

# The Capital Market in the Context of the Integration within the European Union

■

**Gabriela Anghelache**

*Ph.D. Professor*

Academy of Economic Studies, Bucharest

***Abstract.** This work is focusing on the main aspects concerning the present stage of the capital market as well as on the perspective of its evolution after the adhesion to the European Union.*

*After emphasizing the main characteristics, the material is analyzing the financial instruments market – Bucharest Stock Exchange, Monetary-Financial and Commodities Stock Exchange Sibiu, RASDAQ market as well as the collective placement organisms.*

*Finally, there are the main tendencies of the capital market which are pointed out.*

**Key words:** stock exchange; financial instrument; RASDAQ market; depositary; transaction.

■

## 1. Main characteristics

A modern economy, competitive and capable to line up with the present requirements of the globalization process, is not to be conceived without the existence and functioning of an efficient capital market.

The establishment of the capital market in Romania had, as a starting point, the re-setting in 1995, after a brake of about five decades, of the Bucharest Stock Exchange, as a continuous market whose mechanisms are in the position to secure the price forming for equities under transparency conditions and in conformity with the European standards.

The following steps may be considered as the main moments marking, as from 1994 on, the establishment and the development of the capital market in Romania:

- Enforcement, in 1994, of the first law of the capital market, respectively the Law no. 52/1994 concerning the equities and stock exchanges;
- Re-establishment of the Bucharest Stock Exchange, in 1995, when a number of 24 equities companies, members of the Stock Exchange Association, applied for the right to negotiate shares issued by a number of 6 commercial companies;
- Setting-up, in 1996, of the RASDAQ market, meant to secure transactions on shares issued by a very large number (over 5000) commercial companies, resulting out of the Mass Privatization Program;
- Changing the legislative frame, in 2002, by enforcement of a legislative package including four laws:
  - ◆ The law concerning equities, financial investment services and regulated markets;
  - ◆ The law concerning the organisms of collective placements;
  - ◆ The law concerning the regulated markets of goods and derivatives;
  - ◆ The law concerning the approval of the Statute of the National Commission for Equities;
- Drawing-up, in 2004, an unique law, the Law no. 297/2004, concerning the capital market, in order to implement the community acquis to the financial sector, as well as the adoption, within the period 2004-2006, of the necessary regulations meant to allow the application of this law.

As from 2005 on, the capital market in Romania entered a process of profound reconstruction which represents the very foundation of its future development, in the context of the integration of Romania within the European Union. The Bucharest Stock Exchange changed its juridical form, becoming a shareholding company instead of institution of public interest.

The capital market Authority in Romania is the National Commission of Equities, which is regulating, supervising and controlling the capital market, as well as the specific institutions and operations of this market.

The access of the equities issuers and investors on the capital market is achieved through *intermediaries*. There are the financial investment services companies (SSIF) as well as the crediting institutions authorized by the National Bank of Romania to carry out, directly, financial investment services on the capital market. The intermediaries activities is carried out according to the “*unique passport*” principle, implying the possibility for the financial investment services suppliers to operate on the markets of the member-states on the basis of the authorization granted by the country of origin, as well as the free access of the suppliers of investment services from the other member-states to the national market. As from January 1, 2007, i.e., as from the moment of the adhesion of Romania to the European Union, the intermediaries authorized in Romania may provide services in the member-states of the European Union, without any additional authorization, while intermediaries from other member-states may provide services in Romania on the basis of a simple notification submitted to the market authority.

The capital market in Romania is structured by two main: the financial instruments market and the market of the placements being done through organisms of collective placements.

## 2. The financial instruments market

The transactions on financial instruments are achieved in accordance with the European Union standards on regulated markets and the alternative systems of transactions securing, meantime, the finality of all transactions through only one institution meant to

accomplish the storage, the offsetting-discounting and the recording of the operations on equities.

Presently, there are two regulated markets being authorized and in function, namely: *Bucharest Stock Exchange* and *Sibiu Monetary-Financial and Commodity Exchange*.

