THE GLOBAL FINANCIAL CRISIS IMPACT OVER THE REFORMATION OF THE FINANCIAL SURVEILLANCE ARCHITECTURE IN EU: PROSPECTS AND IMPLICATIONS

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Abstract:

The current crisis has revealed the existence of certain fundamental weaknesses in the functioning of financial markets and weaknesses in risk management, which require a deep reform of the financial regulatory and supervisory framework. The magnitude of the current crisis has brought new attention to issues of transparency and liquidity of financial systems.

The current crisis is further proof that free markets are not up to the deregulated markets and that excessive confidence in the self-healing powers / regulation of markets is very dangerous. We must keep in mind that financial innovation benefits when supporting dynamism and growth, but at the same time can lead to additional risks.

In the context of maintaining international financial crisis and the consequences of measures taken to counteract its effects, the reconfiguration problem of the supervisory architecture and how it should ensure the smooth functioning of global and regional financial markets came to the attention of public authorities responsible to issue regulations, best practices and rules in areas which exert a significant influence in achieving this objective.

This paper focuses on the structural causes of the current global crisis expressed by several authors and their views on the need to implement new supervisory architecture internationally and regionally, to ensure global financial stability.

Keywords: financial crisis, financial system, the new architecture of financial supervision, systemic risk.

JEL clasification: G01, G21, G28

INTRODUCTION

The U.S. mortgage securities market with high-risk (sub-prime), in August 2007 was blocked because speculators have started to adjust their respective positions and sell assets, a situation favored by inadequate regulatory framework. This laid the groundwork for further processing into a globally devastating financial crisis which is currently in progress.

Although for a while now, signals were given by some economists about the crisis, they were not taken into account. The magnitude of the global financial crisis was underestimated by everyone until the autumn of 2008.

In light of these realities, governments and central banks in the U.S. and some European countries have responded by taking measures to counter the international financial crisis. Application of these measures has led to loss of confidence among financial market participants who remained non-transparent and thus amplified the financial crisis and ultimately favored its passage in the real sector of economy.

The purpose of this paper is to identify the main causes that triggered the current crisis, confirmed in the literature and then consider whether implementation of the new architecture of financial supervision in the EU, proposed by the Larosiére Report in order to prevent systemic risk in the future learning lessons from the global crisis.

1. APPROACHES ON THE CAUSES OF THE CURRENT GLOBAL FINANCIAL CRISIS

In most cases, financial crises have a habit of coming in waves (Nouriel Roubini, Stephen Mihm, 2010, p.178) and the severity of it has recorded a tidal movement, in the fewest cases it only hits once and then finally mellows. They look like hurricanes that it is stronger, then weak for a while, after which they may gain more destructive power than before. The authors show that the weaknesses that accumulate in preparation for a major crisis penetrate in all directions and are systemic. They cannot be cured by a single bank failure or rescued by the implosion or even a portion of the entire financial sector.

According to the teacher (Daniel Daianu, 2009, p.16), the current financial crisis that hit the center of world finance is "a decisive refutation of the paradigm that glorifies the total deregulation of economies, be they rich or poor." He argues that at its root is

Also, signatories of a letter including Professor Daianu, published on the 22 May 2008, in the French daily "Le Monde", and on 29 May 2008 in Dilema Veche, in Romania showed that "the current financial crisis is no accident. It was impossible to predict, as now claimed not a few politicians and important people in the financial business. This crisis is in fact a market failure of too little or not covered financial markets and shows once again that financial markets cannot govern alone.

It also points out that the current crisis is reducing the ability of the Western World to improve dialogue with the rest of the world in terms of global challenges and particularly the management of the effects of globalization, given that Asia's extraordinary economic progress represents a real unprecedented challenge. They require to the EU's policy makers to come up with a concrete answer to the current crisis, both at Community and national level.

Crotty, J. and Epstein (2008) identifies the same fundamental structural weakness of the U.S. financial system that led to the crisis. An architecture dominated by neoliberal policies based on liberalization, regulatory and a market waiting for a natural adjustment. The authors consider that the main weakness of the system is inadequate reglementation or lack of rules governing commercial banks, investment banks and of the shadow banking system (shadow banking system), which is thinly capitalized. Also, another weakness is to provide incentives for people with leadership positions in the financial system that have taken excessive risks, aiming only financial performance.

Financial innovation in the last two decades is one of the main causes that triggered the financial crisis because it was based on irrational exuberance of individuals. During these operations, large banks have played a key role as „financial wraps" and are thus diversifying and spreading risk. Former head of the Federal Reserve (FED) (Alan Greenspan, 2008), argues that no risk model / econometrics cannot properly capture all the features that define the complexity of real systems.

