ACTUAL BANKING RISK APPROACHES, THEIR REGULATION, POLICIES AND PRACTICES ON BANKING RISK MANAGEMENT

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Abstract:
The banking system is organized and governed by norms, specific rules, but ultimately it obeys to the same common goal of any field of activity, namely the organization of resources so that its own actions can be completed with profit. Banks are essential to the global financial market and are tempted to take advantage of the dominant position they have in financial markets. Credit institutions are the most important players in the financial market, with most of the financial markets centered on banks. The many economic crises have started from the banking system, thus some well established rules and a well-organized banking management are imposed.

Key words: banking prudence, banking risk, management, regulatory framework, rules

JEL classification: G21

1. INTRODUCTION

The diversity and complexity of banking risks has been on the rise in the last period, intensifying mainly due to the growth in the competitive banking environment, due to the growing financial markets, the emergence of more and more products and services, many focused on technology, the pressing need for banking digitization. Changes in banking financial markets lately have led to major changes in the level of risks within banking institutions. These have a particularly important role in the financial sector, economic development and financial stability, so financial risk management has become increasingly important.

Banking prudential rules include the main aspects of banking management, and their compliance determines the banking strategy and allows for harmonization with European and international legislation. Banking prudence can be quantified using the following instruments: bank solvency, high risk coefficient, market risk adjustment ratio, minimum capital level, financial participation level.

2. BANKING RISKS

The risk is that event with negative consequences for those involved in an economic activity, which can be influenced by events or phenomena that act on the business of the economic agent. It is the expression of the failure to achieve the intended gain or loss in economic transactions. Banking risks are those faced by banks to carry out their current operations, which must be maintained in normal parameters to avoid bankruptcy.

Banks are exposed to various risks depending on the activity, strategies and policies adopted, known as banking risks. The creation of a prudential banking framework is the task of the National Banks which issue the authorization for functioning.

Retail banking activity faces the following types of risks:

- credit risk;

- liquidity risk;
- capital risk;
- operational risk including personnel, process, transaction, discount, technology and control risks;
- legal risk;
- market risk that includes interest rate risk, currency risk, price risk;
- country risk;
- transfer risk;
- reputational risk;
- competitive risk;
- product risk.

Among the types of risks a bank may encounter, there are dependence or interdependence relationships, so credit risk can lead to a liquidity risk or capital risk; in the case of multinational retail banks, credit risk can determine the country risk and transfer risk, market risk can cause credit risk, the reputational risk determines the liquidity one.

3. REGULATORY FRAMEWORK FOR BANKING RISKS

Regulatory and prudential supervision of banks, their authorization process is the central objective of the banking system. Banking prudential rules and indicators are designed to prevent systemic risk, with due regard to the autonomy of each bank in organizing and conducting its business on a competitive basis. In order to protect the interests of depositors and ensure the stability and viability of the entire banking system, the National Bank of Romania ensures the prudential supervision of credit institutions, Romanian legal persons, including their branches established in other Member States or in third countries, by establishing indicators of banking prudence and norms. Complying and tracking of them and of other requirements under applicable law and regulations are intended to prevent and limit the risks specific to banking.

Banking surveillance signifies the activity that ensures the control of banks' operation in accordance with banking regulations and performance management in order to maintain a viable and stable banking system. Banking prudence is carried out at the level of banking companies through inspections and examinations at banks or supervisory authorities through the reports received. The Romanian supervisory model includes both reports and inspections, following the whole issue, from verifying compliance with the legal framework to risk assessment and management.

It is the National Bank of Romania that establishes the frequency of checks and evaluations to determine the size, systemic importance, nature, complexity of the activities carried out by each credit institution. It is desirable to establish an effective communication relationship for the in-depth knowledge of the activity, organization and internal process of the credit institution to assess the adequacy of the capital to its risk profile.

In the same time, it is the NBR that can make recommendations to the credit institution to adopt measures aiming to improve the framework of managing its strategies and its financial support, as well as the arrangement of the surveillance measures or the application of sanctions under the banking legislation.

Prudential supervision aims to support the stability of financial institutions by focusing on credit institutions to protect their solvency and viability. These tasks can be carried out single specialized authority or by separate authorities, from which we come to the conclusion that there are two models of supervision, namely: unified and specialized.

Each country has a specific model of prudence surveillance, and in the table below we want to illustrate the diversity of models in a number of 73 countries.

