Capital Market Review of Romania

TOWARDS A NATIONAL STRATEGY

OECD

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BETTER POLICIES FOR BETTER LIVES

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Foreword

In the years before the COVID-19 pandemic, Romania enjoyed strong economic growth which reduced the gap in terms of income per capita with high-income European Union (EU) economies and resulted in a decline in unemployment. The pandemic-induced crisis halted this trend and sharp declines in revenues have caused financial challenges for many companies. The crisis has also revealed a number of long-term structural challenges in the Romanian corporate sector and capital markets. Notably, in contrast to many other economies, the Romanian corporate sector had limited access to long-term market-based financing in 2020. The recovery phase and the long-term strength of the Romanian corporate sector will depend on corporations getting access to a wider range of financing options, such as public equity and corporate bonds, and a more dynamic capital market. In particular, a better balance between traditional bank lending and corporate access to sources of market-based financing will help advance Romania's integration into the European financial system.

Against this background, the Romanian Financial Supervisory Authority, in collaboration with the Ministry of Finance, requested support from the European Commission under the Structural Reform Support Programme to undertake a comprehensive review of capital markets in Romania and to develop a national capital market strategy. The OECD was designated as the implementing partner for the project.

This Review maps capital markets in Romania and assesses the main challenges before putting forward policy recommendations for improving Romanian companies' use of market-based financing. The policy recommendations proposed are intended to provide guidance to policy makers and authorities in their efforts to introduce a Romanian capital market strategy for growth.

OECD CAPITAL MARKET SERIES

This Review is part of the OECD Capital Market Series, which informs policy discussions on how capital markets can serve their important role to channel financial resources from households to productive investments in the real economy.

To prepare this report, the OECD Secretariat conducted substantive research to understand the trends and the functioning of capital markets in Romania. The Secretariat greatly benefitted from consultations with representatives of relevant Romanian authorities, a large number of market participants and other experts. A detailed description of data sources and the methodology for data collection and analysis are provided in the Annex.

The Review was prepared by a team led by Serdar Çelik, Acting Head of the Corporate Governance and Corporate Finance Division within the OECD Directorate for Financial and Enterprise Affairs, composed of Thomas Dannequin, Adriana De La Cruz, Carl Magnus Magnusson, Alejandra Medina, Tugba Mulazimoglu and Yun Tang. The project was produced with the financial assistance of the European Union via the Structural Reform Support Programme.

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Abbreviations and acronyms

AAF	Asociatia Administratorilor de Fonduri (Romanian Fund Managers Association)
AMF	Autorité des Marchés Financiers (French Financial Supervisory Authority)
AMI-SeCo	Advisory Group on Market Infrastructures for Securities and Collateral
ANAF	Agenția Naționala de Administrare Fiscală (Fiscal Administration Agency)
APAPR	Asociatia pentru Pensiile Administrate Privat din Romania (Romanian Pension Funds' Association)
ARB	Asociatia Romana a Bancilor (Romanian Association of Banks)
ASF	Autoritatea de Supraveghere Financiară (Financial Supervisory Authority)
AUM	assets under management
BIS	Bank for International Settlements
BSTDB	Black Sea Trade and Development Bank
BNR	Banca Naţională a României (National Bank of Romania)
BVB	Bursa de Valori Bucuresti (Bucharest Stock Exchange)
BSE	Budapesti Értéktőzsde (Budapest Stock Exchange)
CAGR	compound annual growth rate
CCIR	Chamber of Commerce and Industry of Romania
CCP	central clearing counterparty
CEB	Council of Europe Development Bank
CEE	Central and Eastern Europe
CNP	Romanian National Commission for Strategy and Prognosis
CPI	consumer price index
CSD	central securities depository
DEG	German Investment and Development Society
DVP	delivery versus payment
EBITDA	earnings before interest, taxes, depreciation, and amortisation
EBRD	European Bank for Reconstruction and Development
EC	European Commission
ECB	European Central Bank
EDC	European Data Co-operative
EEA	European Economic Area

EET	exempt-exempt-taxed
EIB	European Investment Bank
EIF	European Investment Fund
ELTIF	European Long-Term Investment Fund
ESMA	European Securities and Markets Authority
EU	European Union
FEAS	Federation of Euro-Asian Stock Exchanges
FESE	Federation of European Securities Exchanges
FIBEN	Fichier bancaire des entreprises (Business banking file)
FMO	Netherlands Development Finance Company
FSA	financial service authority
FTSE	Financial Times Stock Exchange
GAAP	Generally Accepted Accounting Principles
GDP	gross domestic product
GFCF	gross fixed capital formation
HMRC	Her Majesty's Revenue and Customs
IFC	International Finance Corporation
IFRS	International Financial Reporting Standards
IOPS	International Organisation of Pension Supervisors
IPO	initial public offering
IRES	Romanian Institute for Evaluation and Strategy
IRIS	issuers reporting information system
ISDA	International Swaps and Derivatives Association
ISIC	international standard industrial classification of all economic activities
IMF	International Monetary Fund
JEREMIE	Joint European Resources for Micro to Medium Enterprises
MAS	Monetary Authority of Singapore
MFCR	Ministerstvo financí České republiky (Ministry of Finance of the Czech Republic)
MiFID	Markets in Financial Instruments Directive
MSME	micro, small and medium enterprises
MTF	multilateral trading facility
MTPL	motor third party liability insurance
MTS	multilateral trading system
NPL	non-performing loan
OECD	Organisation for Economic Co-operation and Development
OTC	over-the-counter
PE	private equity

PEA	Plan d'Épargne en Actions (Stock Savings Plan)
PMF	Ministerstwo Finansów (Polish Ministry of Finance)
PPP	public-private partnership
PPP	purchasing power parity
PPS	purchasing power standards
PwC	PricewaterhouseCoopers
R&D	research and development
REIT	real estate investment trust
RMF	România Ministerul Finanțelor (Romanian Ministry of Finance)
ROA	return on assets
ROE	return on equity
RON	Romanian Leu
SA	Societate pe Actiuni (joint-stock company in Romania)
SCoRE	Single Collateral Management Rulebook for Europe
SEE	South East European
S&G	Stability and Growth Pact
SIBEX	Bursa din Sibiu (Sibiu Stock Exchange)
SME	small and medium-sized enterprise
SNEF	National Strategy for Financial Education
SOE	state-owned enterprise
SPO	secondary public offering (follow-on offering)
S3	Smart Specialisation Strategy
UCITS	undertakings for the collective investment in transferable securities
UNSAR	Uniunea Națională a Societăților de Asigurare și Reasigurare din România (National Association of Insurance and Reinsurance Companies in Romania)
VAT	value-added tax
VC	venture capital
VCT	venture capital trust
WFE	World Federation of Exchanges

Executive summary

All sectors of the Romanian economy can benefit from a well-functioning capital market that allocates capital towards productive uses and supports the recovery from the COVID-19 crisis. When properly designed, capital markets can help companies and entrepreneurs access the funding they need to invest and expand, and strengthen the resilience of the corporate sector to possible future shocks. They also offer households a way to channel their savings and thereby take part in corporate wealth creation. With these overarching goals in mind, this Review provides policy recommendations to improve the framework and general functioning of Romania's capital market. These recommendations are intended to guide the development of a Romanian national capital market strategy.

Following a period of stagnation and a relatively lengthy recovery following the 2008 financial crisis, the Romanian economy saw a period of reasonably high growth between 2015 and 2019. This led to convergence of per capita income levels towards those in more advanced European economies, and a significant reduction in unemployment. However, the COVID-19 crisis, which significantly impacted the Romanian economy, exposed structural vulnerabilities and threatens this progress. Efficient allocation of capital in the economy will be particularly important in the recovery from the COVID-19 crisis.

The Romanian corporate sector is over-reliant on bank financing and a large share of firms remain credit-constrained. Market-based financing can help fill the financing gap while increasing financial resilience in the corporate sector by supporting viable businesses and reducing the period needed for recovery. A well-functioning capital market will ensure access to different sources of financing which will be essential to foster sustainable economic development in Romania.

The Romanian capital market is currently undersized. The country's share in the European Union's total stock market capitalisation is well below its share in the EU's GDP. In addition, since 2008, 45 companies have delisted from the Main Market of the Bucharest Stock Exchange, compared to only 16 new listings. No capital has been raised through IPOs since 2017, and up until 2020 SPO activity was also non-existent. Credit access, particularly market-based credit, is deficient. Even though 99% of Romanian companies' debt financing is made up of bank loans, total bank loans to GDP represent only one-third of the EU average. Market-based financing, meanwhile, represents only one-eighth of average EU levels. Moreover, SMEs in Romania have low levels of capitalisation and a significant share of companies are credit-constrained. Despite having implemented a funded private pension system, the limited development of the domestic securities market is preventing pension funds from diversifying their portfolios towards a more effective balancing of risk and return.

