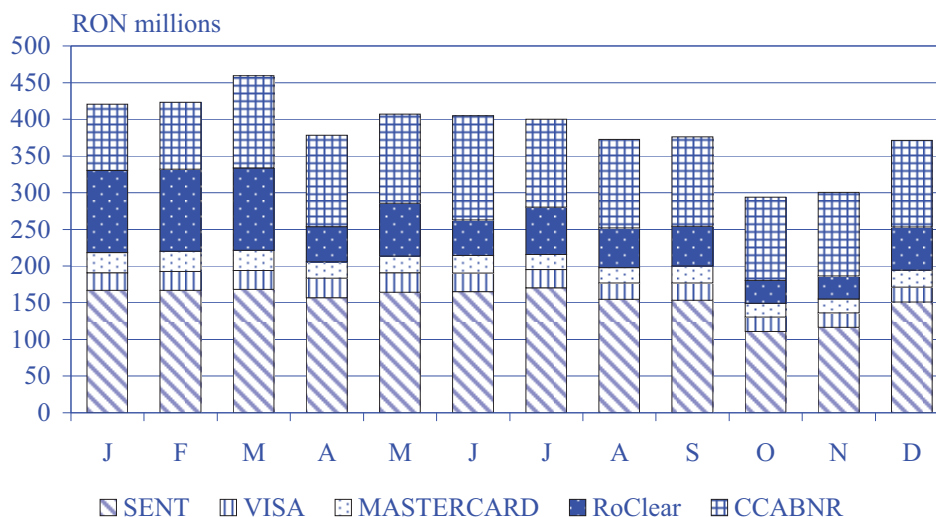
Structure of Transfers in 2008



Real-time interaction with small- and large-value payment systems

SaFIR ensures the infrastructure required for the management of the collateral set up with a view to guaranteeing the settlement of net positions of participants in ancillary systems, as illustrated in the following chart.

Value of Collateral related to Ancillary Systems



Facilities for cash management

In order to ensure the smooth settlement in ReGIS, the central bank grants to participants in ReGIS intraday credit facilities. Credit institutions participating in SaFIR can obtain the intraday credit facility via repo intraday agreements based on eligible assets.

In 2008, participants resorted to the intraday credit facility; 8 operations were carried out in amount of RON 505.4 million.

Availability of the system

SaFIR can ensure the settlement of 1,500 transactions per day, with the possibility to increase its processing capacity by an additional 50 percent. During peak times, the system can process 40 percent of the programmed maximum volume.

In 2008, the average availability of SaFIR reached 99.99 percent (indicator calculated as a ratio of the duration of system interruptions to the programmed operating duration).

Pricing policy

In 2008, the fees related to the services provided by SaFIR were not diminished.

Developments in SaFIR in 2008

As part of the process aimed at improving public debt management and developing the institutional framework and the specific infrastructure of the government securities market, the Minister of Economy and Finance decided that government securities should be listed on the Bucharest Stock Exchange as well, in parallel with their trading on the interbank market.

In order to make possible the trading of government securities on both the interbank market and the regulated market, a connection was developed in 2008 between the depository and settlement systems of the two markets, namely between SaFIR, managed by the National Bank of Romania and RoClear, managed by the Central Depository.

This connection became operational on 1 August 2008 when Order No. 2231/2008 issued by the Minister of Economy and Finance came into force approving the simultaneous trading in government securities on the interbank secondary market managed by the National Bank of Romania and on the regulated market managed by the Stock Exchange.

Following the implementation of this connection, investors can migrate to either of these markets, depending on their own option, transactions in government securities concluded on the interbank market and on the stock market being settled via SaFIR and RoClear respectively.

Furthermore, during 2008, Euroclear, the international central depository implemented an indirect connection with SaFIR via which any non-resident institutional investor has access to the market for government securities in Romania, being able to perform both free of payment and delivery versus payment operations.

4. National Bank of Romania's participation in the activities carried out within the European System of Central Banks

Following Romania's joining the European Union, the National Bank of Romania continued to participate in 2008 as well, with a member status, in all the activities carried out within the structures of the European System of Central Banks and the European Central Bank, performing tasks in the field of financial market infrastructures, namely within the Payment and Settlement Systems Committee (PSSC) including all its sub-structures: Payment Systems Policy Working Group (PSPWG), Payment Systems Oversight Working Group (PSOWG), Securities Working Group (SWG) and Working Group on TARGET2 (WGT2).

5. Regulation, licensing and monitoring of payment systems

Regulation, licensing and monitoring of payment instruments

With a view to fulfilling its task of promoting the smooth functioning of payment systems, the National Bank of Romania added two objectives to those included in its strategy on payments and payment systems, namely that of diminishing the number of debit payment instruments cleared on a paper basis and that of promoting the electronic clearing system of such instruments. The National Bank of Romania's strategy in the field materialised into the launching, starting 10 October 2008, of the automated processing service of debit payment instruments such as cheques, bills of exchange and promissory notes via truncation, within SENT.

The implementation of the new automated processing mechanism of debit payment instruments such as cheques, bills of exchange and promissory notes called for both the amendment of the legal framework applicable to payment instruments that are subject to processing and the adequate alteration of the rules governing the system (SENT) that uses this mechanism.

The legal framework was subject to amendment throughout 2008, new amendments being expected in 2009 as well.

2008 witnessed the following achievements:

1. The amendment of the primary legislation applicable to the mentioned payment instruments, by drawing up the following pieces of legislation:
 - Government Emergency Ordinance No. 38/2008 amending and supplementing Law No. 59/1934 on the cheque;
 - Government Emergency Ordinance No. 39/2008 amending and supplementing Law No. 58/1934 on the bill of exchange and the promissory note;

2. The amendment of the secondary legislation applicable to payment instruments, by drawing up the following pieces of legislation:

- National Bank of Romania Technical Norms No. 4/2008 on the cheque;
- National Bank of Romania Technical Norms No. 5/2008 on the bill of exchange and the promissory note;
- National Bank of Romania Norms No. 6/2008 amending and supplementing National Bank of Romania General Norms No. 7/1994 on the trade of banking companies and other credit institutions in cheques, according to Law No. 59/1934 on the cheque, amended by Government Ordinance No. 11/1993, as approved and amended by Law No. 83/1994;
- National Bank of Romania Norms No. 7/2008 amending and supplementing National Bank of Romania General Norms No. 6/1994 on the trade of banking companies and other credit institutions in exchange bills and promissory notes, according to Law No. 58/1934 on the exchange bill and the promissory note, amended by Government Ordinance No. 11/1993, as approved and amended by Law No. 83/1994;
- National Bank of Romania Regulation No. 12/2008 supplementing National Bank of Romania Regulation No. 10/1994 on multilateral netting of paper-based cashless interbank payments;
- National Bank of Romania Norms No. 10/2008 on the amendment of National Bank of Romania Norms No. 6/2008 amending and supplementing National Bank of Romania General Norms No. 7/1994 on the trade of banking companies and other credit institutions in cheques, according to Law No. 59/1934 on the cheque, amended by Government Ordinance No. 11/1993, as approved and amended by Law No. 83/1994;
- National Bank of Romania Norms No. 11/2008 on the amendment of National Bank of Romania Norms No. 7/2008 amending and supplementing National Bank of Romania General Norms No. 6/1994 on the trade of banking companies and other credit institutions in bills of exchange and promissory notes, according to Law No. 58/1934 on the bill of exchange and the promissory note, amended by Government Ordinance No. 11/1993, as approved and amended by Law No. 83/1994;
- National Bank of Romania Circular No. 39/2008 on the prohibition of the use of the old format of debit payment instruments such as cheques, bills of exchange and promissory notes;
- National Bank of Romania Circular No. 40/2008 amending National Bank of Romania Circular No. 9/1998 on the fees collected by the National Bank of Romania for cashless payment services.

Concurrently with the launching of the new electronic processing-settlement mechanism of debit payment instruments via truncation, the National Bank of

Romania became involved, alongside the banking community, in the process of creating a processing-settlement mechanism of debit payment instruments, such as those previously mentioned, which cannot be processed and settled via truncation – a mechanism used by the whole banking community based on an interbank agreement adopted by all credit institutions that issue and manage payment means such as cheques, bills of exchange and promissory notes.

The processing-settlement mechanism on a bilateral basis of debit payment instruments was completed and implemented by 30 April 2009, which made it possible for the paper-based clearing house, managed by the National Bank of Romania and operated by TRANSFOND in its capacity as agent, to be closed down on that date, according to the calendar.

With a view to containing the operational risk related to the processing of debit payment instruments such as cheques, bills of exchange and promissory notes which cannot be truncated, including the settlement risk, the National Bank of Romania monitored weekly the volume of such payment instruments processed on a daily basis with the aim to prevent the volume of debit payment instruments, such as those previously mentioned from exceeding, upon implementing the new mechanism, the ceiling of 2,000 instruments processed per day – a volume assumed by the banking community for the safe processing of such instruments.

In 2008, credit institutions and non-bank financial institutions were further licensed to put into circulation debit payment instruments such as cheques. Thus, the National Bank of Romania analysed the documents submitted by credit institutions with a view to authorising the putting into circulation of cheques by such institutions, based on the new requirements relative to debit payment instruments such as new-format cheques, in accordance with the provisions of National Bank of Romania Technical Norms No. 4/2008; during the assessment by the National Bank of Romania, institutions putting cheques into circulation were additionally asked, compared to the previous years, to submit feasibility studies concerning the processing mechanisms specific to each credit institution. The assessment was aimed at identifying the existence at the level of each credit institution of adequate own procedures for the safe processing of debit payment instruments, including under circumstances that may render their electronic processing impossible.

The new technical norms applicable to debit payment instruments such as bills of exchange and promissory notes, elaborated by the National Bank of Romania, set forth additional requirements for the safety of instruments, providing the obligation for the institutions that put into circulation such instruments to assign each instrument a unique reference. Each credit institution ensures the management of the ranges of references assigned to promissory notes and bills of exchange, which gives them the possibility to efficiently manage the fraud risk.

In 2008, the institutions issuing electronic payment instruments notified the National Bank of Romania of their putting into circulation:

- 7 new types of remote-access payment instruments (Internet banking)
- 53 new types of cards, of which:
 - 25 types of debit cards
 - 28 types of credit cards.

Authorisation of payment and securities settlement systems

According to the best international practices in the field, the National Bank of Romania asked the managers of payment and securities settlement systems that any alteration of the system rules approved by the National Bank of Romania should be sanctioned by the central bank before implementation. Thus, the National Bank of Romania approved the changes in the rules applying to SENT and RoClear initiated by TRANSFOND and the Central Depository respectively, in their capacity as system managers.

Collection of statistical data on payments and payment and securities settlement systems

With a view to ensuring the database and information necessary for both elaborating papers and assessments, and fulfilling its task, in accordance with the provisions of the Protocol on the Statute of the European System of Central Banks, namely to help the European Central Bank collect statistical data and information, in 2008, the central bank continued to collect primary statistical data on payments, payment and securities settlement systems from reporting institutions (credit institutions non-bank financial institutions, managers of payment and securities settlement systems, as well as central depositories and central counterparties) via the IT reporting system for notifying the National Bank of Romania (SIRBNR), that were subsequently processed in order to obtain some derived/aggregate indicators, in keeping with the reporting requirements of the European Central Bank or with the own needs to substantiate the National Bank of Romania policies in the field.

The access of reporting institutions to the National Bank of Romania's database with a view to obtaining statistical data and information in the field of payments on all reporting institutions shall be partly restricted in order to ensure the compliance with legal requirements. Therefore, in line with the provisions of Law No. 312/2004 – the Statute of the National Bank of Romania, “statistical data and information that enable the identification of statistical subjects, directly or indirectly, thus revealing private information, are deemed to be confidential”, and the National Bank of Romania is bound to ensure “measures for protecting data on individual subjects – natural or legal entities”.

Chapter 5. Management of international reserves

1. Developments in international official reserves in 2008

At end-2008, Romania's international reserves ran at EUR 28.27 billion. Foreign exchange reserves worth EUR 26.22 billion made up 92.75 percent of total reserves. Gold weighing 103.71 tonnes worth EUR 2.05 billion accounted for 7.25 percent of total reserves. Thus, total international reserves increased by EUR 1.08 billion year on year.

Foreign exchange reserves went up about EUR 1 billion to reach EUR 26.22 billion at year-end 2008 versus EUR 25.31 billion at year-end 2007.

In terms of quantity, gold reserves posted a drop of 3.57 kg as a result of further retrocession of gold to the rightful owners in accordance with legal provisions. In terms of value, international reserves witnessed a rise of EUR 170 million, due to the increase in gold price on international market, i.e. USD 882.05 per ounce on the London Metal Exchange at end-2008, up 5.77 percent against end-2007.



2. Strategic goals

2.1. Goals for the period April 2008-March 2009

Based on the expectations of (i) slowdown in global growth, (ii) decrease in interest rates on international markets and (iii) moderation in the depreciation of the USD, the strategy approved by the NBR Board in March 2008 envisaged the following key objectives:

- a currency composition in which the euro accounts for 55 percent - 85 percent of total foreign exchange reserves, depending on the collection and payment flows, the USD for 10 percent - 40 percent, and other currencies for at most 10 percent of total reserves;
- the separation of the bond portfolio in two parts:
 - a part of medium-term investments, over a period of approximately 3.2 years, amounting to the equivalent of EUR 3.1 billion;
 - a liquid part, over a period of 0.8 years, equivalent to EUR 21.3 billion;
- the following categories of issuers: (i) the US government; (ii) government agencies or agencies sponsored by the US government; (iii) the governments of EU Member States; (iv) government agencies or agencies sponsored by the governments of EU Member States; (v) other AAA-rated governments; (vi) supranational institutions; (vii) private entities, issuers of European Covered Bonds;
- the limit of 10 percent exposure of total international reserves to private entities, issuers of European Covered Bonds;
- the limit of 10 percent exposure to private entities other than issuers of European Covered Bonds.

2.2. Developments in the external economic environment

The year 2008 witnessed the deepest global financial crisis of the last decades. In line with expectations, the pace of global growth decelerated versus the year before to 3.4 percent from 5.2 percent. In advanced economies (USA, Canada, euro zone, Japan, the United Kingdom, and the group of recently industrialised countries) the rate of increase slowed on average to 1 percent in 2008 versus 2.7 percent in 2007, while the emerging economies (Sub-Saharan Africa, Central and Eastern Europe, the Commonwealth of Independent States, China, India, the countries in the Middle East, Brazil, Mexico) also saw a moderation in their growth rate from 8.3 percent in 2007 to 6.3 percent.¹ Foreign exchange reserves expanded worldwide by USD 674 billion from USD 1,288 billion in the previous year, with China accounting for 29 percent of total value against 25 percent at end-2007.

In the period under review, the global financial crisis deepened and was characterised by a widespread drop in stock exchange indices, a significant increase in risk premia, highly volatile forex and commodity markets, bank failures and credit-market gridlock. In this context, central banks cut reference rates: the Federal Reserve System to 0.25 percent from 4.25 percent, the European Central Bank to 2.5 percent from 4 percent and the Bank of England to 2.0 percent from 5.50 percent. In order to mitigate the fallout from the crisis on the financial system and fend off panic worldwide, central banks, governments, government agencies and supranational institutions intervened by taking measures such as liquidity injections and easier access to financing so as to help the financial and banking system to recover.

¹ Source: IMF – World Economic Outlook Update (28 January 2009)

Developments in forex market confirmed projections. The USD appreciated during 2008 about 6 percent against a basket of currencies including the euro, the Japanese yen, the British pound, the Canadian dollar, the Swedish crown and the Swiss franc.

3. The manner to achieve strategic goals

In discharging its duties, the Foreign Reserve Management Committee (FRMC) of the NBR examined on a regular basis the developments in financial markets and their impact on the prospects of achieving the goals set by the NBR Board under the approved strategy.

Bond portfolios fared better than expected, in the context of substantial worldwide cuts in interest rates, which led to higher prices of government bonds, the main component of Romania's international reserves.

The global liquidity crunch had a direct impact on the sources of refinancing short-term debt both on interbank markets and real economy, leading to a contraction in economic activity, reflected by key macroeconomic indicators (negative economic growth, higher unemployment rate and a lower inflation in 2008 Q4).

Thus, in the first seven months of the year, when the USD depreciation and the rise in oil prices were rife, American, and European, especially British, banks further reported losses generated by structured financial products linked to the US real estate market. The confidence crunch due to exposure to risky mortgage loans became more pronounced, so that on 16 March 2008 Bear Stearns was taken over by J.P. Morgan, supported by the Federal Reserve System. At the beginning of September, the Federal Housing Financing Agency decided to place the US mortgage agencies Fannie Mae and Freddie Mac under special administration, Lehman Brothers declared on 15 September 2008 the initiation of bankruptcy proceedings, while Merrill Lynch was taken over by Bank of America. These events stirred panic on financial markets, which led to a substantial contraction in the market value of financial institutions' own capital, already eroded by accounting heavy losses due to the subprime mortgage loan crisis. Under these circumstances, the financial standing of these institutions saw a fast deterioration, leading to the authorities' intervention, nationalisations, mergers, takeovers and bankruptcies.

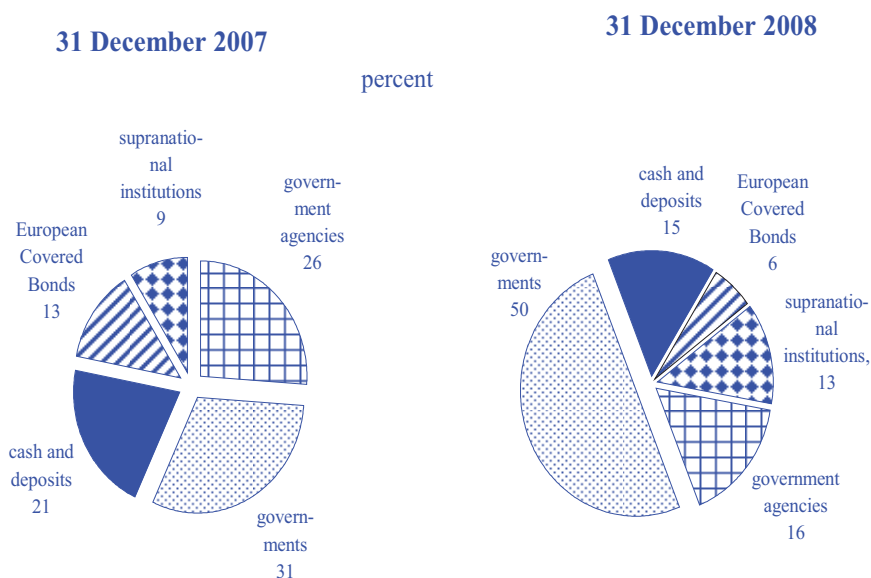
All these developments caused investors' risk aversion to grow, resulting in a significant portfolio shift via sales of assets viewed as highly risky, such as shares, corporate bonds, currencies of emerging economies, as well as via purchases especially of short-term government bonds (US Treasuries being traded at negative yields on several occasions) to the benefit of investors holding such securities.

The Foreign Reserve Management Committee of the NBR decided to reduce exposure to private entities by liquidating all the deposits held with such institutions

after the credit risk became manifest worldwide following Lehman Brothers' bankruptcy.

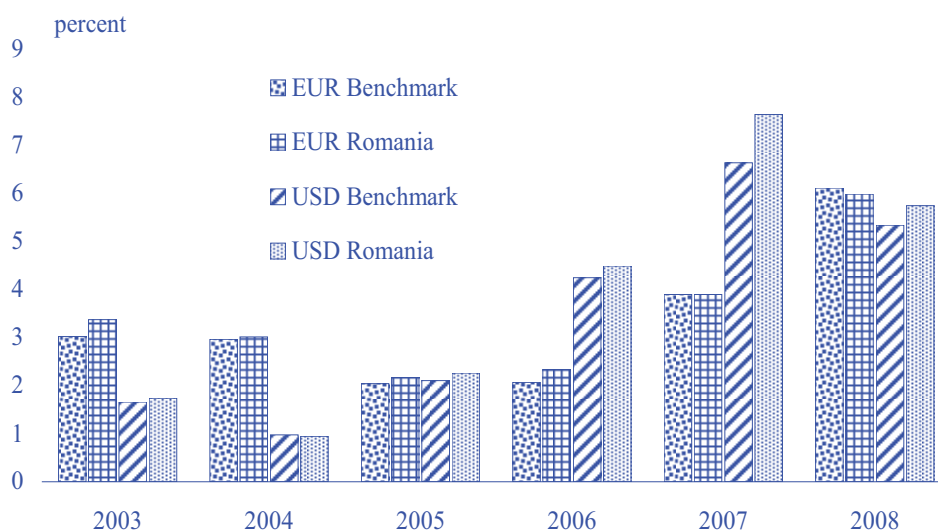
Investors' aversion to every risk hit the European Covered Bonds market as well, despite the higher protection compared to other types of non-government bonds, due to the explicit protection of investors stipulated by law. Therefore, the risk premium required by investors for holding such bonds increased. In this context, the Foreign Reserve Management Committee decided to reduce exposure to European Covered Bonds by reinvesting in government paper along the amounts reaching maturity. Thus, at end-2008, government bonds held 50 percent of total foreign exchange reserves against 31 percent in the previous year.

Romania's Foreign Exchange Reserve Structure



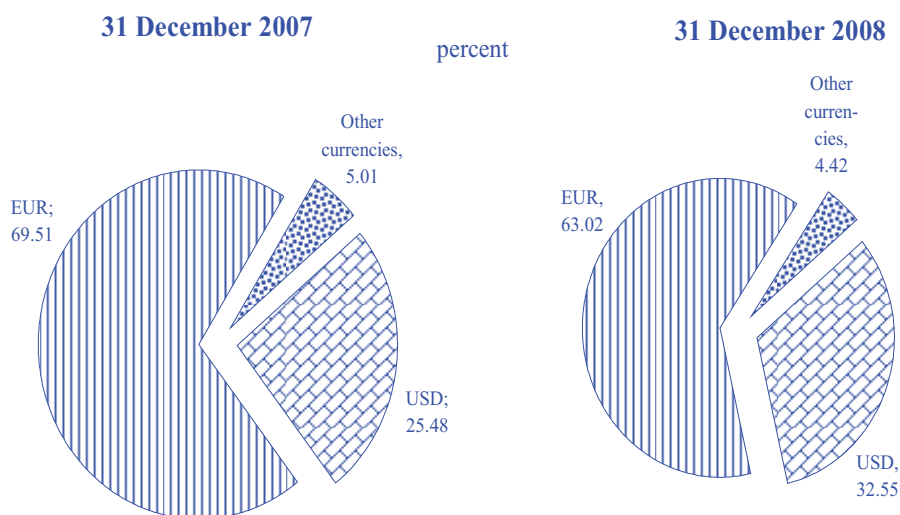
The above-mentioned decisions resulted in a total yield of 5.99 percent for the euro and 5.75 percent for the US dollar. In comparison, in 2008, total yield on government bonds with maturities up to 3 years included in the Merrill Lynch index came in at 6.11 percent for the euro and 5.34 percent for the US dollar.

Yield against Merrill Lynch Indexes



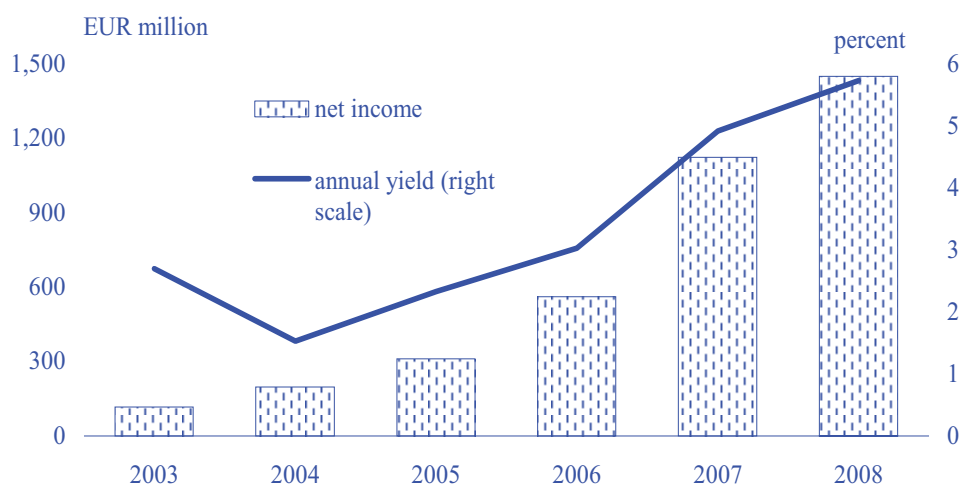
At end-2008, the share of the euro in foreign exchange reserves narrowed to 63 percent from 69.5 percent a year earlier.

Romania's Foreign Exchange Reserve Composition



These developments translated into a record-high total yield of EUR 1.45 billion, up by EUR 330 million against the previous year. The year-on-year increase was attributable mainly to the rise in the market value of bond portfolios and the expansion in foreign exchange reserves.

Outcomes of International Reserve Management



Chapter 6. Balance of payments and international investment position

1. Current account

In 2008, the balance-of-payments current account posted a deficit of EUR 16,897 million, up 1.3 percent year on year, accounting for 12.3 percent of GDP against 13.5 percent in 2007.

Table 1. Current Account

	<i>EUR million</i>	
	2007	2008
a) Trade balance (goods)	-17,822	-18,372
– exports (FOB)	29,549	33,628
– imports (FOB)	47,371	52,000
b) Services, net	477	845
c) Incomes, net	-4,152	-5,371
d) Current transfers, net	4,820	6,001
Current account balance	-16,677	-16,897

In 2008, the trade deficit¹, which has the strongest bearing on the current account, amounted to EUR 18,372 million, up 3.1 percent from the previous year. The growth rate of exports outpaced that of imports by 4 percentage points, whereas the share of trade deficit in GDP narrowed by one percentage point to 13.4 percent. The trade balance structure by production stage highlights deficits under capital and intermediate goods, amounting to EUR 7,191 million and EUR 4,938 million respectively, as well as under commodities and consumer goods amounting to EUR 4,848 million and EUR 1,395 million respectively. In terms of geographical spread, intra-EU trade accounted for the largest share of trade deficit, i.e. 66.8 percent. About 94 percent of the trade deficit recorded in 2008 were due to the trade with Germany, the Russian Federation, Kazakhstan, Hungary, China, Austria, Poland, the Netherlands, the Czech Republic and Italy. The coverage of imports through exports and the openness of the Romanian economy increased year on year by 2.4 percentage points and 0.4 percentage points respectively, to 64.7 percent and 62.6 percent respectively.

Exports of goods came in at EUR 33,628 million², up 13.8 percent from the previous year, as a result of higher external prices, larger export volume and the shift in structure in favour of capital goods, as well as the depreciation of the domestic currency against the euro in real terms. In year on year comparison, the structure of exported goods by production stage is indicative of a rise in the share

¹ More than half of the trade deficit was recorded in Q2 and Q3.

² The share of exports in GDP rose from 23.9 percent in 2007 to 24.6 percent in 2008.

of capital goods by 2.7 percentage points to 15.2 percent and in that of commodities by 1.8 percentage points to 7.0 percent, along with a decline in the share of intermediate goods by 0.8 percentage points to 57.2 percent and in that of consumer goods by 3.7 percentage points to 20.6 percent. In terms of value, the EUR 4,079 million increase was EUR 380 million larger versus the preceding year and stemmed to a proportion of about 70 percent from the increase in external prices (electrical machinery, equipment and apparatus; metallurgy products; petroleum products; boilers; turbines, engines, mechanical apparatus and devices; fertilisers; grains; sunflower seeds; rubber products). Manufactured goods accounted for 94.8 percent of Romania's exports and the value of exported industrial goods amounted to EUR 31,896 million in 2008. Exports of manufactured goods advanced by 11.1 percent against 2007, due to developments in most of the industrial sub-sectors except for pulp and paper, construction materials, wearing apparel, leather goods and footwear, wood processing and wood products, textiles and furniture. Above-average increases were recorded by exports of equipment, radio, television and communication sets; office machinery and computers; tobacco products; food and beverages; medical instruments and devices, precision and optical devices, clocks and watches; petroleum processing, publishing, printing and reproduction of recorded media, rubber products and plastics; chemicals; means of transport³; machinery and equipment excluding electric and optical devices.

