RESEARCH PAPER | Management | Volume : 4 | Issue : 2 | Feb 2014 | ISSN - 2249-555X

Indian Journal Of Applied Research

Going Concern in Actual Banking System – An Accounting Approach in the Context of Financial Crisis

KEYWORDS: Going concern, financial reporting, financial crisis, accounting policies

Ph.D Elena Dobre

Ovidius University Constanta, Romania

ABSTRACT *Financial reporting in any banking activity is the most efficient way to serve public interest. Nowadays, attention is focused on going concern in the context of crisis effects. This paper is about the application of going concern principle in banking accounting and financial reporting. One of the first parts of a larger project we try explain the mechanism of implementing new regulations in this field.*

Research question is to discover the effects implementation of IFRS. Empirical study is based on financial disclosure made by Romanian subsidiaries of foreign banks. The qualitative approach follows the critical research method. The core paper is "going concern" as accounting policy in the context of effects of global financial crisis. The findings are valuable by reliving critical aspects and risks and are quite interesting for professional groups banking managers, accountants and also for students or trainees.

Introduction

Romania became member of European Union in 2007 and is planned to become member of Euro Zone beginning 2015. This membership opened new development opportunities, but also reforms in all fields' activity, including banking financial reporting harmonization. This new implementing brings new challenges in adaptation at less the shape of design and mechanism of provide expected compliance results. So, became interesting and necessary to study the effects of these processes taking in consideration the local specificity.

Romania features and macro banking indicators

Located in the South-eastern 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), Romania is neighboring with 5 countries: Bulgaria, Hungary, Moldova, Serbia and Ukraine. Area measures 238,391 sq. km (ranking 12th in Europe). Population means 21.3 million inhabitants in 2012 (ranking 9th in Europe). Capital city is Bucharest with 1.9 million inhabitants. Romanian leu (RON) is national currency which has full convertibility with reference currency euro (EUR). RON is the functional currency of banking system cause is the currency of the primary economic environment. Exchange rate is set in the interbank "forex" market on a daily basis. The exchange rate used for translating foreign currency balances was: USD 1= RON 3.3393; 1EUR=4.3197, for 2011; USD 1= RON 3.3575; 1EUR=4.4287, for 2012; USD 1= RON 3.2551; 1EUR=4.4847, for 2013.

The European integration and reform delivered rapid growth. Between 1995 and 2007, Eastern Europe, including Romania, grew faster than all other emerging market regions, with the exception only of China and India. Romania has a vast economic potential and has successfully stabilized its economy after being hard hit by the crisis. In the space of three years, Romania reduced its fiscal deficit by more than 6 percent of GDP. Strong cooperation and partnership has also been a hallmark of Romania's successful stabilization [5]. Data released by National Bank of Romania indicates broad money (M3) amount and evolution up 0.5 percent in real terms month on month comparison and 6.4 percent (4.5 percent in real terms) in year on year comparison [3] (Table 1 about here).

Table 1 Monetary aggregates (30 Nov 2013 provisions 2013)

Monetary aggregates	RON mill.
M1 (narrow money)	97,746.1
Currency in circulation	34,226.9
Overnight deposits (current accounts,demand deposits)	63,519.2
M2 (intermediate money)	234,700.0
M1	97,746.1
Deposits with an agreed maturity of up to and including two years (includes also deposits redeemable at a period of notice of up to and including three months)	136,953.9
M3 (broad money)	234,979.6
M2	234,700.0
Other marketable instruments (repurchase agreements, money market fund shares and units, marketable securities with a maturity of up to and including two years)	279.6

Source: http://www.bnr.ro/Press-releases-1104.aspx

Non-government loans and deposits of non-government resident customers are presented below (Table 2 about here).

Table 2 Non-government loans and deposits (30 Nov 2013 provisions 2013)

Non-government loans	RON mill.
Non-government loans (total)	219,703.7
RON-denominated non-government loans:	85,833.7
- household loans	34,737.1
- corporate loans	51,096.6
Deposits of non-government resident customers	RON mill.
RON-denominated deposits of residents:	134,976.8
- household deposits	79,213.5
- corporate deposits (non-financial corporations and non-monetary financial institutions)	55,763.3

Source: http://www.bnr.ro/Press-releases-1104.aspx

Situation of credit institutions, total net assets, impaired loans and loans to deposits ratio (Table 3 about here).

