THE ADEQUACY OF THE CAPITAL - CENTRAL OBJECTIVE OF PERFORMANCE MANAGEMENT AND BANKING RISK

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Rezumat
The main objective of this work is to highlight the role that the methods and techniques for the management of banking risks have in internal process the capital adequacy at risk in the future and to reflect the continued growth of the banking risks in the contemporary age, in conjunction with the intensification of cooperation that led to the internationalizing of regulations, within the meaning of the development of national rules in accordance with the principles accepted by several countries, the kind of international groups of studies organized by the Bank for International Settlements the Basel Convention or the application of Community rules, drawn up in the form of the Directives of the European Communities.

The work has the research field the theoretical and practical aspects of the completion of the internal process the capital adequacy at risk in banks.

Key words: Banking risk; agreement Basel; banking regulations; capital requirement; banking supervision

JEL classification: G21, G32.

1. Introduction

In a banking institution, the main role of the capital, in addition to the transfer of such property, is to act as a buffer in order to absorb unexpected losses to protect depositors and to ensure investor confidence and the rating agencies. In exchange, the capital of the governed refers to the minimum requirements of capital which all banks are obliged to hold in accordance with the rules of the institution of surveillance, from the perspective of the institution of regulations, the objective of the capital requirements is to ensure the stability and viability of the banking system.

In view of the trend of response by the bank of and maximize profits through extensive use of own funds and forcing of exposure to the risk, supervisory authorities impose certain restrictions, which takes the form of prudential rules governing the aspects related to the suitability of the share capital of the bank and who shall make reference to the funds of the bank. In this respect, in 1988 was adopted the Agreement of the Basel Convention, drawn up by the Committee also known under the name of COOKE Committee which includes the recommendations of the Bank for International Settlements in the area of the adequacy of the capital.

In 1988 was developed the Agreement on the International convergence of the estimation of the Capital and the standards of the capital, hereinafter Basel I. The agreement of the Basel Convention has focused on the credit risk, in order to ensure an adequate level of capital in the whole banking system international.

In the year 1999, has been prepared by the Committee at the earliest rectification of capital adequacy, because of changes in the process of risk management used by banks and which grant them more freedom in the management of credit risk. The new Agreement, hereinafter Basel II recognizes the progress made in the management of credit risk and bring the incentives by allowing for the use of the banks with sophisticated models of risk management of their own models.

The agreement of the Basel II describes advanced approaches for the measurement and the set of minimum requirements with regard to the level of capital. The Agreement introduces the concept of the division potential loss of the credit institution in the expected and unexpected.

In addition to the capital of the level of which shall be governed by the supervisory authorities, more banks must hold and a share capital economic, above the level of the governed in order to reduce the losses of the unexpected. The economic capital is estimated as the difference between the capital of the corresponding to the confidence interval chosen and the expected loss estimated. The main reason for which the expected losses are low is that they are already incorporated in the price of the product with the credit risk.

The agreement of the capital Basel II has opened a new era in cooperation international banking, helped to the harmonisation of surveillance activities of the banking, the rules and standards of the capital adequacy.

In response to the crisis global banking, generated by the subprime crisis in the United States, the Committee of banking supervision of the Bank for International Settlements issued in December 2010, an agreement under the name of Basel III.
The provisions of the new agreement have been implemented gradually from 2011, following that up to the end of 2018 to be implemented completely. Since the implementation of the new agreement presupposes the share capital of the banks, extended period of implementation is necessary to grant the banks enough time to constitute the capital of the supplement. According to the initiators of the new agreement, Basel III is trying to reconcile the supervision of micro and macro-prudential supervision, being at the same time a framework of risk management at the level of the bank (taken from the Basel I and Basel II) and a framework for the management of systemic risk at the level of the banking system. Basel III aims at increasing the liquidity of the banks and in decreasing the risk in the banking system.

The motivation of the introduction of the Basel III shall be based on the following considerations (Walter, 2011, pp. 1-2):

![Considerations of the introduction of the Basel III](image)

2. The adequacy of the banking capital

By mutual agreement of the Basel Convention, Bank for International Settlements proposes a standard methodology for the determination of own funds and two indicators the solvency margin to provide cover minimum risky assets (net) by bank capital as defined by both the own funds and through the capital of their own.

In accordance with the provisions of the Rules of the NBR No 7/1999, the own funds of a bank shall consist of the following categories of capital:

![Categories of capital](image)

**Own capital** consists of:
- the paid-up share capital;
- share premium paid;
- profits brought forward from the previous fiscal years;
the profit current result;
the reserve fund set up under the law;
the fund of tangible assets;
general reserve for credit risk, constituted according to the law.
For the purpose of determining the level of own capital will be deducted the following elements:

![Figure 3](image)

**Additional capital** consists of:
- subordinated debt;
- subsidies received and
- differences favorable from the revaluation of the asset.