In order to rekindle economic progress of the pre-COVID years and, more importantly, to ensure that it is sustainable in the long-term, productivity-enhancing investment in both physical and human capital needs to increase. This requires providing Romanian companies with channels through which they can access risk-willing, long-term market-based financing. By rewarding savers that supply the capital with a share in the corporate sector's wealth creation, capital markets also create an important link between businesses and households.

The recommendations provided in this Review are intended to help Romanian authorities improve the legal, regulatory and institutional framework for capital markets and ultimately prepare a national capital market strategy. This process will necessarily involve the collaboration of different government and supervisory authorities as well as private sector entities, notably the Bucharest Stock Exchange. The recommendations are organised under six main areas:

Improving conditions for stock market listing by: reviewing the capital raising procedure from a regulatory perspective, both with regard to initial and secondary public offerings; improving corporate governance standards by promoting increased transparency and disclosure of audit committee activities; listing financially significant SOEs and ensuring they adhere to the highest corporate governance standards; developing a national public-private campaign to encourage companies to use market-based financing; and, prioritising the authorisation and establishment of a Central Clearing Counterparty.

Increasing secondary stock market liquidity by: establishing a mechanism that provides independent quantitative research on smaller companies to market participants at no cost or subsidise brokerage companies for providing such research to the market; creating a country-wide campaign to reach out to inactive shareholders for the liquidation of the shares linked to the privatisation programme of the 1990s; reducing the trading fee charged by the ASF; simplifying the capital gains tax declaration and payment methods to boost investor participation in the stock market; increasing free-float levels of already listed companies; and, improving the efficiency of collateral management in Romania to support the development of securities lending and borrowing, and derivatives market operations.

Nurturing a vibrant SME growth market by: establishing a co-operation between the stock exchange and the Chamber of Commerce and Industry of Romania to promote the use of market-based financing among SMEs; offering seminars and training sessions on market-based financing to SMEs; increasing the threshold to waive the prospectus requirement to encourage SMEs to undertake public offerings to reach a larger pool of investors; supporting smaller companies in preparing relevant and accurate information to be disclosed to investors; designing a mechanism for companies listed on the AeRO Market to transfer to the Main Market; and, increasing the visibility of the Romanian private equity and venture capital market to traditional government agencies, funds-of-funds and others asset managers.

Promoting household savings by: using co-operative banks as key partners in the implementation of a low-cost saving digital tool; leveraging the momentum from the National Strategy for Financial Education to reinforce co-operation among all relevant stakeholders; and, introducing a tax-exempt simplified individual savings account tailored to Romanian households.

Boosting the role of institutional investors by: revising the risk-weighting methodology applicable to pension funds to increase the investable universe of asset classes; allowing pension funds to lend securities; increasing the fiscal deductibility of the annual contribution to Pillar III; and, promoting occupational pension schemes within the scope of the national private-public campaign with the purpose of fostering long-term saving.

Facilitating market-based long-term debt financing by: undertaking a regulatory review to streamline the listing process; re-evaluating the requirement to hold an extraordinary general meeting to issue a bond; considering whether any existing authority has the capacity and the required data to provide credit ratings to the market; adapting the current pension fund regulatory framework that only recognises credit ratings from the three major international agencies to include more credit rating agencies; and, providing incentives for issuers of and investors in green bonds.

1 Key recommendations and implementation roadmap

This chapter provides a summary of the recommendations provided in this Review. The recommendations are organised under six main areas focusing on conditions to improve stock market listing, secondary stock market liquidity, growth market, modalities for household savings, institutional investors and market-based debt financing. The chapter also provides a roadmap indicating possible main responsible authorities for implementing these recommendations as well as an indicative timeline for implementation. Finally it offers a set of key capital market indicators for Romania.

The recommendations provided in this Review are intended to help Romanian authorities improve the legal, regulatory and institutional framework for capital markets and ultimately prepare a national capital market strategy. This process will necessarily involve the collaboration of different government and supervisory authorities as well as private sector entities, notably the Bucharest Stock Exchange. The recommendations are organised under six main areas. In order to facilitate their implementation, a Recommendations Roadmap is provided, summarising all recommendations and providing a possible main responsible authority as well as an indicative timeline for implementation.

1.1. Improving conditions for stock market listing

The Romanian equity market is characterised by a loss of firms and a general lack of activity. Strong equity markets enable innovative firms to access capital and play an important role in improving the productive capacity of the economy at large. They are also a means to give households an opportunity to share in corporate wealth creation. A well-functioning capital market landscape that can mobilise funds and allocate them productively will be particularly important in the recovery period following the COVID-19 crisis. A number of possible policy initiatives to improve the state of Romanian equity markets are outlined below.

The capital raising procedure should be reviewed from a regulatory perspective, both with regard to initial listings but also for secondary public offerings/follow-on offerings. The regulator may assess its internal processes, with a focus on simplifying procedures and shortening the time needed to raise equity capital. To the extent that advisory fees associated with listing represent a barrier to the further development of the equity markets, aside from measures such as alternative markets, the government may consider offering direct or indirect financial support to concerned companies. Frameworks for alternative listing arrangements, such as direct listings and special purpose acquisition companies, could also be considered. Developing a regulatory framework for investment vehicles such as REITs could support the developments of important sectors in the economy by providing access to market-based financing.

Corporate governance standards should be improved. Specifically, disclosure of the number of audit committee meetings and the activity during the meetings should be promoted. Further, listed SOEs should ensure equitable treatment of shareholders.

In order to expand the size of the currently limited investable universe, which is hampering the development of equity markets, the government may consider the listing of financially significant SOEs, along with increasing the low free-float ratios of currently listed SOEs. The power producer Hidroelectrica and the airport company CNAB are two important candidates for public listing. Given their size and the existing institutional investor interest, a minority listing of these companies could be an important catalyst for the Romanian stock market. It is crucial that the process is handled with great transparency in line with international best practices and that the rationale is clearly communicated. Further, in order to promote transparency as well as to set an example for the rest of the market, these companies should adhere to the highest corporate governance standards, with reference to both the *G20/OECD Principles of Corporate Governance* and the *OECD Guidelines on Corporate Governance of State-Owned Enterprises*. Efforts should also be made to move SOEs currently listed on the alternative AeRO Market to the Main Market.

In order to improve the general corporate knowledge of and interest in the capital market, several stakeholders could come together in a *national public-private campaign* to encourage companies to use market-based financing. The ASF and the stock exchange, in co-operation with business and financial market associations, should engage in a dedicated and targeted awareness campaign to inform corporate executives and other relevant actors about the many opportunities of market-based financing. The initiative could also help promote investments in the Romanian capital market by foreign investors. It could be built from the existing platform “Made in Romania”, which is managed by the stock exchange. This platform could be used for information exchange and for guiding companies in their journey to start using market-based financing. As a way to measure progress, an annual target number of new listings could be set.

In parallel to encouraging companies to go public, the government may consider supporting the establishment of publicly listed investment companies or funds that focus on investing in unlisted firms that are not yet ready to go public. This would make a wider range of securities available to prospective investors through the stock market. Having a professional investment firm as an owner could also help unlisted companies prepare for adhering to the standards that are associated with a possible subsequent public listing. Support to this end could include the creation of a platform to match investors with private companies (the agreement between the BVB and equity crowdfunding platform SeedBlink could be an example to build from), and/or financial incentives through tax credits for newly-established such investment companies in the first years. Importantly, because of its effect on the trust in and efficiency of capital markets, the completion of the establishment of a Central Clearing Counterparty (CCP) should be a priority. The private entities that are shareholders in the CCP should continue the process of finalising the documentation and the necessary steps for authorising the entity, and continue the collaboration with the ASF, which acknowledges the importance of the project.

1.2. Increasing secondary stock market liquidity

Well-functioning primary capital markets are dependent on a certain level of activity in the secondary markets that facilitates efficient price discovery and increases the resilience of the market. The Romanian secondary public equity market is characterised by low levels of liquidity, driven by a large number of inactive stocks, in particular in the AeRO Market. Liquidity in the market is dominated by shares of a few large companies.