The activity of a regulated market is organized and administrated by a *market operator*, set-up as a shareholding company. The regulated market is considered to be a system for transactions on financial instruments which is functioning regularly and operates in an ordered manner, being characterized by the fact that the issued regulations define the conditions of functioning and access on the market as well as the conditions for admittance for transactions of a specific financial instrument. The issuers whose equities are transacted on a regulated market are bound to BVB requirements of reporting and transparency, in order to protect the investors and insure their correct, complete and in due time information.

The transparency requirements are referring to both, the pre-transaction and the post-transaction operations. Thus, under the pre-transaction context, the market operator must put at the disposal of the public, in a continuous manner, all over the duration of the transactions normal program and under reasonable commercial terms, the current prices and quantities for sale or for purchase for the financial instruments being accepted for transactions on the respective market. As to the post-transaction operations, the market operator must transmit, in real time, information regarding the price, the volume and the moment the transaction is executed, according the specific rules governing each financial instrument being accepted for transactions on the respective market.

*Bucharest Stock Exchange (BVB)* is disposing of a performing system of transaction, consistent with the one run by the stock exchanges of the developed countries which allowed the number of investors to increase, along with the diversification of the transacted instruments and types of operations as well as drawing of new issuers of developing potential on medium and long term. Contrary to the beginning, when the stock exchange represented a shares market, presently there are also transactions on bonds issued by both the local public authorities and commercial companies.

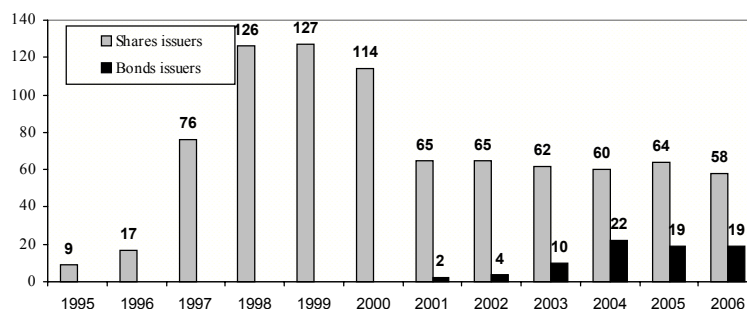


Figure 1. Evolution of the issuers' number listed by the Bucharest Stock Exchange quota within 1995-2006 period

The year 2002 has been considered as the moment of the sudden change for the better of the stock exchange activity, on the ground of the re-launch of the economic activity and a legislation becoming more transparent, more flexible and better adjusted to the national specificity of the capital market.

The following graph is illustrating the evolution of the stock exchange capitalization which, in 2006, counted with 30% higher as comparatively to the previous year, in the context of the increase of shares quotation to the stock exchange as well as the increase of the volume of the transacted stock.

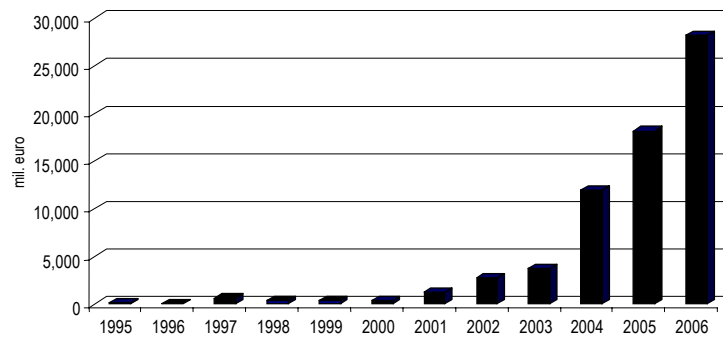


Figure 2. Evolution of the Bucharest Stock Exchange capitalization within 1995 – 2006 period

If one considers its weight in the gross domestic product, the stock exchange capitalization recorded a steadily up-warding evolution during the last six years. If in 2000, it represented 1.37% of GDP, only, in 2004 it reached a weight of 13.86% while in 2006 the stock exchange capitalization exceeded 24% of GDP. The evolution of the ratio stock exchange capitalization/gross domestic product is shown by the following figure.