Imports of goods stood at EUR 52,000 million⁴, up 9.8 percent versus 2007. In 2008, the structure of imports by production stage reflects the rise in the weight of commodities by one percentage point to 13.9 percent and in consumer goods by 0.8 percentage points to 16 percent, along with a decrease in the share of capital goods by 1.7 percentage points to 23.6 percent and that of intermediate goods staying flat at 46.4 percent. One third of imports, among which crude oil; medicines; oil well gas; electrical apparatus for wired telephony and telegraphy; goods transport vehicles; tractor parts and accessories; wires, cables and insulated conductors; petroleum products; pork; integrated circuits; rolled plates; anthracite and pit coal; iron ore; iron or simple steel semi-products and furniture posted above- average growth rates. The rise in import value ran at EUR 4,629 million and resulted to a proportion of 88 percent from the increase in external prices (crude oil; natural gas; natural fuels; petroleum products; cast iron, steel and steel products; electrical machinery and apparatus; boilers, turbines, engines, mechanical apparatus; motorcars and tractors).

In 2008 net terms of trade index⁵ ran at 100.4 percent, against the backdrop of quasi-similar growth rates of export and import prices (3.8 percent and 3.4 percent respectively). Gross terms of trade index⁵ stood at 103.2 percent, as the physical volume of exports rose faster than that of imports (9.6 percent and 6.2 percent respectively).

³ Exports of motorcars and other vehicles for passenger transport accounted for 2.9 percent of exports in 2008, up 24 percent from the previous year.

⁴ The share of imports of goods in GDP shrank from 38.3 percent to 38.00 percent year on year.

⁵ Source: National Institute of Statistics.

Behind the widening of the current account deficit stood also the expansion in incomes of non-residents from direct investment and in interest payments on loans to the real and banking sectors, leading to an increase in the income balance deficit by 29.4 percent over the previous year. The negative impact of goods and income flows on the current account was partly alleviated by the positive developments in the services balance⁶ and current transfers balance⁷.

2. Financial and capital account

In 2008, the positive balance of financial and capital account amounted to EUR 18,331 million, up 6.1 percent over the year before. This was mainly the result of direct investment by non-residents in Romania.

Net direct investment⁸ added 31.6 percent year on year to EUR 9,272 million. Investment by non-residents in Romania totalled EUR 9,085 million, of which 82.6 percent were equity stakes and intra-group loans⁹, whereas the remainder consisted of reinvested earnings and in-kind contributions to the share capital. In 2008, privatisation receipts increased equity stakes by EUR 873 million following the acquisition by Ford Motor Company of 72.4 percent in the capital of S.C. Automobile Craiova S.A. (EUR 57 million) and the acquisition by the Italian group ENEL of 64.4 percent in the capital of S.C. Electrica Muntenia Sud S.A. (EUR 816 million). The major investments were made by the following ten countries: Austria (21 percent), the Netherlands (16.6 percent), Germany (10.9 percent), France (10.5 percent), Italy (7.7 percent), Greece (6.7 percent), Switzerland (4.4 percent), Cyprus (3.9 percent), Turkey (1.8 percent) and Hungary (1.7 percent). Portfolio investment recorded net outflows of EUR 834 million (compared with EUR 482 million worth of net inflows in 2007) from dealings in securities performed by the real sector and from redemption of banks' maturing bonds.

In 2008, net external financing from medium- and long-term loans and borrowings amounted to EUR 6,130 million, up 17.3 percent against the previous year. Behind this performance stood the expansion in loans taken by the real sector, general government and the banking sector. In 2008, net outflows from short-term loans and borrowings worth EUR 1,025 million were recorded, compared with EUR 604 million worth of inflows in the prior year.

⁶ Services balance surplus amounted to EUR 845 million, up 77.1 percent from 2007, on the back of higher receipts from transport.

⁷ Current transfers balance surplus reached EUR 6,001 million, up 24.5 percent over 2007, due to the doubling of structural funds from the EU.

⁸ Net value of non-residents' investment in Romania and the net value of residents' investment abroad

⁹ Loans between the foreign investor and the resident company

In 2008, about 58.4 percent of the current account deficit (EUR 16,897 million) were covered by direct investments and capital transfers, with other capital investment accounting for the remainder.

Table 2. Current Account Deficit Financing

	<i>EUR million</i>	
	2007	2008
Deficit financing	16,677	16,897
Capital transfers, net	704	602
Direct investment, net	7,047	9,272
<i>of which:</i>		
– direct investment by non-residents in Romania	7,251	9,085
⇒ equity stakes	2,220	2,992
⇒ reinvested earnings	1,327	1,585
⇒ intra-group loans	3,704	4,508
Portfolio investment, net	482	-834
Other capital investment:	12,949	7,819
– borrowings (MLT)	5,228	6,130
⇒ inflows	11,113	12,497
⇒ repayments	5,885	6,367
– loans (MLT), net	156	48
– loans (ST), net	604	-1,025
– other*	6,961	2,666
NBR's reserve assets	-4,505	38
(„-” increase)		

*) includes the following items, net: non-produced/non-financial assets, derivatives, cash and deposits, other assets, other liabilities, errors and omissions.

3. Romania's international investment position

At end-2008, official international reserves managed by the National Bank of Romania amounted to EUR 28.3 billion, up EUR 1.1 billion from end-2007. Behind this increase stood exchange rate gains (EUR 284.6 million) and price gains (EUR 836.5 million) related to securities in the NBR's portfolio as well as monetary gold.

Medium- and long-term external debt¹⁰ expanded 31 percent from end-2007 to EUR 50.7 billion, due to EUR 12.8 billion worth of net inflows from external loans. External debt was contained by developments in the EUR/USD exchange rate (EUR -634.3 million), as well as by debt-to-equity swaps (EUR -176.7 million). In 2008, medium- and long-term external debt service ran at EUR 12.4

¹⁰ Debt resulting from external loans and borrowings, bonds a.s.o.

billion, of which EUR 10.4 billion in principal repayments and EUR 2 billion in interest and commission payments.

Composition of medium- and long-term external debt by debtor illustrates the prevalence of non-guaranteed public debt (67.4 percent), followed by direct public debt¹¹ (18.2 percent), guaranteed public debt¹² (3.4 percent) and medium- and long-term deposits (11 percent). In year-on-year comparison, the share of non-guaranteed public debt widened by 2.1 percentage points, that of medium- and long-term deposits by 2.7 percentage points, whereas the weights of direct public debt and guaranteed public debt narrowed by 3 percentage points and 1.8 percentage points respectively.

Composition of medium- and long-term external debt by creditor points to the continuation of the previous year's trend, with the share of private creditors widening from 85.1 percent at end-2007 to 86.8 percent at end-2008. These developments were attributed to the channelling of loans granted by foreign private banks into the Romanian banking system and economy, while the shares of international financial institutions and bilateral creditors in total external debt dropped to 12.6 percent and 0.6 percent respectively.

At end-2008, composition by maturity is indicative of long-term external debt holding the largest share (67.3 percent) of total medium- and long-term external debt, against the background of a 4.2 percentage point rise in long-term private debt in the period under review.

Composition of medium- and long-term external debt by currency at end-2008 shows that the euro was in the lead (69.3 percent, down 2.7 percentage points against end-2007), followed by the leu (16 percent, up 4.9 percentage points), the US dollar (8.8 percent, down 3.3 percentage points), and other currencies (5.9 percent, up 1.1 percentage points). As for the composition of medium- and long-term external debt service, the euro also took the largest share (83.2 percent), ahead of the US dollar (12.2 percent) and other currencies (4.6 percent).

Medium- and long-term external debt accounted for 37.1 percent of GDP at year-end 2008, up 5.8 percentage points from end-2007, and 119.6 percent of exports of goods and services, up 13.5 percentage points. Medium- and long-term external debt service ratio rose from 23.2 percent at end-2007 to 29.3 percent at end-2008. Cover of imports of goods and services by the official reserves dropped year on year, from 6.1 months to 5.7 months.

¹¹ External loans taken by the Ministry of Economy and Finance/local general government in accordance with Public Debt Act.

¹² External loans guaranteed by the Ministry of Economy and Finance/local general government in accordance with Public Debt Act.

Table 3. Key External Indebtedness Indicators

	<i>percent</i>	
	2007	2008
Official reserves/imports of goods and services (months of imports)	6.1	5.7
Medium- and long-term external debt/GDP	31.3	37.1
Medium- and long-term external debt/exports of goods and services	106.1	119.6
Medium- and long-term external debt service ratio	23.2	29.3

At end-2008, short-term external debt stood at EUR 22.4 billion. Its balance posted a 12.8 percent increase versus the previous year, on account of short-term capital inflows (EUR 2.4 billion). Short-term external debt service totalled EUR 28.4 million, due to the renewal of short-term commitments, with the debt service ratio at end-2008 reaching 67 percent, 8.1 percentage points higher than at end-2007.

Chapter 7. International activity

1. Romania as a EU Member State

International developments have had a major influence on the domestic financial system in 2008 more than ever over the past two decades. The magnitude and the complexity of the ongoing global financial crisis – whose origins are both macro- and micro-economic in nature, deepened by the cyclical evolution of the society and by globalisation – tend to amplify the spill-over effects unless macroeconomic balances are re-established at a rapid and sustainable pace. Moreover, as far as Romania is concerned, economic and legal convergence on the path to euro adoption remains the major challenge for the upcoming years, a priority that needs to be proactively considered from at least two standpoints:

- I. the international environment featuring Romania as a EU Member State, namely the drift towards a new global financial architecture and the groundbreaking changes in the monetary and financial system and in international relations;
- II. the European integration capacity in Community institutional structures and domestic policy convergence with the Community policy system and implementation mechanism – the NBR case.

I. The international environment

1.1. International issues: the change in the global financial architecture and macroeconomic policy supervision in the world economy

Given the high degree of economic and financial integration, the global economic environment has a major influence on the conduct of economic policies at EU level. The European Central Bank – along with other European institutions and ESCB members, the NBR included – plays a major role in the international multilateral supervision process in relation to macroeconomic policies. Both in 2008 and in 2009 H1, the economic environment has felt the pinch of the global financial turmoil, which turned into an unprecedented crisis. At the origin of the crisis stood mainly securitisation excesses, faulty financial intermediation, as well as excessive or insufficient regulations that generated deep macro- and micro-economic imbalances. The knock-on effects from the crisis were immediately conveyed via regulating and accounting mechanisms, globalised business models, as well as through opaque and unsustainable cross-border cooperation patterns. Thus, although the turmoil initially surfaced in the United States, a large number of developed and emerging countries in Europe were subsequently influenced in various shapes and sizes, entailing an ample and complex debate on the viability and functionality of the current architecture of the global monetary and financial system.

A first step was taken by the Heads of State and Government of EU Member States, who agreed – during an informal meeting held in November 2008 – on the

joint and coordinated effort to prepare common principles and measures upon which to build a new international financial system. Shortly afterwards, the same topic dominated the agenda of the first two summits on financial markets and the world economy of the Leaders of the Group of Twenty in Washington, DC on 15 November 2008 and in London on 2 April 2009. As an immediate policy response, the first concrete actions were taken by the IMF, by creating a new, more flexible financial instrument, more efficient in extending short-term financing facilities. This was followed by the strong capitalisation of the institution, in response to the wave of financing requests from emerging EU countries (Hungary, Latvia, Romania, Poland) and non-EU countries (Iceland, Serbia, Ukraine, Belarus, Pakistan and Mexico), which had recorded a fast-paced deterioration in economic developments and unsustainable macroeconomic imbalances. Another concerted European approach was discussed during the Financial Stability Forum, which facilitated the coordination of various international initiatives for a unitary monitoring of the ways and methods to implement the G20 decisions. The recommended actions were in five areas: prudential oversight, enhancing transparency and valuation, credit risk, the authorities' responsiveness to risks, and robust arrangements for dealing with stress in the financial system. Other international financial institutions – such as the Bank for International Settlements and the OECD (in Europe) or The Group of Trustees (in the U.S.) – are currently concerned with launching new initiatives and concrete working actions on crisis prevention mechanisms within the process of redefining the global financial architecture.

1.2. European issues

1.2.1. EU economic policy issues

a) The Stability and Growth Pact

In June and July 2008, the ECOFIN Council abrogated the excessive deficit procedure for 4 out of the 6 Member States that had been sanctioned in 2007 pursuant to Art. 104(7) of the Maastricht Treaty and Council Regulation No. 1467/97 on speeding up and clarifying the implementation of the excessive deficit procedure, as part of the Stability and Growth Pact (Czech Republic, Italy, Portugal and Slovakia; the procedure against Poland was closed in August 2008, while Greece revised its statistical data). The worsening of the global economic environment starting with 2008 H2 and the lower budget revenues amid the ongoing financial crisis were the major culprits for the additional pressure on fiscal policies, which translated into wider budget deficits, particularly in Member States faced with a fast-paced deterioration of macroeconomic imbalances. More precisely, a group of 11 Member States (i.e. Bulgaria, the Czech Republic, Denmark, Germany, Estonia, the Netherlands, Poland, Sweden, Finland, Hungary, and the United Kingdom – the latter two being already subject to the excessive deficit procedure opened in 2004 and 2008 respectively, to be corrected by 2009), though hit by the global economic and financial crisis, adopted financial incentives for 2009 aimed at removing the effects of the crisis, according to the Economic Recovery Plan proposed by the EC and adopted by the Heads of State of EU member countries in December 2008. A second group of Member States

(i.e. Spain, Ireland, Greece, Latvia, Malta, France and Romania – the latter two countries received in 2008 early recommendations on adjusting their economic policies) exceeded the budget deficit threshold of 3 percent of GDP for 2008 and, pursuant to Art. 104-107 of the Treaty, are monitored by the EC as follows: (i) the ECOFIN Council meeting in Prague on 10 March 2009 decided to open the legislative proceedings for launching the excessive deficit procedure and setting the admissible deadline for corrective measures with respect to four Member States, namely Greece, Spain, Ireland and France (Greece should correct the deficit by 2010, Ireland by 2013, and the rest by 2012). As regards the United Kingdom, the deadline was extended until fiscal year 2013-2014. On 4 May 2009, the EC opened the excessive deficit procedure against Romania as well; (ii) the ECOFIN Council notified the concerned Member States to take concrete measures with a view to bridging the budget deficit, and (iii) where applicable, sanctions should be imposed in case of exceeding the deadline or failure to comply with the assumed commitments to implement the deficit-cutting measures agreed with the EC.

➤ The EC biannual macroeconomic forecast exercise

As of October 2006, at the request of the EC, Romania has been an integral part of this monitoring and assessment mechanism applied on a biannual basis by the EC to Member States within the framework of the Stability and Growth Pact. The short-term macroeconomic forecasts consider a total of 180 variables covering the current year and the next. In addition, in between the fully-fledged spring and autumn forecasts, interim forecasts are produced, focusing on an update of real GDP growth and inflation by taking into account external factors as well. The NBR plays an active part in these structures, both through biannual meetings with EC/DG ECFIN experts and through the participation of an NBR representative in the EC working group on macroeconomic forecasts.

b) The Lisbon Strategy

The Lisbon Strategy, also known as the Lisbon Agenda or the Lisbon Process, is a set of objectives, priority action plans, targets and measures for guiding economic growth and employment policies at European level with a view to attaining the EU's strategic goal: to become the most competitive and dynamic knowledge-based economy. Amid the ongoing economic and financial crisis, on 26 November 2008, the EC disclosed a European Economic Recovery Plan, endorsed by the European Council in December 2008, which sets out short-term measures to be implemented at Community and domestic levels. The Lisbon Strategy is enforced domestically via the National Reform Programme (NRP) comprising general and specific objectives, actions and guidelines, as well as the necessary funding resources. As a EU Member State, Romania submitted two NRP reports to the EC, in 2007 and in October 2008 respectively. Against this backdrop, the following actions were taken at NBR level: on the one hand, the central bank was consulted in the drafting of the NRP according to its field of activity and legal tasks; on the other hand, the NBR repeatedly highlighted the importance of Romanian authorities focusing on the enforcement of structural reforms with a view to precluding macroeconomic imbalances and safeguarding sound economic growth.

- c) Development of financial markets and financial integration –
Report of the High-Level Group on financial supervision in the EU chaired by
Jacques de Larosière

A high-level expert group set up under the coordination of Jacques de Larosière, former governor of Banque de France and former IMF Executive Director, prepared a report containing a consistent set of 31 detailed recommendations to strengthen cross-border supervision of financial markets and institutions within the EU. Recommendations refer to the reform of the regulatory and supervisory framework both at European and particularly at national level, developing a set of common rules at European level as regards global financial cooperation based on transparent and efficient principles, regulatory policy (especially in relation to investment funds), defining a single, consolidated supervisory framework as well as a common crisis management system throughout the EU. Moreover, the Report advocates a European-wide institutional adjustment by creating two new control bodies, i.e. one for financial supervision (European System of Financial Supervision) and the other for risk management (European Systemic Risk Council). In early April 2009, the Larosière Group Report was discussed at the informal meeting of EU Finance Ministers and Central Bank Governors. Participants, including the representative of the Romanian Ministry of Economy and Finance and the NBR representative, generally agreed with the principles and recommendations to reform supervision of EU financial markets and institutions, by highlighting the need for: (i) a more efficient coordination among macroeconomic and microeconomic measures; (ii) identifying and separating the European level from the national level in terms of institutional tasks and responsibilities; (iii) increased harmonisation at European level by eliminating national protectionism from sectoral legislation in the financial services field; (iv) settling any issues that might arise with the creation of the European System of Financial Supervision: institutional, managerial, legal issues (the independence criterion), tasks and responsibilities, voting system, fiscal burden sharing. Mention should also be made of the “Memorandum of Understanding on cooperation between the financial supervisory authorities, central banks and finance ministries of European Union on cross-border financial stability”, which came into force in June 2008.

- d) 10 years of Economic and Monetary Union (EMU)

The year 2008 marked the tenth anniversary of the ECB, of the Eurosystem and the ESCB. This anniversary provided the ECB and ESCB members with an opportunity to review the first decade of EMU and to draw lessons from the experience gained during this period, by analysing the major challenges faced in a highly-complex economic environment at European and global levels. The event was properly celebrated by the ECB, the EC, the ECOFIN Council and the European Parliament. The general and unanimously-accepted message was that, ten years after the introduction of the single currency, the euro is a success. Nonetheless, further action should be taken to improve coordination and surveillance within EMU, to enhance the euro area’s international role and to promote effective governance of EMU. The Romanian delegation, headed by the President of Romania and including the NBR governor, the deputy governor in

charge of European affairs and the chairman of the Romanian Banking Association, was invited by Jean-Claude Trichet to attend the anniversary events scheduled in Frankfurt on 2 June 2008, chaired by the president of the European Parliament, the German Chancellor and the ECB President. Such events coincided with the closing ceremony of the “Cultural Days of the ECB – EU 2008” project, whose seventh edition will showcase Romania’s cultural wealth during 21 October – 9 November 2009 in Frankfurt.

1.2.2. EU institutional issues

a) The Lisbon Treaty

The “Treaty of Lisbon amending the Treaty on European Union and the Treaty establishing the European Community” (referred to as the Lisbon Treaty), signed on 13 December 2007 by representatives of the 27 Member States, is a major international agreement meant to replace the European Constitutional Treaty. According to Art. 6 of the Treaty of Lisbon, “this Treaty shall enter into force on 1 January 2009, provided that all the instruments of ratification have been deposited, or, failing that, on the first day of the month following the deposit of the instrument of ratification by the last signatory State to take this step”. In other words, in order for it to become effective, the Lisbon Treaty needs to be ratified by all Member States. The EU set 1 January 2009 as the deadline for adoption, so that the Lisbon Treaty might come into force prior to the June 2009 elections for the European Parliament. As far as the ratification process is concerned, 24 Member States have so far given the green light on the Treaty (Romania included, on 4 February 2008), Germany and Poland are very close to concluding the procedure, while Ireland is expected to organize a new ratification round by end-2009, after initially rejecting the Treaty in a referendum held in the summer of 2008.

b) The 2008 Convergence Report

The Convergence Report prepared by the ECB and that drafted by the EC are useful tools in assessing whether Member States with a derogation fulfil the convergence criteria laid down in the Maastricht Treaty for adopting the single currency. Art. 122 of the Treaty requires the Commission and the ECB to report simultaneously to the Council, at least once every two years, on the Member States with a derogation. Alongside Romania, the regular biennial report examined nine other countries, namely Bulgaria, Czech Republic, Estonia, Latvia, Lithuania, Hungary, Poland, Slovakia and Sweden. The EC and the ECB published their Convergence Reports simultaneously, on 7 May 2008, referring to the period 2006-2008 and including – for the first time since EU accession – assessments on Romania and Bulgaria as Member States. Moreover, Slovakia was examined in view of its intention to adopt the euro as of 1 January 2009 (the application was approved by the ECOFIN Council on 7 July 2008, after the EC had given the nod), while Lithuania was assessed only with respect to economic convergence, since the May 2006 Report had already acknowledged the fulfilment of legal convergence criteria.

The NBR was actively involved in analysing and approving the ECB’s Convergence Report as follows:

- at ECB level, by participating in the editorial working group set up within the Communication Committee;
- at NBR level through: (i) debates in the NBR Board on the fulfilment by Romania of economic and legal convergence criteria for joining the Eurosystem and, hence, introducing the single currency and (ii) participation of the NBR governor in the approval procedure during a special teleconference meeting of the General Council.

The EC's 2008 Convergence Report was analysed within the Economic and Financial Committee, in the presence of the MEF representative and the deputy governor in charge of European affairs.

II. The NBR's European integration in the ESCB in terms of institutional issues and monetary and financial policies – major fields of action

2.1. NBR integration in ECB/ESCB decision-making bodies – NBR participation in ESCB General Council reunions

Along with the other 26 governors of NCBs that are ESCB members and with the members of the ECB's Executive Board, the NBR governor and deputy governor in charge of European affairs attend the quarterly meetings of the General Council. The major topics covered during the reported period included: (i) regular macroeconomic analyses, main monetary and financial developments both within and outside the euro area with a view to contributing to a stable macroeconomic framework for promoting sound macroeconomic and financial policies; (ii) ERM II functioning principles; (iii) issues related to financial stability of the Eurosystem and of non-euro area countries; (iv) EU labour market developments; (v) the ECB's Convergence Report adopted in May 2008; (vi) monitoring the compliance by ESCB members with the provisions of Art. 101 and 102 of the Treaty establishing the EC as regards the prohibition of monetary financing and privileged access of the public sector to financial institutions, except for prudential considerations; (vii) issues related to the reform of the international financial architecture (debates on global imbalances, the underlying reasons and the magnitude of the financial crisis, the agenda of G20 working groups reporting to the finance ministers and central bank governors on enhancing the transparency of regulations and financial institutions, increasing the role of international cooperation and promoting the principle of financial market integrity, IMF reform).

2.2. NBR's participation in the ECB's written consultation procedure

Legal grounds: Pursuant to Art. 105(4) of the Treaty establishing the European Community and Art. 2(1) of Decision 98/415/EC on the consultation of the European Central Bank by national authorities regarding draft legislative provision, the written consultation procedure is mandatory in relation to any proposed legislation within the ECB's field of competence. The opinions issued shall be binding and generally applicable in the Member States, particularly with regard to:

(i) currency matters; (ii) means of payment; (iii) national central banks; (iv) the collection, compilation and distribution of monetary, financial, banking, payment systems and balance of payments statistics; (v) payment and settlement systems; (vi) rules applicable to financial institutions insofar as they materially influence the stability of financial institutions and markets. In addition, the ECB shall be consulted on any draft law regarding monetary policy instruments.

Participation in the written procedure consultation mechanism involves the NBR's obligation to consult the ECB on any legislative draft falling within its fields of competence, but also the possibility of commenting on any ECB draft opinions on the new European legislative proposals concerning issues related to the ESCB/ECB and/or Member States.

Concrete actions:

- a) consultation procedure by other national authorities: during 2008 and so far this year, the ECB has been consulted by the Parliament of Romania and by the National Institute of Statistics on the following legislative proposals:
 - amending and supplementing Law No. 312/2004 on the Statute of the NBR, upon initiative of several members of parliament – ECB Opinion No. 31/2008 (CON/2008/31);
 - using the NBR's foreign reserves for developing and modernising tourism, initiated by several members of parliament – ECB Opinion No. 72/2008 (CON/2008/72);
 - Law on the organisation and functioning of official statistics in Romania – ECB Opinion No. 42/2009 (CON/2009/42).
- b) cases of non-consultation: the ECB was not consulted by the Romanian authorities on draft legislative provisions transposing Directive 2006/43/EC on statutory audits of annual accounts and consolidated accounts into Romanian law (Government Emergency Ordinance No. 90/2008 on statutory audits of annual accounts and consolidated accounts was approved by the Parliament of Romania through Law No. 278/2008); the ECB should have been consulted since some of the provisions concerned the NBR's field of competence.
- c) NBR actions during 2008 and so far this year:
 - the NBR consulted the ECB on a draft regulation on the liberalisation of correspondent banking services for payments in national currency and on related statistical reporting requirements – ECB Opinion No. 43/2009 (CON/2009/43);
 - the NBR submitted comments on (i) ECB's draft regulation concerning statistics on the assets and liabilities of financial vehicle corporations engaged in securitisation transactions, (ii) the draft regulation amending Regulation No. 63/2002 (ECB/2001/18) concerning statistics on interest rates applied by monetary financial institutions to deposits and loans vis-à-vis households and non-financial corporations, and (iii) an ECB working paper.

- internal organisation: the NBR has formulated internal procedures and has designated the internal institutional entity in charge of disseminating the documents submitted by the ECB to the competent departments and of preparing the NBR's consolidated position on ECB's draft opinions, while ensuring the monitoring of the written procedures calendar so as to allow their timely identification and follow-up.

2.3. NBR integration in ESCB structures and substructures from an institutional perspective and in terms of decision-making / decision-taking at ESCB level

As of 1 January 2007, when Romania joined the EU, the NBR became a full member of the ESCB. NBR representatives attend – with equal rights and responsibilities as other Member States' representatives – the meetings of the 12+1 ESCB committees and relevant substructures, playing a major role in formulating and implementing the decisions of the General Council and of the Governing Council. Furthermore, these structures ensure an optimal framework for developing NCB cooperation as per their fields of competence, namely: monetary policy, open market operations, international relations, supervision, payments, currency issue, communication, statistics, internal audit, IT, accounting, legal matters and human resources. Both the NBR Board and its executive management attach particular attention to NBR's participation in ESCB structures and substructures by monitoring any issues related to streamlining the involvement and external representation of the National Bank of Romania, based on weekly and monthly reports submitted by the relevant institutional entity within the NBR. As far as internal procedures are concerned, reviews focus on the yearly schedule of each structure/substructure and on the mandates and reports prepared by NBR representatives for each meeting they attend. This is aimed at depicting the overall picture of the topics discussed by each structure/substructure and identifying the themes/subjects that might be included on the agenda of several structures/substructures within a single European institution (ECB, EC, EU Council) or on that of structures/substructures within distinct European fora. The issues debated by a structure/substructure are then reiterated for information purposes or in order to be approved by high-level decision-making structures (the Governing Council for Eurosystem members, the General Council for ESCB members, the EU Council, the ECOFIN Council and the Economic and Financial Council for all EU Member States).

2.4. NBR integration in EC and EU Council structures and substructures: NBR representatives' participation in these meetings, in line with the tasks and limitations prescribed by law

The structures and substructures of the European Commission and of the EU Council where the NBR is represented consist of several committees and working groups that tackle issues related to financial services, preparing Community legislation, banking sector supervision, statistics, and payment systems. Such entities are either clearly specified in the Treaty or they are created on an *ad-hoc* basis depending on the needs prevailing at a certain point in time. New working

groups or workshops that NBR representatives may be invited to attend are created as new regulatory needs are identified, whenever Commission initiatives need to be prepared or the enforcement of legislative measures already in place requires further monitoring and clarification.

Some of the most important Community structures that the NBR is actively involved in include: (a) the ECOFIN Council, which the NBR attends on a biannual basis (at executive management level), at the invitation of MEF, when central banking matters are on the agenda; (b) the Economic and Financial Committee (EFC), whose meetings are attended by the deputy governor in charge of European affairs; the meetings in the first part of 2009 focused on establishing an institutional mechanism and EC procedures for providing financial assistance to non-euro area countries, within the framework of the EC's instrument already in place, namely the Community financial assistance facility over the medium term; (c) the Financial Services Committee; (d) the European Banking Committee; (e) the Committee of European Banking Supervisors; (f) the Committee on Financial Conglomerates; (g) the Committee for the Prevention of Money Laundering and Terrorist Financing.