In order to support secondary market liquidity of small companies, the Romanian authorities may consider establishing a mechanism that provides independent quantitative research on smaller companies to market participants at no cost or by subsidising brokerage companies for providing research to the market. Alternatively, the authorities may consider supporting the recent programme launched by the stock exchange aimed at increasing research coverage of small to mid-cap companies. The BVB could also consider expanding the coverage of the programme to include companies from the AeRO Market. Another strategically important issue, that Romanian policy makers have begun to address, is the dissolution of the inactive shareholders linked to the privatisation programme of the 1990s in the stock market. Such an initiative would stimulate liquidity in the market. Authorities may also consider creating a country-wide campaign to reach out to investors for the liquidation of the shares. Within the campaign, a one-time capital gains tax exemption could be offered to encourage investors to go through the process of claiming their shares and selling them. Alternatively, investors could be offered to transfer their shares to an active account from where they can sell in the future. The government may also appoint a brokerage company to support investors through the process at a pre-set fee negotiated by the authorities.

The cost of trading in the stock market has already decreased significantly thanks to efforts by the stock exchange and the ASF. However, the ASF should consider whether there would be a market-wide benefit from reducing the trading fee it charges to the buy side to further ease the cost of trading and ultimately increase secondary market liquidity. Additionally, a burdensome payment and declaration process of the capital gains tax could be discouraging investors from participating in the capital markets to a certain extent. Therefore, a simplification of the capital gains tax declaration and payment methods may boost investors' participation in the stock market. Authorities may also consider introducing a withholding tax system for capital gains to facilitate the tax collection system. In addition, greater clarity with respect to the categories of tax-deductible and non-deductible expenses for financial firms would be beneficial to industry participants. In addition, to make the stock market more attractive, providing a fiscal credit or a temporary tax exemption on capital gains in the secondary market could be considered.

The free-float level of the companies in the stock market is an essential component to ensure liquidity. The current low levels of free-float on the Romanian stock market and the limited number of companies with higher free-float levels pose a challenge to the overall liquidity of the market. In this respect, and in addition to efforts to bring large companies to the public equity markets, authorities may consider measures to increase the free-float levels of already listed companies. One step could be assessing the regulatory and market conditions for follow-on offerings, and providing companies with support to partially or fully cover the cost of such offerings. To this end, EU funds provided in the context of the Romanian Recovery and Resilience Plan could be used. On top of this, in order to increase the number of financial instruments traded on the BVB, the exchange should consider introducing the possibility of trading open-ended investment funds (UCITS) through its systems, similar to the services provided by Euronext Fund Services.

Additionally, a well-functioning derivatives market enhances investors' ability to hedge their risks, complements the development of capital markets and provides opportunities to increase the liquidity of the underlying instruments. In particular, having a well-functioning currency derivatives market would allow institutional investors to hedge their current and future investments and, importantly, would also increase the attractiveness of the Romanian market for foreign investors. The Romanian authorities and relevant private stakeholders should increase their efforts to develop a well-managed derivatives market in Romania, including developing oversight systems for the possible vulnerabilities that a derivatives market could create. Another important measure that would also support the development of securities lending and borrowing operations is if the Central Depository would increase its efforts in preparing adaptation plans for the AMI-SeCo Standards, to improve the efficiency of collateral management in Romania.

1.3. Nurturing a vibrant SMEs growth market

SMEs in Romania face significant barriers to access financing. Low capitalisation levels, significant credit constraints and limited sources of external financing have prevented them from grasping growth opportunities. Well-functioning public equity markets targeting SMEs, as well as private equity markets, can play an important role in supporting their growth.

A high degree of reliance on internal financing and bank loans could indicate that SME entrepreneurs lack knowledge about other sources of financing. One useful initiative could be establishing a co-operation between the stock exchange and the Chamber of Commerce and Industry of Romania (CCIR) to promote the use of market-based financing among SMEs. As the CCIR represents over 15 000 companies in the country, it could play a key role in reaching SMEs that have the potential to grow but lack the necessary financing. Within the scope of the *national public-private campaign*, experts from the stock exchange could offer seminars and training sessions on market-based financing to selected SMEs, especially those operating in the areas identified in the Romanian Smart Specialisation Strategy. Such programmes may help to increase awareness among SMEs about the benefits of market-based financing and relevant procedures.

Despite the establishment of the AeRO equity market in 2015, equity offerings have been limited and almost all offerings have been carried out as private placements. The Prospectus Regulation has granted EU member states the flexibility to waive the prospectus requirement if the issuance is below EUR 8 million. In Romania, the current threshold is only EUR 1 million, which is significantly lower than other member countries. In order to encourage SMEs to undertake public offerings to reach a larger pool of investors, the government may consider increasing this threshold. This could facilitate the use of public offerings and enable firms to reach a wider pool of investors. In addition, in order to support smaller companies in the process of being admitted to trading on the AeRO Market, the Romanian authorities may consider subsidising brokerage companies to help them prepare a relevant and accurate assessment of their financial prospects. In doing so, market trust and confidence can be increased for new AeRO Market issuers. Funds provided by the EU in the context of the Romanian Recovery and Resilience Plan could be used to this end.

Moreover, as the AeRO equity market grows, a number of companies have shown significant growth and could start planning, with the help of the stock exchange, for a future transfer to the Main Market. It is important to design a mechanism for the companies listed on the AeRO Market to eventually transfer to the Main Market and not to stay listed on the alternative market indefinitely. Aside from helping position the AeRO Market as a marketplace for smaller companies, the prospect of graduating to the Main Market could also be seen as an incentive for some SMEs to list on this market.

Private equity, in particular venture capital and growth capital, can be an important source of alternative financing for SMEs. This is particularly important for growth companies that lack collateral or a stable stream of cash flows. The Romanian private equity industry lags behind those in peer countries, particularly in terms of fundraising. The government and a relevant industry association could join forces to increase the visibility of the Romanian private equity and venture capital market to traditional government agencies, funds-of-funds and other asset managers. To promote the development of the Romanian private equity market, the government may encourage fundraising by establishing a personal income tax benefit, such as the VCT scheme in the United Kingdom. Such a scheme would allow investors to deduct taxes when investing in private equity funds and encourage more participation from retail investors. In addition, the Romanian authorities could evaluate the possibility to support SMEs to take advantage of the financing available via the SME IPO Fund that will provide financing during the pre-IPO, IPO and post-IPO stages. For example, the authorities and/or business associations could group a number of SMEs in search of financing, provide support via information sessions and help these companies meet with fund managers. It is also worth considering that within the portfolio of unlisted SOEs, there are many companies that would benefit from having a private equity fund as an investor.

The Romanian Smart Specialisation Strategy (S3) has identified four clusters of specialisation with innovation potential that could contribute to the country's transition towards a knowledge-based economy. These selected clusters should be given priority when it comes to support with market-based financing, co-operation programmes and growth strategies, as well as other financial support in the form of grants and research funding. Moreover, a collaboration programme could be established to create more links between the business sector and research institutions.

The framework for ELTIFs in Europe can be used as an investment vehicle to bridge the gap between retail investors and SMEs. The ELTIF regulation not only requires that ELTIF funds provide retail investors with a key information document in addition to the prospectus, it also grants retail investors more flexibility when selling assets to incentivise their participation. With the recent review of the ELTIFs framework, there is an opportunity to engage retail investors in investing in SMEs and further support SME financing in Romania.

1.4. Promoting household savings

Well-functioning capital markets provide households with more saving opportunities and allow for diversification and better planning for retirement. However, one of the main obstacles to the expansion of the Romanian capital markets is the limited levels of household savings and their low allocation to capital market securities. Financial inclusion in Romania has improved considerably recently, but still lags behind peer countries.

In order to increase the portion of the population that has access to a bank account, co-operative banks could become a key partner in implementing a low-cost saving digital tool. Under the supervision of the National Bank of Romania, the central body of credit co-operatives – the *Banca Centrala Co-operatista*

Creditco-op – can gain scale by implementing cost-saving digital tools, for example via mobile phone access to services, that could enable them to reach financially excluded households.

Although several programmes to improve financial literacy have already been established, further efforts are needed to reach levels of financial literacy that can help develop a retail investor base in Romania. For this purpose, the Romanian authorities may consider using the momentum from the National Strategy for Financial Education, developed with the support of the OECD, to reinforce co-operation among all relevant stakeholders. Within this framework, seminars and trainings designed specifically to private investors should be implemented, with the aim of raising awareness about the benefits of actively participating in the country's capital markets. The Bucharest Stock Exchange should join this crucial initiative that will enable households to improve their understanding of and confidence in the Romanian capital market. In particular, the fact that the BVB recently established a co-operation programme with a crowdfunding platform, places it in a good position to attract more retail investors to its platforms.

