

## THE EURO-LEU ARGUMENT IN THE POPULATION'S PREFERENCES FOR SAVINGS PLACEMENT

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### 1. Introduction

EU statistics regarding the eurozone at the end of last year indicated that the 4th trimester of 2009 was the second successive trimester of economic growth, a tendency that is going to be maintained in 2010 as well according to the forecasts of EU specialists. The economic growth was due especially to the favourable evolution in exportation but also to consistent capital infusions in the banking system as well as in economy, which led to a remission in unemployment evolution and to the sustentation of the population's purchasing power.

As for Romania, in spite of all the optimistic affirmations at the end of 2009 stating that decrease was over and in 2010 the country will undergo a process of economic growth, statistical data for the month of February published in the Monthly Bulletin no. 2/2010 of NBR indicate that the growth rate of production volume lowered at -0.4%; unemployment rate was 7.7%, registering only 0.1 percentage points over the average of the last three months which stands for a stabilization of unemployment level around this figure; annual net salary incomes increased with 3.9%, exclusively under the impact of salary growth in the private sector, which was mainly due to laying off employees earning low salaries (regarding public sector employment, the annual dynamic of salary incomes became negative again, unlike January 2010, as a consequence of enforcing the single salary and increment and bonus limiting law.

However, having to consider the drastic limitation of the population's access to lending as a consequence of their lowered incomes and of the less favourable perspective of preserving their jobs, not to mention creating new ones, funding the population's need for investments can be achieved only by saving. Therefore, we consider that guiding the population towards placements for these savings is of great interest.

### 2. What are the population's placement preferences?

In the Financial Stability Report of 2009 elaborated by NBR<sup>1</sup>, at page 90 is shown that "indebtedness continued its increasing trend, payment rate increased, and net assets deteriorated. The risks generated by population upon financial stability are increasing, the alert level is medium-high". The unfavourable evolution of the assets price in the population's portfolio brought about diminution regarding both components of the population's asset: financial and non-financial assets. The financial asset is calculated as the difference between financial assets (life insurance and retirement benefit plans, liquid shares and ventures, liquid shares, bank deposits, government bonds, cash) and financial liabilities (mortgage NBFC<sup>2</sup> loans, loans for other purposes and consumption loans, mortgage bank loans, loans for other purposes and

<sup>1</sup> Comprises data up to 12/31/2008;

<sup>2</sup>NBFCs= non-banking financial institutions, especially leasing societies

consumption loans. Non-financial assets comprises real estate assets.

The structure of the liquidity of financial assets improved in 2008, as the population focused more on owning liquid assets with a lower reevaluation risk (cash, bank deposits and government bonds, all together representing 95% of liquid assets) and less on liquid shares respectively quoted shares or shares that are part of closed or open investment funds. The weight of liquid assets decreased considerably as a consequence of the crash of market exchange rates, as well as consequence of the diminution of their quantity, respectively of the number of shares owned by the population.

Under these circumstances, "the growth of active saving becomes more and more important"<sup>3</sup>. Active saving implies an increase in the net assets of the population due to the quantitative effect, namely financial assets purchasing (asset increase as a consequence of the effect of prices, that is favourable reevaluation of the already purchased assets is due to passive saving).

However, there are factors that favour saving: mainly the tendency to reduce some expenses during the crisis period, the favourable output for bank deposits and government bonds, which are above the rate of inflation, tightening loan and funding conditions which determines the population to save money in order to fund their investment necessities; there are also factors prone to dissaving such as the reduction of the population's incomes, both from the public and private sector, or unemployment increase.

Having to consider these circumstances, among all the saving possibilities bank deposits remain a more appreciated option, although according to the calculations of NBR over 25% of

bank deposits value would maintain above the guaranteed limit, if the guaranteed limit<sup>4</sup> reached 100,000 euros equivalent.

The experience of 2008 shows that even against a certain distrust in the banking system, due to reverberating crashes or rumours about the policy of foreign banks with subsidiaries in Romania consisting of transferring funds from Romania in order to support parent banks, withdrawals led to a reduction of only 3.5% of the deposit value. This amount was stored under the form of cash, inclusively in bank deposit boxes or placed in government bonds, making bank deposits abroad or buying foreign currency.

The output of bank deposits is different depending on whether the placement is in lei or foreign currency – especially euros – regarding the interest, as well as on the exchange rate.

Then arises the question: to save lei or euros?

Analysis undertaken by bank analysts by virtue of the official data published in NBR statistics regarding savings placement options of the population emphasize the high interest in EURO placements in EURO to the detriment of those in lei.