The current financial crisis has its roots in much deeper causes of core, such as macroeconomic and microeconomic in nature, which were in interconditioned in the production of the crisis, as NBR's governor shows (Mugur Isarescu, 2009, p.2). The cause of deep financial crisis is considered abundant liquidity created by major central banks of the world (FED, BOJ) and the willingness of oil and gas exporting countries to limit currency appreciation. Also, at the level of some countries (China, Southeast Asia) has shown super-saturation with savings as a result of their increasing integration into the global economy. Supersaturated with abundant liquidity and savings created the possibility of guiding the available resources to investments, including sophisticated financial instruments that are not understood by all investors.

In this context, the investor's appetite increased for assets with high returns and low market volatility has led to the underestimation of the risks they are exposed. Also, there were a number of microeconomic cases: frenzy securitization, which led to the credit market hazing, cracks in the business model of rating agencies, and an intense activity for international deregulation.

In addition to the foregoing, in our opinion, we believe that these operations helped the underestimation of the risk, maintained the old regulatory structures and the use of poor risk management practices. Thus, regulators and supervisors have been overcome by innovations in the markets, fueled by excessive liquidity, which caused them to meet investor's earnings. In conclusion, we find that in most approaches there are treated the non-traditional factors in particular, that are specific to the global financial crisis.

Unfortunately, the effects of the international financial crisis have spread over the economy of Romania, on multiple channels (Isarescu, 2009).

Thus, through the commercial channel, which has meant since 2009 - 2010, a drastic reduction in exports, through the financial channel, limiting access to external financing, reducing the volume of loans, through the exchange rate channel, reducing external financing has reflected the currency depreciation (of a course for 3,4 RON/ EURO in the first half of 2007, at a rate of 4.3 RON / EUR, in the first half of 2010), through the reliability channel, where there was a reduction of Eastern European investors (an event on the monetary market- exchange of moments of panic and speculative attacks - October 2008) and through the effects of wealth and balance sheet channel where we are faced with the deterioration of the net assets of people and companies.

It is necessary to specify that there are some similarities and differences when talking about financial and economic crisis in the developed and emerging countries including Romania (Liviu Voinea, 2009, p.36) if we consider the structural causes and the mechanisms of transmission and adjustment. We really have two crises: one that erupted in the U.S. and expanded on account of toxic assets from non- U.S. banks, in developed countries like Britain, Germany, France, Japan and another crisis, triggered by too much account deficit, specific to emerging economies, some new EU member states and Euro zone countries, like Greece, Spain or Ireland, where we can speak of an economic crisis. In Romania, the economic crisis is internal, it would have occurred even without the U.S. financial crisis and because the causes and mechanism of transmission are different, also the measures of response to the adverse effects of the crisis may not be similar in Romania to those in U.S. or in some European countries.

2. NATIONAL MEASURES DISPOSED FOR THE DIMINUATION OF THE CRISIS EFFECTS

In order to minimize the effects of the financial crisis, EU authorities have acted in two stages. Thus, in a first stage, a number of states have adopted a gradual approach, combining intervention tools for monetary policy actions aimed at improving liquidity and ad-hoc interventions with specific actions to rescue financial institutions in difficulty. Since these interventions had no effect on restoring confidence in the financial system it has moved to implement measures under the second phase, these rescue packages at the financial system level, which had a much more comprehensive effect.

The solutions proposed to overcome the financial crisis of solvency were the combination of three essential elements: guarantee obligations, recapitalization of the institutions which were in difficulty but solvable and the separation of assets with problems.

The measures provided for reducing the national crisis contributed in part to restore the financial market's stability for liquidation the interbank markets and capital deficit reduction. However, financial markets have not completely recovered to the normal situation, needing for further concerted measures at European level, involving the intervention of the government's members, central banks and the European Commission.