Lastly, following the successful examples of several European countries that have introduced individual savings accounts offering a favourable tax treatment for individual investors, the authorities may consider designing a tax-exempt simplified individual savings account tailored to Romanian households. Either investment firms, pension fund management companies or asset management companies could offer this savings account that invests following similar investment rules as Pillar II funds at a low cost. This would not only increase household participation in the capital market but could also help pension fund management companies reach greater economies of scale.

1.5. Boosting the role of institutional investors

Romanian institutional investors could help drive the development of capital markets by providing the real sector with long-term capital to invest, innovate and grow. This has been the case in many other countries that have established funded pension systems. However, the system in Romania is still young and many challenges remain. In order to continue boosting the role of institutional investors in capital markets the authorities may consider the policy initiatives outlined below.

As the pension system in Romania matures, the regulator should consider developing a strategic approach to further advance the system. Both Pillars II and III of the pension system currently follow investment limits in different assets classes in order to ensure a balanced diversification of risks and have to apply a risk-weighted assets approach. These restrictions, combined with very few available securities, will eventually make it harder for pension management companies to deliver an adequate return to their beneficiaries. Therefore, the regulator should consider revising the risk weighting methodology currently applicable to pension funds with a view to effectively increasing the investable universe of asset classes.

Moreover, the authorities should consider allowing pension funds to lend securities, with the aim of providing an extra return for beneficiaries and to support secondary market liquidity given the limited rotation of pension funds' portfolios. Considering the social purpose of pension funds, securities lending will require the completion of the establishment of a Central Clearing Counterparty (CCP) and a well-functioning market that ensures harmonisation and integration of securities settlement, and collateral management as well as the proper execution of guarantees.

The voluntary saving system has not grown as expected and the balance in each account remains modest. Therefore, the government may consider increasing the fiscal deductibility of the annual contribution and indexing it to a relevant income measure in the country. Romania needs a fiscal system that encourages long-term savings, and fiscal incentives is one among many tools that the government can use to boost savings. In addition, the authorities may prioritise improving communications to the public aiming to increase knowledge and awareness of the need for a higher savings rate. The promotion of long-term investment products targeted to households could also be part of the *national private-public campaign* mentioned above. Occupational pension schemes should also be promoted within the scope of the *national private-public campaign*, since they represent another alternative to foster long-term savings.

The investment fund industry is still underdeveloped in Romania. Moreover, probably due to the lack of listed securities, investment funds allocate a small share of their assets to these instruments. Similarly, the insurance industry is still immature and further efforts are needed to continue expanding it beyond the property and motor third party liability insurance. The investments of insurance corporations are highly concentrated in government bonds. However, if the industry develops further, it can be expected that insurance companies will increasingly demand other long-term securities that can provide higher returns. Therefore, promoting the participation of more issuers in the capital market, either via listed equity or corporate bonds, could contribute to further developing the entire market. In addition, a simplification of the approval process for funds, for example by standardising some of the required documents, could further support the development of the industry.

1.6. Facilitating market-based long-term debt financing

The Romanian corporate bond market is undersized, but could be further developed by addressing a number of inefficiencies. The general lack of access to market-based credit for many companies has left the Romanian economy over-reliant on bank financing – when available – and on foreign financing in particular. An expansion and deepening of the local bond market would be both an important step towards increasing the resilience of the corporate sector and a way to satisfy the existing demand from local institutional investors to invest in long-term local currency fixed income securities. A number of policy measures can be taken to this end.

Several market participants have raised concerns about the time required to issue a bond. A regulatory review should be undertaken with a view to streamlining the listing process. In order to prevent any delays in the approval of prospectuses, the ASF may consider expanding its staff to support companies in ensuring the documentation is submitted in the correct form. Further, the requirement to hold an extraordinary general meeting to issue a bond should be re-evaluated.

To increase activity in corporate fixed income markets, it is important to address the role of credit rating systems. It should be assessed whether any existing authority has the capacities and the required data to provide credit ratings to the market. Alternatively, subsidies for the establishment of a domestic rating agency could be considered. A third option is to simply provide financial support to smaller companies in obtaining credit ratings from an already established credit rating agency. Finally, the current pension fund regulatory framework only recognises credit ratings from the three major players. It should be adapted with a view to including more rating agencies that follow rigorous standards and use solid methodologies.

Investors and their investment policies play a key role in developing the domestic market. Currently, institutional investors' participation in the corporate bond market is very limited. While traditional institutional investors are still at an early stage of development and remain small, diversification of their investments with increasing allocation to corporate bonds could generate increased demand for these instruments and encourage other issuers to make use of this market. This would enable a simultaneous development of institutional investors and corporate bond markets over time. In this respect, the Romanian authorities should encourage collective investment vehicles to create diversified products including non-financial corporate bonds. A special focus could be given to the instruments issued on the AeRO Market to support the financing of mid-sized companies through corporate bonds. Finally, promoting the investment in non-financial corporate bonds by the banking sector would also create additional demand.

To promote the development of the corporate bond market and to finance Romania's large scale infrastructure needs, the authorities should consider financing these projects via corporate bonds.

There are a number of projects in progress, but the financing model used has mostly been bank loans. Romanian authorities could design public-private partnerships where the private sector company or an entity created for the purpose of the execution of the project could issue corporate bonds to fund the investment. This would support an increase in corporate bond activity in Romania, while providing longer-term investment opportunities to institutional investors.

As a combined measure to stimulate the market for corporate bonds and to facilitate Romania's green transition, the government should consider providing incentives for issuers of green bonds such as covering the cost related to obtaining an external review or rating for bonds within an internationally recognised green, social or sustainability bond framework. Such a measure recognises the additional expenses that might be associated with issuing a green bond compared to a regular bond, and can therefore be helpful in the development of green corporate bond markets.

One important step to support the development of the corporate bond market is to ensure a well-functioning government bond market. Therefore, it is crucial that Romanian Government debt managers continue to employ strategies to build a liquid local currency benchmark yield curve while also increasing the average maturity of government bonds.

In line with the objectives stated in the Romanian National Recovery and Resilience Plan to create opportunities for businesses to diversify their financing sources, authorities could consider allocating part of the funds received from the EU to further develop the corporate bond market. In this respect, EU funds could be used to finance the above recommendations to support smaller companies to obtain credit ratings, subsidise the establishment of a domestic rating agency, and/or incentivise the issuance of green bonds.

Recommendations roadmap

Recommendations, responsibilities authorities and proposed timelines for implementation

Recommendation	Responsible authority	Recommended timeline for implementation
Improving conditions for stock market listing		
Undertake a regulatory review of the capital raising procedure, both for initial and secondary public offerings with a view to simplifying procedures and shortening the time required to raise equity capital.	ASF	Short-term
Consider providing direct or indirect financial support for advisory fees associated with the equity listing process to companies for which such costs constitute a barrier to public listing.	Ministry of Finance	Medium-term
Improve corporate governance standards by promoting increased transparency and disclosure of the audit committee's activities.	ASF, Ministry of Finance, Ministry of Justice	Medium-term
Expand the investable universe by listing minority shares of financially significant SOEs (Hidroelectrica and CNAB are notable candidates) and increasing the free-float ratios of currently listed SOEs. Encourage SOEs listed on the alternative AeRO Market to transfer to the Main Market. Ensure that SOEs adhere to the highest corporate governance standards.	Relevant SOEs, Ministry of Finance	Medium-term
Introduce a *national public-private campaign* to encourage companies to use market-based financing by informing corporate executives and other relevant actors about the many opportunities of market-based financing.	ASF, BVB,and other relevant private stakeholders	Short-term
Consider supporting the establishment of publicly listed investment companies or funds that focus their portfolios on unlisted firms that are not yet ready to go public. This could be done by providing tax credits to newly-established such companies or by developing platforms to connect investors and private corporations searching for capital.	Ministry of Finance	Medium/Long-term
Prioritise the authorisation and establishment of a Central Clearing Counterparty (CCP).	Shareholders in the CCP	Short-term
Develop a regulatory framework for investment vehicles such as REITs. These vehicles could support the development of important sectors in the economy by providing access to market-based financing.	Ministry of Finance and ASF	Medium-term
Increasing secondary stock market liquidity		
Establish a mechanism that provides independent quantitative research on smaller companies to market participants at no cost or subsidise brokerage companies for providing such research to the market. Alternatively, the authorities may consider supporting the recent programme launched by the stock exchange aimed at increasing research coverage of small to mid-cap companies. The BVB could also consider expanding the coverage of the programme to include companies from the AeRO Market.	BVB, Ministry of Finance	Medium/Long-term