2.5. NBR integration in the European process of preparing, transposing, implementing and notifying Community legislation

The process consisted of:

- a) preparing Community legislation at EU level, within the EU Council and EC working groups attended by representatives from NBR, MEF and/or other state institutions. The most important Community legislative proposals include:
 - the Regulation on credit rating agencies;
 - revisions to E-Money Directive;
 - amendments to the Directive relating to the taking up and pursuit of the business of credit institutions;
 - amendments to the Regulation on cross-border payments in euro.
- b) transposing and implementing EC regulations at NBR level

Pursuant to Art. 249 para. (2) of the Treaty establishing the European Community, Community regulations shall be binding in their entirety and directly applicable in all Member States and thus do not have to be transposed into national law. Member States shall make sure that such regulations are actually applied in their national law and, hence, each institution must take responsibility for implementing the regulations in its field of competence. To this end, the NBR – alongside all domestic institutions with regulatory and supervisory tasks and under the co-ordination of the Department for European Affairs – checks the EC database (*Eur-lex*) on a regular basis so as to track any newly-adopted Community regulations applicable to its scope of business. The list of Community regulations that the competent departments within the NBR undertake to comply with is approved by the NBR Board and then posted on the institution's website, with a

view to informing the entities under NBR's regulatory/supervisory scope on Community legislative provisions directly applicable to them.

- c) implementing Community legislation in a centralised and coordinated manner across all ESCB members. At NBR level, an example in this sense is the public procurement law. Originally launched within the Eurosystem, by setting up the Procurement Coordination Office (EPCO) in July 2007, based on a Governing Council decision, the affiliation proposal to this type of centralised activity was submitted for review and approval to non-euro area NCBs as well. As a result, three other central banks, the NBR included, volunteered to join the other 17 Eurosystem NCBs, by attending EPCO meetings on a regular basis. This working group hosted by Banque centrale du Luxembourg over a five-year period (2008-2012) has been assigned the mandate of preparing and developing the infrastructure required for launching the first joint procurement procedures at European level.
- d) informing the EC about the transposition of Community legislation, representing the NBR's institutional accountability under the National Programme for Transposing and Notifying Community Directives; during the period under review, the program was carried out in several stages:
- During 2008, the NBR forwarded to the EC, via the Department for European Affairs, the compliance tables related to the transposition and notification of directives in its field of competence:
 - Directive 2007/44/EC of 5 September 2007 amending Council Directive 92/49/EEC and Directives 2002/83/EC, 2004/39/EC, 2005/68/EC and 2006/48/EC as regards procedural rules and evaluation criteria for the prudential assessment of acquisitions and increase of holdings in the financial sector as well as the pieces of legislation transposing such Directive;
 - Directive 86/635/EEC of 8 December 1986 on the annual accounts and consolidated accounts of banks and other financial institutions, as subsequently amended and supplemented;
 - Directive 89/117/EEC of 13 February 1989 on the obligations of branches established in a Member State of credit institutions and financial institutions having their head offices outside that Member State regarding the publication of annual accounting documents.
 - The notification and transposition process is currently underway for the following directives:
 - Directive 2007/64/EC of 13 November 2007 on payment services in the internal market;
 - Directive 2009/14/EC of 11 March 2009 amending Directive 94/19/EC on deposit-guarantee schemes.

- e) informing the EC about any changes in the standing of credit institutions in Romania: the harmonious functioning of the domestic banking market requires not only legal regulations, but also tight and regular cooperation as well as enhanced convergence of regulatory and supervisory practices enforced by competent authorities in the Member States. In this vein, particular importance is attached to tackling issues related to each individual credit institution and to the exchange of information between Member States and the EC. Consequently, pursuant to Art. 14 of Directive 2006/48/EC relating to the taking up and pursuit of the business of credit institutions, transposed in the domestic legislation via Government Emergency Ordinance No. 99/2006 (approved by the Parliament of Romania through Law No. 227/2007), every authorisation granted to a credit institution shall be notified to the Commission. The name of each credit institution to which authorisation has been granted shall be entered in a list. The Commission shall publish that list in the Official Journal of the European Union and shall keep it up to date. Based on these provisions, the NBR informed the EC during the reported period on the authorisation of BCR – Banca pentru Locuințe S.A. Furthermore, in accordance with Art. 17 of Directive 2006/48/EC, the competent authorities may withdraw the authorisation granted to a credit institution in well-defined situations and any such withdrawal shall be notified to the Commission. Hence, the NBR informed the EC on the withdrawal of the operating license of Citibank Romania S.A., whose activity was taken over by Citibank Europe plc Ireland through a newly-established branch in Romania.

2.6. NBR integration in the joint working platform with government authorities on European affairs

In line with its statutory tasks on the *ex ante* consultative role played in the institutional relations with government authorities, the NBR is represented on a weekly basis in the European Affairs Coordination Committee meetings, which are held in parallel at the head office of the Department for European Affairs and that of the Ministry of Foreign Affairs. The two institutions coordinate the decision preparation process and formulate Romania's stance with regard to European affairs (Government Decision No. 115/2008 on establishing the European affairs national coordination system). Based on the received requests and within the limits of its lawful tasks, the NBR submitted its contributions or opinions in respect to the following topics on the agenda of European Affairs Coordination Committee meetings, according to its field of competence:

- a) draft Community directives or regulations; NBR contributions are then forwarded to Romania's Permanent Representative Office with the European Union, to be integrated in the country's stance upheld by the ambassador of Romania and his assistant during COREPER II and COREPER I meetings respectively;
- b) preparing the participation folder of the Romanian delegation at European Council reunions;

- c) various issues, the most relevant being: (i) the reasoned opinion for failure to comply with Community provisions as regards caller location information in relation to the Single European Emergency number 112 and placing in default for failure to notify the Commission of the rules on applicable penalties in line with Art. 15 in EC Regulation No. 1781/2006; (ii) assessing the nationwide exposure ceiling of the Deposit Guarantee Fund in the Banking System and possibilities of enhancing the Fund activity, also by raising the guarantee ceiling applicable to household deposits; (iii) connecting the Romanian authorities to the Consumer Protection Cooperation System (TESTA network); (iv) the EC Communication on financial inclusion; (v) assessment of the de Larosière Group Report on cross-border supervision in the EU; (vi) transposing Directive 2007/64/EC on payment services in the internal market with respect to the relevant institutions' commitment to comply with Titles III and IV for legal entities.

2.7. NBR integration in the ongoing global process of strengthening international relations

2.7.1. Technical cooperation with the European Central Bank

- a) As a technical assistance provider, the NBR is actively involved in two projects coordinated by the ECB:
 - the technical assistance programme for the National Bank of Serbia (NBS). Aimed at strengthening its relations with Balkan countries, the ECB – in cooperation with 17 partner NCBs, NBR included – launched on 1 September 2008 a nine-month, EU-funded technical assistance project for the National Bank of Serbia in the requested areas, in preparation for Serbia's accession to the European Union. The six areas covered include: supervision of banks; harmonisation of legislation in line with the *acquis communautaire* under the competence of the NBS; liberalisation of capital movements; conduct of monetary policy and foreign exchange rate regime; financial and balance of payments statistics; and financial services consumer protection. Building on the experts' recent experience in the pre-accession process and based on the offers made by participating NCBs and on the list of topics communicated by the ECB, the NBR Board has reviewed and approved the bank's participation in the technical assistance project, with a focus on the NBS draft Law under the harmonisation of legislation section;
 - the cooperation programme with the Central Bank of Egypt, under ECB coordination, with the support of seven ESCB members, NBR included. The project is financed by the European Commission and spans a three-year period, marking a new stage in the previous cooperation between the ECB and the Central Bank of Egypt for enhancing regulation and supervision. The primary objective of the

programme is to support the Central Bank of Egypt in implementing the Basel II provisions. The project consists of three stages, as follows: (i) know-how transfer, completed when achieving a national strategy for implementing the Basel II framework in Egypt; (ii) consultation with the banking system, following which the Central Bank of Egypt will formulate a set of principles underlying the new regulations for transposing the Basel II principles; (iii) organising and implementing the process of enforcing Basel II regulations, as well as preparing a new scheme for statistical data reporting by commercial banks to the central bank, with a view to implementing the new Basel II regulations. NBR regulation and supervision experts will provide technical assistance to the Central Bank of Egypt throughout the duration of the project. NBR experts' participation in this technical assistance project was approved by the NBR Board at end-2007.

- b) As a recipient of technical assistance, the NBR focused on strengthening cooperation with the ECB via short-term exchanges of experience on various issues: monetary analysis within the ECB, preparing the monetary analysis materials for the Governing Council, describing the structure and functions of the ECB intranet and website.
- c) A major step towards strengthening institutional cooperation between the ECB and the NBR is the latter's affiliation – at the ECB's invitation – to the “Cultural Days” project. After teaming up with the other ESCB members for the Cultural Days of the ECB – EU 2008, Romania will be the theme country of the seventh edition of this project, scheduled in Frankfurt during 21 October – 9 November 2009.

2.7.2. The technical cooperation with other ESCB members materialised in various technical assistance programs, ranging from workshops related to the reunions of ESCB working groups and committees – focusing on payment systems, IT, financial stability, statistics – to conferences, exchanges of experience and working meetings at NBR executive management level or at expert level, to discuss important topics on the NBR agenda (for instance, the exchange of experience with Oesterreichische Nationalbank on “The OeNB Euro Survey in Central, Eastern and Southeastern Europe – The 2008 Spring Wave Update”).

2.8. Management of ECB documents

In its relation with the ECB as regards all General Council documents, the written consultation procedure and other institutional issues, the NBR has created, developed and monitored a well-articulated institutional framework, with the following tasks: (i) disseminating information to the NBR's executive management and competent departments in compliance with the applicable confidentiality and embargo rules, (ii) managing access to ECB documents sent via EXTRANET and CebaMail (where still applicable), according to ECB guidelines, (iii) storing and archiving all these documents through the NBR's own means, abiding by the ECB principles governing information flow management, security and embargo, (iv) cooperation with the ECB for any exchange of documents between the

management of the two institutions, (v) cooperation with the NBR Security Section for harmonising the legislative framework, in case of amended or supplemented provisions.

2. Cooperation with international financial and economic institutions

International Monetary Fund (IMF)

Romania has been a member of the International Monetary Fund since 1972.

At present, Romania's subscription quota (subscribed and paid-up capital) in the IMF share capital is SDR 1,030.2 million, of which SDR 243.8 million in gold and foreign currencies and SDR 786.4 million in lei, in an IMF account opened with the National Bank of Romania.

In April 2008, an IMF mission visited Bucharest in order to assess together with the Romanian authorities the economic developments of 2007, against the background of the yearly consultations laid down in Article IV of the IMF's Articles of Agreement.

Furthermore, at the request of the Romanian authorities, a joint IMF-World Bank mission visited Bucharest in November 2008 for a follow-up on the financial system stability assessment under the Financial Sector Assessment Program (FSAP). This program represents an important tool employed by the International Monetary Fund and the World Bank in identifying potential vulnerabilities and analysing the priorities of Member States' financial sector, so that the latter might develop diversified and competitive financial sectors¹.

Given that Romania's financial liabilities to the IMF in 2008 consisted solely of the quarterly payment of interest on SDR allocations and the annual fee covering the administrative expenses of the SDR department, as well as the fact that the state's foreign exchange reserves administered by the NBR are at a comfortable level, the NBR Board approved the repurchase of the amount of SDR 75.95 million (representing SDR allocations received from the IMF during 1979-1981²), to be deposited in Romania's account with the IMF.

¹ The latest FSAP on Romania dates back to 2003.

² As an IMF member country, Romania accepted to take part in the second SDR general allotment conducted by the Fund during 1979-1981 (in line with its statutory provisions). Against this backdrop, Romania was allotted the amount of SDR 75.95 million, which was made available in its SDR account with the IMF. These amounts represent assets of the countries to which they were allotted, while the said countries may either keep the amounts in the SDR account with the IMF or use them. In the latter case, the beneficiary pays interest to the Fund while using such amounts.

Given the economic environment of 1990, when financial resources were scarce and payment liabilities ran high, Romania chose to use the allotted SDR amount. Thus, in December 1990, the Government of Romania ordered that the SDR 75.95 million in Romania's account with the IMF be sold for US dollars.

In 2008 payments to the International Monetary Fund amounted to SDR 835,208 in net interest on SDR allocations-holdings.

World Bank Group

a) International Bank for Reconstruction and Development (IBRD)

Romania joined the IBRD in 1972, an institution in which it holds 4,011 shares and a voting power accounting for 0.26 percent of total.

Since the recommencement of its activity in Romania in 1991 and until end-2008, the IBRD has provided a total of USD 5.5 billion in loans to our country. The IBRD's financial assistance to Romania amounted in 2008 to USD 133.1 million via two projects. At end-2008 there were 23 projects in progress, totalling USD 1,831.27 million.

Since no significant fluctuations occurred in the RON/USD exchange rate, the year 2008 saw no payments arising from the procedure of maintaining the value of Romania's subscription in domestic currency to the IBRD capital, a procedure which has been in force since 1986.

b) Financial institutions affiliated to the World Bank

International Finance Corporation (IFC)

Established in 1955, the IFC is an international financial organisation affiliated to the World Bank Group. Romania joined the IFC in 1990 and currently holds 2,661 shares worth USD 2,661,000 and a 0.12 percent voting power within the organisation.

In 2008, IFC financing in Romania targeted the banking sector, aimed at fostering lending to small- and medium-size enterprises. Thus, Banca Transilvania and ATE Bank were granted loans totalling around EUR 40 million.

The cumulated volume of IFC investments in Romania during 1996-2008 reached almost USD 950 million. During the period, the IFC participated with almost USD 385 million in syndicated loans to support several projects in key sectors of the economy, such as: industry, infrastructure, oil and gas, telecommunications, financial markets.

Multilateral Investment Guarantee Agency (MIGA)

Romania has been a member of MIGA, established in 1988, since 1991. Our country currently holds 978 shares representing SDR 9,780,000 (around USD 10.58 million) and a voting power of 0.56 percent within the organisation.

Throughout 1997-2008, the MIGA portfolio for Romania consisted of 13 guarantees totalling a cumulated exposure of USD 437.79 million for supporting certain investment projects. Most of these guarantees were provided to Austrian

investors in the banking sector, for covering the risks of transfer restriction and expropriation. Three of these projects are currently in progress, amounting to USD 111.65 million.

European Bank for Reconstruction and Development (EBRD)

Romania is a founding member of this institution (established in 1991) and currently holds 9,600 shares worth EUR 96 million, accounting for 0.485 percent of total capital.

Over an 18-year period, the EBRD granted Romania assistance with a cumulated value of almost EUR 4 billion (as of end-2008), with 249 signed transactions, of which 71 percent were destined to support the private sector. Funds amounting to EUR 2.9 billion were actually drawn from the overall investment volume. In 2008 the business volume stood at about EUR 318 million.

Amid the ongoing global economic crisis, the EBRD's strategic projects in Romania included a EUR 100 million loan to Banca Transilvania at end-2008 for reviving SME lending.

In its meeting on 29 April 2008, the EBRD Board of Directors approved the 2008-2010 Country Strategy for Romania. Thus, the EBRD will focus on the following priorities over the strategy period:

- addressing challenges to the private enterprise sector through finance and expertise;
- energy generation, transmission and distribution (both public and private sectors);
- improving infrastructure, particularly in the transport sector.

Black Sea Trade and Development Bank (BSTDB)

With a start-up capital of SDR 1 billion (USD 1.5 billion), the BSTDB was established in 1994 by the 11 member countries of the Organization of Black Sea Economic Cooperation³ (OBSEC), Romania included.

On 5 October 2008, the Board of Governors decided to triple the bank's authorised capital to stand at USD 4.5 billion. The new shares were fully subscribed and allocated. As a result of the capital increase, Romania's quota in the new shareholding structure of BSTDB reached 14 percent.

According to end-of-year data, the institution recorded a cumulated volume of commitments to Romania worth USD 82.5 million and EUR 25 million, through 11 projects, including two regional financing funds and collateral provided to Banca Românească.

³ Eleven countries are OBSEC founding members: five Balkan states (Albania, Bulgaria, Greece, Romania, Turkey), three adjacent countries (Moldova, Russia, Ukraine) and three Caucasian countries (Armenia, Azerbaijan and Georgia).

European Investment Bank (EIB)

The EIB was established in 1958, in line with the provisions of the Treaty of Rome, as the long-term lending bank of the European Union through projects supporting European integration. Romania became a EIB member upon joining the European Union. Romania's subscribed capital amounts to EUR 863.5 million, accounting for 0.524 percent of total capital. Each Member State's share in the Bank's capital is calculated in accordance with its economic weight within the European Union (expressed in GDP) at the time of its accession.

In 2008, the EIB signed 7 agreements with our country (for projects in industry, municipal utilities, transports, and global SME lending through leasing companies), representing a commitment worth EUR 1.1 billion. Thus, the cumulated value of the financial assistance provided by the EIB to Romania during 1991-2008 exceeded EUR 6 billion.

Bank for International Settlements (BIS)

The BIS was established in 1930 with the aim of fostering cooperation among central banks. The NBR, which has been a BIS member ever since the latter's creation, holds 1.33 percent of the institution's capital.

In 2008, the NBR received EUR 2.4 million in dividends for the 2007-2008 financial year in relation to the 8,564 shares held in the BIS capital. According to the decision passed by the Annual General Meeting of member central banks, the value of a dividend was set at SDR 265, based on the actual results at the closure of the financial year, i.e. on 31 March 2008.

Organisation for Economic Cooperation and Development (OECD)

Underpinning Romania's efforts towards becoming a member of the OECD, the National Bank of Romania contributed – at the request of the Ministry of Foreign Affairs – to the initiatives of involving our country in the OECD activity.

Thus, with a view to obtaining the membership status, the Romanian authorities and the NBR stepped-up their participation in the working structures and in the drafting of documents promoted by the OECD. To this end, based on an NBR Board decision, the central bank formally expressed its willingness to participate in several working groups and committees in the financial and banking areas. Furthermore, the NBR regularly forwarded comments and suggestions in relation to various documents and studies prepared by the OECD, such as proposals on the Programme of Work of the OECD Development Centre during 2009-2010, "Black Sea and Central Asia Initiative 2009-2010", and the 2009-2010 programme of studies having "Shifting Wealth" as core theme. The National Bank of Romania will further cooperate with the Ministry of Foreign Affairs for strengthening Romania's position as an active candidate to OECD membership.

International events organised by the NBR

On 6 June 2008, the NBR hosted the meeting of the ECB's International Relations Committee (IRC), which acts as a forum for exchanging views on matters of common interest in international cooperation.

The June 2008 reunion in Bucharest was attended by deputy governors or their alternates (directors/heads of international relations departments) from the 27 IRC member countries. The main topics discussed on this occasion referred to economic policy issues and evolutions both in the major developed economies and in emerging economies as well as the impact of the global financial market turmoil.

Chapter 8. Preparation of the euro adoption process

1. Romania's progress towards convergence

Romania's integration with the European Union implies, once with the fulfilment of the necessary conditions stipulated by the Maastricht Treaty, the adoption of the European single currency. Adopting the euro is a crucial step for the economy of a Member State, given that the responsibility for monetary policy is transferred to the European Central Bank, which conducts it independently for the euro area as a whole. The European Central Bank's "one-size-fits-all" monetary policy is aimed at a group of supposedly homogenous economies, without focusing on each one's particular features. In the context of preparations for euro adoption, economic integration with euro area members is required. The Romanian economy will make the necessary adjustments by January 2015 – the target date for adopting the euro. The European Council's favourable judgement on the euro adoption is conditional upon the participation of the Member State in the Exchange Rate Mechanism (ERM II) for at least two years. The compatibility with the mentioned objective points to Romania's entry into ERM II in 2012.

The "convergence criteria", as laid down in the Maastricht Treaty are the formal framework for assessing whether a Member State is prepared for adopting the single currency. The criteria are defined as a set of macroeconomic indicators measuring price stability, the soundness and sustainability of public finances, the exchange rate stability and the dynamics of long-term interest rates. The latest Convergence Report elaborated by the European Commission in May 2008 analyses Romania's prospects to adopt the euro, emphasising that only public finance criteria are met.

The following table shows where the Romanian economy stands in relation to the nominal convergence criteria¹.

Maastricht Criteria (Nominal convergence indicators)			
Nominal convergence indicators	Maastricht Criteria	Romania 2008	Romania Apr-09
Inflation rate (HICP*) (percent, annual average)	<1.5 pp above the average of the three best performing EU Member States	7.9 (criterion: 4.0)	7.4 (criterion: 3.4)
General government deficit (percent of GDP**)	below 3 percent	5.4	...
Government debt (percent of GDP**)	below 60 percent	13.6	...
Exchange rate vs. euro (2-year maximum percentage change ***)	+/- 15 percent	+9.7/-14.6	+7.2/-22.7
Long-term interest rates (percent p.a., annual average)	<2 pp above the average of the three best performing EU Member States by inflation rate criterion	7.7 (criterion: 6.2)	8.3 (criterion: 6.4)

Source: Eurostat, ECB, EC, NIS, NBR

*) HICP – harmonised index of consumer prices. **) According to ESA95 methodology. ***) Calculations for April 2009 are based on the maximum change for May 2007-April 2009 compared to the exchange rate average in the month preceding this period. The same procedure was used for the January 2007-December 2008 period.

¹ See Box 1 in Chapter 8 of Annual Report 2006 for further details.

By mid-2007, the disinflationary process manifest since 2000 came to a halt, which persisted for a year. Behind this performance stood the drought, the pick-up in prices of commodities and fuels on the international markets, the depreciation of the domestic currency, as well as the persistent pressures from aggregate demand and wage rises. Starting with the latter half of the year, the 12-month inflation rate resumed its downward trend. In terms of nominal convergence, the average annual HICP inflation exceeded the price stability criterion by 4 percentage points in April 2009.

In the previous years, the general government deficit-to-GDP ratio stood below the level provided by the Maastricht Treaty. However, in 2008, under the adverse impact exerted for the year as a whole by the substantial increase in public expenditures and the strong deceleration of GDP dynamics in Q4, the budget deficit-to-GDP ratio exceeded the 3 percent level established by the criterion. On the other hand, in 2008, government debt remained well below the threshold set by the Maastricht Treaty.

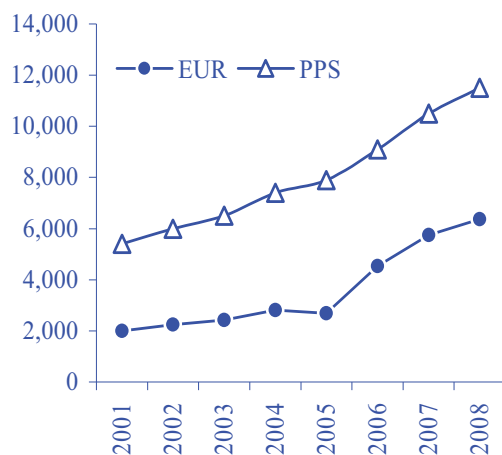
The RON/EUR exchange rate reached an all-time low in July 2007. Subsequently, the emergence of the turmoil on world financial markets, its gradual worsening, as well as the reassessment by foreign investors of the risk associated with Central and Eastern Europe led to significant depreciation pressures on the domestic currency. During 2007-2008, the change in the RON/EUR exchange rate did not exceed the standard fluctuation band of ± 15 percent versus the reference level (the average for December 2006). Starting 2008 Q4, the upward revision of the risk associated with Romania brought about a depreciation trend of the leu, which became more pronounced in early 2009. In this context, during May 2007-April 2009, the maximum depreciation versus the reference level (the average for April 2007) exceeded 20 percent.

Long-term interest rate criterion refers to the assessment of the sustainability of the convergence achieved by meeting the other criteria. In mid-2008, the long-term interest rate neared the reference criterion (to almost 0.6 percentage points from it) amid the financial turbulences which caused a step-up in financial investors' risk aversion, whereas in April 2009, it moved away to 1.9 percentage points from this criterion.

The assessment of the euro area entry timeliness also takes into account some indicators that reveal the real convergence of the economic performance of Member States, in order to ensure a high cohesion between the economies of monetary union members. The main criteria envisaged are real GDP/capita, the sectoral structure and openness of the economy and the share of trade with the EU in total foreign trade.

Romania:

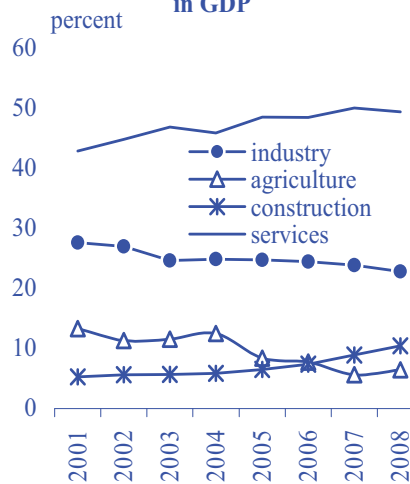
Development of GDP per Capita



PPS = Purchasing Power Standards

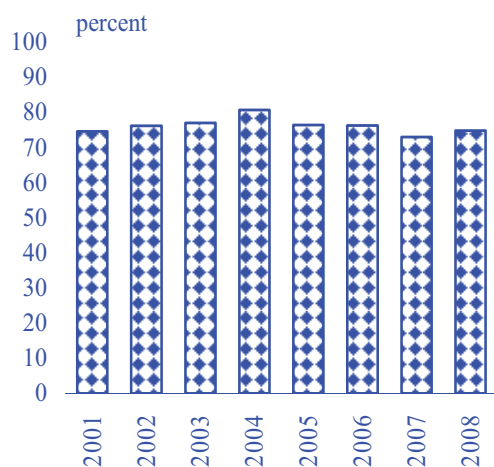
Source: Eurostat, NIS, NBR

Share of Economic Sectors in GDP



Source: NIS

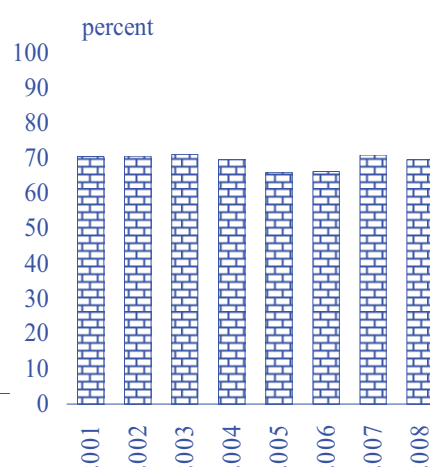
Economy Openness*



*) (imports and exports of goods and services)/GDP

Source: NIS

Share of Trade with the EU* in Total Foreign Trade



* EU-26

Source: NIS

GDP per capita, in terms of purchasing power standards, went up, following a sustained catching-up with the euro area, to reach roughly 40 percent of GDP/capita in the euro area in 2008. This development took place against the background of the convergence of the structure of economic sectors. Economy openness² remained at about 75 percent over the past years, given that the EU is Romania's main trading partner, accounting for approximately 70 percent of total foreign trade. Apart from the aforementioned indicators, an analysis of the financial sector is also important. This sector is highly integrated with that of the

² Calculated in the chart as the ratio of imports plus exports of goods and services to GDP, expressed in lei.

European Union, in the context of the prevalence of foreign capital (coming from the euro area) in the shareholding structure of commercial banks on the Romanian market. Also, the banking sector has developed rapidly, with the indirect financial intermediation recording a significant expansion, albeit below that in the euro area³. Direct financial intermediation via the capital market stood at a low level (considerably below that in the euro area).

After assessing various alternatives⁴, the NBR maintains its view that early 2012 is the appropriate timing for the entry into ERM II. A decision in favour of adopting the euro is expected to be made in 2014, after having participated for at least two years in EMR II and after meeting the convergence criteria, with the actual adoption following to take place in 2015. The Romanian economy needs to be sustainably adjusted for some time in order to become consistent with the euro-area economy and contribute therefore to a feasible implementation of the euro. Thus, apart from meeting the nominal criteria, a series of structural adjustments are envisaged, such as:

- synchronisation of the business cycles in Romania and the euro area;
- rendering labour market more flexible;
- adjustment of the external deficit towards sustainable levels in the medium term;
- consolidation of the domestic financial market in the long run.

The NBR has supported further the joint efforts of government institutions for consolidating reforms and adjusting macroeconomic imbalances. By the inflation targeting strategy, monetary policy envisages directly the fulfilment of the nominal criterion on price stability. The compatibility of this strategy with the fulfilment of the nominal criterion is ensured by setting an inflation target trajectory in line with this objective and by adjusting the monetary policy conduct with a view to placing inflation rate on a path convergent to the targets set in the medium run. Within the same strategy, the managed float exchange rate regime, preceding the ERM II entry, ensures a flexible monetary policy response to shocks affecting the economy with a view to alleviating their unfavourable impact on the central bank's objectives.