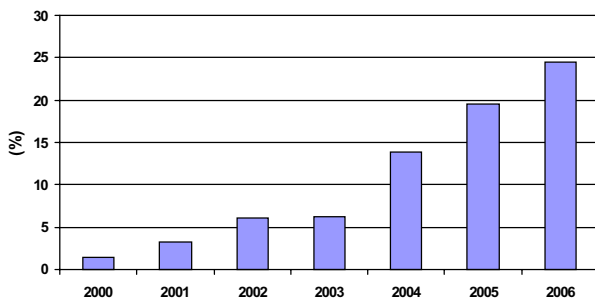


Figure 3. Weight of the stock exchange capitalization within 2000-2006 period

The policy run by CNVM as regards the development of the capital market is targeting for 2007 a stock exchange capitalization amounting 30% of GDP. The target is a realistic one under the circumstances of the increase recorded by the number of transactions and the diversification of the financial instruments being transacted at the stock exchange. Drawing new financial flows from resident and foreign investors, on the ground of a positive evolution of the entire Romanian economy, represents the warranty for an up-warding evolution of all the stock exchange indices. All these statements are confirmed by the fact that during the first quarter 2007 only, the capitalization of the Bucharest Stock Exchange reached an amount of EUR 24,296.6 millions, exceeding by 13% the value recorded all over the entire previous year.

The total amount of the transactions in 2006 counted for EUR 2,756.31 millions, recording thus a daily average of over EUR 10 millions, as well as an increase of over

30% as comparatively the year 2005.

The Bucharest Stock Exchange keeps on remaining, significantly, a shares market. The evolution of the transactions on bonds is relatively limited even if there are record-transactions being concluded, such as those generated in 2006 by the issue of the bonds of the International Bank for Reconstruction and Development. During the year 2006, there were 19 municipal and corporate bonds being transacted, out of which five represented newly listed bonds.

As an opening for the capital market in Romania, starting the year 2005, the investors took the advantage of dealing, at the stock exchange, with preference rights attached to the newly issued shares by the occasion of the increases of the social capitals.

The activity of any stock exchange is evaluated in terms of stock indices, considered as barometers of the market.

Since the moment of launching the first indices BET and BET – C up to middle of the year 2002, their level kept on remaining below 1000 index points. But, these last years, all indices of BVB followed an up-warding trajectory, recording levels which have been historical maxima.

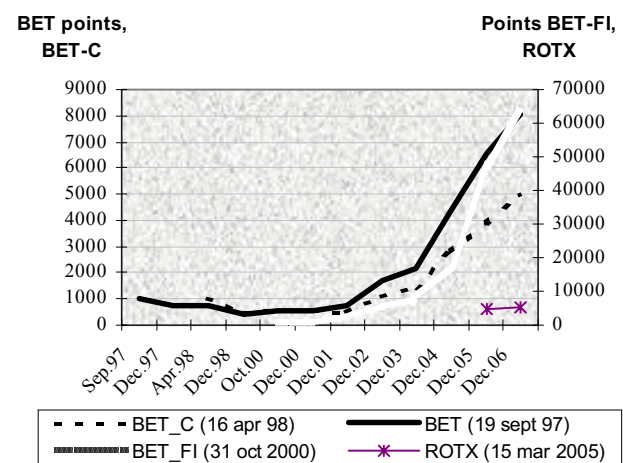


Figure 4. Yearly evolution of the Bucharest Stock Exchange indices

The BET index being computed by the end 2006 counted for 8,050.18 points, 22.23 % over the value recorded during the last day of transactions of the year 2005.

The historical maximum of 5,169.21 points has been reached by the index BET-C in October, being 25.81 % higher than the previous year record.

The most spectacular increase has been recorded by the index BET-FI, the maximum value reached counting for 63,606.97 points in November 2006. Thus, the index BET-FI holds the 21<sup>st</sup> position in the classification of the international stock exchange indices.