Recommendation	Responsible authority	Recommended timeline for implementation
Create a country-wide campaign to reach out to the inactive shareholders linked to the privatisation programme of the 1990s for the liquidation of their shares. Within the campaign, consider offering a one-time capital gains tax exemption to encourage investors to go through the process of claiming their shares and selling them.	ASF, Ministry of Finance, Central Depository	Medium/Long-term
If there is a market-wide benefit, consider eventually reducing the trading fee charged by the ASF from the buy side to further ease the cost of trading and ultimately increase the secondary market liquidity.	ASF	Short-term
Simplify the capital gains tax declaration and payment methods in order to boost investor participation in the stock market, e.g. by introducing a withholding tax system for capital gains.	Ministry of Finance, ANAF	Short/Medium-term
Consider a fiscal credit or a temporary tax exemption on capital gains in the secondary market to make the stock market more attractive.	Ministry of Finance, ANAF	Short/Medium-term
Assess the regulatory and market conditions of follow-on offerings to encourage companies to increase their free-float levels, and consider providing support to partially or fully cover the cost of such offerings.	ASF, BVB	Medium/Long-term
Increase efforts to develop a well-managed derivatives market in Romania, and develop oversight systems for the possible vulnerabilities that derivatives market could create.	ASF, BVB, CCP and other relevant stakeholders	Short/Medium-term
Improve the efficiency of collateral management in Romania to support the development of securities lending and borrowing, and derivatives market operations, e.g. by preparing adaptation plans of AMI-SeCo Standards.	Central Depository	Short/Medium-term
The BVB should consider increasing the number of financial instruments traded on the exchange by introducing the possibility to trade open-ended investment funds (UCITS) through its systems.	ASF, BVB, CCP Central Depository, AAF and other relevant stakeholders	Medium/Long-term
Provide clarification with respect to the categories of tax-deductible and non-deductible expenses related to financial activities.	Ministry of Finance, AAF	Short-term
Nurturing a vibrant SMEs growth market		
Establish a co-operation between the BVB and the Chamber of Commerce and Industry of Romania to promote the use of market-based financing among SMEs. Within the scope of the *national public-private campaign*, seminars and training sessions could be provided to selected SMEs, particularly those operating in the areas identified in the Romanian Smart Specialisation Strategy.	BVB, CCIR Ministry of Economy, Entrepreneurship and Tourism	Short/Medium-term
Assess the adequacy of the threshold below which public offers of securities are exempt from the requirement to publish a prospectus. At present the threshold is set at EUR 1 million, which is significantly lower than the EUR 8 million set in the Regulation (EU) 2017/1129.	ASF	Short-term
Subsidise brokerage companies to help smaller companies prepare a relevant and accurate assessment of their financial prospects to increase market trust and confidence in AeRO Market issuers.	Ministry of Finance, ASF, BVB	Short/Medium-term

Recommendation	Responsible authority	Recommended timeline for implementation
Design a mechanism for companies listed on the AeRO Market to transfer to the Main Market.	ASF, BVB	Long-term
Create a personal income tax benefit for households investing in private equity funds.	ANAF	Medium-term
Support SMEs in taking advantage of the financing available via the SME IPO Fund, for instance by grouping a number of SMEs in search of financing, providing support via information sessions and helping these companies meet with fund managers.	ASF, BVB	Short/Medium-term
Promote the use of the ELTIF framework as an investment vehicle for SMEs to further improve access to funding.	ASF, BVB Ministry of Economy, Entrepreneurship and Tourism	Short-term
Promoting household savings		
Increase the portion of the population that has access to a bank account through co-operative banks. Implement cost-saving digital tools, for example via mobile phone access to services that could enable them to reach financially excluded households.	NBR	Medium-term
Use the momentum from the National Strategy for Financial Education to reinforce co-operation among all stakeholders involved.	Ministry for Education and Research, Ministry of Finance, NBR, ASF, ARB, AAF	Short-term
Consider introducing a tax-exempt simplified individual savings account tailored to Romanian households. Investment firms, pension fund management companies or asset management companies could offer a low-cost savings account that invests following the same investment rules used by the pension funds.	Ministry of Finance, ASF, ANAF, AAF	Medium/Long-term
Boosting the role of institutional investors		
The ASF should consider revising the risk-weighting methodology currently applicable to pension funds with a view to effectively increasing the investable universe of asset classes.	APAPR, ASF, Ministry of Labour and Social Justice	Short-term
Consider allowing pension funds to lend securities with the aim of providing an extra return for beneficiaries and at the same time supporting the secondary market liquidity given that pension funds do not rotate their portfolios often, once a CCP has been established and is operational.	APAPR, ASF Ministry of Labour and Social Justice, CCP	Short-term
Consider increasing the fiscal deductibility of the annual contribution to Pillar III and indexing it to a relevant income measure in the country. In addition, improve communications with the public to educate and increase awareness of the need for a higher savings rate.	ANAF, APAPR, ASF	Medium-term

Recommendation	Responsible authority	Recommended timeline for implementation
Promote occupational pension schemes within the scope of the *national private-public campaign* with the purpose of fostering long-term saving. Local asset management companies can play an important role in promoting and managing occupational pension schemes.	Ministry for Education and Research, Ministry of Finance, NBR, ASF, ARB, AAF	Short-term
Simplify the approval process for funds, for example by standardising some of the required documents.	ASF	Short-term
Facilitating market-based long-term debt financing		
Undertake a regulatory review to streamline the listing process of corporate bonds. Consider whether the ASF needs to expand its staff in order to support companies in ensuring the documentation is submitted in the correct form.	ASF	Short-term
Re-evaluate the requirement to hold an extraordinary general meeting to issue a bond.	Ministry of Finance, Ministry of Justice	Short-term
Consider whether any existing authority has the capacity and the required data to provide credit ratings to the market. Alternatively, consider providing subsidies for the establishment of a domestic rating agency or simply providing financial support to smaller companies in obtaining credit ratings from an already established credit rating agency.	ANAF, ASF	Medium-term
Adapt the current pension fund regulatory framework that only recognises credit ratings from the three major international agencies with a view to including more credit rating agencies that follow rigorous standards and use solid methodologies.	ASF	Short-term
Encourage the creation of collective investment vehicles that invest in diversified products including non-financial corporate bonds. A special focus could be given to the instruments issued on the AeRO Market to support the financing of mid-sized companies through corporate bonds.	AAF, ASF	Medium-term
Promote the investment in non-financial corporate bonds by the banking sector and other institutional investors to help support the development of the corporate bond market.	ASF, NBR	Medium-term
Design public-private partnerships where a private sector company or entity is created for the purpose of executing infrastructure projects, which they could finance by issuing corporate bonds.	Ministry of Finance, Ministry of Transport and Infrastructure	Medium/Long-term
Provide incentives for issuers of and investors in green bonds such as covering the cost related to obtaining an external review or rating for bonds within an internationally recognised green, social or sustainability bond framework.	Ministry of Finance	Short/Medium-term

Key capital market indicators: Romania

Table 1.1. Overview of the economy

	2012	2013	2014	2015	2016	2017	2018	2019	2020
Real GDP growth (%)	2.0	3.8	3.6	3.0	4.7	7.3	4.5	4.1	(3.9)
Unemployment rate (%)	6.8	7.1	6.8	6.8	5.9	4.9	4.2	3.9	5.0
Labour productivity growth (%)	2.7	5.0	3.6	4.7	4.5	6.2	4.3	3.9	(2.3)
Gross public debt to GDP (%)	37.1	37.6	39.2	37.8	37.3	35.1	34.7	35.3	47.3
Non-performing loans to total lending (%)	18.2	21.9	20.7	13.4	9.7	6.6	5.0	4.3	3.9

Note: Data on non-performing loans are from Eurostat from 2014 onwards. Prior years use World Bank data.
Source: Romanian National Institute of Statistics, OECD Economic Outlook 109, Eurostat, World Bank, OECD Productivity Statistics.

Table 1.2. Institutional investors

	Pension funds	Insurance companies	Investment funds	Banks
Total assets, as end of 2020 (EUR, billions)	15.9	3.8	8.8	125.4

Source: ASF, National Bank of Romania.

Table 1.3. Non-financial corporate sector

	2012	2013	2014	2015	2016	2017	2018
Number of companies	47 698	49 189	50 229	52 201	53 623	53 597	53 959
Return on equity (%)	5%	7%	7%	9%	12%	13%	13%
Annual sales growth (%)	2%	-1%	5%	7%	5%	5%	8%
Leverage (%)	61%	61%	61%	61%	60%	59%	58%
Share of loss-making firms (%)	27%	26%	23%	18%	17%	18%	17%

Note: Leverage is measured as total liabilities over total assets. The share of loss-making firms is measured as the percentage of Romanian firms with negative net income in the total number of firms. See annex for detail information on how the number of companies is computed.
Source: OECD-ORBIS Corporate Finance dataset.