2. Experience of countries that have recently joined the Economic and Monetary Union

According to the Maastricht Treaty, the countries joining the European Union become Member States with a temporary derogation from adopting the single currency. Out of ten countries that joined the European Union on 1 May 2004, only four (Slovenia, Cyprus, Malta and Slovakia) entered the euro area so far. Lithuania was very close to the euro adoption on 1 January 2007, as the assessment revealed

³ Financial intermediation, calculated as the ratio of non-government credit to GDP, rose in 2008, both in Romania and the euro area, coming in at 39.3 percent and 117.1 percent respectively at year-end. Source: NIS, Eurostat, NBR.

⁴ Box 2 in Chapter 8 of Annual Report 2006 shows a series of benefits and drawbacks of adopting the euro both over a short- and long-time horizon.

its compliance with three of the nominal convergence criteria; however, the inflation rate exceeded marginally the reference level and its moderate sustainability was deemed insufficient.

Slovenia

Slovenia was the first country in this group that met all the Maastricht criteria. The joint Programme unfolded by the Government of Slovenia and Banka Slovenije for ERM II entry and adoption of the euro was drafted in 2003 and set 1 January 2007 as the target-date for the entry into the euro area. Slovenia joined the EMU as provided, i.e. less than three years after joining the European Union.

The Slovenian currency started its participation in ERM II on 28 June 2004, illustrating the authorities' option to adopt as soon as possible the European currency. During the years preceding the ERM II entry, the central bank of Slovenia implemented a policy of steady nominal depreciation of the Slovenian tolar against the euro, albeit at an increasingly slower pace. This exchange rate policy, designed to support nominal convergence, was abandoned once with the participation in ERM II. The central rate for the Slovenian currency against the euro was set at the market exchange rate upon the entry into ERM II and the fluctuation band around the central rate at ± 15 percent.

During its participation in ERM II, the Slovenian currency was traded at levels very close to the euro central rate, the exchange rate volatility being very low. Nevertheless, mention should be made that, shortly after ERM II entry, Banka Slovenije signalled its intention to maintain the tolar exchange rate close to the central rate, by temporarily resorting to interventions in the foreign exchange market aimed at strictly containing exchange rate deviations from the central rate. Furthermore, during the participation in ERM II, Banka Slovenije acted with a view to maintaining short-term interest rates on the money market at levels higher than those in the euro area, allowing however the differential between such interest rates to decline gradually in order to comply with the nominal convergence criterion upon assessment. From the very beginning, the Slovenian authorities' intention was to contain the tolar's participation in ERM II to the minimum two-year stay, viewing this exchange rate arrangement as enhancing the risk of a speculative attack on the domestic currency.

As regards price stability, during the ten-year period prior to adopting the euro, Slovenia reported one-digit inflation rates. The highest average annual inflation was recorded in 2000, i.e. 8.9 percent. Subsequently, the inflation rate entered a downward trend to reach 2.5 percent both in 2005 and 2006. Behind this development stood also the change in the monetary policy strategy in 2001, when monetary targeting was abandoned in favour of a more eclectic monetary regime based on monitoring real and nominal economic developments.

Nominal convergence criteria were met against the background of a robust economic expansion steadily surpassing that reported by the euro area. The nominal and real convergence of the Slovenian economy stood out by the absence

of any slippage, as both current account and fiscal deficits recorded steadily moderate levels, without threatening the macroeconomic equilibrium. Moreover, unlike other countries that joined the European Union in 2004, in Slovenia, monetary and fiscal policies were very well matched, as the Ministry of Finance and Banka Slovenije acted in a concerted manner.

Cyprus

Cyprus joined the euro area on 1 January 2008, along with Malta.

The first convergence programme was drafted in 2004 and envisaged the changeover to the euro as fast as possible, considering even the ambitious objective of switching to the euro in 2007. Such a scenario became soon unrealistic, as in 2004 Cyprus was subject to the excessive deficit procedure that provided the gradual contraction of the fiscal deficit to less than 3 percent of GDP in 2006. Following the fiscal consolidation, in 2006, the budget deficit came at 1.5 percent of GDP only, so that the fiscal deficit procedure was terminated that year. The general government debt-to-GDP ratio was on a downward path, without, however, falling within the 60 percent ceiling in 2006. The criterion on the sustainability of public finances was deemed to be met, given that the general government debt-to-GDP ratio was reporting a significant decrease, nearing the reference value.

On 2 May 2005, Cyprus joined ERM II, concurrently with Malta and Latvia, one year after they became EU Member States. The central rate of the Cyprus pound was set at 0.585274 pound per euro – also the rate at which the pound was linked unilaterally to the euro in 1999 – with a standard fluctuation band of ± 15 percent. As a matter of fact, this fluctuation band was used also prior to joining ERM II, being introduced ever since January 2001. During its participation in ERM II, the Cyprus pound remained close to its central rate, showing very low volatility.

The average 12-month inflation rate stayed close to 2 percent in 2005 and 2006 and during April 2006-March 2007 period – considered while assessing the fulfilment of the convergence criteria. Given the 3 percent reference value, Cyprus easily met the criterion on price stability. The long-term interest rate stood at 4.2 percent during the reference period, falling safely within a 6.4 percent limit.

The Cyprus economy rose at a roughly steady pace throughout the period in between EU accession and the entry into the euro area, ranging between 3.5 percent and 4.5 percent, whereas current account deficit stayed at sustainable levels.

Malta

Malta joined the euro area on 1 January 2008.

On 2 May 2005, Malta joined ERM II, the central rate of the Maltese lira being set at 0.429300 lira per euro, i.e. the market rate at that time, with a standard fluctuation band of ± 15 percent. Upon joining ERM II, the Maltese lira was pegged to the euro and the previously-used foreign currency basket (including the single currency, the pound sterling and the US dollar) was abandoned. The exchange rate

was maintained at the central rate level throughout the reference period for assessing the exchange rate stability (May 2005-April 2007).

Malta met the Maastricht criteria against the background of an economic growth of more than 3 percent during 2005-2007 and of a low current account deficit, the financing of which did not pose any problems.

The average 12-month inflation rate came in at 2.2 percent over the reference period (April 2006-March 2007), i.e. 0.8 percentage points below the specific level of this criterion. In fact, Malta recorded a relatively stable inflation rate during a long period of time, in a range from 2 percent to 3 percent since 1999. During the reference period, the long-term interest rates stood at 4.3 percent, markedly below the 6.4 percent reference value for the interest rate criterion.

Subsequent to Malta's EU accession, price stability benefited largely from the fiscal policy support. In 2004, Malta was subject to the excessive deficit procedure, following its reporting a fiscal deficit of 9.7 percent of GDP in the year before. After the initiation of this procedure, Malta adopted fiscal policy measures that led to a gradual decrease in fiscal deficit to 2.6 percent of GDP in 2006. Furthermore, the general government debt-to-GDP ratio went down markedly from 72.4 percent in 2005 to 66.5 percent in 2006. Under the circumstances, the excessive deficit procedure was terminated in 2007 and the criterion on the sustainability of public finances was deemed to be met.

Slovakia

Slovakia joined the euro area on 1 January 2009, four years and eight months after the EU accession.

In 2003, Slovakia elaborated a first euro adoption strategy, forecasting the changeover to the euro to take place around 2008-2009. Subsequently, in 2004, the Slovak authorities set 1 January 2009 as the target-date for adopting the euro, an objective undertaken and reiterated in the following years as well.

On 28 November 2005, Slovakia joined ERM II, relatively shortly after the EU accession. A standard fluctuation band of ± 15 percent was set around the central rate. During the first months of participation in ERM II, the Slovak currency posted a relative volatility around the central rate, without however nearing the bounds of the fluctuation band. Subsequently, starting August 2006, the strong underlying economic fundamentals of the Slovak economy caused the koruna to enter a significant nominal appreciation trajectory. Consequently, the central rate was revalued by 8.5 percent with effect from 19 March 2007. Thereafter, the Slovak currency consistently fluctuated above the new central parity, the maximum upward deviation amounting to 8.9 percent. As a result, in May 2008, the central rate of the koruna was revalued again, this time by 17.6 percent.

The Slovak Koruna's participation in ERM II overlapped with a period of surplus liquidity worldwide and a very favourable perception by investors of emerging

economies, particularly of new EU Member States. The massive capital inflows covered current account deficits (which, although still significant were on a decrease from 8.6 percent of GDP in 2005 to 5.1 percent of GDP in 2007) leading at the same time to a considerable strengthening of the domestic currency. Overall, the period of participation in ERM II was characterised by the appreciation of the Slovak koruna vis-à-vis the euro, which made it more difficult to analyse how the Slovak economy operated under conditions of irrevocably fixed exchange rates.

During the reference period (April 2007-March 2008) the average 12-month inflation rate stood at 2.2 percent, i.e. one percentage point below the ceiling calculated according to the provisions of the Maastricht Treaty. This outstanding performance in terms of price stability was facilitated mainly by the strong nominal appreciation of the Slovak koruna and by the moderate developments in domestic energy prices. Subsequently, inflationary pressures escalated markedly, while the average annual rate of increase of consumer prices stood at 3.9 percent in 2008.

The criterion on the convergence of interest rates was easily met, during the reference period, the long-term interest rates posting an average level of 4.5 percent per annum, i.e. considerably below the 6.5 percent reference value.

Both fiscal deficit and general government debt came in significantly below the reference values. However, mention should be made that starting 2004, Slovakia was subject to an EU Council decision on the existence of an excessive deficit. The deadline for correction of the deficit was 2007. In June 2008, the EU Council abrogated the excessive deficit procedure, as deficit was diminished credibly and sustainably to a level below 3 percent of GDP. The termination of the excessive deficit procedure was, as a matter of fact, a pre-requisite for Slovakia's entry into the euro area in 2009.

Slovakia's successful euro adoption may be attributed to a series of favourable factors. First, the political and popular support in favour of this objective was considerable. The authorities never tried to postpone the target-date for adopting the euro, on the contrary, they acted in a concerted manner, including with a view to minimising the ERM II participation period. Second, among the countries joining the EU in 2004, Slovakia was the first one to meet the criteria for the euro adoption, by applying an inflation targeting strategy and a free floating exchange rate regime. Given the substantial appreciation of the Slovak koruna, amid the massive capital inflows and the sound macroeconomic fundamentals, Slovakia proceeded to adjusting the central rate, by strengthening the domestic currency. Third, the relatively rapid nominal convergence was accompanied by a fast progress in real convergence. After the EU accession, economic growth recorded an increasingly faster dynamics each year, to reach 10.4 percent in 2007 from 5.2 percent in 2004. In 2008, the economic growth rate slowed down, remaining however at a high level, i.e. 6.4 percent. Throughout this period, economic expansion sustainability was not endangered, as the economic policies pursued ensured moderate inflation and current account deficit.

Chapter 9. External communication of the National Bank of Romania

In 2008, the external communication of the National Bank of Romania continued to be in line with the objectives of the central bank amid the inflation targeting strategy and the major challenges posed by the effects arising from the gradual intensification of the international financial and economic crisis. Under the circumstances, the central bank adopted a pro-active approach, increasing significantly the frequency and intensity of communication with the target public, with the view to ensuring correct, transparent and immediate information on its decisions and actions and to preventing potential disruptions.

Communication of the NBR aims at providing the general public, the national and international business environment, general government institutions and the academic community with a clear image of the policies and measures adopted by the NBR for fulfilling its tasks, according to Art. 56 para. 3 of Law No. 312/2004 on the Statute of the National Bank of Romania.

In this respect, the central bank pursues to enhance the target public's understanding of the NBR's role and functions within the economy, as well as of its decisions to maintain price stability and ensure financial stability, which contributes to a higher transparency and efficiency of decisions and to a stronger credibility of the institution.

In 2008, the NBR acted further with a view to increasing transparency (an essential feature of the inflation targeting strategy adopted in August 2005) by providing detailed information and explanations on monetary policy decisions and assessments via press releases, press conferences aimed at offering an overview of the quarterly Inflation Report or via public events attended by senior executives.

In the last part of 2008, as the effects generated by the international economic and financial crisis started to be felt in Romania as well, the NBR enhanced its communication with different categories of target public, emphasising the specific features of the Romanian economy and the position of the Romanian banking system.

External communication activities

The NBR addresses specific categories of public, such as financial experts, the media, government and non-government institutions, researchers, the general public that show a different interest in and have varying levels of knowledge of economics and finance. Therefore, it resorts to a various range of communication tools for each type of audience, adjusting its messages based on the international and national economic and financial context.

During 2008, the NBR organised – with a view to informing both the general public and the communities of experts – 172 events, of which 136 were press conferences and briefings; the central bank has become highly visible especially starting 2008 Q3.

The communication activities of the National Bank of Romania were aimed at ensuring efficient information and maintaining a high transparency of adopted decisions and measures, amid the heightening of the crisis on international financial markets. The NBR senior executives and experts made a direct contribution to enhancing public knowledge and understanding of the role played by the central bank by granting interviews to the media, by delivering public speeches on financial and banking issues during radio and television shows and debates, by presenting speeches to students and to the academic and university environment, as well as by giving testimonies before the Romanian Parliament.

The prompt response of the central bank in its external communication activities, as reflected by the media, helped maintain its credibility among the general public, even when some financial analysts and representatives of the banking community contested publicly some of the NBR decisions, especially in the latter half of 2008. In spite of these, sometimes strongly negative, critical remarks on the NBR's policies, the central bank succeeded in maintaining the public's confidence. The enhanced transparency, the larger number of press conferences and briefings, as well as the interviews and press statements made by senior executives and also by other NBR representatives had a pivotal role in preserving credibility.

Meetings on a regular basis of NBR senior executives and experts with financial analysts and representatives of the business environment became more frequent in the last part of 2008, helping enhance transparency and credibility.

The central bank and its representatives appeared much more often in the media than in the previous years. Over 2,400 articles were published by the national and international press, out of which 198 were editorials. The number of public appearances on radio and television was also high. During 2008, the articles published in journals, magazines and newspapers were increasingly favourable, remaining positive even in 2008 Q4 when the economy deteriorated both nationally and internationally.

Economic sentiment was further favourable, in a range from neuter to positive, amid the economic pressures in late 2008 (in spite of repeated critical comments on some decisions), which proves that the NBR managed efficiently and transparently its main objectives, including the objectives pertaining to external communication, and prevented the emergence of a potential image crisis. The central bank sent messages in which it coherently argued its position, thus strengthening its image as a professional and trustworthy institution both in Romania and worldwide.

In 2008, the NBR organised a number of seminars, symposia, conferences and other events on economic, financial and banking history topics aimed at enhancing

the knowledge of various types of audiences on its role and responsibilities within the economy.

The central bank organised the highest number of events April through May on the occasion of NBR's anniversary and October through November in the context of the intensification of the international financial crisis. Most press conferences and briefings were held in February (33) and October (47).

The high-profile public events encompassed a series of manifestations celebrating the NBR's anniversary. Thus, on 16 April 2008, the National Bank of Romania, *Magazin Istoric* Cultural Foundation and the Romanian Banking Association organised the 16th edition of the Symposium of Banking History and Civilisation "Cristian Popișteanu" on the topic "At the service of the banking system – people and facts". The NBR also started to organise a string of symposia under the aegis of "Monetary policy colloquia" which were aimed at developing the dialogue with the academic environment, the banking community, financial analysts, as well as with the media. The first edition took place on 17 April 2008 and the topic discussed was "Monetary Policy: Developments and Challenges". In 2008, the central bank communicated directly with both national and international academies. The Romanian Academy and universities acted as authorised, trustworthy message multipliers, benefiting also by the support offered by the National Bank of Romania in the field of financial education. Some of the most important academic events that took place in 2008 were: the NBR governor's participation in and allocutions at *Real Academia de Ciencias Económicas y Financieras* in Spain on the occasion of his becoming a member in his own right of the prestigious academic community, the international Conference entitled "Enhancement of Knowledge on Higher Education and its Dissemination: Imperative for Policy and Practice", organised by "Babeş-Bolyai" University in Cluj-Napoca together with the UNESCO European Centre for Higher Education and the European Council on 26 September 2008 and the session organised by the Romanian Academy "The Strategy for Adopting the Euro and the World Financial Crisis" in Bucharest on 2 October 2008. The main messages delivered on these occasions focused on topical issues such as the European Union and the changeover to euro, the impact of the international crisis, price stability and financial stability, macroeconomic policies, etc.

The NBR also continued to cooperate with banking institutions, the Romanian Banking Association and the Romanian Banking Institute, by organising a series of meetings and seminars aimed at enhancing the knowledge of media representatives and financial analysts in the financial and banking field by pointing at new notions and national and international economic developments. Presentations and debates on the occasion of both the Conference organised on 23 September 2008 in Râmnicu Vâlcea "The Path to European standards for financial services" and the Conference "Young economists" held at the NBR headquarters focused on several topics such as the international financial crisis and the unprecedented anti-crisis measures taken by central banks and governments; the low vulnerability of the Romanian banking system to the effects of the international turmoil; identifying

significant risks to the Romanian economy in the short run, and also in the medium and long run with a view to adopting the measures required for their correction; challenges to the Romanian banking system against the background of the crisis.

Furthermore, the NBR intensified its communication activities with the other institutions and particularly with those institutions in charge of supervising other segments of the financial market in Romania, in view of the public's increasing interest in issues relative to the financial and banking environment. In this context, a common communication strategy was developed by all the institutions that are members of the National Financial Stability Committee with a view to enhancing transparency and understanding of decisions made in the field of financial stability and financial crisis management.

The website became one of the most important communication tools, ensuring transparency and providing on a continuous basis the latest information on the central bank's policies for meeting its objectives and responsibilities, as well as specific indicators. In 2008, the NBR initiated and unfolded a project for completely streamlining its website, which was relaunched on 9 March 2009.

The new website is in line with the present tendencies and standards in the field, being a complex and interactive communication tool that provides a wide range of information, as well as new functionalities. Its main features consist in: (i) an overview on the front page of the most relevant and accessed information on the central bank's activity: the NBR interest rates, the inflation target and current inflation rate readings, the exchange rate; (ii) rapid access to information by notification via email or RSS, as well as to statistical data in a specific format for researchers; the information dissemination calendar; the glossary; the search engine; (iii) improvement in the number of sections simultaneously with the reduction of the extant ones and the introduction of new fields.

NBR Publications

NBR publications were further an important communication tool of the central bank, which showed an ongoing interest in improving their informational contents, structure and graphical layout. In 2008, a new publication was launched *Regional Seminar on Financial Stability*, which gathers together the papers presented within the annual seminar on financial stability matters, hosted by the National Bank of Romania, with the participation of renown specialists from central banks in the region, the International Monetary Fund and the European Central Bank.

Most NBR publications are available both on paper and in electronic format, in Romanian and English.

Moreover, in 2008, the NBR ensured the translation into Romanian of the following publications of the European Central Bank: the Convergence Report, the Annual Report, General Documentation on Eurosystem Monetary Policy Instruments and Procedures, the Monthly Bulletin (the March, June, September and

December editions, as well as the special edition dedicated to the 10th anniversary since the establishment of the ECB), which can be referred to on the ECB's website, by accessing the publication page.

The NBR publishes in Romanian on its internet page the quarterly editions and editorials of the ECB Monthly Bulletin.

Public Information Activity

In 2008, the NBR continued to meet a large number of information requests submitted based on Law No. 544/2001 on the free access to public interest information and on Government Ordinance No. 27/2002 on the regulation of petition settlement, approved by Law No. 233/2002.

During 2008, public interest information requests submitted to the National Bank of Romania amounted to 10,046, i.e. 39 requests per business day on average, including a total number of roughly 12,240 information requests.

The most frequent information requests referred to the following issues:

- the exchange rate of the leu against various currencies;
- developments in different interest rates (the NBR reference rate, the monetary policy rate, average lending/deposit rates applied by credit institutions);
- updates on amounts of money;
- statistical data published by the NBR;
- pieces of legislation adopted by the NBR and their interpretations;
- clarification in the field of foreign currency operations and payments in foreign currency;
- information on prices of precious metals;
- information on the activity of Deposit Guarantee Fund in the Banking System;
- the manner of applying the provisions of Law No. 348/2004 on the redenomination of domestic currency;
- asking for information from the Central Credit Register;
- the documents necessary in Court for recovering some precious metal objects.

Also, written answers were given in response to the denunciation of some credit institutions and non-bank financial institutions, the activities of which are subject to the NBR regulation, authorisation and prudential supervision.

The National Bank of Romania ensures transparency and access to public interest information via its website (www.bnro.ro), press releases, answers to written requests (sent by post mail, e-mail, fax) or over the phone, as well as through its Information-Documentation Point operating within the NBR headquarters.

Preparation of “The Cultural Days of the ECB – Romania 2009” event

In an effort to prove social responsibility and show visibility, in 2008, the NBR cooperated with the European Central Bank, as well as with the other central banks of European Union Member States with a view to organising “The Cultural Days of the European Central Bank – EU 2008” event. Each year, the ECB holds in Frankfurt “The Cultural Days of the ECB” event in order to present and promote the cultural richness of EU Member States.

The NBR continues to cooperate with the ECB in 2009 as well, when the cultural events to be held in Frankfurt during 21 October – 9 November 2009 are dedicated to the Romanian culture. “The Cultural Days of the ECB – Romania 2009” event, which will be carried out under the high patronage of the President of the ECB and the NBR Governor, is an excellent opportunity for promoting national values in the European context and the Romanian culture and spirituality as part of the universal consciousness.

A partnership agreement was completed between the European Central Bank, in its capacity as general coordinator of the project, and the National Bank of Romania with a view to ensuring the smooth unfolding of the event. The agreement includes the technical details on the concept, structure, stages of the project, in line with the format used by the European Central Bank during the six editions dedicated to promoting particular countries with great cultural diversity (2003 – Portugal, 2004 – Poland, 2005 – Hungary, 2006 – Austria, 2007 – Greece and 2008 – the European Union). This partnership is aimed at identifying an optimal combination between the philosophy of the event and the specificity of national values, in the spirit of the European Union’s *motto* “Unity in Diversity”.

Chapter 10. Macroeconomic research activity

Macroeconomic research activity within the National Bank of Romania focuses on applicative issues that play a major part in the substantiation of the decision-making process. In 2008, the priorities on the agenda included monetary analysis, macroeconomic modelling, financial stability and real-sector developments. According to the organisational structure, the departments conducting economic research activities are: the Economics Department, Monetary Policy and Macroeconomic Modelling Department, and the Financial Stability Department.

1. Macroeconomic modelling

Macroeconomic modelling activity within the National Bank of Romania is mainly aimed at providing support to monetary policy decisions. Given that macroeconomic forecasts play a major part in the inflation targeting framework, several projects were directly related to developing the model for analysis and medium-term forecasting of inflation (MAMTF). In this vein, the key priority consisted in developing and implementing satellite models for forecasting aggregate demand components, their deflators, as well as the main blocks within the balance-of-payments current account. Once developed, the models were estimated / calibrated, while their forecasting performance was tested by conducting in-sample projections (over different historical periods). Satellite forecasting models for GDP components are currently part of the quarterly projection exercise carried out by the National Bank of Romania.

The core MAMTF was also significantly improved during 2008, by redefining some of its equations (including the estimation/recalibration of relevant parameters) and/or including new ones. One of the changes consisted in explicitly modelling the impact of Romania's trade flows with major foreign partners, by integrating external demand for domestic products in the model itself. Furthermore, the first exploratory steps were taken towards the analytical modelling of financial market mechanisms, mainly as regards the impact of policy rate changes on money market rates and eventually – via specific operations conducted by financial institutions – on real economy.

Such reassessments of the models used are required on a regular basis so as to take on board any information provided by the latest economic developments. This is all the more valid in case of Romania, where the short available data series and frequent structural changes call for the regular revision of estimated or calibrated parameters.

New tools were implemented in 2008 to assess the forecasting activity carried out within the National Bank of Romania, the most noteworthy being those aimed at evaluating forecast errors of projection cycles August 2005 through December 2008. Such an assessment is useful in identifying the underlying reasons for the discrepancy between the projected and the actual values of different

macroeconomic variables. As part of this project, starting with its November 2008 issue, the Inflation Report depicts a synthetic assessment of forecast errors in the shape of an uncertainty interval built around the projected 12-month CPI inflation rate¹.

During the year under review, the NBR continued to participate with its own forecasts in the ECB's half-yearly coordination exercises for monetary policies within the European Union.

Along with the development of MAMTF, particular attention was given in 2008 to the project whose end goal is to implement a new DGE (Dynamic General Equilibrium) type macroeconomic forecasting and analysis model. The main concern was to finalise the specification of this model's theoretical structure, while also taking the first steps in calibrating and incorporating the key (empirically-identified) features of the Romanian economy.

2. Macroeconomic analyses and surveys

The objective of the central bank's liquidity management under the inflation targeting strategy is to keep short-term money market rates in line with the policy rate by resorting to the entire array of monetary policy instruments. Thus, depending on the central bank's position in its relation to credit institutions (creditor or debtor), particular importance is attached to monitoring the NBR's management of banking system liquidity and identifying the solutions for rendering this process more efficient.

The year under review saw a progressive reduction in structural excess liquidity in the banking system, with the NBR shifting in 2008 Q4 to creditor position vis-à-vis credit institutions. In anticipation of these developments, the central bank conducted successive analyses throughout 2008, aimed primarily at assessing the impact of the shift in the net position of banking system liquidity on the functioning of money market segments, on the configuration of the monetary policy operational framework as well as on the monetary transmission mechanism. Most of the outcomes of these assessments were made public in the presentation titled "Liquidity Management in the Banking System" delivered during the first edition of the NBR Monetary Policy Colloquia held on 17 April 2008.

Since developments in productivity stand out as a key element in assessing the current economic environment, a major research topic approached during 2008 consisted in the dynamics of labour productivity indicators and the ensuing macroeconomic consequences. After the thorough analysis conducted in 2007 on the dynamics of total factor productivity and labour productivity across manufacturing, the research activity in the reported year focused on assessing the simultaneous impact of wage and labour productivity dynamics on the inflation rate, by analysing the relationship between unit labour cost (ULC) developments

¹ See Section 1.4., *Risks associated with the projection*, in the *Inflation outlook* chapter for further details.

and the evolution of certain price indices, namely the industrial producer price index (IPPI) and CORE2 inflation.

Thus, a causal relation was identified between ULC dynamics across manufacturing and IPPI developments, on one hand, and between ULC dynamics economy-wide and developments in adjusted CORE2 inflation, on the other. Furthermore, the analysis revealed that, although the short-term influence of ULC dynamics on the inflation rate is subdued, pay rises in excess of productivity gains generate longer-term inflationary pressures. This analysis was presented to the public on 17 April 2008, during the first edition of the NBR Monetary Policy Colloquia.