"Starting with July there has been a decrease in the balance account of natural persons' lei deposits and an increase in their foreign currency deposits. Can it be asserted that we are witnessing the beginning of a change in the population's saving behaviour?"<sup>5</sup> In our opinion, the answer to such a question noastră cannot be categorical if taking into account the history of saving after 1990 as well as the suggestions of NBR representatives who almost always wagered on the leu currency in the course of time.

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<sup>4</sup> 50000 euros equivalent at present.

<sup>5</sup> M. Ion – How should we understand and how profitable is the Romanians' preference for placements in euro?, Staff Only Raiffeisen Bank Magazine, no. 7/2009, page 13

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<sup>3</sup> Financial Stability Report (FSR), page 91;

In the first place, the evolution during the second part of 2009 can be partially explained by the seasonality criterium, because it is also maintained during wintertime. Generally during summertime lei saving is reduced, while foreign currency saving is higher in comparison to the rest of the year most probably because of the resources repatriated during the holidays by the Romanians working abroad. Excluding the month of October of 2008, when some Romanians withdrew their bank deposits due to the credibility crisis generated by the Lehman Brothers crash, negative lei saving can be explained by the reduction of saving potential in Romania. However, it is also possible an exchange of some amounts from lei to foreign currency against the exchange ratio between euro and dollar, as well as against other foreign currencies.

In the second place, this evolution is determined by the fact that the economic environment in Romania

does not seem to be improving. Under these circumstances, although foreign currency flows are balanced, the external trade deficit being overcompensated by direct foreign investments, the expectations in the economic environment are directed rather towards leu currency depreciation. They are also fed by various affirmations of some public persons in Romania who induce expectations regarding the decay of the national currency. Within this context, preserving the interest in euro savings for a period of a couple of trimestres more is predictable.

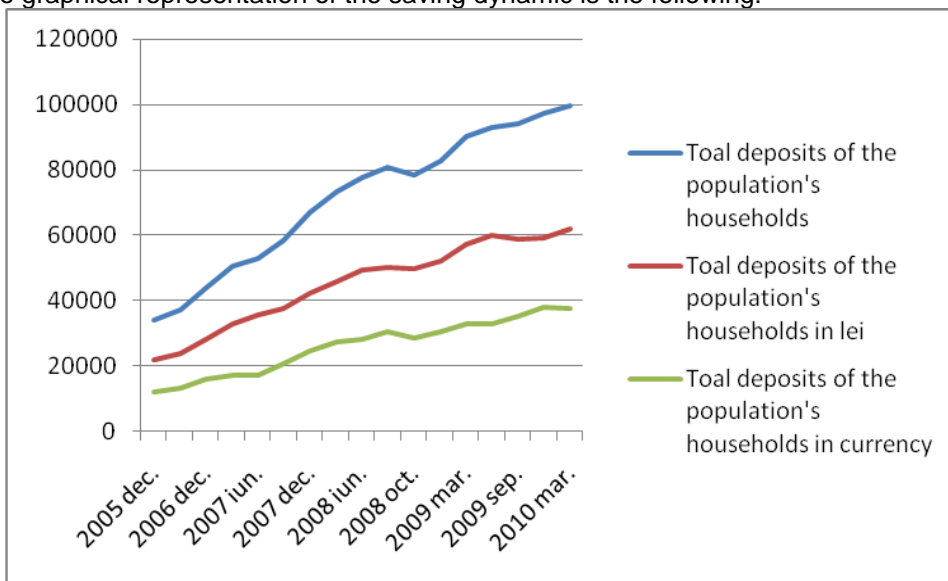
Therewith, the tendency towards foreign currency saving gained a traditional character in our country after 1989. In an economy where euro reference is present in various market segments, the precarious confidence in one's own economy and in the national currency also influences the saving behaviour. The evolution of the two saving components appears as follows:

Tabel no. 1- The evolution of the population's bank deposits (mil.lei; end of period)

Period	Total deposits of population's households	out of which			
		in lei	% of the total	in foreign currency	% of the total
Dec. 2005	34227.6	22014.7	64.3	12213.0	35.7
Jun. 2006	37377.8	24130.8	64.6	13247.0	35.4
Dec. 2006	44124.0	28174.3	63.9	15949.7	36.1
Mar. 2007	50533.7	33049.5	65.4	17484.3	34.6
Jun. 2007	53185.4	35770.0	67.2	17415.3	32.8
Sep. 2007	58546.2	37722.2	64.4	20824.0	35.6
Dec. 2007	67315.6	42415.1	63.0	24900.4	37.0
Mar. 2008	73273.2	45846.6	62.6	27426.6	37.4
Iun. 2008	77929.6	49655.3	63.7	28274.3	36.3
Sep. 2008	81085.1	50316.2	62.1	30769.0	37.9
Oct. 2008	78611.0	49980.7	63.6	28630.3	36.4
Dec. 2008	82879.7	52394.3	63.2	30485.4	36.8
Mar. 2009	90145.9	57269.3	63.5	32876.6	36.5
Iun. 2009	93153.7	60044.2	64.4	33109.5	35.6
Sep. 2009	94271.2	59014.9	62.6	35256.3	37.4
Dec. 2009	97305.1	59197.1	60.8	38108.0	39.2
Mar. 2010	99751.4	62055.0	62.2	37696.4	37.9