Table 1.4. Public equity market (as of end 2020)

		Number of listed companies	Market capitalisation (million EUR)
Listed companies (excl. investment funds and REITs)		318	29 984
Main Market	Standard	54	1 727
	Premium	19	15 551
	Int'l	3	11 523
MTS	AeRO Base	3	3
	AeRO Standard	222	1 021
	AeRO Premium	17	159

Note: Investments funds, ETFs and REITs are excluded. Companies issuing more than one share class are only counted once.
Source: Bucharest Stock Exchange, Thomson Reuters Eikon, see Annex for details.

Table 1.5. Public equity market (proceeds in 2020 EUR million)

		2012	2013	2014	2015	2016	2017	2018	2019	2020
IPOs and SPOs										
Number of IPOs		-	2	1	-	1	3	-	-	-
Total proceeds of IPOs		-	501	479	-	45	69	-	-	-
Number of SPOs		1	4	6	2	2	2	1	-	1
Total proceeds of SPOs		42	302	253	209	305	110	1	-	120
Listings and delistings in the stock market										
Main Market	New listings, incl. IPOs	-	2	1	1	1	4	1	-	-
	Delistings	2	3	7	11	-	2	1	4	1
MTS	New listings, incl. IPOs	1	1	1	4	2	3	1	1	3
	Delistings	-	-	-	2	6	7	7	9	13

Note: Investments funds, ETFs and REITs are excluded.
Source: Bucharest Stock Exchange, Thomson Reuters Eikon, see Annex for details.

Table 1.6. Corporate bond market (proceeds in 2020 EUR million)

	2012	2013	2014	2015	2016	2017	2018	2019
Non-financial companies								
Number of issues	1	1	-	-	2	3	3	5
Amounts issued	52.8	40.2	-	-	2.1	36.1	4.8	213.4
Financial companies								
Number of issues	4	2	2	1	-	3	2	9
Amounts issued	67.6	154.9	158.5	3.5	-	205.9	297.5	818.9

Source: OECD Capital Market Series dataset, Refinitiv, Bloomberg, FactSet.

Table 1.7. Private equity market (proceeds in 2020 EUR million)

	2012	2013	2014	2015	2016	2017	2018	2019
Amounts raised	52.4	1.2	-	-	-	26.8	50.6	14.3
Amounts invested	37.4	108.2	94.1	174.7	155.0	508.6	323.7	413.1
Amounts of divestment	128.3	45.0	69.0	73.4	134.1	140.4	95.0	53.4

Source: Invest Europe / EDC.

Table 1.8. EU benchmarking

Romania's share in EU…	2012	2013	2014	2015	2016	2017	2018	2019
GDP (‰)	11.7	12.5	12.8	13.1	13.5	14.4	15.1	16.0
IPO proceeds (‰)	-	46.7	17.2	-	1.9	2.5	-	-
SPO proceeds (‰)	0.6	3.1	2.3	2.1	4.8	1.0	0.0	-
Stock market capitalisation (‰)	3.8	4.2	4.0	4.3	4.2	4.1	4.2	4.5
Corporate bond issuance (‰)	0.1	0.2	0.1	0.0	0.0	0.2	0.3	0.9
Private equity (‰)								
Fundraising (‰)	1.7	0.02	-	-	-	0.3	0.5	0.1
Investment (‰)	0.8	2.5	1.8	3.0	2.5	6.5	3.8	4.4

Source: Eurostat, OECD Capital Market Series dataset, ECB, Invest Europe.

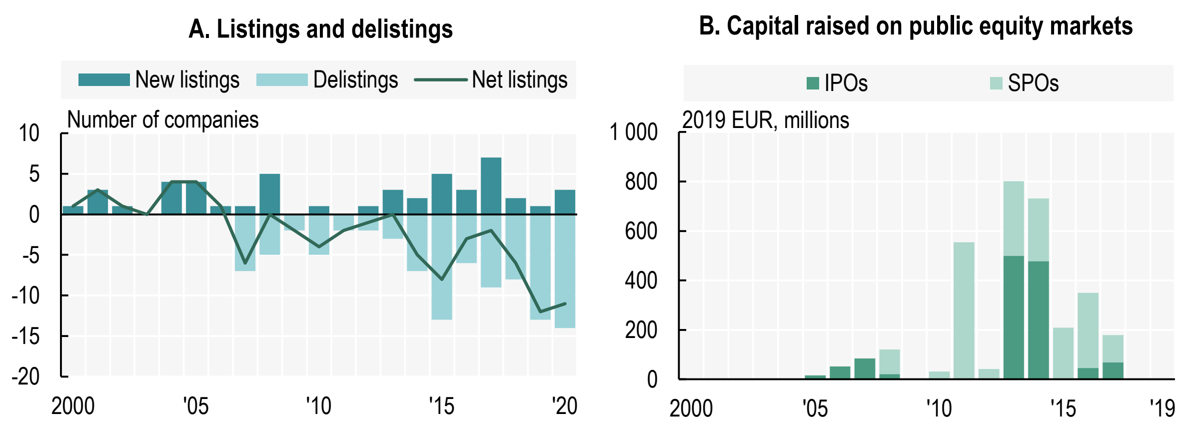
2 Assessment and recommendations

This chapter assesses the six areas that are being considered in the recommendations. It provides an assessment of the conditions for stock market listing, the levels of secondary stock market liquidity, the conditions for growth companies to access financing, the levels and modalities for household savings, the current role in capital markets by institutional investors and the use of market-based debt financing. For each of these areas, the assessment provides an overview of their state and evolution in Romania. Additionally, where relevant, it provides comparison with selected peer countries. The chapter also includes policy recommendations to be implemented by Romanian policy makers for each area under assessment.

2.1. Improving conditions for stock market listing

The Romanian stock market, like many other European markets, has seen a pronounced decline in the number of listed companies in recent years. In spite of relatively favourable macroeconomic conditions and strong economic growth, the Romanian equity market has remained small and is characterised by a lack of dynamism. At the end of 2019, the stock market capitalisation in Romania represented only 0.5% of total European Union (EU) market capitalisation, less than a third of the country's share in total EU GDP (1.6%). Since 2008, 16 companies have listed on the Main Market of the Bucharest Stock Exchange, compared to 45 delistings. The trend for the alternative SME-focused AeRO Market is similar, albeit less pronounced (Figure 2.1, Panel A; see also Chapter 4).

Figure 2.1. Public equity market activity in Romania



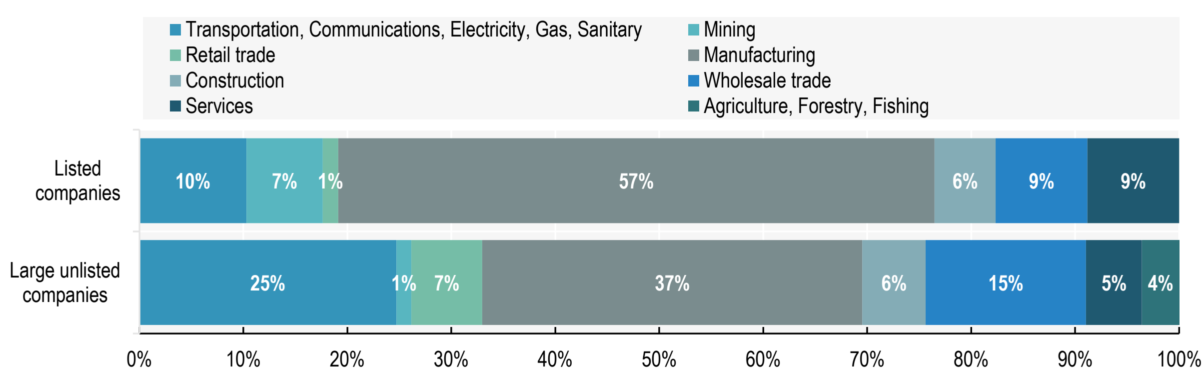
Note: Data in the figures refer to the Main Market and the AeRO Market. Investment funds and REITs are excluded.
Source: Bucharest Stock Exchange, OECD Capital Markets Series dataset; see Annex for details.