In order to determine the level of own funds banks must simultaneously comply with the following requirements:

![Figure 4](image)

According to data provided by the National Bank of Romania, in the Financial Stability Report 2015, the Romanian banking sector continues to be characterized by an adequate level of indicators of capitalization, including as a result of the use of proactive by the central bank of instruments of regulations and prudential supervision. High capacity of coverage of losses plays an essential role in the context of a macroeconomic framework characterized by the interest rates low and the accentuation of the competition.
Romanian banking sector is formed in a measure of credit institutions which come from European space. The 34 credit institutions with foreign capital (in the vast majority the foreign capital comes from the European Union) totalling over 90 % of the assets of the banking sector, the romanian what situating Romania on the place of the officer in the EU after the share ownership foreign Graphic(no. 1)

![Graphic no. 1 Market share and number of credit institutions with foreign capital](image)

**Source:** NBR, ECB (Structural Indicators for the EU Banking Sector)

3. The importance of the banking solvency

In the framework of the analyzes carried out by the institutions of the surveillance, the rating agencies and other international financial bodies, a special attention is given to the rate of the solvency margin, due to the relevance of the on the financial strength of the bank analyzed. This quantify, mainly, the ratio of the own funds of a bank has available and the quality of the assets from the point of view of the risk of reimbursement, at maturity, associated with them. In other words, the quality of the assets is higher, the probability to be reimbursed at maturity increases, the bank is not having to bear, from its own funds, the obligations to maturity.

There is a close connection between the concepts of liquidity and solvency margin of the banking, as follows:

- The increase of the quality of the assets both leads to an increase in the rate of the solvency margin and the improvement of the indicators of liquidity;
- The increase in the own funds of the bank generates the increase of the quality of both of the solvency ratio, and indicators of liquidity;
- In both of the methodology for determining the rate of solvency and indicatorilor of liquidity is used a system of the weights applied to the assets in order to quantifying their quality;
- Increasing the level of the solvency ratio can lead to the improvement of the indicators of liquidity.

Monitoring of solvency, falling under the supervision of the prudential supervision of the banking system, has a great importance for the environment financiar-banking system.

At the level of the romanian banking system, data provided by the National Bank of Romania in the Financial Stability Report 2015, indicators of the capital adequacy noted an ascending trend in the period June 2014 to June 2015 (Graphic 2).

![Graphic nr. 2 Capital adequacy indicators](image)

**Source:** NBR

The implementation of the new CRD IV/CRR regulatory framework as from 1 January 2014 helped strengthen the capital position of EU banking sectors (Chart 3). The capitalisation of the Romanian banking sector is similar to that of countries in the region, comparing favourably with most countries of origin having subsidiaries in Romania.
According to the data provided by the NBR, the leverage ratio calculated for the Romanian banking sector further stood at an appropriate level (8.0% in June 2015), following the substantial increases in shareholders’ capital contributions. The EU legislation requires the compulsory use of this indicator as a macroprudential instrument, in view of mitigating the risk of excessive leverage, starting with 2018. At EU level, the leverage ratio witnessed mixed developments, the Romanian banking sector faring better than most countries of origin of capital of foreign bank subsidiaries.

4. Conclusions

The adequacy of the capital is the importance of at least three reasons:
- in the first place, the application of the capital affect prices and availability of credit for all bank customers, influencing the efficiency of the financial systems of all countries;
- secondly, the capital is a determining factor in the competitiveness of the banking system;
- thirdly, the appropriateness of the capital influence the sustainability of the whole of the international community.

It is essential to monitor the risks of banking type and also increase the transparency and the ability of the banks to manage the risks in the banking system. The provisions of this Agreement Basel II lead to better control of the risks in the banking sector. There is a significant connection between the importance of the growth of liquidity and close the implementation of the Agreement and Basel III, with a view to the creation of a climate of protection by banks in Romania.

The Agreements Basel are intended to give a better capitalisation of banks, an appropriate supervision of the banking activities, which causes the business environment, customers banks to ends confidence in banks and to begin the credit activity.

Basel III is more than a regulation for financial institutions in a world of post-crisis and will affect the fundamental profitability of the banking industry. The reforms affects microprudential level in order to increase the resistance of the banking institutions of the individual periods of stress and respectively macroprudential level, in order to reduce the frequency of financial crises. The new standards are intended to improve the ability of the banking sector to absorb shocks, by a top management of risk under the co-ordinates of a consolidated governnesses in a transparent and flexible.

5. Bibliography