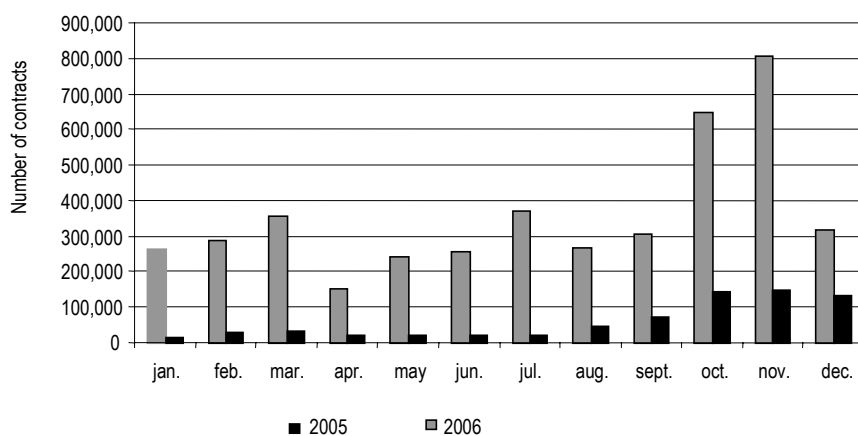
The index ROTX reached a maximum value of 18,809.88 point in October 2006.

The increases recorded by all the indices of BVB took place on the ground of the performances of the Romanian economy and the increase of the autochthonous and foreign investors' confidence in the performances of our market, characterized by more transparency and governed by a modern legislation, perfectly adjusted to the European standards. For the year 2007, once the adhesion of Romania to the European Union took place, the expectation is that the up-warding trend of the stock exchange indices keeps on continuing, simultaneously with the introduction of new stock exchange products.

A particular position in the frame of the financial instruments market goes to the *SIBIU MONETARY-FINANCIAL AND COMMODITIES STOCK EXCHANGE (BMFMS)*, as a regulated market, authorized to organize and administrate *transactions on derivatives*. This market has been established as a commercial company, ever since 1994, and launched the first futures contracts in 1997, while the options on futures contracts started to be transacted since 1998, after the setting-up of the Offsetting Romanian House.

The futures contracts and the options are addressing to the investors both as instruments for covering the risk in case there is an unfavorable evolution of the price for the underlying asset and for the purpose of getting profits on the basis of the arbitrage operations between the price on the spot market and the price on the market at term. The underlying assets of the contracts at term are represented by shares belonging to attractive issuers who are transacted at BVB, stock exchange indices as well as foreign exchange rate (RON/EUR, RON/USD, EURO/USD) and the 3 and 6/ months interest rate.

As far as BMFMS is concerned, the year 2006 meant a year of historical maximum, characterized by a high liquidity, with an up-warding volume of the transactions.



**Figure 5.** Evolution of the total volume of transacted contracts

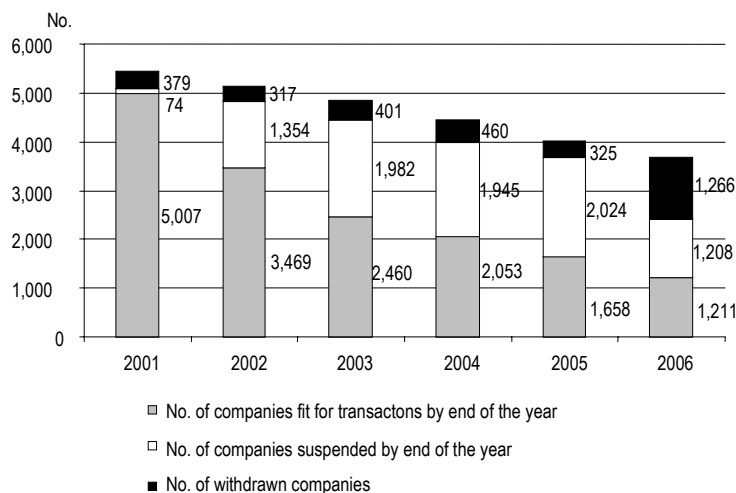
In 2006, the total value of the transactions on derivatives counted for EUR 2,770 millions.