Although more capital was raised through initial public offerings (IPOs) in Romania in 2010-19 than during the previous decade, the figures remain low compared to regional peers. Since 2000, 18 Romanian companies have conducted IPOs, raising a total of EUR 1.3 billion (Figure 2.1, Panel B). This compares to, for example, 748 companies raising EUR 23 billion in Poland, or 14 companies raising EUR 1.6 billion in the Czech Republic. Between 2000 and 2019, the amount of capital raised through IPOs in Romania represented 0.24% of the total IPO amounts raised on EU public equity markets. The combination of a decreasing number of listed companies and the sluggish growth in total IPO proceeds has resulted in a situation where the Romanian stock market has increasingly been dominated by a small number of larger companies. The trend is similar when looking at equity market activity by already-listed companies in the form of secondary public offerings (SPOs) or follow-on offerings. No SPO took place between 1996 and 2008 and since 2008, 28 SPOs have been conducted for a total of EUR 1.9 billion, the lowest amount among European peer countries. With the exception of 2011 and 2016, which were largely driven by offerings by the state controlled energy company OMV Petrom, activity has been scant (Figure 2.1, Panel B). Participants and stakeholders in the Romanian equity markets have indicated that the process for share capital increases can be time-consuming and cumbersome.

While there is room for improving business dynamism in Romania generally, it would be incorrect to attribute the lacklustre activity on public equity markets solely to this broader issue. The equity market's performance is partly a reflection of the state of the corporate sector in Romania more generally, but even when considering only the current universe of firms in Romania, the stock market appears to be performing significantly below its potential. As of 2018 there were 279 large unlisted companies in Romania, defined as firms with assets above EUR 89 million (USD 100 million) in 2019 real terms. Many of these firms are eligible for listing on the Bucharest Stock Exchange and exhibit solid financial performance that could significantly improve the profile of the equity market, although it bears mentioning that an important share is made up by subsidiaries of large multinational companies. The minimum criteria for listing on the Main Market of the Bucharest Stock Exchange (BVB) is to have equity or an anticipated market capitalisation of at least EUR 1 million, a free-float of at least 25% and a minimum of three years of financial reporting (see Chapter 4 for further details). Using shareholders' equity as reported on the balance sheet as a proxy for anticipated market capitalisation, 91% of the large unlisted companies in Romania fulfil the equity size criteria. The average company age in the category is 17 years, indicating that many are mature firms. In 2018, the median asset size in the company category was EUR 166 million, with shareholders' funds of EUR 59 million and sales of EUR 157 million. The median company was also profitable with a return on equity of 9.3%.

In terms of industries, over a third (37%) of companies in the large unlisted companies category are active in the manufacturing sector, followed by transportation, communications, electricity, gas and sanitary (25%), and wholesale trade (15%). This differs somewhat from the universe of currently listed companies, where manufacturing companies make up a much larger share. Transportation, communications, electricity, gas and sanitary make up only 10%, four-tenths of the share in large unlisted companies. The service and wholesale trade sectors are the third most common, each making up 9% of currently listed companies (Figure 2.2). If some of the large unlisted companies were to go public, the industry composition on the public markets could be diversified away from the current concentration in manufacturing.

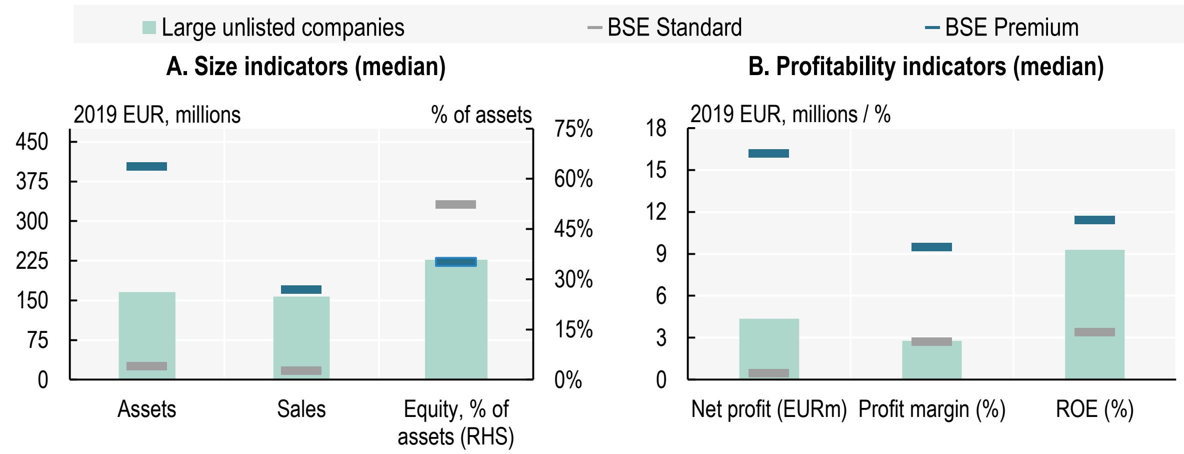
Figure 2.2. Industry distribution of large unlisted companies in Romania by number



Note: Large unlisted companies are defined as private companies with assets in excess of EUR 89 million (USD 100 million) in 2019 real terms. Financial companies are excluded.
Source: OECD Capital Markets Series dataset, OECD-ORBIS Corporate Finance dataset; see Annex for details.

Aside from fulfilling the minimum criteria, many large unlisted companies outperform the currently listed ones both in terms of size and profitability. Figure 2.3 shows a comparison of median values between the group of large unlisted companies and the Standard and Premium Tiers of the Main Market of the Bucharest Stock Exchange. The large unlisted company category has a larger median size and higher median profitability than the Standard Tier equivalent. However, companies listed on the Premium Tier have both higher median size and profitability than most large unlisted companies and those listed on the Standard Tier. The equity share in total assets is similar between large unlisted companies and the Premium Tier, whereas it is higher for the median Standard Tier company.

Figure 2.3. Median financial indicators for listed companies and large unlisted companies



Source: OECD-ORBIS Corporate Finance dataset; see Annex for details.

The fact that the equity market is under-developed in terms of size and growth rates poses a problem for Romanian institutional investors. As the assets under management of institutional investors grow, there needs to be a corresponding growth in the universe of investable securities for these investors. In order to enable this growth, a first step in improving conditions for stock market listings is to consider why these eligible companies have decided to stay private. Aside from the paramount issue of low market liquidity (addressed separately under the assessment *Increasing secondary stock market liquidity*), there are a number of relevant issues related to market infrastructure and governance that affect the performance of a stock market. For example, if the fees charged by the stock exchange for equity listings are excessive or their structure overly complex, they can constitute a barrier to go public. Table 2.1 compares the stock exchange fees associated with an IPO between the Bucharest Stock Exchange and regional peers. It does so both for a company with a market capitalisation of EUR 9 million – the median of companies listed on Standard Tier of the BVB as of November 2020 – and for one with a market capitalisation of EUR 59 million, the median large unlisted company's shareholders' funds. In terms of price competitiveness, the BVB performs rather well. Although it is the only exchange that charges a processing fee, the total listing fee for a company with an anticipated market capitalisation of EUR 9 million is EUR 3 360, the second-lowest after the Prague Stock Exchange. This ranking holds true for a larger company with a market capitalisation of EUR 59 million as well, and for larger companies the fees are significantly lower than the Budapest and Warsaw stock exchanges.

It is important to note that the largest costs associated with an IPO process are not exchange fees, but advisory costs and permanently higher post-listing costs in the form of investor relations staff, increased compliance requirements and so on. For example, in the United States, Japan and the People's Republic of China, the largest direct costs, representing 60% of total IPO costs, are arrangement and underwriting fees (OECD, 2017[1]). Certain fees are fixed or have a high base level, meaning they can constitute a significant challenge for smaller companies wanting to tap public equity markets. To address this issue, certain countries (e.g. Italy and Hungary) provide government support financing to companies for which IPO costs are an impediment to using public equity markets.

Another important factor in the quality and performance of a stock market is the corporate governance standards. Numerous studies have found that higher corporate governance quality is associated with higher liquidity and better firm performance (Bhagat and Bolton, 2008[2]; Chung, Elder and Kim, 2010[3]), (IMF, 2016[4]). The *G20/OECD Principles of Corporate Governance* (henceforth the *Principles*) state that "[e]ffective corporate governance requires a sound legal, regulatory and institutional framework that market participants can rely on when they establish their private contractual relations" (OECD, 2015[5]). In order to increase efficiency and prevent overregulation, corporate governance regulation should also be flexible enough to be able to meet the needs of companies operating under significantly different circumstances, without compromising the focus on maintaining economic performance and market integrity (OECD, 2018[6]). Further, the *Principles* recognise that stock markets can and should work to enhance corporate governance practices. The Bucharest Stock Exchange adopted its current code of corporate governance in 2015 and it is encouraging that the exchange has recently launched an educational programme to promote better corporate governance together with a partner organisation (BVB, 2021[7]).