3. Financial stability

The main research topics approached during 2008 in the field of financial stability were as follows:

a) Analysis of external risks on financial stability. The paper investigated: (i) the contagion risk via the external channel and the potential spill-over effects on the domestic economy and financial system and (ii) the real sector's ability to cope with a currency shock and an external liquidity shock. Contagion channels are: (i) from developed countries through parent banks and (ii) from emerging countries via investors' risk aversion to CEE markets. The domestic forex market is fraught with volatility, being subject to shifts in investor sentiment. Hence, exchange rate developments might feel the pinch of the turmoil more visibly than other countries in the region. As regards the adjustment of the current account deficit, the authors concluded that it would most likely be achieved based on a mixed scenario, including both domestic demand corrections and a weaker domestic currency. The importing companies' sector is better positioned to face an average exchange rate shock, whereas companies having incurred short-term external debt and not engaged in foreign trade are much more vulnerable.

b) Analysis on the effects of a possible external liquidity shock on domestic credit institutions and non-financial corporations. The aim of the study was to analyse different scenarios in which financing lines to Romanian companies and banks would no longer be renewed in various proportions. The stress-test analysis on external liquidity identified the economic sectors and the credit institutions that would bear the brunt of liquidity risk materialising. It also revealed the actual volume of domestic companies' newly-incurred external arrears, the new default rate level in the banking sector as well as the capitalisation needs for ailing banks. The paper also set forth several measures to mitigate the effects of a potential external liquidity shock.

c) Improving the early warning model vis-à-vis currency crises. This is one of the tools employed in monitoring risks to financial stability and it was improved primarily by correcting the bias in estimating the currency crisis probability in line

with the method proposed by King and Zeng (2001)². The correction was required due to the small number of pre-crisis periods, as the unconditional probability of the sample stood at a mere 5 percent.

d) Household sector analysis in terms of financial and macroeconomic stability. The paper highlighted the challenges to financial stability generated by developments in households' net wealth in terms of credit, market and liquidity risks. From a macroeconomic perspective, the analysis focused on the correlation between consumer credit and the trade balance, on one hand, and between trade deficit and changes in consumer prices, on the other. The paper laid down several actions, such as: (i) supplementing the data collected via the Central Credit Register with information concerning the value of debtors' collateral and the disposable income of indebted households as well as identifying any off-balance-sheet loans and (ii) amending Regulation No. 11/2008 on limiting credit risk associated with loans to households, for an enhanced shock management by banks.

e) Operational risks in ReGIS – a system of systemic importance. The first financial stability analysis in the field of payments, focusing on systemically-important components of the domestic payments system, revealed that ReGIS is solid and stable, capable of absorbing liquidity shocks of average intensity. Moreover, its functioning has not been affected by the liquidity crunch generated by the global turmoil. The analysis was conducted with the help of the Payment and Settlement System Simulator developed by the Bank of Finland (BoF PSS2), a tool appreciated by central banks worldwide for the possibility to construct “reproduction” models of the real operating environment. These models can be used for scenario testing and observation with a view to determining the shock absorption capacity.

f) Developing the stress-test analysis aimed at identifying the domestic banking system's vulnerabilities to shocks amid exceptional, yet plausible events. In cooperation with IMF experts, during the FSAP mission of November 2008, the National Bank of Romania enhanced the stress test application by including in the analysis a set of bridge equations that shape the connections between macroeconomic variables and companies' balance sheet items. This development stands out as a key element of the analysis shaping credit risk pertaining to the real sector. The banking sector faces this risk via the indirect effect induced by the worsening of macroeconomic conditions (economic growth, exchange rate of the domestic currency, interest rate changes regardless of denomination) on the quality of the credit portfolio. The recapitalisation cost for several banks in the system was determined based on the outcome of the latest running of this application.

g) Analysis on the interbank contamination risk in the domestic banking system. The methodology aims at assessing the impact of unexpected insolvencies on the stability of the Romanian banking system. The process has an iterative nature, as

² King Gary and Langche Zeng – *Logistic Regression in Rare Events Data*, Society for Political Methodology, Harvard University, 2001.

the number of steps is determined by the actual stage in which no new cases of insolvency are recorded for previously-solvent banks.

Designed as a complementary tool to the bank stress test, the methodology of the interbank contamination test has a distinctly conservative character, as highlighted by the following working assumptions: 1) there are no clearing agreements between credit institutions; 2) no provisioning for interbank losses; 3) no adjustments in relation to interbank exposures of banks that become insolvent. Three other hypotheses – not necessarily conservative in nature – were taken into consideration, namely: 4) interbank losses are allotted on a proportionate basis, in line with the weight of the exposure to the insolvent bank in the latter's total interbank liabilities; 5) the occurrence of insolvencies is exclusively due to a factor that is peculiar to the concerned credit institution; 6) any shifts in depositor behaviour, likely to trigger disproportionate market reactions in relation to solvent credit institutions, as a result of ailing banks' default (the banking panic phenomenon), are excluded.

From a methodological point of view, identifying credit institutions likely to set off a bankruptcy chain reaction and quantifying the potential severity of such interbank contamination phenomena imply: a) simulating the initial shock; b) calculating the interbank loss allocation matrix; c) identifying insolvency events.

Testing the interbank contamination process assumed the iterative default of a single bank, of two or three banks simultaneously.

The conclusion of the analysis reveals a low systemic risk, as bilateral interbank exposures are generally subdued by comparison to the own funds and liquid assets of banks holding a creditor position.

4. Conferences organised by the NBR

On 17 April 2008, the National Bank of Romania organised the first edition of the Monetary Policy Colloquia, whose central theme was "Monetary Policy: Developments and Challenges". The event was attended by specialists from the central bank, the Ministry of Economy and Finance and commercial banks, as well as numerous representatives of the domestic academia. The following topics were discussed during the seminar: monetary policy and the new global economic environment; monetary policy – art and rules; macroeconomic volatility and the symptoms of turmoil that might emerge in the economic area; liquidity management in the banking system; labour productivity and its impact on inflation and exchange rate.

During 18-19 September 2008, the National Bank of Romania in cooperation with the International Monetary Fund organised in Sinaia the annual regional financial stability seminar. The event was attended by representatives of the central banks in Bosnia and Herzegovina, Bulgaria, Croatia, Greece, Hungary, Kazakhstan, Macedonia, Moldova, Montenegro, Poland, Turkey, and Ukraine. IMF experts were joined by economists from the Italian, Austrian and Swedish central banks as

well as from the ECB. Participants also included specialists from competent Romanian institutions, namely the NBR, the Ministry of Economy and Finance, the Deposit Guarantee Fund in the Banking System, the Insurance Supervisory Commission, the Private Pension Scheme Supervisory Commission as well as representatives from the Romanian Banking Institute. The seminar was aimed at providing participants with information on the latest trends and developments in the field of financial stability, while also facilitating the exchange of experience in practical issues. The event consisted of two theme sessions – households and the private sector and their role in maintaining financial stability – with a focus on central banks' tools for monitoring these sectors and the financial stability risks generated by households and the private sector.

Also in 2008 the National Bank of Romania hosted a series of conferences attended – alongside NBR Board members and central bank specialists – by representatives of the banking community in Romania, of the academic world and specialised institutes, economic analysts, MEF and NSC representatives, officials from the Insurance Supervisory Commission and the Private Pension Scheme Supervisory Commission, as well as media representatives:

- the conference titled “The Euro: 10 years soon. Facts. Lessons. Prospects”, held by Mr. Guy Quaden, Governor of Nationale Bank van België/Banque Nationale de Belgique, on 12 May 2008;
- the conference titled “Risk in Performance Measurement”, held by Sir Andrew Likierman, Professor at the London Business School, on 26 May 2008;
- the conference titled “Issues Related to U.S. Economy and Economic Policies”, held on 5 June 2008 by Mr. Marc-Olivier Strauss-Kahn, Banque de France visiting senior advisor to the Federal Reserve;
- the conference “How is the World Different after the Financial Turmoil”, held on 12 December 2008, on which occasion presentations were delivered by Mr. Maxwell Watson, fellow at Wolfson College, Oxford, Mr. Gikas Hardouvelis, Head of the Economic Office of the Greek Prime Minister and Professor at Piraeus University, as well as Mr. Patrick McGuire, BIS senior economist.

5. Guidelines and objectives of research activity in 2009

The year 2009 will further see the drafting of studies and analyses meant to support the decision-making process in the NBR by supplying a wider range of relevant information.

Over the medium and long term, the focal point of macroeconomic research within the NBR is to implement the dynamic general equilibrium (DGE) model for the Romanian economy. The first steps towards achieving alternative macroeconomic projections by using this particular model (instead of the MAMTF) are expected to be completed in 2009.

Another topic of major interest during the period under review consists of research projects subordinated to the objective of enhancing MAMTF properties. To this end, the year 2009 will see either the launch or the completion of projects aimed at identifying alternative specifications for shaping the dynamics of the risk premium associated with foreign investor placements in leu-denominated financial assets, extending the scope of procedures employed for assessing the potential growth rate of economic activity or the analytic shaping of the monetary policy transmission mechanism in the central bank – money market – commercial banks – real economy sequence.

Particular attention will be paid to conducting an analysis regarding the transmission of changes in industrial producer prices onto consumer price shifts. Identifying a link between the two is all the more important that, 2002 through 2008, Romania has steadily witnessed significant positive gaps between the annual growth rate of industrial producer prices for the domestic market and the annual dynamics of consumer prices.

As regards financial stability research, the assessment will focus on the impact of the decision to raise the deposit coverage level (as stipulated in European regulations, i.e. Directive 2009/14/EC) on participant credit institutions in the Deposit Guarantee Fund in the Banking System. The paper will be aimed at: (i) analysing the distribution of deposits in the banking system; (ii) calculating the degree of concentration of deposits; (iii) identifying any major risks that might emerge in an environment of instability; (iv) evaluating, based on extreme scenarios, credit institutions likely to be vulnerable to outflows via withdrawals during a crisis; (v) describing the domestic framework regulating the Guarantee Fund and the actions taken by the European Commission to harmonise legislation at European level, as well as (vi) assessing the impact on credit institutions as a result of raising the minimum coverage level for household and corporate deposits to the RON equivalent of EUR 50,000 starting 1 July 2009. The analysis will also set forth proposals on increasing the Fund's resources as well as reducing the time limit for the verification of claims and the payout delay.

Chapter 11. Other activities of the National Bank of Romania

1. Human resources management

In 2008, human resources management was aimed at improving the issues related to the institutional and organisational architecture of the National Bank of Romania, as well as to the adoption and transposition of the European System of Central Banks' common values as regards human resources strategies, in compliance with the value system and traditions governing the organisational culture of the National Bank of Romania.

Changes in the organisation chart

An operational organisation structure is a key factor for the activity conducted by the National Bank of Romania. In terms of flexibility, the organisation structure developed further, matching the objectives pursued by the central bank. In this context, the merging of the Monetary Policy Department and the Macroeconomic Modelling and Forecasting Department was completed in the first part of 2008. This process was required by the improvement in activities regarding the laying-out, designing, formulation and release of monetary policy measures.

Based on a previous decision concerning the setting-up of a coordination unit for the training and social activity centres, a technical team for the unitary assessment and coordination of their activity was established. The newly defined coordination unit became operational since March and its main task was to ensure the technical and administrative conditions necessary for the in-house training courses of the NBR staff.

Furthermore, the Communication Department was set up and its duties established in the context of external communication and transparency strategies, drawn up in compliance with the accountability requirements for a central bank.

The endowment of the territorial cash centres with state-of-the-art and complex technology required their coordination via a specialised division, which was set up within the Issue, Treasury and Cash Management Department and whose objective was to focus on getting uniform and comparable results and performance. This division became operational on 1 September 2008 by taking over the tasks and employees from the Bucharest branch and by developing new duties concerning the technological, methodological and logistics coordination of cash centres' activity.

Promotion and granting of incentives

The common values of the European System of Central Banks (competence, efficacy and effectiveness, integrity, team spirit, communication, transparency and accountability) were further incorporated in the human resources strategies implemented by the National Bank of Romania in order to transpose them into the daily activity and behaviour of employees and assess them via the instruments specific to human resources activity (for instance, the activity assessment, selection and secondment procedures, education and professional training). A strategic issue for stimulating staff was to foster the internal mobility as a competitive factor in the professional career of employees, which materialised in 54 employees shifting their position inside the NBR.

Moreover, 88 employees were promoted to top executive positions and 18 employees advanced to managerial ranks in 2008.

Recruitment and selection

The regulation of recruitment and selection ever since 2007 implied the drawing-up of the necessary legal framework for the standardisation of applied procedures and, implicitly, of general and special conditions required for applicants. Considering both the features of specific activity fields in the National Bank of Romania and its own criteria, the objective was to hire adequately skilled staff or persons showing a real professional development potential. The transfer of activities from one structure to another or the setting-up of new departments underlined the shift in focus to a larger extent to staff recruitment and selection from within the central bank's employees.

In the context of increased competition on the labour market, particularly in early 2008, the central bank organised 38 examinations at its head office and 46 examinations at its branches and hired 103 people (58 at the NBR head office and 45 at the NBR branches). It is also worth mentioning that, in 2008, 89 employees were no longer on the bank's payrolls (54 at the NBR head office and 35 at the NBR branches). Hence, in 2008, the staff turnover rate in the National Bank of Romania stood at 5.2 percent, according to the records on the number of employees.

Staff professional training

In 2008, 747 employees (44 percent of the NBR staff) attended training courses. Out of the total number, 543 employees attended local training courses, 106 participated in foreign courses, and 98 attended both local and foreign courses.

In line with the actions concerning the transformation of the Romanian Banking Institute into the main supplier of training courses to the NBR staff, 2008 saw an increased cooperation with this institution. Hence, nearly 45 percent of total employees participating in training courses organised by institutions countrywide attended courses at the Romanian Banking Institute, particularly IT courses (with the granting of ECDL licence) and English and French language courses.

In line with the special programme for branches, their staff benefited from local training courses, mainly foreign language courses (123 employees) and ECDL courses (61 employees).

The professional training and social activity centres hosted mostly in-house courses and seminars on different topics, such as *Banca Națională a României – istorie, valori, perspective* (The National Bank of Romania – history, values, perspectives); *Aspecte practice privind implementarea standardelor internaționale în domeniul combaterii spălării banilor și finanțării terorismului* (Practical issues regarding the implementation of international standards in the field of money laundering and terrorist financing prevention); *Relații publice și comunicare* (Public relations and communication); *Conturi financiare* (Financial accounts); *Cercetarea statistică directă* (Direct statistical research); *Managementul numerarului* (Cash management); *Audit intern* (Internal audit) etc.

The same as in previous years, one of the main objectives was to have the young employees selected by a special commission participate in professional training activities; those young employees should be aged up to 35 years and be able to represent the NBR in the ECB and ESCB committees and subcommittees.

2. Statistical activity

In line with the ECB and Eurostat requirements, 2008 saw the continuation of statistical activities regarding the external sector (balance of payments statistics, survey on foreign direct investment), monetary statistics (statistics on the balance sheet of monetary financial institutions and statistics on interest rates applied by credit institutions to households and non-financial companies) and the statistics on national financial accounts (annual financial accounts of institutional sectors and quarterly financial accounts of general government).

Moreover, new statistics were developed, in order to provide additional data regarding the Romanian financial system and meet the requirement for aligning the NBR statistics to the EU standards, with a view to supporting Romania's entry into the euro zone.

Statistical reporting of balance sheet assets and liabilities of non-bank financial institutions

As of 1 January 2008, NBR Norms No. 12/2007 on the statistical reporting of assets and liabilities of non-bank financial institutions came into force. According to these Norms, non-bank financial institutions enrolled in the General Register opened with the National Bank of Romania must report statistical data on balance sheet assets and liabilities on a quarterly basis starting with 2008 Q1. The Norms use the ESA95 methodology regarding the breakdown of institutional units by sector and the classification of assets and liabilities, which was incorporated by the National Bank of Romania in all regulations on monetary and financial statistics. The collected data are compiled and used in the analysis of the lending activity carried out by financial institutions in Romania, as well as in the preparation of

national financial accounts. A number of 32 aggregate indicators are reported on a quarterly basis to the European Central Bank, as part of the NBR obligations within the European System of Central Banks.

Statistical reporting of balance sheet assets and liabilities of investment funds

With a view to implementing the EU regulations on statistics, the National Bank of Romania drafted the Methodology for statistical reporting based on EC Regulation No. 958/2007 of the European Central Bank of 27 July 2007 concerning statistics on the assets and liabilities of investment funds (ECB/2007/8), whereby the investment management companies and self-managed investment companies are required to report, on a monthly basis, statistical data on the balance sheet assets and liabilities of resident investment funds they manage starting with December 2008. The classification of balance sheet assets and liabilities, as well as that of the contract parties of financial instruments are based on ESA95 methodology.

The investment management companies and the self-managed investment companies report monthly data on balance sheet assets and liabilities of resident investment funds they manage, broken down by initial maturity, home country and institutional sector of the counterparty, and the currency of denomination. Furthermore, these companies report, on a monthly basis, the revaluation adjustments due to changes in prices for financial instruments in the balance sheet of investment funds, the sales and repurchases of unit funds of investment funds and the ISIN securities in the portfolio of investment funds. Data compiled nationwide are used by the National Bank of Romania for the laying out of monetary and financial stability policies, as well as for the preparation of financial accounts. In addition, the National Bank of Romania reports to the European Central Bank on a monthly basis as part of its obligations within the European System of Central Banks.

3. Information technology

In 2008, the IT activity was aimed at meeting the objectives formulated by way of the computerisation strategy approved by the NBR Board in 2002.

An important step was to continue to develop the IT system for reporting to the NBR (SIRBNR), which simplifies the collection of primary indicators from reporters, enabling the modern, consistent and efficient data collection. Thus, throughout the year, 15 new reports were registered with the system, out of which 6 financial and prudential reports consistent with FINREP and COREP standards. Moreover, the Consolidated Banking Data (CBD) report was drafted and used in an annual report submitted to the European Central Bank.

In order to support the diversification of reporters, for the purpose of improving the analysis capacity of macroeconomic processes, a software for the collection of statistical data on balance sheet assets and liabilities of non-bank financial institutions was created. The respective data are received by secured e-mail from

250 non-bank financial institutions entered into the General Register. Subsequently, data are validated, processed and compiled in order to fulfil the reporting obligations to the European Central Bank and prepare the national financial accounts. In addition, a software was implemented in order to support the validation, processing and reporting to the European Central Bank of statistical data on balance sheet assets and liabilities of resident investment funds, reported by investment management companies of these funds and self-managed investment companies.

With a view to counteracting the expansion of IT criminality, a secured portal for security incidents was set up. The system is operational based on the technological platform developed, made available and managed by the National Bank of Romania, its contents being directly monitored by the Romanian Banking Association. The purpose of this portal is to establish a mutual warning and prevention system for the possible IT security incidents, being created exclusively for persons responsible with IT security in banks. Moreover, the National Bank of Romania intends to host a Response Centre for IT Security Incidents, which will be managed in association with a group of IT security information experts from banks, members of the Romanian Banking Association.

Year 2008 saw the ongoing virtualisation of part of server fleet and consolidation of storage space, aimed at ensuring the more efficient use of the available calculation capacity, the easier management of operational IT systems, as well as the creation of conditions for faster solving IT incidents and increasing stored data security.

Moreover, in 2008, the connection of NBR users to the available IT applications and services within the secured communication network of the European System of Central Banks continued, in line with the schedule agreed upon with the European Central Bank.

4. Internal audit

In 2008, the Internal Audit Department performed 30 audit missions, out of which 26 missions were included in its annual plan and 4 missions were carried out at the request of the Board or some other organisation structure of the bank. The same as in prior years, the 2008 audit plan was drawn up based on the systematic assessment of risks associated with the central bank's activities.

Out of the total audit missions performed, 26 missions focused on assessing the efficiency and effectiveness of the internal control system and the risk management of the activity subject to auditing. As concerns the additional audit missions, two focused on the advisory input and their gradual objectives were established by common agreement with the beneficiary of the audit mission, whilst two examinations were carried out at the request of the executive management of the central bank.

Apart from the above-mentioned commitments, according to its Statute, internal audit also implied advisory inputs: (i) formulation upon request of opinions and viewpoints as concerns several draft pieces of legislation initiated by different bank departments; (ii) advise teams responsible with the implementation of some development projects, as concerns risk management and internal control (NBR website); (iii) participation in debates on some important regulation projects in order to provide advisory input in terms of control and risk management; (iv) support in implementing some recommendations of internal audit missions or complex corrective measures, by organising multi-departmental working meetings.

In line with the Standards for Professional Practice of Internal Audit issued by the Institute of Internal Auditors – IIA, the first external audit mission of the NBR internal audit was carried out by Deloitte Audit SRL in 2008. Following the assessment, the internal audit of the NBR was classified as being generally consistent¹ with the Professional Practice Standards and the IIA Ethics Code. Moreover, the external auditor formulated several recommendations in order to improve performance as regards staff training, the annual and multiannual schedule of internal audit missions or develop the methods for testing/analysing data and information during on-site examinations.

During 2008, methodological development activities were also performed, the most important being that of revising the internal control framework of the central bank, in line with developments at domestic and international level.

5. Legal activity

In 2008, the Legal Department was instrumental in endorsing 142 draft pieces of legislation initiated by the central bank (98 external and 44 internal pieces of legislation), as well as 12 draft pieces of legislation governing financial and banking matters which were initiated and submitted for review to the NBR by other institutions.

In order to extend the international financial relations of the National Bank of Romania, 3 draft international arrangements were analysed and endorsed from a legal standpoint.

Due to its co-operation with the Legal Committee in the European Central Bank, the Legal Department is responsible, based on NBR Regulation No. 4/2007 on the participation of the NBR representatives in the ESCB committees, for the initiation of written procedure on draft pieces of legislation of the NBR, the object of which falls within the ECB scope of competence.

Legal advisors participated in the Legal Committee meeting where legal issues were discussed concerning Romania's failing to consult the ECB as regards the draft law for approving Government Emergency Ordinance No.90/2008 on the

¹ On a three-level scale: general conformity, partial conformity, non-conformity.

statutory audit of annual accounts and consolidated accounts, a legal act transposing the provisions of Directive 2006/43/EC on statutory audits of annual accounts and consolidated accounts.

In 2008, also due to its cooperation with the Legal Committee, the Legal Department participated in the FLEX (Financial Law Experts) working sub-group meeting, in extended composition, where legal aspects related to TARGET 2 SECURITIES – securities clearing and settlement system were discussed, as well as in the Payment Services Directive Transposition Group meeting, where legal aspects concerning the implementation of the provisions of Directive 2007/64/EC on payment services in the internal market within the ESCB were debated.

Moreover, the Legal Department participated in the legislative section of the meeting of the editorial group established within the ECB in order to prepare the 2008 Convergence Report.

Additionally, the NBR representatives participated in the meetings of the Eurosystem Procurement Coordination Office (EPCO) whose main tasks are to facilitate the adoption of the best procurement practices within the Eurosystem, develop the infrastructure required for joint procurement, identify the potential cases for joint procurement for the national central banks in the Eurosystem and prepare the annual procurement plans for joint tender procedures.

In 2008, observations and proposals were formulated with regard to the following draft pieces of legislation submitted to the NBR for review: Law on payment services, Law amending and supplementing Government Emergency Ordinance No. 99/2006 on credit institutions and capital adequacy, Law amending Law No. 312/2004 on the Statute of the National Bank of Romania, Law amending Law No. 206/2005 on the imposition of some international sanctions, Law on the organisation and operation of official statistics in Romania, Law No. 93/2009 on non-bank financial institutions, Law on the statutory audit (as regards the adoption of Government Emergency Ordinance No. 90/2008 on the statutory audit of annual accounts and consolidated accounts), Law amending Art. 5 of Government Emergency Ordinance No. 39/1996 on the establishment and operation of Bank Deposit Guarantee Fund, Law amending and supplementing Law No. 411/2004 on privately managed pension funds, Government Emergency Ordinance amending Law No. 571/2003 on Tax Code, Government Emergency Ordinance No. 5/2009 on the establishment of Credit Agency for Students in Public and Private Universities Eligible for Educational Accreditation.

Furthermore, legal advisors endorsed 414 notes and draft orders on the implementation of sanctions and measures against some authorised entities, drawn up by the specialised departments in the NBR's head office. The Legal Department also endorsed 749 draft responses prepared by the specialised departments in the NBR's head office for the requests formulated particularly by the Ministry of Administration and Interior and the Ministry of Economy and Finance. In addition, at the request of the specialised departments in the NBR's head office, legal advisors formulated 23 legal opinions on one-off issues.

At the request of credit institutions, the Legal Department formulated 19 legal opinions on the implementation or legal interpretations of regulations issued by the National Bank of Romania. The Legal Department prepared draft responses to 33 petitions and 37 papers submitted to the central bank by different legal entities and public institutions and represented the central bank before the Court of Law in 234 cases (168 civil cases, 41 commercial cases, 6 contentious, administrative and fiscal cases, 15 garnishment cases and 4 bankruptcy cases). Legal advisors defended the National Bank of Romania, having 843 court appearances.

In 2008, the Legal Department reviewed and endorsed 64 documents related to requests for forced sale by way of garnishment and 58 restitution requests formulated by natural persons concerning the restitutions of precious metal objects, based on the provisions of Government Emergency Ordinance No. 190/2000 on the regime of precious metals, alloys and precious stones in Romania, as subsequently amended and supplemented.

The Legal Department also endorsed contracts and additional notes to contracts, as well as notes issued by the specialised departments in the NBR's head office and the Governor's orders, in order to observe the legal proceedings necessary for the NBR to conclude contracts.

6. NBR Archives, Museum and Library

In 2008, the activity of the General Archives and Museum of the NBR focused on the preservation and processing of documents, the turning to account of the archives and collections of the NBR Museum.

The preservation and processing of the documents materialised in:

- the continuation of the programme for electronic and analogical filing of the documents in the historical archives of the NBR by initiating organisation procedures of a new auction in order to select a new operator with a view to scanning and microfilming all the documents in the Archives “The Minutes of the NBR Boards”;
- the taking over of documents from NBR departments;
- the inventorying of the document stocks in the NBR Archives (circulars issued by the NBR management during 1945-1950 and the organisation fund 1941-1954).

The turning to account of the documents in the General Archives and of the collections in the NBR Museum materialised in a series of actions dedicated to issues related to economic, financial and banking history and numismatics research, the most representative being the following:

- documentation activities in places where the NBR had branches and agencies during the inter-war period (Southern Dobrudgea, Bucovina and Bessarabia) in order to identify the former offices of the central bank, for

- the purpose of corroborating with information in the NBR Archives necessary for the compilation of a complete history of the NBR;
- annual session of papers and presentations on issues relative to banking history entitled “The NBR branches in the inter-war period: Bucovina, Bessarabia, Southern Dobrudgea” (December 2008);
 - summer schools organised by the European Association of Banking and Financial History in Athens and Venice and the conferences organised by prestigious universities and research institutions in Romania (the Bucharest Academy of Economic Studies, Babeş-Bolyai University in Cluj-Napoca, the National Institute for the Study of Totalitarianism, the National Archives of Romania, the National Numismatics Society, etc);
 - providing advisory input to Romanian and foreign researchers who documented in order to prepare some studies – *Sistemul bancar din România de la sfârşitul secolului XIX şi începutul secolului XX* (The Romanian banking system in late 19th century and early 20th century), *Biografia guvernatorului Dimitrie Burillianu* (The biography of Governor Dimitrie Burillianu), *Cooperarea economică în cadrul Micii Înţelegeri* (The economic cooperation in the context of the Little Entente), *Europa Centrală în cadrul rivalităţilor politico-financiare dintre Franţa şi Marea Britanie (1919-1939) – exemplul României* (The Central Europe in the context of political and financial tensions between France and the United Kingdom (1919-1939) – Romania’s case), *Datoria externă a României după al Doilea Război Mondial* (Romania’s external debt in the aftermath of World War II);
 - participation in the working group representing the NBR in the South-Eastern Europe Monetary History Network, whose objective is to create some historical and statistical databases on exchange rates, volume of currency circulation, discount rate, international reserves during 1881-1914; statistical series were presented during meetings organised by the central banks of Bulgaria, Greece and Austria, under the auspices of which the papers were also published;
 - preparation of the second volume of The history of the National Bank of Romania in figures (1915-1918), a paper turning to account new documents and illustrations in the NBR Archives, containing four chapters dealing with numerous aspects of the central bank’s activity during the neutrality years and then after Romania’s participation in World War I.

In 2008, the Commission for procurements and increase in assets of the NBR’s Museum identified and purchased 391 artefacts: Dacian, Greek, Roman, Byzantine and Romanian coins, tokens, banknotes, assignats, emergency money, shares, picture postcards etc., particularly those pieces illustrating the history of currency circulation in Romania, the history of the NBR and the banking system in Romania.

In 2008, the employees of the General Archives and Museum of the NBR participated in the activity conducted by the Commission for the analysis of the

annual programme, as well as by the Commission for preparing and approving the booklets of numismatic issues and contributed to the papers presented on the occasion of the Cristian Popișteanu symposium on banking history and civilisation, with the title “In the service of the banking system – people and facts”.

In 2008, the activity of the NBR Library was marked by the completion of the new office and implicitly by the reorganisation and inventorying of the whole book stock. The new office of the NBR Library, which was entirely restored, is located at the ground floor of the Old Palace in Lipscani street and ensures optimal conditions for consulting the whole book stock in a reading room with a capacity of 20 seats.

Due to its status as a specialised library, the NBR Library supports the research activity, as well as other activities carried out within the institution. In order to support the readers, three types of regular publications are prepared: (i) Information Bulletin – theme selection of main economic, financial and banking articles in the Romanian press; (ii) Documentation Bulletin – economic and financial studies and articles from foreign publications; (iii) Bibliographic Bulletin – new acquisitions of the NBR Library. In 2008, the number of readers registered with the NBR Library totalled 481.

The collection of the NBR Library continued to improve via: (i) the systematic purchases of Romanian and foreign books and (ii) donations received throughout the year. The book stock includes a wide range of Romanian and foreign documents, such as treaties, monographic papers, manuals, courses, encyclopaedias, dictionaries, annual reports, magazines and papers.