Table no 1. Surveillance structures in different countries

Separate agents for each subsector	35
Unified surveillance of insurance and capital market	3
Unified surveillance for banks and the capital market	9
Unified surveillance for banks and insurances	13
Unified surveillance inside the central bank	3
Unified surveillance outside the central bank	10

Source: processing after International Monetary Fund-Issues in the Unificationa of Finacial Sector Supervision-Washington, july 2000

In recent years, it has been particularly important to improve the quality of banks' examination with support systems that can assist supervisors in identifying future unfavorable trends in a bank's business that could lead to the emergence of serious future problems. These support systems are represented by the banking supervision instruments, which are the basis of the models addressed by each bank. At the same time, relevant information is used in this process, information that includes the characteristics of a credit institution and its counterparties so that a synthetic measure of their performance and vulnerability can be provided.

Thus, the Basel Committee was set up as a forum where representatives of banking supervisors, Central Bank experts meet to discuss fundamental issues, learn from each other, exchange information on banking techniques in each of their countries.

The Romanian banking system had to adopt the requirements of the European community. Changing the accounting methodology, in line with the International Financial Reporting Standards and adopting the principles of the Basel Accord, posed real challenges for the Romanian financial-banking environment. Alignment with the European directives has entailed very high costs on the part of the banks, so a clean-up of troubled banks has followed after joining the European Union.

The emergence of a new Basel agreement, the so-called Basel II, led to the development of risk management systems by banks, introducing three levels of risk management. Novelty in Basel II with implications for credit risk is a new approach to prudential supervision of credit institutions. In addition, detailed reports are required on their activity to market discipline.

The National Bank of Romania had several objectives regarding Basel II, namely:

- transposing the new prudential requirements into primary and secondary legislation;
- developing prudential supervision means appropriate to the new context;
- development of credit risk management systems at the level of credit institutions.

The Basel III Capital Accord brings large quantitative and qualitative capital requirements, new liquidity requirements, a credit risk review, and a leverage indicator for banks. The regulatory framework and future industry surveillance have been the key points of Basel III as the ultimate goal of strengthening the financial system.

The main reasons for the emergence of Basel III were the negative outcomes of bank crises, their frequency and the many benefits of implementation that exceed the costs. The new standards provide for improved risk management, increased transparency and disclosure requirements for credit institutions, demanding standards to mitigate the negative effects of financial crises.

In Romania, the impact of Basel III has been more limited, yet credit institutions have adopted a series of measures to mitigate the impact of alignment with new standards, including: adjusting the business model, banks focusing on products that meet customer needs at lower costs, launching packages that combine finance with saving. The series of regulations adopted in Romania in 2019 prove the fact that the NBR wants prudential to take the place of the last years of intense lending by lowering the indebtedness of its customers and adopting the consumption index instead of ROBOR. These have been presented in the idea that the population will benefit from the adoption of the new regulations, yet we can state that this is in fact the NBR's strategy to reduce bank risks in order to prepare people for a future financial crisis.

4. BANK MANAGEMENT

The profitability of any financial-banking institution depends on its ability to assess risk and protect its global exposures. To reach a high level of risk management, a retail bank has to take several steps, including:

Banking management has its specific functions, mechanisms and techniques, its own objectives, for which four categories of resources are used: human, financial, physical and informational. Of course, managers have certain roles and qualities that condition success, including the professional qualities for carrying out the specialized activities, the interpersonal qualities they rely on, the managers' abilities of communication, understanding and motivation of the people they relate to, and the conceptual qualities that depend on the ability of the manager to think abstractly, plus the diagnostic and analytical skills necessary to identify the nature and causes of problems and solving them.

The essence of banking activity is determined by five areas of bank management:

• Management of bank assets and liabilities
• Banking risk management
• Human resources
• Marketing
• Management of Own resources

The first field reflects the entire balance sheet of the bank, the management of bank assets and liabilities determines its current situation, as well as the decision-making that enables it to achieve this situation.

Banking risk management is very important because all banking operations have a degree of risk, so managers' attention is important in specific activity.

Human resources are the most important because it is the resource that produces value and profit.

Marketing is indispensable for banks, and in this way banks know market and customer requirements by properly organizing the process of selling of products and services and monitoring the competition.

The last field is one of the most important because, after all, the bank aims to obtain profit, which is why the performance management is very necessary.

CONCLUSIONS

The beginning of the third millennium is characterized by globalization, dynamism, complexity, and technological developments that bring about major changes in market operations, and risk is defined as a likely danger, loss generator as an integral part of this landscape. The problem of risk management at the banking level did not have the same overwhelming importance in the past, as it has now, and is relatively low in impact.

Every business is subject to risks and their management, which involves identifying, measuring, managing and monitoring risks, should not be seen as a centralized function, but should be integrated into the culture itself about business and operations.

Market risk or credit risk management is very complex because the component risks are independent and dynamic.

In the context of an increasingly sophisticated market for financial and banking services, where competition is fierce, good risk management through quality management will lead to the creation of a competitive advantage of the bank that operates in this way in the perspective of self-analysis, internal audit, evaluation by external rating agencies, or the most demanding analysis, that of clientele.

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