The volume of the transacted futures contracts was 6 times larger in 2006, as comparatively to 2005, while the options contracts doubled within the same period. The year 2006 marked a major difference between the total number of transactions on derivatives having shares as underlying asset (99% of the total) and the one of the transactions on derivatives having foreign currencies as underlying asset (1% of the total).

The derivatives market is subject of a process of development and diversification taking into consideration the increasing need for covering the loss risk run by the portfolio investors.

*RASDAQ* market recorded a continuous transforming process, since it has been established in 1996, up to 2007

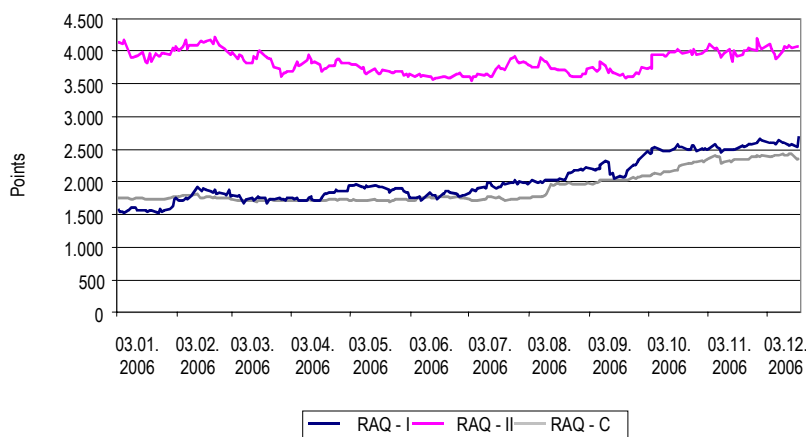
when it started functioning according to the rules of an alternative system of transactions. A significant moment is given by its merge with the Bucharest Stock Exchange, initiated in 2002, when the denomination of *RASDAQ Electronic Stock Exchange (BER)* has been adopted. This is this context which involved the identification of the most attractive companies, grouped by categories of excellence, as a first step towards promoting them the stock exchange quota. Meantime, the number of listed issuers has been gradually reduced, by withdrawing them from the market, based on the decision of the shareholders as well as in conformity with the degree of meeting the listing requirements, so that the number of companies fit for transactions get reduced from over 5,000 in 1996, to about 1,200 in 2007.



**Figure 6.** Evolution of the number of listed issuers on RASDAQ market

On the ground of the decrease on the number of the listed companies, the capitalization recorded by the RASDAQ Electronic Stock Exchange counted for EUR

3,126.44 millions in 2006, as against EUR 1,943.72 millions in 2003.



**Figure 7.** Evolution of RASDAQ indices

The investors who placed the available resources on stocks transacted on the RASDAQ market recorded, during the year 2006, an average yield counting for 22.74%, measured by the evolution of the index RASDAQ – C.

The year 2007 will represent the transformation of the RASDAQ market into an alternative transactions system, in conformity with the legislation in force and aiming to line up with the requirement of the European Union directives.

*The alternative transactions system (ATS)*, links together several parties who buy and sell financial instruments, in a manner which leads to contracts conclusion, being administrated by a *system operator*. As a system operator, there are the authorized intermediaries or a market operator who can act. In the frame of an alternative transactions system there are, basically, the financial instruments belonging to issuers not complying with the conditions of admittance on a regulated market, which are transacted. The alternative transactions system

is on the way to be authorized. This is set up in order to put at the investors’ disposal an organized and transparent framework, required by transactions on stocks belonging to issuers listed on the RASDAQ market.