The book stock of the NBR Library comprises not only economic and financial volumes, but also books from other fields, such as history and economic history, law, IT – the new collections being compiled at the request of the readers.

Chapter 12. Financial statements of the National Bank of Romania as at 31 December 2008

1. Overview

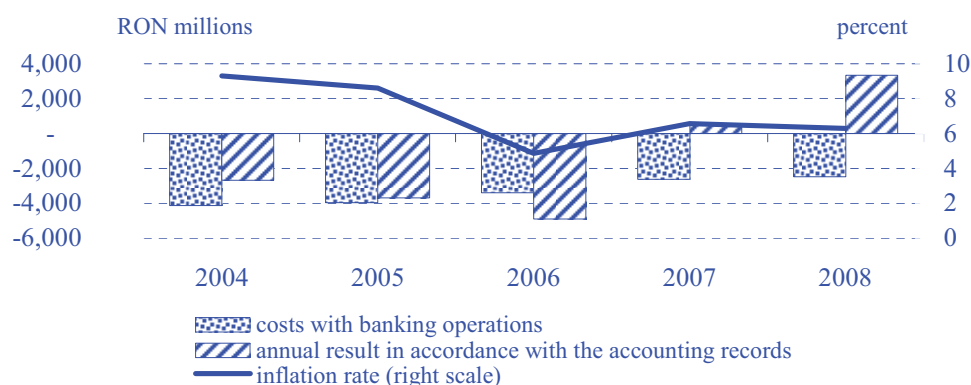
According to Law No. 312/2004 on the Statute of the National Bank of Romania, the primary objective of the central bank is to ensure and maintain price stability.

The National Bank of Romania, abiding by the provisions of the *acquis communautaire*, does not focus on attaining concomitantly business-related objectives, such as maximisation of return, but rather on limiting its operating costs.

According to Law No. 312/2004 on the Statute of the National Bank of Romania, starting with financial 2005, the NBR has been applying the International Accounting Standards used by the central banks, which are acknowledged by the European Central Bank, for which it issued its own norms based on EU regulations (for 2005 and 2006: Guideline ECB/2002/10¹; for 2007: Guideline ECB/2006/16²; for 2008: Guidelines ECB/2006/16 and ECB/2008/21³).

The National Bank of Romania achieved its primary objective by curbing the annual inflation rate in 2004-2008 (from 9.3 percent in 2004 to 6.3 percent in 2008) amid the efficient management of public resources at its disposal.

Developments in NBR's Costs with Banking Operations - inflation-adjusted data as at 31/12/2008 -



¹ OJ L 58, 03.03.2003, p. 1

² OJ L 348, 11.12.06, p. 1

³ OJ L 36, 05.02.09, p. 1

The NBR's financial results as at 31 December 2008 showed a profit in amount of RON 3,338,305 thousand – seven times higher than the 2007 profit of RON 458,463 thousand, mainly on the back of the following:

- the 2008 operating profit equalling RON 4,078,802 thousand – three times higher than the 2007 figure of RON 1,375,745 thousand – as a result of the 68 percent increase in income (RON 2,781,713 thousand) and the mere 3 percent rise in operating costs (RON 78,655 thousand);
- expenses from unfavourable revaluation differences associated with net assets in foreign currency totalling RON 740,497 thousand as at 31 December 2008 stood 19 percent (RON 176,785 thousand) below the end-2007 figure.

The key factors that generated profit for the central bank in 2008 are as follows:

- the increase in profit from management of international reserves, following the rise in both average foreign currency reserves and return from the efficient management of international reserves;
- the decline in the loss arising from monetary policy operations, following the cut in costs associated with sterilisation operations as compared with prior years amid the decrease in excess liquidity and the rise in RON-denominated interest income. In fact, at end-2008, the central bank shifted from a net debtor position to a creditor position towards the banking system.

It is worth mentioning that the ratio of operating costs to total income continued to decrease from 6.5 percent in 2007 to 4.5 percent in 2008. Furthermore, the ratio of staff costs to total income dropped to 2.4 percent in 2008 from 3.5 percent in 2007.

Pursuant to the provisions of Art. 43, para.1, point b) of Law No. 312/2004 on the Statute of the National Bank of Romania, the profit corresponding to the 2008 financial year is fully distributed to cover the loss carried forward from the previous years, thus marking the ongoing recovery of 2005 and 2006 losses. This favourable development is attributable to the resumption of disinflation in the latter half of the year, the central bank further aiming at curbing inflation rate in a sustainable manner, which complies with its primary objective, namely to ensure and maintain price stability.

2. Recognition of monetary policy operations

Due to the gradual contraction of the structural excess liquidity, in the context of the current features of the national economy and amid the global economic crisis, the central bank had a creditor position towards the banking system at end-2008, which entailed a 7 percent decline in costs associated with sterilisation operations and a 12-time increase in RON-denominated interest income as compared with the prior year.

The central bank's position as a creditor towards the banking system as at 31 December 2008 was generated by the *net liquidity position in the banking system*⁴ in amount of RON 848,374 thousand. The value of this indicator reflects the net liquidity injection made by the central bank in the banking system.

The balance sheet as at 31 December 2008 (Table 1) highlights the following:

- foreign assets accounted for 97 percent of total assets;
- loans to credit institutions made up 1 percent of total assets;
- deposits the NBR took from credit institutions for the purpose of meeting its monetary policy objectives held 61.4 percent of total liabilities (61 percent – minimum required reserves of credit institutions and 0.4 percent – deposits taken from credit institutions);
- currency in circulation accounted for 24 percent of total liabilities;
- deposits of State Treasury with the NBR made up 1.2 percent of total liabilities.

**Table 1. Balance Sheet of the National Bank of Romania
as at 31 December 2008**

ASSETS	Average annual return -%-	LIABILITIES	Average annual interest rate -%-
Foreign assets 97%	5.78	Required reserves of credit institutions (18% in RON and 43% in foreign exchange)	RON: 3.55
		61%	foreign exchange: 1.62
		Deposits taken from credit institutions 0.4%	9.67
		Currency in circulation 24%	-
		Foreign liabilities 5%	2.59
Loans to credit institutions 1%	14.25	Deposits of State Treasury (in RON 0.01%, in foreign exchange 1.19%)	RON: 10.44
Other assets 2%	-	1.2%	foreign exchange: 1.75
		Capital, reserves a.s.o. 8.4%	-

As at 31 December 2008, some 64 percent of the NBR's foreign assets were financed from deposits taken from credit institutions by resorting to specific monetary policy instruments.

As shown in Table 1, an average annual return of 5.78 percent resulted from foreign asset management. In the case of most liabilities (sources of foreign assets), average annual interest rates (payable by the NBR) were lower than the average annual return on assets (receivable by the NBR), which entailed an operating profit in amount of RON 4,078,802 thousand in 2008, three times higher than the previous year's figure.

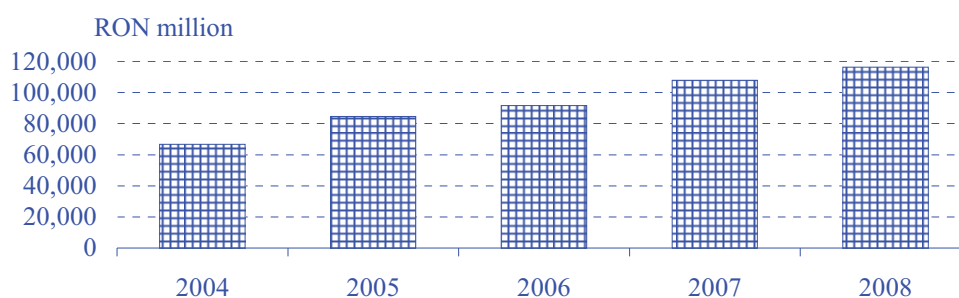
⁴ Computed as the difference between loans to credit institutions (RON 1,402,109 thousand) and their deposits with the central bank (RON 553,735 thousand) as at 31 December 2008.

Consequently, the operating profit recorded by the NBR was directly and significantly influenced by the favourable difference between incomes from international reserve management (assets) and the costs related to the use of monetary policy instruments on the domestic market (liabilities); in 2008, net income from international reserve management totalled RON 5,498,849 thousand, while interest costs associated with monetary policy operations stood at RON 1,110,106 thousand, down 80 percent. Interest costs associated with sterilisation operations represent also the costs associated with the achievement of the primary objective of the central bank established by law, namely to ensure and maintain price stability. It is worth noting that, in late 2008, the central bank recorded interest income from loans to credit institutions, thus shifting to a creditor position towards the banking system.

3. Recognition of international reserve management operations

In 2008, the value in RON of foreign assets picked up 14.8 percent (RON 14,986 million) from 2007, due to the increase in international reserve and the depreciation of the domestic currency versus the euro.

**Developments in NBR's Foreign Assets
- inflation-adjusted data as at 31/12/2008 -**



In 2008, the management of international reserves materialised into incomes equalling RON 6,572,736 thousand and expenses totalling RON 1,073,887 thousand, which entailed a profit amounting to RON 5,498,849 thousand (Table 2), 89.6 percent higher than in the previous year (RON 2,899,633 thousand), under the positive impact of several factors (higher efficiency of international reserve management, rise in average foreign currency reserves, hikes in prices for foreign currency-denominated securities on the international market, etc.).

Table 2. Results of Transactions Performed in 2008

	<i>RON thousand</i>		
	Incomes	Expenses	Profit/Loss
Foreign currency-denominated securities	3,669,546	232,785	3,436,761
Other deposits and foreign currency operations	2,903,157	840,814	2,062,343
Gold	33	288	-255
Total	6,572,736	1,073,887	5,498,849

4. Effects of developments in the exchange rate of the domestic currency

In 2008, the domestic currency depreciated by 10.4 percent in nominal terms versus the euro (from RON/EUR 3.6102 on 1 January 2008 to RON/EUR 3.9860 on 31 December 2008) and by 14.2 percent in nominal terms versus the US dollar (from RON/USD 2.4564 on 1 January 2008 to RON/USD 2.8054 on 31 December 2008), while it appreciated by 16.9 percent in nominal terms versus the pound sterling (from RON/GBP 4.9095 on 1 January 2008 to RON/GBP 4.0777 on 31 December 2008).

The strengthening of the domestic currency versus the pound sterling, as well as other developments, had a negative impact on the NBR's financial performance and was conducive, according to the new accounting policy implemented in 2005 for the harmonisation with ECB standards, to losses in amount of RON 740,497 thousand representing unfavourable differences from the revaluation of assets and liabilities (Table 3), which generated the reduction of profit to RON 3,338,305 thousand.

Table 3. Revaluation Differences as at 31 December 2008

	<i>RON thousand</i>	
	Gains (recognised in the special revaluation account under liabilities)	Losses (recognised in the profit and loss account)
Foreign currency-denominated securities	1,804,918	6,438
Other deposits in foreign exchange	4,906,390	734,059
Gold	3,963,924	-
Total	10,675,232	740,497

Given the implementation of the International Accounting Standards specific to central banks, 2008 was the fourth year when losses from the revaluation of assets and liabilities at the end of the financial year (RON 740,497 thousand) were recognised as expenses without being subject to clearing, as they had been prior to end-2004 with revaluation gains (RON 10,675,232 thousand on balance – as liabilities – at end-2008), according to the new accounting methodology.

5. Conclusions

5.1. The financial position of the National Bank of Romania as at 31 December 2008 improved on the back of the increase in Tier 1 capital amounting to RON 9,577,204 thousand (Table 4), 40 times higher than at end-2007 (RON 242,318 thousand), under the favourable impact of the following factors:

- significant profit in amount of RON 3,338,305 thousand, 7 times higher than the previous year's figure of RON 458,463 thousand;

- significant favourable differences from revaluation of monetary gold holdings at 31 December 2008 (recorded under “Special revaluation account”), due to the further high price for gold on international markets;
- significant favourable differences from revaluation of net assets in EUR and USD at 31 December 2008 (recorded under “Special revaluation account”), due to a weaker revaluation rate at 31 December 2008 (RON/EUR 3.9852 and RON/USD 2.8342) than the average cost of the foreign currency position prior to revaluation (RON/EUR 3.5693 and RON/USD 2.4563);
- significant favourable differences from mark-to-market of foreign currency security portfolio as at 31 December 2008.

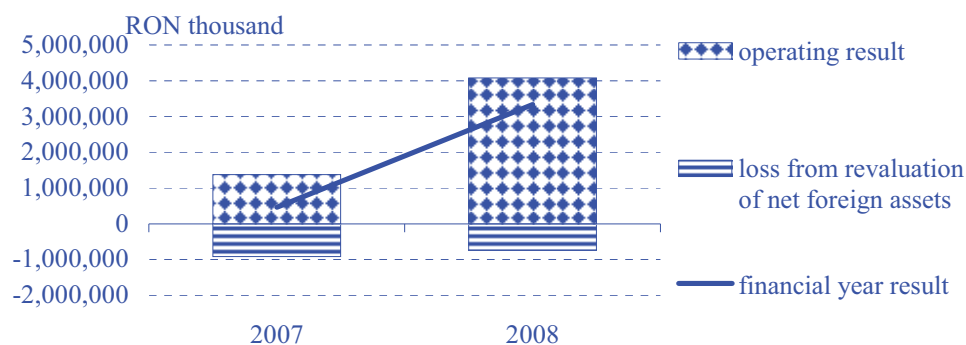
Table 4. Equity

	<i>RON thousand</i>	
	31 December 2008	31 December 2007
Capital	30,000	30,000
Reserves	1,693,495	1,693,495
Special revaluation account	10,675,232	4,678,651
Profit/Loss for the financial year	3,338,305	458,463
Retained earnings	-6,159,828	-6,618,291
Total	9,577,204	242,318

5.2. The 2008 financial result in terms of activities performed by the National Bank of Romania is presented below:

Table 5. Performance of Financial 2008

	<i>RON thousand</i>		
Activity	Revenues	Expenses	Profit/Loss
Monetary policy	110,023	1,220,129	-1,110,106
Management of international reserves	6,572,736	1,073,887	+5,498,849
Currency issue and payment settlement	144,392	158,407	-14,015
Other operations, including administrative costs	35,792	331,718	-295,926
Subtotal – operational activity	6,862,943	2,784,141	+4,078,802
Revaluation of assets and liabilities as at 31.12.2008	-	740,497	-740,497
Total	6,862,943	3,524,638	+3,338,305

NBR's Financial Result Structure during 2007-2008

The chart above shows the significantly positive financial result recorded by the NBR in 2008, the profit amounting to RON 3,338,305 thousand, 7 times higher than the previous year's figure, following the structural change of the financial result illustrated by the following co-ordinates:

- significant operating profit in amount of RON 4,078,802 thousand, 3 times higher than the previous year's figure of RON 1,375,745 thousand;
- costs associated with unfavourable differences from revaluation of net assets in foreign currency at 31 December 2008 tantamount to RON 740,497 thousand, 19 percent lower than end-2007 figure (RON 917,282 thousand), generated particularly by the appreciation of the domestic currency versus the pound sterling and, implicitly, by the decline in net foreign currency assets expressed in GBP. It is worth noting that the unfavourable differences from the revaluation of net foreign currency assets, even though they arose from movements on the foreign exchange market rather than from the current operational activity of the central bank, are recognised in the income statement (the same as the operating results) for reasons attributable to economic prudence (in compliance with the provisions of Regulation ECB/2006/16, as subsequently amended and supplemented).

5.3. The operating financial result gives a fair description of the effectiveness of the activity performed by the National Bank of Romania. Therefore, year 2008 saw a significantly positive financial performance that entailed an operating profit totalling RON 4,078,802 thousand, three times higher than the previous year's figure of RON 1,375,745 thousand, as a result of favourable developments recorded under all categories of activities, as follows:

Table 6. Profit/Loss for Financial 2007 and 2008

Activity	Profit/Loss (RON thousand)		Percentage change (%)
	2007	2008	
Monetary policy	-1,273,412	-1,110,106	-13
Management of international reserves	+2,899,633	+5,498,849	+90
Currency issue and payment settlement	-8,342	-14,015	+68
Other operations, including administrative costs	-242,134	-295,926	+22
Total operating result	+1,375,745	+4,078,802	+196

Table 6 shows that the positive performance of the operating result in 2008 as compared to 2007 is due largely to the surge in incomes from the management of international reserves and lower losses arising from monetary policy operations.

5.4. Pursuant to the provisions of Art. 43, para.1, point b) of Law No. 312/2004 on the Statute of the National Bank of Romania, **the profit corresponding to the 2008 financial year (RON 3,338,305 thousand) is fully distributed** to cover the loss carried forward from the previous years in amount of RON 6,159,828

thousand. The uncovered loss from the above-mentioned operation (RON 2,821,523 thousand) will be covered from future profit.

It deserves mention that the central bank's profit for January-May 2009 equalled RON 3,537,572 thousand (the equivalent of EUR 837 million – at an average exchange rate for January-May 2009), which covered the loss recorded at end-2008. As a result, the National Bank of Romania transferred RON 607,878 thousand to the State budget, according to the law. The adjustments related to financial 2009 as concerns the 80 percent share of net revenues transferred to the State budget will be made until the submission date of the annual balance sheet, namely 31 May 2010, according to the law.

Moreover, mention should be made about an outstanding event: on 4 May 2009, the IMF Executive Board approved Romania's request for the completion of a 2-year interest- and commission-bearing stand-by arrangement in amount of SDR 11.44 billion (about EUR 12.9 billion or USD 17.1 billion). The first tranche worth of SDR 4.37 billion (about EUR 4.9 billion or USD 6.6 billion) was released on 6 May 2009.

To sum up, in 2008, acting for the public good in order to curb inflation and consolidate the foreign exchange position of the government, the National Bank of Romania ended the considered year with an operating profit, due to significant interest costs associated with monetary policy operations (fully offset by the favourable result of international reserve management), which represents particularly the disinflation cost – an essential condition for the adoption of the euro.

**Financial Statements
of the National Bank of Romania
as at 31 December 2008**

(audited by Deloitte)



Deloitte Audit SRL
Șos. Nicolae Titulescu nr. 4-8
Intrare Est, Etaj 3
Sector 1, București, 011141
România

Tel: +40 (21) 222 16 61
Fax: +40 (21) 222 16 60
www.deloitte.ro

Reg.Com J40/6775/1995
C.U.I. 7756924

To the Board of Directors of the National Bank of Romania

REPORT OF THE FINANCIAL AUDITOR

1. We have audited the accompanying financial statements of the National Bank of Romania (“the Bank”), which comprise the balance sheet as at 31 December 2007, the income statement for the year then ended, and a summary of significant accounting policies and other notes to the financial statements, presenting the following:

■ Total assets:	RON 120,145,487 thousand
■ Net assets/Total equity and reserves:	RON 9,577,204 thousand
■ Net profit for the year:	RON 3,338,305 thousand

Management’s Responsibility for the Financial Statements

2. Management is responsible for the preparation and fair presentation of these financial statements in accordance with the Norm on organizing and conducting the accounting of the National Bank of Romania (“Norm 1/2007”) and as described in the accounting policies presented in the notes to the financial statements. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

Auditor’s responsibility

3. Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with the Standards on Auditing as adopted by the Romanian Chamber of Financial Auditors. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance whether the financial statements are free from material misstatement.
4. An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor’s judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity’s preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity’s internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

Member of
Deloitte Touche Tohmatsu

5. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

6. In our opinion, the financial statements present fairly, in all material respects, the financial position of the National Bank of Romania as of 31 December 2007, and its financial performance for the year then ended in accordance with the Norm for organizing and conducting the accounting of the National Bank of Romania (Norm 1/2007) and as described in the accounting policies presented in the notes to the financial statements.

Other matters

7. The accompanying financial statements are prepared based on legal and accounting regulations applicable to the National Bank of Romania in force at 31 December 2007. Accordingly, the accompanying financial statements are not designed for those who are not informed about these legal and accounting regulations, respectively, the Norm for organizing and conducting the accounting of the National Bank of Romania (Norm 1/2007).

**Refer to the original signed
Romanian version**

Ahmed Hassan, Audit partner



*Registered with the Chamber of Financial Auditors
of Romania with certificate No.1529/25.11.2003*

On behalf of:

DELOITTE AUDIT SRL

*Registered with the Chamber of Financial Auditors
of Romania with certificate No.25/25.06.2001*

Bucharest, Romania

6 May 2009

Member of
Deloitte Touche Tohmatsu

BALANCE SHEET
AS AT 31 DECEMBER 2008

		<i>RON thousand</i>	
	Note	31 December 2008	31 December 2007
Cash and other cash equivalents		13,173	11,023
Precious metals and stones		103,445	92,817
of which:			
Non-monetary gold		86,128	73,493
Other precious metals and stones		17,317	19,324
Foreign assets, of which:		116,394,294	101,408,006
Current account in SDR with IMF		345,018	1,238
Monetary gold	4	8,153,487	6,774,214
Demand deposits placed	5	10,334,481	5,413,778
Time deposits placed	6	4,093,396	13,451,955
Foreign currency placements	7	1,532,662	1,243,877
Foreign currency securities	8	87,320,085	57,689,543
Lent securities	8	-	12,733,686
Quotas in international financial institutions	9	4,615,165	4,099,715
of which IMF		4,497,276	3,994,479
National currency securities		-	270
Loans to domestic credit institutions, of which:	10	1,377,100	-
Lombard loans and other credits		1,377,100	-
Loans to domestic credit institutions		11,800	11,800
Loans in litigation		13,209	13,209
Credit risk provision – principal		(25,009)	(25,009)
Other assets		1,373,911	1,366,701
Loans to employees		344	466
Property and equipment	11	1,315,060	1,325,057
Inventory		2,554	3,033
Participating interests	12	2,313	2,306
State budget receivables	13	14,166	21,081
Other settlement accounts		57,989	65,639
Off-balance sheet revaluation accounts	14	13,823	-
Other assets		27,515	26,964
Provisions for other assets	15	(59,853)	(77,845)
Accrued interest receivables		883,564	924,821
Accrued interest receivables	16	889,632	930,889
Credit risk provisions – interest	17	(6,068)	(6,068)
TOTAL ASSETS		120,145,487	103,803,638

Notes from page 176-204 are an integral part of these financial statements

**BALANCE SHEET
AS AT 31 DECEMBER 2008**

		<i>RON thousand</i>	
	Note	31 December 2008	31 December 2007
Currency in circulation	18	29,060,808	25,455,633
Foreign liabilities, of which:		6,071,785	4,867,018
Due to international financial institutions of which:		4,527,354	4,045,431
<i>due to IMF</i>	19	4,497,298	3,994,498
Demand deposits taken		1,209,184	523,051
Time deposits taken		-	-
Borrowings from banks and other financial institutions	20	3,692	4,049
SDR allocations from IMF	21	331,555	294,487
Due to domestic credit institutions, of which:		73,933,593	64,682,887
Current accounts of domestic credit institutions		21,420,118	23,427,815
Amounts withheld at court disposition		12,920	4,560
Time deposits of domestic credit institutions		535,900	4,045,700
Foreign currency minimum reserves		51,959,740	37,202,791
Accounts of bankrupt credit institutions		4,915	2,021
Current accounts of the State Treasury	22	1,428,038	8,499,449
Other liabilities, out of which		20,228	25,145
Borrowings and other similar liabilities		1,015	1,034
Sundry creditors		6,960	8,611
Salaries and other personnel accounts		1,780	2,190
Due to State budget		4,887	5,284
Settlement accounts		3,575	5,683
Other liabilities		2,011	2,343
Accrued interest payables	23	53,831	31,188
Equity, of which:		9,577,204	242,318
Capital		30,000	30,000
Reserves		1,693,495	1,693,495
Special revaluation account	25	10,675,232	4,678,651
Profit for the year		3,338,305	458,463
Profit distribution for the year		(3,338,305)	(458,463)
Accumulated losses from previous years		(2,821,523)	(6,159,828)
TOTAL LIABILITIES AND EQUITY		120,145,487	103,803,638

<p>Refer to the original signed Romanian version</p>

The financial statements were approved by the Board of Directors on 6 May 2009
and were signed on its behalf by:

Governor

Mr. Mugur Isărescu

**INCOME STATEMENT
FOR THE YEAR ENDED 31 DECEMBER 2008**

RON thousand

	Note	31 December 2008	31 December 2007
Interest income	26	3,752,910	3,677,389
Interest expenses	27	(2,208,831)	(2,053,600)
Net interest result		1,544,079	1,623,789
Fee and commission income	28	162,659	118,149
Fee and commission expenses	29	(43,457)	(40,884)
Net fee and commission result		119,202	77,265
Net realised losses from foreign currency operations	30	2,317,936	(33 550)
Net realised gains/losses from securities operations	31	509,091	28,656
Net realised losses from precious metals operations	32	(261)	(315)
Unrealised losses from revaluation differences	33	(740,497)	(917,282)
Net result from financial operations		2,086,269	(922,491)
Currency issue expenses	34	(104,791)	(82,359)
Income/(expenses) from credit risk provisions		(13,847)	(3)
Other expenses from specific operations		3,217	4,321
Net result from specific operations		(115,421)	(78,041)
Other income		17,762	22,347
Salary and other personnel costs		(167,005)	(145,313)
Administrative expenses		(37,196)	(29,604)
Depreciation and amortisation expenses		(34,875)	(20,703)
Other operating expenses		(74,510)	(68,786)
Net PROFIT for the year		3,338,305	458,463

**Refer to the original signed
Romanian version**

The financial statements were approved by the Board of Directors on 6 May 2009 and were signed on its behalf by:

Governor

Mr. Mugur Isărescu

NOTES TO FINANCIAL STATEMENTS AS AT 31 DECEMBER 2008

1. General information

The National Bank of Romania (the “Bank” or “NBR”) was set up in 1880 as the central bank of Romania. The current registered headquarters are located in 25 Lipsicani Street, Bucharest, Romania. The Bank is managed by the Board of Directors. The executive management of the Bank comprises the Governor, the First Deputy Governor and two Deputy Governors. The Parliament appoints the Directors for a period of five years. The Bank is fully owned by the Romanian state.

The operations of the Bank during the financial year 2008 were governed by the ‘Law on the Statute of the National Bank of Romania’ (Law No. 312/2004), in effect since 31 July 2004, except for a number of provisions related to statutory financial reporting that became effective commencing on 1 January 2005. The purpose of Law No. 312/2004 is to ensure the compliance of the NBR’s statute with the European Union legislation and, in particular, with the provisions on central bank independence of the European Community Treaty.

In accordance with the effective legislation, the primary objective of the Bank is to ensure and maintain price stability. Likewise, the Bank has the exclusive right to issue banknotes/ coins and the duty to regulate and supervise the Romanian banking system.

2. Significant accounting policies

a) Preparation of financial statements

The NBR’s financial statements are prepared in accordance with the accounting principles and rules established by the International Accounting Standards, applicable to central banks, acknowledged by the European Central Bank and include the following: the balance sheet, the profit and loss account and the explanatory notes.

The financial statements for the year ended 31 December 2008 have been prepared in accordance with the Norms for organizing and conducting the accounting of the National Bank of Romania (Norms No. 1/2007, no. 1/2008 and no. 3/2008). These norms were introduced to update Norm no. 2/2005 for organizing and conducting the accounting of the National Bank of Romania - developed based on Guideline 2003/131/EC of the European Central Bank of 5 December 2002 regarding the legal framework for accounting and financial reporting in the European System of Central Banks (ECB/2002/10⁵) - with the provisions of Guideline 2006/887/EC of the European Central Bank of 10 November 2006 regarding the legal framework

⁵ OJ L 58, 03.03.2003, p. 1

for the accounting and financial reporting in the European System of Central Banks (ECB/2006/16⁶) and with the provisions of Decision 2009/98/EC of the European Central Bank of 11 December 2008 amending Guideline ECB/2006/16 regarding the accounting procedures and financial reporting legal framework within the European System of Central Banks (ECB/2008/21⁷).

Thus, Norm No. 1/2007 with all the subsequent amendments sets up the basic accounting principles and rules, the form and the content of the annual financial statements, complying with the International Accounting Standards applicable to central banks and recognized by the European Central Bank:

The process of updating the accounting norms mentioned above mainly consisted in replacing the provisions of the cash approach with the ones of the economic approach stipulated in Guideline 2006/887/CE, introducing the new accounting policies regarding the securities held to maturity promoted by Decision 2009/98/EC, thus resulting the incorporation of the following accounting rules as part of Norm 1/2007 with all the subsequent amendments:

- the recording in the off balance sheet accounts of the events/transactions as at the transaction date followed by the transfer of the related amounts in balance sheet accounts as at the settlement date (the operations with securities in foreign currency – further accounted only as at settlement date – represent exceptions to this rule);
- the impact on the foreign currency position of the inflows/outflows of foreign currency as at the transaction date, the related gains and losses being calculated as at the transaction date;
- the daily recording in the accounts of the interest expense/income, the premium/discount for the financial instruments denominated in foreign currency (independent of the real cash flow) and, respectively, the daily impact of the related amounts on the foreign currency position;
- the securities classified as “held to maturity” and the non-marketable securities are valued in the balance sheet at amortized cost less impairment losses, if any. The premiums/discounts are amortized.