Table 3 Aggregate indicators for credit institutions (30 Nov 2013 provisions 2013)

INDICATORS	Sep 2012	Sep 2013	%
Number of credit institutions	41	41	
Total net assets (RON bill.)	373.5	353.6	94.67

Volume : 4 | Issue : 2 | Feb 2014 | ISSN - 2249-555X

Assets of private-owned institutions (% in total assets)	90.7	92.0	101.43
Assets of foreign-owned institutions (% in total assets)	81.3	90.6	111.43
Capital Adequacy Ratio (≥8%) (%)	14.67	13.92	94.88
Leverage Ratio (%)	8.30	7.49	90.24
Impaired loans (% in total loans)	11.66	12.42	106.51
Impaired loans (% in total assets)	6.94	7.32	105.47
Impaired loans (% in total debt)	7.77	8.21	105.66
Loan-to-Deposit Ratio (%)	120.69	111.50	92.38
Credit Risk Ratio (%)	26.78	31.77	118.63
Non-performing Loans Ratio (%)	17.34	21.56	124.33

Own processing on Source: http://www.bnr.ro/Press-releases-1104.aspx

The period on period comparison show an increase of impaired loans ratio with 6.1 percent and non-performing loans ratio with 24.33 percent. In the same time the loan to deposit ratio is decrease with 7.62 percent. This is an already usual characteristic feature of global financial crisis in banking system.

New challenges on short term for the banks

All this indicators studied above are provided by central bank and nowadays, increasing the role of central banks has created the false impression that these institutions can solve all economic problems [1]. In this context, the critical issue for the future of the banking industry is to wisely use the opportunity brought by the financial crisis in order to perform a major overhaul to ensure its efficiency and performance over the next decades. But, new challenges arise on short term for the banks around the world and these elements will weigh on the business model and on their contribution to growth [4]. One of them is the test for the banking industry to survive the deleveraging process. European Central Bank statistics are showing that outstanding loans to non-financial sector remains negative on annual growth rates, i.e. -2.3% in 2012, -3.8% in 2013. Emerging countries like Romania are among the first ones to receive the full blow in case of a messy deleveraging. Until now foreign banks have repatriated around 26.2% of their exposure, amounting to around EUR 5 billion.

As a conclusion, the long term financing is becoming a priority for Romania and all EU member countries. It's necessary to take into consideration the diversity, the business model and the risk profile of each bank and the specific situation in each country when implementing the new regulations. But, which are the threats of Romanian banking corporate governance in the context of new regulations regarding financial reporting, according IFRS as adopted by the European Union, instead Romanian Accounting Standards? This is the research question!

Going concern as accounting policy in the context of effects of global financial crisis

Romanian banking accounting is aligned on IFRS requirements which became basis of preparation of closing financial statements. IFRS was adopted by National Bank of Romania Order 27/2010, amended lately. The most important difficulties are about fair value accounting valuation and the intricacy of financial instruments such as derivatives. In this respect, the financial statements have been prepared under the historical cost convention as modified by the reevaluation of available for sale investments (through other comprehensive income), trading securities and derivative transactions at fair value through profit and loss account. For 2013, was needed to understand the fair value in light of IFRS 13. Fair value is a market-based measurement, not an entity-specific measurement [2].

Our case study research focus on public data provide by financial disclosure of subsidiaries of foreign banks such Piraeus Bank Romania SA.

This is one of subsidiary of Piraeus Group Bank registered in Greece. This theme is representative in Romanian banking system, because there are many others Greek subsidiaries such as Banc Post SA. So, it deserves to be presented as a Group and its international operations.

Piraeus Group's presence abroad is mainly focused in SE Europe and Eastern Mediterranean. The main cross-border business activities regard retail banking, large-business banking and capital management and treasury. The Group's international network included 449 branches, versus 499 in 2011. Es an effect of crisis, staff numbers were reduced by 402 people, at 6,232 from 6,634 at year-end 2011. The Group has complete branch networks in Albania, Bulgaria, Romania, Serbia, the Ukraine, Cyprus and Egypt, and one branch in London and Frankfurt. Bank policy in international operations was adopted to each country's unique conditions, but focused on deposit growth, preservation of loan portfolio quality and reduction of operating costs.

Piraeus Bank Romania was established to cover the needs of Greek businesses operating in Romania, but it quickly to all bank sectors for local businesses and households and developed into an important bank in the country. Piraeus Bank Group has been present in Romania since 2000, and its network numbered 167 branches witch placed particular emphasis on:

- efforts towards high quality customer retention and expansion of deposit base;
- reduction of costs and enhancement of operating efficiency;
- network restructuring with cease of operation of 34 branches;
- careful liquidity management;
- effective management of portfolio quality.