*The post-transaction operations* due to both the regulated market being operated by the Bucharest Stock Exchange and the alternative transactions system are carried out through the *Central Depository*, authorized to function as a shareholding company. Thus, in order to carry out, in a centralized manner, the operations on stocks and to secure an unitary recording of these operations, all the classes of equities being transacted at the Bucharest Stock Exchange and in the frame of the alternative transactions system are compulsory deposited to the Central Depository. The main operations carried out by the Central Depository are the following: offsetting-discounting the transactions on stocks, recording the new holders and identifying, by any time, of one issuer’s shareholders and their holdings, allocating serial numbers to the equities issues by setting

up ISIN codes, keeping the equities in custody, providing services for the exercise of the rights due to equities as well as management of the guaranties (the collateral) on the equities.

On the derivatives market from Sibiu, the post-transaction operations are carried out by the Offsetting Romanian House, a distinct entity, having as main part to guarantee the good execution of the transactions, through the intermediate of the compensating members, on the basis of a system of multiple levels of warranty: margins – joint warranty fund – individual warranty fund – warranties of the compensating members.

### 3. Collective placement organisms

The second segment of the capital market is given by the *collective placement organisms*, grouped in two main categories: the *collective placement organisms on equities (OPCVM)*, harmonized with the European Union directives, as well as collective placement organisms, other than those on equities, which are not harmonized, being known as the *other collective placement organisms (AOPC)*.

The category of *collective placement organisms on equities* includes the *investment open funds*, established on the basis of a civil contract and the *investment companies*, established by a constitutive act, organized as shareholding companies with variable capital.

The organisms of collective placement on equities have as an unique purpose to perform collective investments, by placing the money resources in liquid financial instruments and by operating on the principle of risk diversification and prudential management. The issue of

the participation assets is achieved on the basis of a continuous public offer, in conformity with the information included by the issuance prospectus, so that the investors may evaluate, mainly, the risks implied by the proposed investment. The participation assets are re-purchasable in a continuous manner out of the assets of the respective organisms of collective placements on equities.

The organisms of collective placements on equities are administrated by investment administration companies (SAI), which entrust to depositaries (credit institutions) all the assets of the OPCVM, which they are administrating, in order to be kept under security conditions.

Presently, in Romania, there are 34 *investment open funds* in function, which are classified in four types of funds: of shares, diversified, of bonds and of fix income instruments as well as monetary. To note that the number of investors increased as a result of regaining the confidence in this type of investment, after the failures of certain funds in 2000, as well as a result of a favorable evolution of the prices for the equities transacted at the Bucharest Stock Exchange. The number of the participation assets in circulation increased also, quite significantly, which is a positive fact attesting that this segment of the capital market changed for the better.

These favorable tendencies are explained also by the fact that the investment open funds have generated superior gains, in comparison with both the inflation rate and the foreign currency investments, being judged through the angle of the evolution of the exchange rate, leu/dollar și leu/euro. The average net unitary value of the participation assets to the mutual funds increased with over 80% all over the year 2006, while the inflation level reached 4.87% only.