Source: NBR Monthly Bulletin;

The graphical representation of the saving dynamic is the following:



"Approximately 40% of the natural persons' saving is realized in foreign currency, this level maintaining its value relatively unmodified (between 35 and 45%) during the last seven years, in spite of the convergence process undergone by Romanian economy and of the increase of over seven times in the population's bank deposits. In addition, the slight (temporary) decrease remarked in 2005 can be attributed to a lower lei equivalent of euro bank deposits, rather than to the factual decrease in the balance account of deposits"<sup>6</sup>.

During the interval taken into account for the calculation, the previous findings are maintained, the foreign currency bank deposits represent on average 38.0% of the population's deposits, slightly increasing except the first trimestre of 2010 when there was a slight decrease, which will probably constitute the tendency of the entire saving process, having to consider the special economic and social situation in Romania. This saving dynamic where

euro currency is preferred is registered in spite of national currency interests with values higher than those of strong foreign currencies. Such an absolutely natural trend of decrease in foreign currency possessions has been observed during the last decade in other countries of Central and Eastern Europe, such as Poland and the Czech Republic or even Hungary, due to the improvement of internal economic conditions. Relatively speaking, at present Romanians make foreign currency placements more than the Czech, the Polish or the Hungarians who own only 5%, 8.2% and 16.7% respectively of the foreign currency funds. From this point of view, Romania is more similar to Albania, Bulgaria or the countries of the former Republic of Yugoslavia.

Regarding saving in territorial profile it is confirmed the correlation between the level of economic development and economic-financial education and the appetite for euro. High weights of such placements are in Bucharest (51.2%), Timis (52.4%), Arad (42.3%), Brasov (42.7%), Sibiu (39.4%), Constanta (40.7%) and other districts in Transilvania, whereas much lower

<sup>6</sup> M. Ion - How should we understand and how profitable is the Romanians' preference for placements in euro?, Staff Only Raiffeisen Bank Magazine, no. 7/2009, page 13

weights are observed in Gorj (15.1%), Ialomița (15.9%), Călărași (16%), Teleorman (18.8%), that is in less economically developed areas dezvoltate that have lower financial resources. It is highly probable that in the areas where the amounts saved are higher some of the customers have a portfolio approach and place part of the money in foreign currency, a thing which is common to a lesser extent in poorer districts.

The higher the number of potential customers of high financial power, the intenser the reaction to changes in the economic environment, taking into account that this category of depositors is the first to adapt its saving behaviour to new circumstances. An eloquent proof is the end of the fall of 2008, when part of the money were withdrawn from the banks during the acutest moment of the financial crisis, generally amounts in euro belonging to Private Banking customers. Still these customers are the first who are now able to show a tendency of saving in euro currency, because of the same reasons.

As for the efficiency of deposits, the calculations of experts regarding the last seven years, 2002-2009, confirmed the advice of NBR officials, as choosing the lei currency proved a lot more beneficial. The output of lei interests could have reached approximately 115%, while deposits in euro would have brought an output of 30%. During the same period of time, the lei currency lost 32% in favour of the euro; consequently choosing lei would have brought a benefit of  $(1+115\%)-(1+32\%)*(1+30\%) = 43\%$  in 7 years. It is true that during some intervals characterized by a dramatic depreciation placements in euro are more beneficial,

but the relatively reduced modification of euro amounts weight in the banking system in the course of time shows that most of the foreign currency depositors would have gained more by lei saving. Most probably foreign currency saving is considered rather a means of protection against currency depreciation than a measure for output optimization and possibly a more convenient way of owning euro savings at the moment Romania will have accessed to the eurozone.

### 3. Conclusions

In 2010 challenges for the banking system will be more demanding than in 2009. The pressure of bad loans will be maintained, and their administration will continue to be the main preoccupation of banks this year. Regarding the population segment, mainly under the pressure of adjustments in the public as well as the private sector, unemployment will probably continue to increase, and the population's income to decrease, thus continuing to pressure the natural persons' capacity of loan back payment. Therefore the amount of the population's savings will register a recoil regarding both lei and euro segments. As we are dealing with a profound economic and financial crisis it is possible that out of the scarce future savings of the population the euro component be beneficial, as it is well known the population's high confidence in this currency, but also the efforts the EU officials are making in order to maintain euro parity in relation to USA dollarul as well as to the other foreign currencies.

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