The accounting policies have been consistently applied by the Bank for the year ended 31 December 2008.

b) Basis of preparation

The financial statements are prepared on a going concern basis and presented in Romanian lei, rounded to the nearest thousand.

Income and expenses are recognized in the accounting period in which they are earned or incurred and not according to the period in which they are received or paid (the accruals principle).

⁶ OJ L 348, 11.12.2006, p. 1

⁷ OJ L 36, 05.02.2009, p. 1

c) The transfer of the Bank's net revenues to the State

The Bank is exempted from paying income tax, but, in accordance with Law No. 312/2004, distributes to the state budget a share of 80 percent of the net revenues – after deducting the expenses related to the financial year and the loss related to the previous financial years that remained uncovered from other available sources (see Note 2u).

d) Significant accounting principles

Substance over form: Transactions are recorded and disclosed in accordance with their substance and economic reality and not merely with their legal form.

Prudence: the valuation of assets and liabilities and the recognition of income and expense are carried out prudently. However, prudence does not allow the deliberate understatement of assets and income or overstatement of liabilities and expenses.

Post-balance-sheet events: assets and liabilities are adjusted for events that occur between the annual balance sheet date and the date on which the financial statements are approved by the Board of Directors, if they are indicative of the condition of assets or liabilities existing at the balance sheet date. No adjustment is made, but disclosure is required for those events occurring after the balance sheet date that do not affect the condition of assets and liabilities at the balance sheet date, but which are of such importance that non-disclosure would affect the ability of the users to make proper evaluations and take economic decisions.

Materiality: deviations from the accounting rules, including those affecting the income statement, are not allowed unless they can reasonably be judged to be immaterial in the overall context and for the presentation of the Bank's financial statements.

e) Estimates

In preparing the financial statements in accordance with Norm No. 1/2007 with all the subsequent amendments, the management is required to make estimates and assumptions affecting the reported amounts of the assets, liabilities, revenues and expenses for the period. Actual results could differ from these estimates. The estimates are periodically revised and, if necessary, adjustments are recorded in the income statement of the period when these occur. Although these individual estimates carry some uncertainty, their cumulative effect on the financial statements is not significant.

f) Recognition of assets and liabilities

Financial assets/liabilities shall be recognised in the balance sheet only when:

- it is probable that future economic benefits associated with the asset/liability will flow to or from the Bank;

- substantially all the risks and rewards associated with the asset/liability have been transferred to the Bank; and
- the value of the asset/liability can be measured reliably.

Financial assets and liabilities are initially recognised at the acquisition value as presented hereinafter.

g) Foreign currency position

The foreign currency position represents the net position determined as the difference between the total receivables (balance sheet assets and off balance sheet accounts in the nature of assets) and total payables (balance sheet liabilities and off balance sheet accounts in the nature of liabilities) denominated in the respective currency, with minor exceptions. The monetary gold is considered as a foreign currency, forming the gold position.

The items not included in the foreign currency position are the foreign currency amounts booked in the following accounts: Cash in foreign currency, Foreign currency in transit, Sundry suppliers, Sundry debtors, Settlement accounts and Prepayments.

During 2008, the Bank held long positions for all foreign currencies and gold (total receivables exceeding total payables denominated in the respective foreign currency), apart from the SDR position which switched in March 2008 from a short to a long position.

h) Average cost method

The average cost method is applied to the following:

- the foreign currency position, including SDR;
- the monetary gold position; and
- the foreign currency securities portfolio – for each ISIN/CUSIP (security series).

The average cost of the foreign currency position is determined on a daily basis as an indirect quotation (lei/1 FCY). In case of the long foreign currency position, net acquisitions of currencies made during the day are added, at the average cost of the purchases made during the day, to the previous day's ending balance, to determine a new average cost. In case of net sales, the average cost remains unchanged. For the gold position, the same principles apply.

The average cost of the foreign currency securities is determined for each ISIN/CUSIP (International Securities Identification Number) by dividing the transaction value by the correspondent nominal value. All purchases made during the day are added at cost to the previous day's ending balance to produce a new average cost for each ISIN/CUSIP (security series).

The net average cost of the foreign currency securities is determined for each ISIN/CUSIP by dividing the holding at the average cost – adjusted by the cumulated premium/discount amortization – to the correspondent nominal value. The premiums/discounts from purchases of securities are amortized over the remaining life of the securities, using the straight-line method. However, the internal rate of return method is used for the discount securities with a remaining maturity of more than one year at the time of acquisition.

The gains/losses arising from transactions in foreign currency, gold/silver in standard form and foreign currency securities are assessed based on the average cost of the respective holding (Note 2i and Note 2j).

At the end of the financial year, in accordance with the revaluation procedure (Note 2q), the average cost of the foreign currency position and the net average cost of the foreign currency securities – in the event where there have been recorded unrealized losses as at 31 December for the respective foreign currency position or holding of ISIN/CUSIP (security series) – are written down to the revaluation rate and the market price of the securities, respectively.

i) Foreign currency transactions

Foreign currency transactions are converted into lei based on the exchange rate ruling at the transaction date. The monetary assets and liabilities denominated in foreign currencies at the balance sheet date are converted into lei based on the exchange rate ruling at that date.

Forward and spot purchases and sales in case of the foreign currency/RON swaps are recognised in off-balance-sheet accounts from the trade date to the settlement date based on the spot rate of the transactions and in on-balance-sheet accounts at the respective settlement date. The difference between spot and forward rates is treated as interest payable or receivable. The foreign currency position is changed as a result of accruals denominated in foreign currency.

In accordance with the average cost method for the long foreign currency holding, any sale of foreign currency (outflow from the foreign currency position) generates a gain/loss assessed as follows:

- if daily acquisitions exceed daily sales, then the gain/loss arising from the daily sales is computed as the total sales multiplied by the difference between the average price of the daily sales and the average cost of the daily acquisitions;
- if daily sales exceed daily acquisitions, then the gain/loss arising from the daily sales is computed as the sum of the following:
 - the gain/loss arising from the sales covered by the daily acquisitions: computed as the total daily acquisitions multiplied by the difference between the average price of the daily sales and the average cost of the daily acquisitions;

- the gain/loss arising from the sales covered by the previous day foreign currency holding: computed as the net sales multiplied by the difference between the average price of the daily sales and the average cost of the respective foreign currency position on the preceding day.

j) Foreign currency securities

The premiums/discounts arising on the acquisition of securities are amortized over the remaining life of the securities using the straight-line method, the amortization being booked daily on accruals basis. The amortization of the discount/premium is presented as part of interest income/expense. The receivables for the securities are booked daily on an accrual basis, being expressed in lei at the Bank exchange rate of the day.

The internal rate of return method is, however, used for the discount securities with a remaining maturity of more than one year at the time of acquisition.

The gain/loss arising from *the sale of securities* is determined as the nominal value multiplied by the difference between the selling price and the average cost of the respective security. The components of the aforementioned gain/loss are the following:

- the market price effect representing the sold nominal value multiplied by the difference between the selling price and the net average cost of the respective security – recorded in the income statement as at the settlement date;
- the interest rate effect representing the sold nominal value multiplied by the difference between the net average cost and the average cost of the respective security – recorded in the income statement by the procedure of daily amortization of the related premiums/discounts in foreign currency.

The gain/loss from the mark-to-market is determined as difference between the market rate and the net average cost. Short-term securities – traded on markets where there are less than three market makers – are accounted for at cost. From 31 December 2008, no mark-to-market is performed for held-to-maturity securities.

k) Loans granted to credit institutions and other entities

The loans are stated in the balance sheet at the amount of the outstanding principal, adjusted with the provision for loan impairment, in order to reflect the estimated recoverable amount.

l) Participating interests

In accordance with Norm No. 1/2007 with all the subsequent amendments, the participating interests, including those holdings reflecting a significant influence, are booked at cost; thus, these financial statements are not consolidated.

m) Tangible and intangible assets

The tangible and intangible assets are stated at historical cost or the revalued cost, less accumulated depreciation or amortization.

Capital expenditure on property and equipment in the course of construction is capitalized and depreciated once the assets enter into use.

The expenditure incurred to replace a component of an item of tangible and intangible assets, including the modernization expenditure, is capitalized. All other expenditure (repairs, maintenance etc.) is charged to the income statement as incurred, representing operating expense.

The depreciation is provided on a straight-line basis over the estimated economic useful life of property and equipment. The depreciation is recognized as a write-down of the costs of the items of property and equipment. The land is not depreciated. The legal economic useful life is as follows:

Buildings	20 – 60 years
Equipment	5 – 20 years
Motor vehicles	5 years
Computer equipment	3 years

n) Provisions for impairment of assets

As part of its monetary and exchange rate policies, the Bank is entitled to grant loans to the credit institutions. The Bank books credit risk provisions in accordance with its own norms, drawn up under the approval of the Board of Directors and the advisory approval of the Ministry of Public Finances.

The provisions for impairment losses from loans are charged to the income statement as specific expenses and offset against the carrying value of the loans and accrued interest receivables.

The loans are written off and charged to the income statement as they become unrecoverable and all the necessary legal procedures have been carried on.

Other provisions than those for credit risk are covered from the remaining profit – net of the state share (80%) from the Bank's net revenues. The financial assets are reviewed to determine whether there is any indication of impairment. If any such indication exists, the asset recoverable amount is estimated. An impairment loss is recognized whenever the carrying amount of an asset exceeds its recoverable amount.

The provisions for impairment losses are fully/partially reversed if there has been a change of the previously used estimates to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's new carrying amount does not exceed the carrying amount that would have been determined, net of

depreciation or amortization, if no impairment loss had been recognized in previous years.

o) Currency in circulation

The Bank prepares the program of banknotes and coins issue, ensures the printing, distribution and administration of the cash reserve, in order to meet the cash requirements in accordance with the real needs of money circulation.

Currency in circulation is booked at the value of the banknotes and coins produced/received by/from the NBR Printing and Minting Units and other foreign suppliers, less the value of the banknotes and coins destroyed and other similar items (the withdrawn banknotes and coins, the withdrawn banknotes and coins not exchanged within the legal period), the value of the banknotes and coins included in collections, the value of the banknotes and coins sold as numismatic products, the value of the banknotes and coins from the reserve fund kept in the Central Vault and the Bank's branches, the value of the banknotes and coins in course of expedition.

p) Deposit certificates issued by the Bank

The deposit certificates issued by the Bank are denominated in lei and are sold to the domestic credit institutions. These are discount instruments, being redeemed at their nominal value on the maturity date.

At the issuance date of the deposit certificates, their nominal value is recorded as a liability. The discount is booked as a prepayment on the assets side of the balance sheet and it is amortized over the useful life of the deposit certificates, using the straight-line method and the accruals principle.

q) Revaluation

The revaluation of the foreign currency assets and liabilities is performed monthly and booked in the special revaluation account as the difference between the revaluation rate (the official rate available on the last working day of the month) and the average cost of the foreign currency position. The exceptions are the assets (quotas in IMF) and liabilities (allocations and deposit from IMF) denominated in SDR which are revalued on 30 April and 31 December based on the exchange rates communicated by the International Monetary Fund.

The mark-to-market is performed on a monthly basis both for the holdings of gold/silver in standard form and foreign currency securities, with the exceptions listed below; the differences are recorded in adjustments accounts in the balance sheet. The revaluation of the gold is performed based on the lei price per defined unit of weight of gold derived from the lei/USD exchange rate and the fixing quotation on the London Bullion Market. The revaluation of the foreign currency securities implies the comparison of the mid market price at the end of the last working day of the month and the net average cost of the respective security. Short term securities – traded on markets where there are less than 3 market makers – are

accounted for at cost. Starting 31 December 2008, held-to-maturity securities are accounted for at amortized cost less impairment losses, if any.

Offsetting unrealized losses for securities, currencies or gold balances against unrealized gains in other securities, currencies or gold is not permitted.

At the end of the financial year, the unrealized losses are charged to the income statement without the possibility of subsequent cancellation against new unrealized gains. Subsequently, the average cost of the foreign currency position and the net average cost of the foreign currency securities – which generated the aforementioned unrealized losses – are written down to the revaluation rate and the market price respectively. At the end of the financial year, the unrealized gains are booked in the special revaluation account in the balance sheet.

r) Pension obligations and employee benefits

The Bank, in the normal course of business, makes payments to the Romanian state funds on behalf of its Romanian employees for pension, health care and unemployment benefit. During 2008, as well as during the previous years, all Bank's employees have been included in the state pension system. Also, starting with 2007, according to the legal framework, all the eligible Bank's employees have been included in the private pension system (compulsory and optional).

In compliance with the collective labour agreement currently in force, the Bank pays on the retirement of its employees a benefit based on the salary on the date of the retirement. The collective labour agreement is subject to annual approval by the Board of the Bank. The Bank recognizes the benefits related to the retirement on the date these are due to the employees of the Bank.

s) Income and expense recognition

The revenues and expenses are recognized according to the accruals principle. The losses/gains arising from sale of the foreign currency, gold or securities holdings are charged to the income statement. These are determined as the difference against the average cost of the respective asset.

The unrealized gains are not recognized as income, but transferred directly to the special revaluation account.

At the end of the year, the unrealized losses are charged to the income statement if they exceed revaluation gains previously recorded in the corresponding revaluation account. There is no netting of unrealized losses for securities, currencies or gold balances against unrealized gains in other securities, currencies or gold.

t) Capital and statutory reserves

The *capital* is fully owned by the Romanian state and is not divided into shares. As at 31 December 2008 the Bank's capital was in amount of lei 30,000 thousand.

The *statutory reserves* were set up on 1 January 2005 in accordance with Law No. 312/2004, incorporating the remaining balance of the reserve fund. As at 31 December 2008, the statutory reserves are nil, as a consequence of covering the 2006 and 2005 financial losses (see Note 2u). The statutory reserves are subject to a maximum increase limit of 60% from the annual profit, net of the state share (80%) of the Bank's net revenues.

u) Distribution of profit, loss coverage

The loss of the financial exercise is covered from the available sources, in the following priority order: a) special revaluation account as at 31 December 2004; b) statutory reserves; c) future profits.

According to the legal framework, taking into account the wearing out of the first sources for covering the previous years losses (the special revaluation account at 31 December 2004 and statutory reserves), the profit corresponding to the 2008 financial year is fully distributed to cover the losses from the previous years.

3. Risk management policies

The main risks associated with the Bank's activities are financial and operational risks arising from the Bank's responsibility to ensure and maintain the price stability in Romania. The most important types of financial risks to which the Bank is exposed are credit risk, liquidity risk and market risk. Market risk includes currency risk and interest rate risk.

a) Credit risk

The Bank is exposed to credit risk through its trading, lending and investing activities and in cases where it issues guarantees.

Credit risk associated with trading and investing activities is managed through the Bank's market risk management process. The risk is mitigated through selecting counterparties of high credit standing and monitoring their activities and ratings and through the use of exposure limits.

The Bank's primary exposure to credit risk arises from granting short-term loans in lei to domestic credit institutions. The amount of credit exposure in this regard is represented by the carrying amounts of the loans on the balance sheet. Short-term loans in lei extended to banks are normally secured with treasury securities issued by the Romanian Government or with term deposits. However, the Bank may, in special circumstances, grant unsecured loans to banks and other credit institutions in order to prevent systemic crises.

Maximum credit risk exposure, representing the maximum accounting loss that would be recognized at the balance sheet date if counterparties failed completely to perform as contracted and any collateral proved to be of no value, is estimated to amount to lei 1,377,444 thousand (31 December 2007: lei 466 thousand).

b) Liquidity risk

The Bank is the lender of last resort to credit institutions in Romania. The main objective of its day-to-day operations is to ensure that adequate liquidity exists on the domestic market.

The Bank also manages the international foreign currency reserve, through planning and diversification, in order to ensure the foreign obligations are timely met.

c) Interest rate risk

The Bank incurs interest rate risk mainly in the form of exposure to adverse changes in the market interest rates to the extent that interest-earning assets and interest-bearing liabilities mature or reprice at different times or in different amounts.

For financial receivables and liabilities in lei, the Bank endeavours to match the current market rates. Obtaining a positive margin is not always possible given that the levels of such assets and liabilities are dictated by the objectives of the monetary policy. However, the Bank is constantly monitoring the costs of implementing the policies against the estimated benefits.

For financial receivables and liabilities in foreign currency, the Bank attempts to maintain a net positive position. The Bank uses a mix of fixed and variable rate instruments.

d) Currency risk

The principal foreign currencies held by the Bank are EUR and USD. Due to the volatility of the exchange rate and of the financial markets, there is a consequent risk of loss in value in respect of net monetary assets held in foreign currency. Open foreign exchange positions represent also a source of currency risk.

The Bank is exposed to currency risk through foreign currency transactions. There is also a balance sheet risk that the net monetary liabilities in foreign currencies will have a higher value when translated into lei as a result of currency movements.

In order to avoid losses that may arise from adverse movements in exchange rates, the Bank, within the framework of its objectives for managing international reserves, is currently pursuing the policy of diversifying its portfolio, in order to ensure a balanced foreign currency distribution, whilst maintaining, generally, an overall long foreign exchange position.

The assets and liabilities held in EUR, USD and other foreign currencies at the balance sheet date are presented in Note 35.

The revaluation rates of the principal foreign currencies at the end of the year were:

Currency	RON thousand		
	31 December 2008	31 December 2007	% Increase (decrease)
euro (EUR)	1: RON 3.9852	1: RON 3.6102	10.4
US Dollar (USD)	1: RON 2.8342	1: RON 2.4564	15.4

4. Monetary gold

	RON thousand	
	31 December 2008	31 December 2007
Gold bullion in standard form	2,196,419	1,824,911
Coins	1,134,021	942,059
Deposits abroad	4,823,047	4,007,244
Total	8,153,487	6,774,214

At 31 December 2008, the Bank had a sole foreign deposit amounting to lei 4,823,047 thousand. As at 31 December 2008, the gold revaluation price came to lei/g 78.75 and the Bank's gold holdings amounted to 103,536.35 Kg (as at 31 December 2007, the revaluation price came to lei/g 65.43 and the Bank's gold holdings amounted to 103,533.76 Kg).

5. Demand deposits placed

	RON thousand	
	31 December 2008	31 December 2007
Demand deposits at international financial institutions	10,139,996	5,264,662
Demand deposits at central banks	178,494	130,104
Demand deposits at foreign banks	15,991	19,012
Total	10,334,481	5,413,778

As at 31 December 2008, the position demand deposits comprises mainly the current account held with Bank for International Settlements (BIS) in amount of lei 10,139,996 thousand (31 December 2007: lei 5,264,662 thousand), representing the lei equivalent of EUR 2,320,110 thousand (31 December 2007: EUR 1,457,946 thousand), USD 315,391 thousand (31 December 2007: USD 477 thousand) and CHF 5 thousand (31 December 2007: CHF 5 thousand), as well as other demand deposits. The structure of the demand deposits by currency is presented in Note 35.

6. Term deposits placed

	<i>RON thousand</i>	
	31 December 2008	31 December 2007
Term deposits at central banks	4,093,396	954,994
Term deposits at foreign banks	-	12,427,310
Term deposits at international institutions	-	69,651
Total	4,093,396	13,451,955

As at 31 December 2008, the term deposits held with central banks include a deposit held with an European central bank in amount of lei 3,447,198 thousand (EUR 865,000 thousand) (31 December 2007: lei 115,888 thousand, the equivalent of EUR 32,100 thousand) and, respectively, a deposit held with a non-European financial institution in amount of lei 646,198 thousand (USD 228,000 thousand) (31 December 2007: lei 839,106 thousand, the equivalent of USD 341,600 thousand).

7. Foreign currency placements

	<i>RON thousand</i>	
	31 December 2008	31 December 2007
Placements at World Bank, out of which:		
– in deposits, out of which:	510,602	492,329
- demand deposits at Fed	730	628
– in securities	1,022,060	751,548
Total	1,532,662	1,243,877

In October 2002, the Bank and the International Bank for Reconstruction and Development (IBRD) concluded an investment management agreement providing for the IBRD's role as an investment advisor and agent for the Bank's foreign assets, subject to a 20% limit of the Bank's international reserves. As at 31 December 2008, the deposits managed by IBRD amounted to lei 509,872 thousand, the equivalent of USD 179.9 million (31 December 2007: lei 491,701 thousand, the equivalent of USD 200.2 million).

As at 31 December 2008, the Bank's placements managed by the World Bank (in securities) according to the investment management agreement amounted to lei 1,022,060 thousand – USD 360.6 million (31 December 2007: lei 751,548 thousand – USD 305.9 million).

8. Foreign currency securities

	<i>RON thousand</i>	
	31 December 2008	31 December 2007
Discount treasury bills – US Treasury	113,031	-
Discount treasury bills – European Treasuries	13,708,239	979,552
Discount treasury bills – Credit Institutions and Banks	14,613,082	16,502,308
Discount notes – International financial institutions (EIB)	3,752,348	-
Coupon bonds – US Treasury	11,599,215	-
Coupon treasury bills – European Treasuries	23,618,757	14,819,829
Coupon treasury bills – Credit Institutions and banks	10,292,177	17,845,232
Coupon treasury bills – International financial institutions – BIS (MTI)	8,511,424	7,542,622
Coupon bonds – International financial institutions – (EIB, IBRD, NIB, EBRD)	1,111,812	-
Total	87,320,085	57,689,543

The coupon treasury bills issued by the European Treasuries, credit institutions, banks and BIS bear fixed interest rates. Interest rates range between 2.5% and 6.5% per annum for the bills in EUR (2007: between 2% and 8.7% per annum), between 0.9% and 5.1% per annum for the bills in USD (2007: between 3% and 6.5% per annum) and between 4% and 9% for the bills in GBP (2007: 3.5% and 6.3%).

As at 31 December 2008, the foreign currency securities portfolio included short-term securities in amount of lei 25,230,919 thousand (at 31 December 2007 – in amount of lei 17,655,604 thousand). Short term securities – traded on markets where there are less than three market makers – are accounted for at cost.

As at 31 December 2008, there were no held-to-maturity securities. As at 31 December 2008, there were no lent securities (as at 31 December 2007, the lent securities amounted to lei 12,733,686 thousand)

9. Quotas in international financial institutions

	<i>RON thousand</i>	
	31 December 2008	31 December 2007
Romania's quota at IMF	4,497,276	3,994,479
Participation in the share capital of Bank for International Settlements	77,412	68,567
Participation in European Central Bank	40,477	36,669
Total	4,615,165	4,099,715

This item comprises the government funds representing the participation quota in other international financial institutions.

The Bank, in accordance with Law No. 97/1997, exercises all the rights and obligations arising from Romania's membership in IMF.

Romania's quota at IMF is recorded as an asset denominated in SDR. At 31 December 2008 and 31 December 2007, Romania's total quota in IMF came to SDR 1,030 million. The IMF maintains deposits with the Bank in relation to the participation.

The current account in SDR with IMF is held by each member state of IMF and is used to conduct the borrowings and other related operations with IMF. This account bears the same interest rates as the SDR allocation from IMF.

10. Loans to domestic credit institutions

	<i>RON thousand</i>	
	31 December 2008	31 December 2007
Lombard loans and other credits	1,377,100	-
Loans to credit institutions	11,800	11,800
Loans in litigation	13,209	13,209
Specific provision for credit risk (for principal amount)	(25,009)	(25,009)
Balance at the end of year	1,377,100	-

The Lombard loans and other credits outstanding as at 31 December 2008 were granted to credit institutions according to Law No. 312/2004 on the Statute of the National Bank of Romania.

The loans granted to credit institutions include the loan granted to Credit Bank S.A., a bankrupt credit institution, according to Emergency Ordinance No. 26/2000; the loan in litigation was granted before the bankruptcy of Credit Bank S.A.

11. Property and equipment

	<i>RON thousand</i>				
	Land and buildings	Equipment	Work in progress	Intangible assets	Total
<i>Cost or revalued amount</i>					
As at 31 December, 2007	1,253,918	88,832	33,372	15,971	1,392,093
Additions	30,171	6,245	17,490	161	54,067
Disposals	(79)	(1,421)	(28,167)	(268)	(29,935)
As at 31 December 2008	1,284,010	93,656	22,695	15,864	1,416,225
<i>Cumulated depreciation</i>					
As at December 31, 2007	-	54,824	-	12,212	67,036
Depreciation during the year	24,835	8,008	-	2,205	35,048
Disposals	-	(669)	-	(250)	(919)
As at 31 December 2008	24,835	62,163	-	14,167	101,165
Net book value					
as at 31 December 2008	1,259,175	31,493	22,695	1,697	1,315,060
As at 31 December 2007	1,253,918	34,008	33,372	3,759	1,325,057

As at 31 December 2008, the item “equipment” includes fixed assets acquired through finance lease agreements in progress (31 December 2008: gross value – lei 5,491 thousand, and cumulated depreciation – lei 1,037 thousand; 31 December 2007: gross value – lei 26,172 thousand and cumulated depreciation – lei 10,602 thousand).

During 2008, financial lease agreements for IT equipment were concluded, with gross value of lei 927 thousand, the total depreciation for 2008 being of lei 357 thousand.

12. Participating interests

The participating interests are stated at cost, in accordance with Norm No. 1/2007 with all the subsequent amendments; thus, these financial statement are not consolidated.

As at 31 December 2008, the participating interests, in amount of lei 2,313 thousand, included the shares held by the Bank in TRANSFOND S.A. (lei 2,240 thousand) – a joint stock company providing settlement services for the inter-bank operations of the local banks (the Bank’s shareholding represents 33% of the TRANSFOND S.A. share capital) - and 8 shares held by the Bank in SWIFT, as a result of the reallocation procedure performed on 20 February 2006 and unmodified at 2008 reallocation procedure having a carrying value of EUR 18,220 (lei 73 thousand).

Summarized financial data of TRANSFOND S.A. are disclosed in the following table:

	<i>RON thousand</i>	
	31 December 2008	31 December 2007
Equity	159,681	159,106
Total assets	166,357	171,250
Net profit for the year	21,266	20,691

13. State budget receivables

State budget receivables include amounts due to the Ministry of Public Finance, representing mainly to the cost of gold reimbursed to the population following court decisions. In accordance with legislation in force, NBR has the right to receive the related amounts from Ministry of Public Finance.

14. Off-balance sheet revaluation accounts

As at 31 December 2008, the amount of lei 13,823 thousand represents the revaluation differences for the foreign currency transactions booked in off-balance-sheet accounts as at the end of the year. These transactions are monthly revalued and the revaluation result is booked in the balance sheet. On settlement date the aforementioned transactions will be booked in on-balance-sheet accounts.

15. Provisions for other assets

	<i>RON thousand</i>	
	31 December 2008	31 December 2007
Provisions for:		
Receivable from KOLAL BV Amsterdam (a)	35,983	53,975
Guarantees paid by NBR for Credit Bank S.A. (b)	23,848	23,848
Receivable from S.C. Logic Telecom (amount in litigation) (c)	22	22
Total	59,853	77,845

a) The NBR's receivable against KOLAL BV Amsterdam is written off during a period of 5 years, starting in 2006, according to Emergency Ordinance No. 68/2001 regarding the regulation of the receivables of the National Bank of Romania and the Savings House against "Dacia Felix"-S.A.. In 2008, the provision was decreased by an amount of lei 17,992 thousand representing the third of the five instalments. The aforementioned provision represents an adjustment figure of the balance sheet item "Settlement accounts", including the "Prepayments" account where the receivables against KOLAL BV Amsterdam were booked.

b) As at 31 December 2008, the equivalent in lei of the collateral paid by the Bank as guarantor for Credit Bank S.A. amounts to lei 23,848 thousand.

c) The provision for the NBR's receivables against S.C. Logic Telecom was booked further to the bankruptcy of the aforementioned counterparty and the Bank's related legal action.

The provisions b) and c) represent adjustment figures of the balance sheet item "Other assets".