About the portfolio quality in 2012 customer deposits amounted to €896mn from €915mn in 2011. Group gross loans amounted to €3,052mn in 2012 from €3,002mn in 2011.

Going concern as accounting policy is presented by Piraeus Bank Romania SA as part of Notes to the Financial Statement in Annual Report 2012 [6], in terms of cause and effect approach and includes:

- Impact of the economic crisis and situation in Greece;
- Position of the Group regarding European factors providing support to the Greek economy and Greek banking sector;
- Position of the Bank regarding funding solutions and management confidence in a going concern in the foreseeable future.

In this matter, some issues are important for demonstrate difficulties as threats and others providing support factors as opportunities. It deserves to take in consideration the impact of the economic crisis focusing on Greece situation and the position of the Group and also, the position of the Bank.

Since late 2009, fears of a European sovereign debt crisis developed among investors as a result of the rising government debt levels, together which a wave of downgrading of government debt in some European states. The three countries most affected by this were Greece, Ireland and Portugal. Greece entered into a new restructuring with the European Commission, aimed at bringing the country's public debt-to-GDP ratio below 120% by 2020. On February 2012 the Euro-area finance agreed a "bailout", including financial assistance and forgiving 53,5% of the face value of Greek debt. The new Greek government bonds were recognized at fair value, based on market quotes.

Piraeus Bank Group has incurred substantial impairment losses as a result of the Hellenic Republic's debt restructuring and it is affected by the ongoing economic variability to risks.

The economic situation in Greece, though improving fiscally, still remains the main risk factor for the Greek banking sector in general. Negative developments in this area may signifi-

Volume : 4 | Issue : 2 | Feb 2014 | ISSN - 2249-555X

cantly affect the Piraeus Bank Greece' liquidity, the quality of its loan portfolio, its profitability, and ultimately, its capital adequacy. Despite the risks existing in the Greek banking system, certain factors provide support to the economy and the Greek banking sector and shall therefore be taken into consideration, as opportunities:

- The recapitalization and restructuring;
- The availability of additional capital, if necessary;
- The financial support mechanism from the International Monetary Fund and European Union;
- The capability to raise liquidity through the Euro system.
- The intention of Greek Authorities to strengthen the Greek economy.
- The strengthening of the Piraeus Bank Greece' position in the banking sector and the enhancement of its funding access.

Taking into consideration the above factors, management estimates that the Group will continue in operational existence for the foreseeable future. Accordingly, the annual consolidated financial statements of Piraeus Bank Greece have been prepared on a going concern basis.

Piraeus Bank Romania does not rely on additional funding from the Parent bank but predominantly on locally collected deposits. The management is confident that these critical accounting estimates and judgments are adequate. Is also confident that the main shareholder Piraeus Bank Greece, the parent of the Group of entities which the bank belongs to, will continue to provide the necessary financial support to the bank and related parties with which the bank has significant intra-group transactions, for at least 12 months from the date of approval of these financial statements. On this basis, the management believes that the Bank will be able to continue operating as a going concern in the foreseeable future.

Conclusions

The Piraeus Bank's financial statements at the end of 2012 have been prepared based on the going concern principle, which assumes that will continue to operate in the foreseeable future, especially due the locally collected deposits. This is yet a great potential for essential banking activity. The confidence that critical accounting estimates and judgments are adequate, the management of the Bank is also confident in future financing provide in intra-group transactions. As a final conclusion, the long term financing is becoming a priority for Romania and all EU member countries. About Romania, we are proud by IMF officials' characterization: Romania is both undeniably unique, yet also profoundly European. As part of the European family, as part of the global community, Romania can go from strength to strength.

REFERENCE

[1] Cerna S., The role of central banks: Unforeseeable future, ECONOMISTUL, Nr. 47-48, dec 2013 | | [2] Dobre E., Fair Value Measurement Of Financial Instruments in Banking Accounting System, The International Conference GLOBAL ECONOMY UNDER CRISIS, Dec, 2013, Ovidius University Constanța | | [3] http://www.bnr.ro/Press-releases-1104.aspx | | [4] http://www.bnro.ro/Banking-for-the-Future-CA-BNR-10213.aspx | | [5] http://www.imf.org/external/np/speeches/2013/071613.htm | | [6] http://www.piraeusbank.ro/Bank/About-us/Piraeus-Bank-Romania-En/rez_fin_en.html