3. THE IMPLEMENTATION OF THE NEW EUROPEAN ARCHITECTURE FOR FINANCIAL SUPERVISION

In response to financial turmoil in the years 2008 and 2009, several actions have been taken, both short and long term, as follows:
a) in October 2008 it was adopted a plan of concerted action, which included a series of temporary measures (funding to ailing banks with additional capital in financial institutions, recapitalization of banks with problems, raising the minimum level of guaranteed deposits from 20,000 Euros to 50,000 Euros);
b) it has called for better coordination of fiscal policies from Member States to counter the recession by building an economic recovery plan, which is based on two pillars. The first pillar has targeted a cash injection to boost demand in the economy and boost confidence, and the second is based on the need to act to revive short-term European competitiveness;
c) the adoption of the European Commission of their Work and Legislative Program in 2009, has two outstanding strategic initiatives, namely:

- a package of measures for reforming the financial sector;
- a review of Lamfalussy "Architecture" and the consolidation of the arrangements for financial stability and strengthening at EU level;

In this respect, the European Commission has mandated a group of experts (High Level Expert Group on Financial Supervision) chaired by former IMF Managing Director Jacques de Larosiere, which aimed to make recommendations on strengthening the supervisory arrangements in the European Union in terms of efficiency and integration between all components of the financial system.

In Lorasiére Group Report it was presented a comprehensive analysis on the causes of the current financial crisis and a set of recommendations both for improving the EU regulatory framework and restructuring the current architecture of prudential supervision achievement - the creation of a European System surveillance and crisis management.

The reform which experts suggest is composed by two areas:

- Prudential supervision;
- Micro-prudential supervision.

Thus, for the macro-prudential supervision it has been proposed the establishment of the European Council for Systemic Risk (systemic Risk The European Council - CESR) under the guidance and logistical support of the European Central Bank.

The new body will ensure the collection and analysis of information relevant to financial stability, macroeconomic conditions and corresponding macro-prudential developments in EU financial area, will regularly exchange information with the supervisors of micro-and will provide early warnings about the systemic risks can accumulate and if necessary, recommendations on measures needed to manage those risks.

Given that the risks are alarming, CESR will work with the European Commission to identify appropriate solutions. Also, globally, CESR will work with the International Monetary Fund, with the G20 and the Financial Stability Forum. Regarding the micro-prudential supervision the European Union considers necessary to establish a European System of Financial Supervision (ESFS) to ensure supervision of financial institutions. The new system will result in the transformation of the Level 3 committees with an advisory role (CEBS, CESR, and CEIOPS) in three new European authorities, as follows: the European Authority for Banking, the European Authority for Securities and the European Authority for Insurance.

The new micro-prudential supervisors will take over all functions from level 3 committees and in addition will have additional powers, namely:

- Developing proposals for technical standards, having regard of the principles of better regulation;
- Abilities of mediation between national supervisors (resolving cases of disagreement between the national supervisory authorities, under legislation that requires them to cooperate or to reach an agreement);
- Helping to ensure consistent application of the Community's technical rules;
- Licensing and supervision of specific institutions at EU level (for example, the European Authority for Securities and Markets will have direct supervisory power of credit rating agencies);
- Mandatory cooperation with the CERS to ensure appropriate macro-prudential supervision;
- A coordination role in emergency situations.

Compared to the draft reform of prudential supervision at EU level have been many opinions expressed.

As regards the European Council's position, it considers the recommendations from the Lorasiére Report to improve regulation and supervision of financial institutions in the EU. The European Commission's adoption of the important package of draft laws to create new European supervisory authorities strengthened the financial sector, the European Commissioner for Economic and Monetary Affairs Joaquin Almunia argued: "the creation of a European Committee for systemic risks in order to detect and prevent risks related to financial stability in the EU and new mechanisms to improve surveillance at an institutional level will greatly help to correct imbalances in our financial systems and the correction of weaknesses in our system of financial supervision are at least partly responsible for financial crisis".

In our view, reforming the current EU supervisory architecture is a priority, especially given that the current financial crisis has highlighted weaknesses in the supervisory framework at Community level.

The proposal to establish a Pan-European authority in the EU, with the political support of the Member States and based on the Lorasiére Report is a way to remedy the shortcomings in the European financial supervision and will help prevent future financial crises.

We consider very important functions assigned to the three new authorities at micro level, in particular the role of coordinator in emergency situations.

This new system should ensure the protection of European taxpayers in situations such as those occurring in the autumn of 2008 and may inspire the creation of one worldwide.

CONCLUSIONS

In the current global crisis, sophisticated risk management methods specific to the banking sector, promoted by Basel II have shown their limits. Therefore, there must be addressed new prudential regulatory reforms and measures proposed by the Basel III, with its emphasis on the early warning component of the risk of escalation.

In this sense, we consider of utmost importance the need for better regulation in all areas, from the rethinking of market structure, risk management and control activities of rating agencies and the remuneration of managers, especially those in the banking sector.

Governments, central banks and supervisory authorities of financial markets should ensure that recent history will not repeat and that economies are entering a phase that would benefit from a sound financial system, and effective solvent.

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