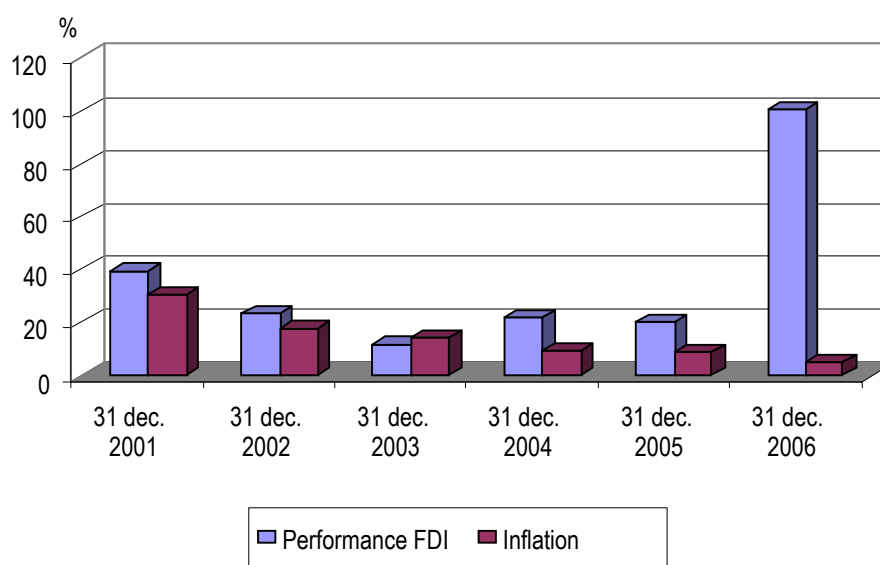


Figure 8. Evolution of the performances of the investment open funds during 2006 against the inflation level

The evolution of the portfolios of the investment open funds, by types of financial instruments, in 2006 against 2005, reflects the orientation of the placements towards equities being transacted on the regulated markets and towards the banking deposits. To underline the fact that the weight of the banking deposits within the structure of the funds assets decreased from 35% in 2005 to 22% in 2006, while the weight of the equities transacted on the regulated markets increased from 25% to over 37% within the same period.

The performance of the investment open funds is evaluated also from the point of view of the evolution of the net assets, which increased in 2006, as comparatively with 2005, by approximately 86%. The net assets have increased significantly as a result of launching new investment open funds and of the increase of the prices for the equities on which the investment was done.

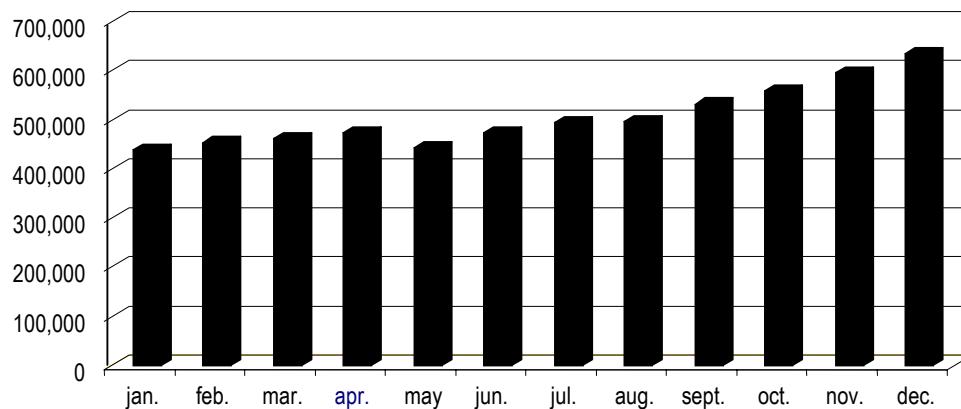


Figure 9. The net assets of the investment open funds in 2006

Out of the 34 investment open funds existing in 2006, the biggest market quota was holds by the diversified funds and by the shares funds.

The non-harmonized collective placements organisms (AOPC) are established as:

- *Investment closed funds*, set-up on the basis of a civil company contract, which are bound to repurchase the participation assets by pre-set intervals of time or by certain dates in conformity with the constitutive documents;
- *Investment companies of closed type*, set-up by a constitutive act, which issue a limited number of shares and are transacted on the market. This category is including the financial investment companies (SIF).

The non-harmonized collective placement organisms are characterized by more permissive legal regulations, they addressing mainly to the investors who accept to undertake the risk generated by a non-diversified portfolio.

The closed investment funds are administrated by an investment administrating company on the basis of specific rules, self-established and may issue funds units of a single kind, registered, dematerialized, which confer equal rights to the holders.

The investment companies of closed type can be administrated by an investment administrating company (such as the case of SIF-Muntenia) or by an administration council (typical for the other four SIFs) and are bound to secure the transactions for the issued shares on a regulated

market, the repurchase of their own shares being also allowed.

The financial investment companies are the sole closed funds being listed at the Bucharest Stock Exchange.

The SIFs management aims to diversify the portfolios by achieving placements of yields as high as possible and low risks, so that the unitary value of the net asset records an up-warding trend.