16. Accrued interest receivables

	<i>RON thousand</i>	
	31 December 2008	31 December 2007
<i>Accrued interest receivables from:</i>		
Foreign currency securities	872,416	720,744
Foreign currency deposits and placements	6,509	71,613
Lent securities	-	130,262
Loans granted to banks	8,870	6,068
Other	1,837	2,202
Total	889,632	930,889

17. Credit risk provisions - interest

As at 31 December 2008, the credit risk provision for interests receivable in amount of lei 6,068 thousand relates to the interest receivables for the loan granted to Credit Bank S.A. according to Emergency Ordinance No. 26/2000.

18. Currency in circulation

	<i>RON thousand</i>	
	31 December 2008	31 December 2007
Banknotes	28,848,712	25,289,447
Coins	212,096	166,186
Total	29,060,808	25,455,633

19. Due to IMF

	<i>RON thousand</i>	
	31 December 2008	31 December 2007
Deposits from IMF	4,497,298	3,994,498
Total	4,497,298	3,994,498

As at 31 December 2008, the balance on the IMF account, in amount of SDR 1,030,205,036 (the equivalent of lei 4,497,298 thousand) was revalued based on the SDR exchange rate confirmed by IMF.

20. Borrowings from banks and other financial institutions

As at 31 December 2008, the Bank had borrowings in amount of lei 3,692 thousand (EUR 926.4 thousand) representing a financial lease agreement for the acquisition of banknote processing systems/machines.

21. SDR allocations from IMF

This item includes a non-reimbursable loan bearing the same interest rate as the SDR current account at IMF. As at 31 December 2008, SDR allocations from IMF had an interest rate of 0.82% per annum (31 December 2007: 3.50% per annum).

22. Current accounts of the State Treasury

	<i>RON thousand</i>	
	31 December 2008	31 December 2007
Lei current account of the State Treasury	17,295	80,076
Foreign currency current account of the State Treasury	1,410,743	8,419,373
Total	1,428,038	8,499,449

The State Treasury current account bears variable interest rate.

23. Accrued interest payables

	<i>RON thousand</i>	
	31 December 2008	31 December 2007
<i>Accrued interest payables to:</i>		
Foreign borrowings	2,792	4,800
Minimum compulsory reserves of credit institutions	50,107	21,478
Deposits of the credit institutions	93	4,067
Current accounts of the State Treasury	839	843
Total	53,831	31,188

24. Related party transactions

The Government of Romania, through the State Treasury, maintains current accounts with the Bank, for which the operations bear commissions starting from 31 December 2005. Furthermore, the Bank acts as a registry agent on behalf of the State Treasury as regards treasury bills and notes, manages the international reserves and ensures timely servicing of Romania's foreign public debt.

The Bank exercises influence, through Board members, over two other state institutions: the National Printing and Minting Units.

In 2008, the total purchases of banknotes and coins from the aforementioned two entities amounted to lei 107,979 thousand (31 December 2007: lei 42,531 thousand). As at 31 December 2008, the Bank had no outstanding balances payable to the National Printing and Minting Units. The transactions with these two entities were carried out on normal commercial terms and conditions.

The Bank has significant influence over TRANSFOND S.A., an entity established in 2000 to outsource the Bank's settlement activities of domestic inter-bank operations. On 8 April 2005, the gross real-time settlements system (REGIS) became operational; afterwards, during the year, the SENT module (for small value payments – fully managed by TRANSFOND S.A.) and the SaFIR module (for treasury bills and deposit certificates issued by the Bank – managed by the Bank) entered into operation.

For its agent services, TRANSFOND S.A. receives 95% of the settlement commissions cashed in by the Bank from the domestic banks and other varying percentages according to the contracts regulating the other modules of the Electronic Payment System. The total commissions paid to TRANSFOND S.A. by the Bank during 2008 amounted to lei 40,233 thousand (31 December 2007: lei 34,052 thousand). As at 31 December 2008 the TRANSFOND S.A. had no liability to the Bank, and the Bank had no liability to the TRANSFOND S.A.

25. Special revaluation account

	<i>RON thousand</i>	
	31 December 2008	31 December 2007
Favourable revaluation differences from holdings of gold, precious metals and stones	3,963,924	2,572,247
Favourable revaluation differences from foreign currency holdings (revaluation performed based on the exchange rate as at balance sheet date)	4,906,390	1,621,428
Security denominated in foreign currency (market value revaluation)	1,804,918	484,976
Total	10,675,232	4,678,651

As at 31 December 2008, the balance on the special revaluation account represents the favourable revaluation differences. Offsetting unrealized losses for securities, currencies or gold balances against unrealized gains in other securities, currencies or gold is not permitted. The unfavourable revaluation differences as at 31 December 2008 were charged to the income statement.

26. Interest revenue

	<i>RON thousand</i>	
	2008	2007
<i>Foreign currency/gold operations</i>		
Interest and similar income from:		
Foreign currency securities	3,106,340	2,531,452
Time deposits and reverse repo operations under securities lending agreement	-	298,831
Foreign currency placements	518,561	835,935
Amounts in SDR	17,948	103
Total interest income from foreign currency and gold operations	3,642,849	3,666,321
<i>Lei operations</i>		
Interest and similar revenue from:		
Loans to credit institutions	72,739	6,058
Other income	37,322	5,010
Total interest revenue from lei operations	110,061	11,068
Total interest revenue	3,752,910	3,677,389

In the financial year 2008, interest income from foreign currency operations comprises mainly the foreign currency placements (lei 518,561 thousand), the amortisation of discounts arising from securities acquisitions (lei 946,108 thousand) and the accumulated coupon (lei 2,160,232 thousand).

27. Interest expense

	<i>RON thousand</i>	
	2008	2007
<i>Foreign currency operations</i>		
Interest and similar expenses from:		
Foreign currency securities, minimum mandatory reserves and deposits taken	980,884	436,460
Borrowings under securities lending agreement	-	290,608
Loans from International Monetary Fund	7,679	16,672
Total interest expenses from foreign currency operations	988,563	743,740
<i>Lei operations</i>		
Interest and similar expenses from:		
Term deposits of credit institutions	219,449	487,841
Minimum reserves of credit institutions	718,085	336,405
Current account of the State Treasury	282,595	314,023
Deposit certificates issued by the Bank	-	171,476
Other expenses	139	115
Total interest expenses from lei operations	1,220,268	1,309,860
Total interest expense	2,208,831	2,053,600

In the financial year 2008, the interest expense from the foreign currency operations comprises mainly the interest paid on foreign currency minimum mandatory reserves and on deposits taken (lei 802,215 thousand), the amortization of net premium from securities acquisitions (lei 178,669 thousand).

28. Fee and commission income

The fee and commission income in lei represents the commission income from settlement of the operations between local credit institutions and the State Treasury.

	<i>RON thousand</i>	
	2008	2007
Fee and commission income in lei	141,175	105,577
Fee and commission income in foreign currency	21,484	12,572
Total fee and commission income	162,659	118,149

The fee and commission income also include the amount of lei 21,484 thousand, representing the 2008 net income from lent securities – operation based on an agent contract between the Bank and the Bank of New York.

29. Fee and commission expenses

	<i>RON thousand</i>	
	2008	2007
Fee and commission expenses in lei	39,763	37,326
Fee and commission expenses in foreign currency	3,694	3,558
Total fee and commission expense	43,457	40,884

The fee and commission expense in lei represents the commissions for services received by the Bank, including the services provided by TRANSFOND S.A. - an entity created in 2000 to outsource the Bank's settlement activities of domestic inter-bank operations. TRANSFOND S.A. receives for its agent services 95% of the commissions cashed in by the Bank for the settlement of the domestic credit institutions operations (see Note 24).

30. Net realised gains/(losses) from foreign currency operations

	<i>RON thousand</i>	
	2008	2007
<i>Income from foreign currency operations</i>		
Income from exchange rate differences	2,327,602	127,933
Dividends on shares in Bank for International Settlements	17,562	8,030
Total income from foreign currency operations	2,345,164	135,963
<i>Expenses from foreign currency operations</i>		
Expenses from exchange rate differences	(25,447)	(167,725)
Other expenses from foreign currency operations	(1,781)	(1,788)
Total expenses from foreign currency operations	(27,228)	(169,513)
Net realized gains/(losses) from foreign currency operations	2,317,936	(33,550)

The income and expense from exchange rate differences booked in 2008 are generated mainly by the outflows from long foreign currency positions and are assessed based on the average cost method (see Note 2i).

31. Net realised gains from securities operations

	<i>RON thousand</i>	
	2008	2007
<i>Income from securities operations</i>		
Gains from securities operations	563,206	105,067
Total income from securities operations	563,206	105,067
<i>Expenses from securities operations</i>		
Net realized gains from securities operations	509,091	28,656

The gains/losses represent the market price effect resulting from the sales of the foreign currency securities and are assessed based on the average cost method (see Note 2j).

32. Net realised losses from precious metals operations

	<i>RON thousand</i>	
	2008	2007
Income from precious metals operations	33	1
Expenses from precious metals operations	(294)	(316)
Net realized losses from precious metals operations	(261)	(315)

Expenses from precious metals operations represent the deposit fees paid for the gold kept at the external depository.

33. Unrealised losses from revaluation differences

	<i>RON thousand</i>	
	2008	2007
<i>Expenses from unfavourable revaluation differences</i>		
Revaluation of the net assets denominated in USD	-	787,603
Revaluation of the net assets denominated in GBP	732,820	-
Revaluation of the net assets denominated in other foreign currencies	1,239	72,835
Market value revaluation of the foreign currency securities	6,438	56,844
Unrealized losses from revaluation differences	740,497	917,282

As at 31 December 2008, net losses generated by the unfavourable revaluation differences and assessed on the basis of the average cost method were charged to the income statement.

Offsetting unrealized losses for securities, currencies or gold balances against unrealized gains in other securities, currencies or gold is not permitted. The favourable revaluation differences as at 31 December 2008 were booked in the special revaluation account (see Note 2q).

34. Currency issuance expenses

This item comprises the expenses with printing and minting the banknotes and coins.

35. Currency risk

The currency structure of the Bank's assets at 31 December 2008 is the following:

	<i>RON thousand</i>						
	LEI	EUR	USD	SDR	Gold	Other	Total
Cash and other cash equivalents	13,018	120	35	-	-	-	13,173
Non monetary gold stones	-	-	-	-	86,128	-	86,128
IMF	-	-	-	345,018	-	17,317	345,018
Monetary gold	-	-	-	-	8,153,487	-	8,153,487
Demand deposits placed	-	9,307,046	905,026	-	-	122,409	10,334,481
Term deposits placed	-	3,447,198	646,198	-	-	-	4,093,396
Foreign currency placements	-	-	1,532,662	-	-	-	1,532,662
Foreign currency securities	-	52,393,692	30,810,762	-	-	4,115,631	87,320,085
Lent securities	-	-	-	-	-	-	-
Quotas in international financial institutions	-	40,477	-	4,574,688	-	-	4,615,165
Lombard loans and other credits	1,377,100	-	-	-	-	-	1,377,100
Loans to domestic credit institutions	11,800	-	-	-	-	-	11,800
Loans in litigation	13,209	-	-	-	-	-	13,209
Credit risk provision – principal	(25,009)	-	-	-	-	-	(25,009)
Loans to employees	344	-	-	-	-	-	344
Property and equipment	1,315,060	-	-	-	-	-	1,315,060
Inventory	2,554	-	-	-	-	-	2,554
Equity investments	2,313	-	-	-	-	-	2,313
State budget receivables	14,166	-	-	-	-	-	14,166
Other accounts for settlements	57,989	-	-	-	-	-	57,989
Revaluation differences for the off balance sheet items	13,823	-	-	-	-	-	13,823
Other assets	27,515	-	-	-	-	-	27,515
Provisions for other assets	(36,005)	-	(23,848)	-	-	-	(59,853)
Accrued interest receivables	10,706	716,351	122,901	658	-	39,016	889,632
Credit risk provisions - interest	(6,068)	-	-	-	-	-	(6,068)
Total assets	2,792,515	65,904,884	33,993,736	4,920,364	8,239,615	4,294,373	120,145,487

The currency structure of the Bank's liabilities and capital at 31 December 2008 is the following:

	<i>RON thousand</i>						
	LEI	EUR	USD	SDR	Gold	Other	Total
Currency in circulation	29,060,808	-	-	-	-	-	29,060,808
Demand deposits taken	-	1,209,184	-	-	-	-	1,209,184
Due to international financial institutions	29,630	-	426	4,497,298	-	-	4,527,354
Borrowings from banks	-	3,692	-	-	-	-	3,692
SDR allocations from IMF	-	-	-	331,555	-	-	331,555
Current accounts of							
domestic credit institutions	21,420,118	-	-	-	-	-	21,420,118
Amounts withheld at court disposition	12,920	-	-	-	-	-	12,920
Term deposits taken from domestic banks	535,900	-	-	-	-	-	535,900
Foreign currency minimum reserves	-	41,904,931	10,054,809	-	-	-	51,959,740
Accounts of bankrupt credit institutions	4,915	-	-	-	-	-	4,915
Current accounts with the State Treasury	17,295	1,387,972	22,771	-	-	-	1,428,038
Borrowings and other similar liabilities	1,015	-	-	-	-	-	1,015
Sundry Creditors	6,960	-	-	-	-	-	6,960
Salaries and other personnel accounts	1,780	-	-	-	-	-	1,780
Due to State budget	4,887	-	-	-	-	-	4,887
Settlement accounts	3,575	-	-	-	-	-	3,575
Other liabilities	2,011	-	-	-	-	-	2,011
Accrued interest payables	24,285	26,562	2,351	633	-	-	53,831
Total liabilities	51,126,099	44,532,341	10,080,357	4,829,486	-	-	110,568,283
Net assets / (net liabilities)^{*)}	(48,333,584)	21,372,543	23,913,379	90,878	8,239,615	4,294,373	9,577,204

*) represent the Bank's equity and reserves

The currency structure of the Bank's assets at 31 December 2007 is the following:

	<i>RON thousand</i>						
	LEI	EUR	USD	SDR	Gold	Other	Total
Cash and other cash equivalents	10,964	44	15	-	-	-	11,023
Non monetary gold	-	-	-	-	73,493	-	73,493
Other precious metals and stones	-	-	-	-	-	19,324	19,324
Current account in SDR with IMF	-	-	-	1,238	-	-	1,238
Monetary gold	-	-	-	-	6,774,214	-	6,774,214
Demand deposits placed	-	5,343,417	3,760	-	-	66,601	5,413,778
Term deposits placed	-	8,560,145	4,822,159	-	-	69,651	13,451,955
Foreign currency placements	-	-	1,243,877	-	-	-	1,243,877
Foreign currency securities	-	48,963,478	4,326,656	-	-	4,399,409	57,689,543
Lent securities	-	-	12,733,686	-	-	-	12,733,686
Quotas in international financial institutions	-	36,669	-	4,063,046	-	-	4,099,715
National currency securities	270	-	-	-	-	-	270
Loans to domestic credit institutions	11,800	-	-	-	-	-	11,800
Loans in litigation	13,209	-	-	-	-	-	13,209
Credit risk provision – principal	(25,009)	-	-	-	-	-	(25,009)
Loans to employees	466	-	-	-	-	-	466
Property and equipment	1,325,057	-	-	-	-	-	1,325,057
Inventory	3,033	-	-	-	-	-	3,033
Equity investments	2,306	-	-	-	-	-	2,306
State budget receivables	21,081	-	-	-	-	-	21,081
Other accounts for settlements	65,639	-	-	-	-	-	65,639
Other assets	26,964	-	-	-	-	-	26,964
Provisions for other assets	(53,997)	-	(23,848)	-	-	-	(77,845)
Accrued interest receivables	8,281	688,978	199,177	8	-	34,445	930,889
Credit risk provisions - interest	(6,068)	-	-	-	-	-	(6,068)
Total assets	1,403,996	63,592,731	23,305,482	4,064,292	6,847,707	4,589,430	103,803,638

The currency structure of the Bank's liabilities and capital at 31 December 2007 is the following:

	<i>RON thousand</i>						
	LEI	EUR	USD	SDR	Gold	Others	Total
Currency in circulation	25,455,633	-	-	-	-	-	25,455,633
Sight deposits taken	-	523,051	-	-	-	-	523,051
Due to international financial institutions	50,564	-	369	3,994,498	-	-	4,045,431
Borrowings from banks	-	4,049	-	-	-	-	4,049
SDR allocations from IMF	-	-	-	294,487	-	-	294,487
Current accounts							
of domestic credit institutions	23,427,815	-	-	-	-	-	23,427,815
Amounts withheld at court disposition	4,560	-	-	-	-	-	4,560
Term deposits taken from domestic banks	4,045,700	-	-	-	-	-	4,045,700
Foreign currency minimum reserves	-	36,912,049	290,742	-	-	-	37,202,791
Accounts of bankrupt credit institutions	2,021	-	-	-	-	-	2,021
Current accounts with the State Treasury	80,076	8,401,808	17,565	-	-	-	8,499,449
Borrowings and other similar liabilities	1,034	-	-	-	-	-	1,034
Creditors	8,611	-	-	-	-	-	8,611
Salaries and other personnel accounts	2,190	-	-	-	-	-	2,190
Due to State budget	5,284	-	-	-	-	-	5,284
Settlement accounts	5,683	-	-	-	-	-	5,683
Other liabilities	2,343	-	-	-	-	-	2,343
Accrued interest payables	15,108	14,224	96	1,760	-	-	31,188
Total liabilities	53,106,622	45,855,181	308,772	4,290,745	-	-	103,561,320
Net assets / (net liabilities) ^{*)}	(51,702,626)	17,737,550	22,996,710	(226,453)	6,847,707	4,589,430	242,318

*) represent the Bank's equity and reserves

36. Commitments and contingencies

As at 31 December 2008, the Bank had in custody promissory notes issued by the Ministry of Public Finance in favour of EBRD and MIGA amounting to EUR 162,000 and USD 600,510 respectively (31 December 2007: the promissory notes issued by MPF in favour of EBRD in amount of EUR 486,000 and MIGA in amount of USD 600,510).

37. Profit distribution

According to the law, the profit of the 2008 financial year in amount of lei 3,338,305 thousand is fully distributed to cover the losses carried forward from the previous years (Note 2u).

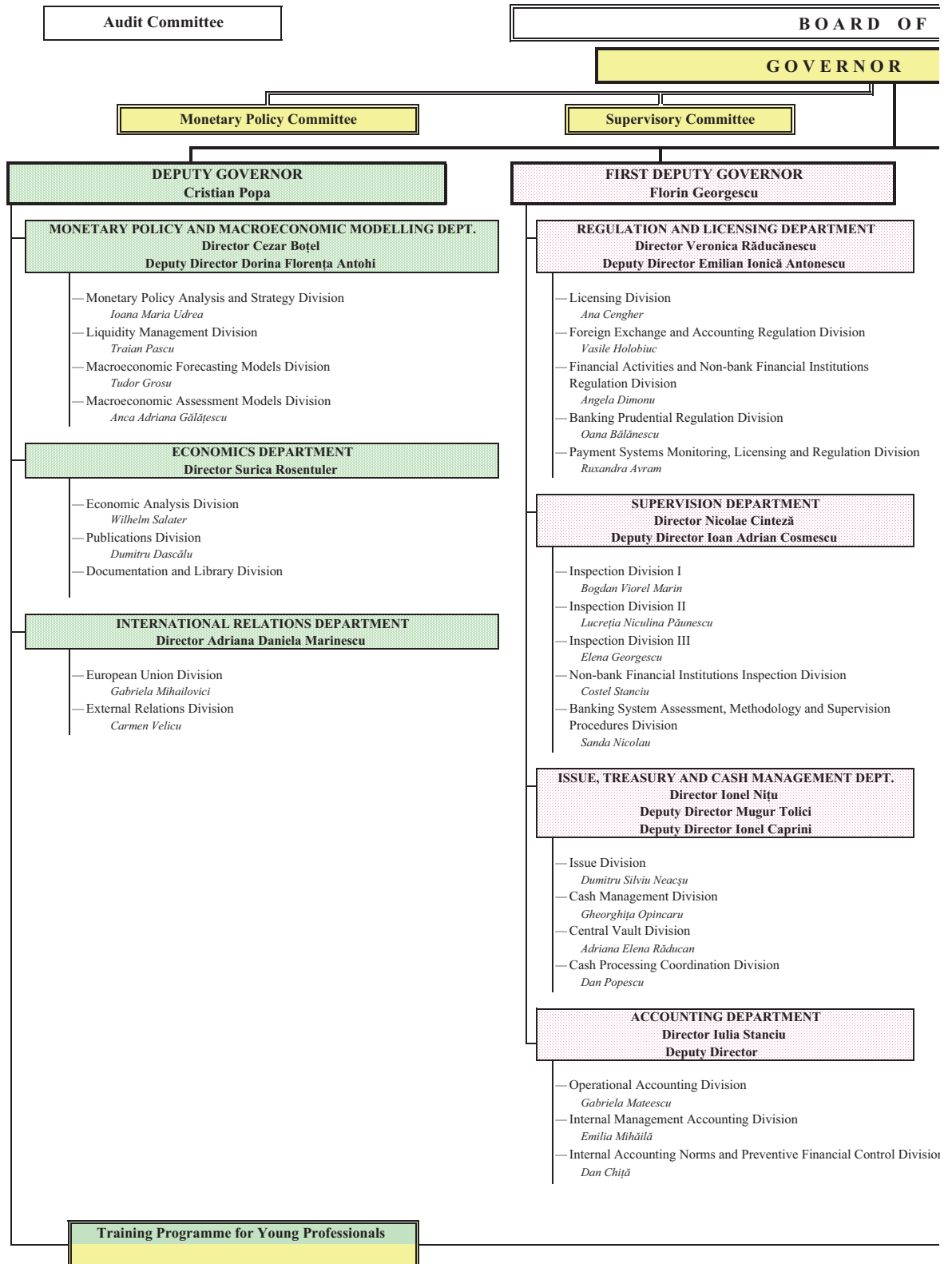
38. Events subsequent to the balance sheet date

In accordance with Law No. 312/2004, the Bank transfers to the state budget a share of 80 percent of the net revenues - after deducting the expenses related to the financial year and the loss related to the previous financial years that remained uncovered from other sources (see Note 2u). The payment is made on a monthly basis, representing income to the state budget.

As at 31 March 2009, the Bank has fully covered the losses from the previous years. Thus, according to Law No. 312/2004, the Bank paid to the state budget – until 25 April 2009 – the quota of 80% of its net revenues as at 31 March 2009. All the adjustments for the financial year ended at 31 December 2009 will be performed until the date for submission of the annual balance sheet according with the legislation in force.

Annexes

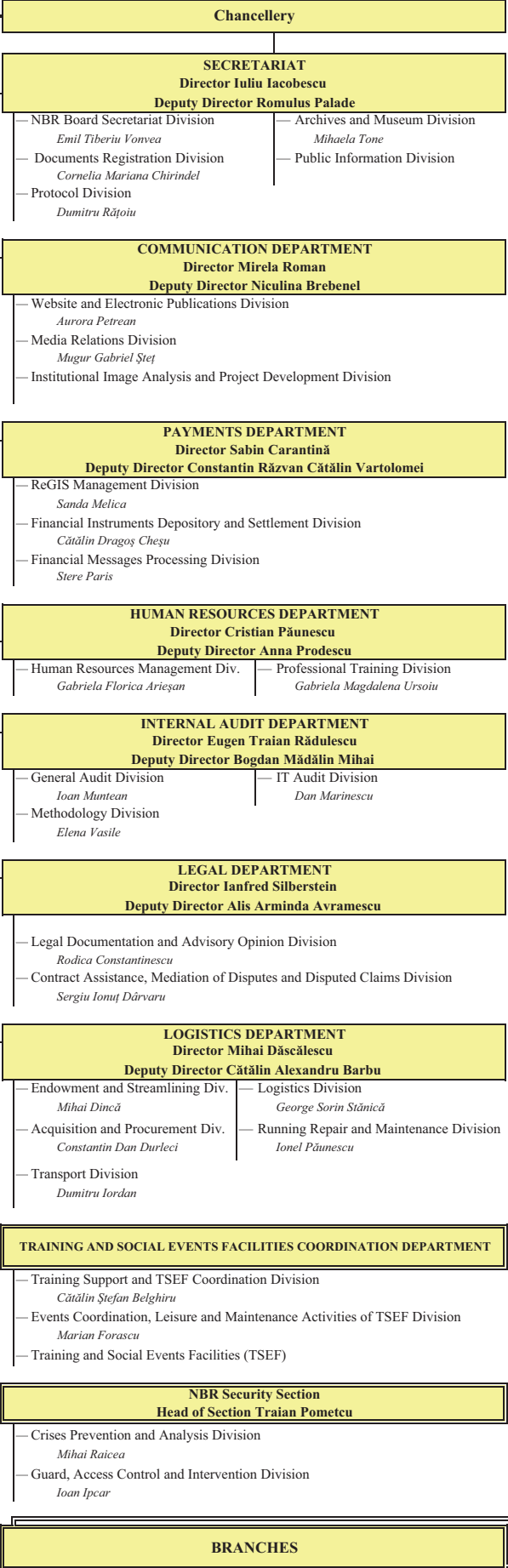
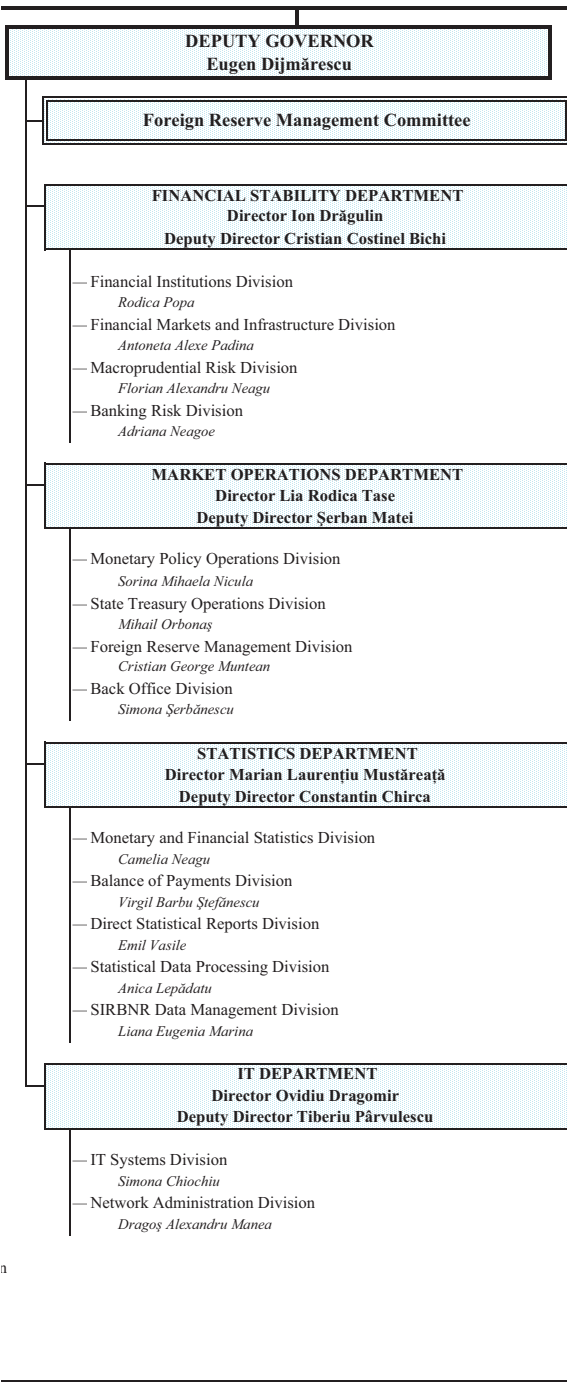
ORGANISATION CHART OF THE NATIONAL BANK



Note: Colour patterns show the departments' co-ordination

DIRECTORS

Mugur Isărescu



1

**National Bank of Romania publications
as of 31 December 2008**

1. Annual Report
2. Annual Report on Balance of Payments and International Investment Position of Romania
3. Financial Stability Report
4. Inflation Report
5. Monthly Bulletin
6. Business Survey
7. Financial Accounts
8. Working Papers
9. Occasional Papers
10. “Cristian Popișteanu” Banking History and Civilisation Symposium
11. *Restitutio*
12. “Romania’s Banknotes” series
13. Regional Seminar on Financial Stability

**Main papers submitted to Parliament
by the National Bank of Romania in 2008**

1. Annual Report for 2007
2. Financial Stability Report for 2008
3. Inflation Reports
4. Monthly Bulletins
5. Balance of Payments and International Investment Position of Romania – Annual Report for 2007
6. Financial Accounts – 1998-2007