The price for the shares issued by the five SIFs being transacted at BVB kept on increasing, as a result of the increased interest of the investors for holding this kind of shares bringing in high yield for both the distributed dividends and the gains as difference between the re-selling price and the acquisition price of the respective shares. The performances recorded by the SIFs shares are reflected also by the evolution of the index BET-FI. The diminishing of the difference between the market price of the financial investment companies shares and the unit value of the net assets of these investment funds reflects the fact that the foundation of the investment decision is closely linked to the potential of increasing the assets hold by the portfolios of the five SIFs.

#### 4. Tendencies of the capital market development

In order to achieve the capital market transformation, so that it becomes a viable alternative for financing the national economy, there have been joint steps adopted aiming a correct and complete information of the investors,

the increase of the market transparency, the increase of the investors protection, the insurance of a supervision in real time of the transactions from the regulated markets and the achievement of controlling actions with the purpose to prevent the negative effects and the risks identification. All these steps are meant to secure the consolidation and the development of the capital market.

The Bucharest Stock Exchange is placed on the 4th place within the area, after the stock exchanges from Poland, Czech Republic and Hungary and, as for 2007, it is intended that the gap diminishes. The Bucharest Stock Exchange intends to open a new sector of its activity, by initiating a market section for financial derivative instruments. The first financial derivative instruments which will be transacted on this market administrated by the Bucharest Stock Exchange will consist of futures contracts on stock index BET. Another step meant to improve the market capacities is given by the fact that the shares of the listed companies are possible to be bought by the investors on credit as well, through transaction within the margin, according to the new Stock Exchange Code, entered into force by the end of September 2006.

In 2007, the market of the financial derivative instruments will keep on developing with the same alert rhythm. The number of intermediaries and that of the sophisticated investors who participate to the transactions with derivatives is recording a continuous increase and for 2007 there is a net increase of minimum 20% as to the market participation and minimum 70% as to the volume of transactions to be expected.

As far as the evolution by groups of financial instruments is concerned, there is a more significant increase to note for the futures, which will continue the tendencies already recorded in 2006. The options contracts will have a positive trend as well but the variation of this trend is hard to be predicted presently, as the market is still sophisticated

enough to allow that this financial instruments are used at their full capacity. Nevertheless, taking into account the tendencies of the other European stock exchanges for derivatives, an increase of the transactions on options is to be expected in Romania as well.

On an overall basis, the capital market in Romania will continue the process of development, trying to recover the gap against the European strong markets, this effort being a general and well sustained one. For the year 2007, there is a positive evolution to expect for all the segments of this market. The potential for the future development of the capital market in Romania is a particular one if to consider the fact that, presently, less than 0.05% of the population of Romania is involved in activities on the capital market. It may be estimated that, during the forthcoming years also, Romania will attract significant financial flows, which would be found inclusively in the increase of the weight held by the portfolio foreign investors within the total turn-over of the stock exchange market. On medium and long term, there are conditions already set-up, for increasing the investment belonging to both, residents and non-residents, the participation on the market of the institutional investors being more and more active. As far as the foreign investors are concerned, the opening of the capital market of Romania for the intermediaries registered in other countries members of the European Union might be a good reason for the stock exchange market to become more attractive and more accessible for non-resident individuals. As a result of these possible evolutions, there will be not only liquidity increases to be recorded but also a market volatility more tempered. A better regulated capital market, a correct, complete and operative information of the investing public in respect of the important events, a careful supervising in real time, as well as a more efficient control may offer to the autochthonous and foreign investor the warranty for an attractive and safe placement.

---

## References

Anghelache, Gabriela (2004). *Piața de capital. Caracteristici, evoluții, tranzacții*, Editura Economică, București

Anghelache, Gabriela (2000). *Bursa și piața extrabursieră*, Editura Economică, București 2000

Nițu, A. (2002). *Burse de mărfuri și valori*, Editura Economică, București

www.kmarket.ro