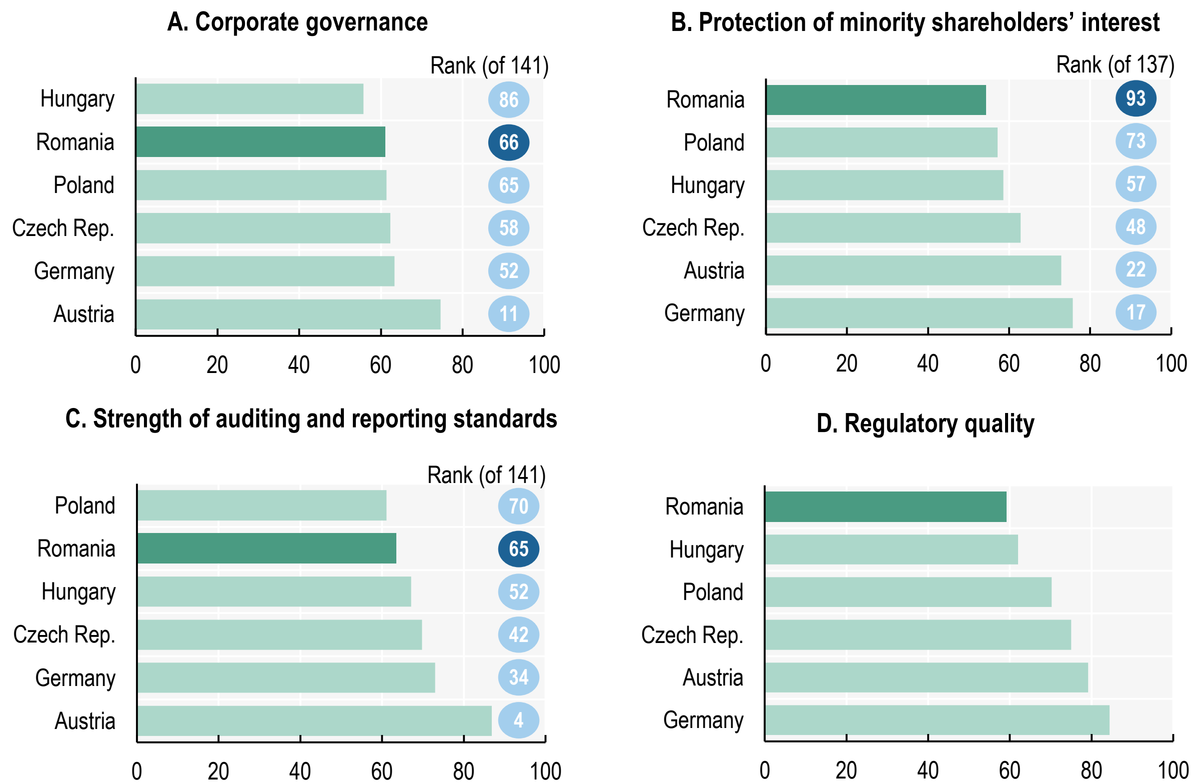
Table 2.1. IPO listing fees by size on different markets

	Bucharest	Prague	Budapest	Warsaw
	Market capitalisation: EUR 9 million			
Processing fee (one-off)	240	0	0	0
Admission fee (one-off)	900	0	0	4 020
Maintenance fee (annual)	2 400	390	8 400	1 350
Total (first year)	**3 540**	**390**	**8 400**	**5 370**
	Market capitalisation: EUR 59 million			
Processing fee (one-off)	240	0	0	0
Admission fee (one-off)	1 440	0	0	3 080
Maintenance fee (annual)	5 000	390	28 150	17 700
Total (first year)	**6 680**	**390**	**28 150**	**20 780**

Note: Assumes listing on the Standard/Main Tier of each market. The fees indicated are for the first year of listing. The Warsaw Stock Exchange increases the maintenance fee in subsequent years. The assumed issue amounts to 100% of equity.
Source: Bucharest Stock Exchange, Prague Stock Exchange, Budapest Stock Exchange, Warsaw Stock Exchange.

Despite efforts to improve corporate governance standards, Romania still scores low on a range of governance and regulatory indicators. Compared to a group of peer countries, Romania scores the lowest on protection of minority shareholders' interests (93 out of 137 globally) (Figure 2.4, Panel B) and regulatory quality with respect to private sector development (Figure 2.4, Panel D), and the second lowest on corporate governance (66 out of 141 globally) (Figure 2.4, Panel A) and auditing and reporting standards (65 out of 141 globally) (Figure 2.4, Panel C). A corporate governance assessment conducted by the EBRD in 2016 found mixed results for Romania, noting that while performance was relatively solid in terms of shareholder rights and transparency and disclosure, there was room for improvement with regard to issues within the following three categories: structure and functioning of boards, internal control and stakeholders and institutions. In particular, there are inadequacies around board effectiveness and the functioning and independence of the audit committee. For example, while six out of the ten largest companies listed in Romania reported having an audit committee in place, only in one was it made up by a majority of independent members (EBRD, 2016[8]). This is contrary to many other countries. The *OECD Corporate Governance Factbook* shows that almost all (45 out of 50) jurisdictions covered require an audit committee by law or regulation, with the remaining recommending it in the corporate governance code (OECD, 2021[9]). This is in line with the *Principles*, which state that it is good practice to have an independent audit committee. Further, the EBRD notes that only two out of the six companies that do have an audit committee disclose the number of meetings per year, and that disclosure on the activity of the committee is very limited. In terms of board effectiveness, the Company Law does not recognise the board's authority to approve a company's budget. That authority is instead vested in the general shareholders' meeting, which is an unusual practice and one which undermines the role of the board (EBRD, 2016[8]). In the case of listed SOEs, the board of directors decides on the budget for the next year which is then approved by the public supervisory authority in accordance with the legislation on corporate governance of public enterprises (GEO, 2011[10]).

Figure 2.4. Quality of governance indicators (100 = highest quality)



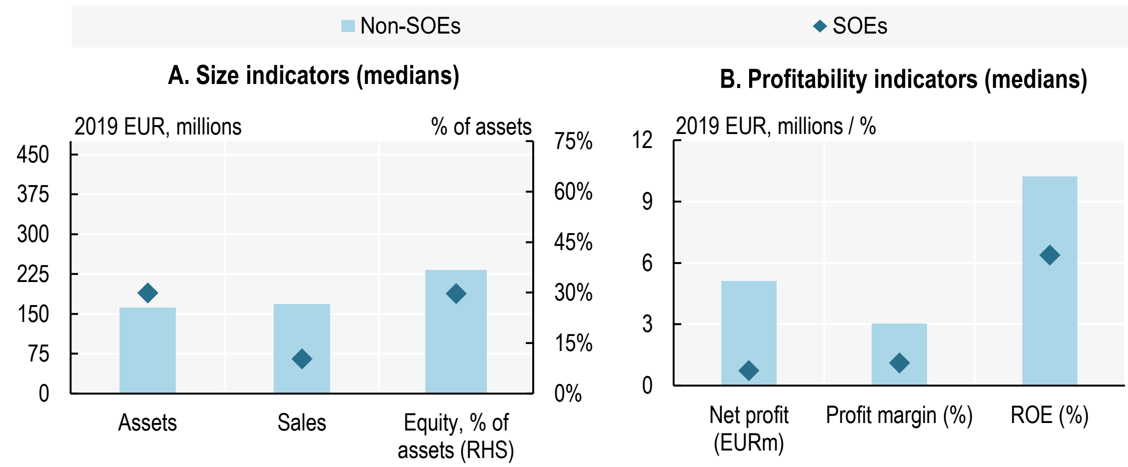
Note: Values and rankings for Panels A and C are for 2019. Those in Panel B are for 2017-18. Panel D measures perceptions of the ability of the government to formulate and implement sound policies and regulations that permit and promote private sector development, values are for 2019. Panels C and D have been rebased to a scale of 100 from initial values ranging between 1 to 7 and -2.5 to 2.5, respectively.
Source: World Economic Forum Global Competitiveness Index (Panels A, B, C), World Bank Worldwide Governance Indicators (Panel D).

State-owned enterprises (SOEs) in particular should be well-governed and set an example in terms of governance standards for the private sector. Without prejudice to the quality of Romania's legal framework for corporate governance of SOEs, the European Commission (EC) notes that implementation and enforcement have been limited and that governance must be improved. The EC has noted this in several Romania country reports, deeming in the most recent one that no progress had been made towards this end. Simultaneously, SOEs' operational and financial results have been deteriorating (EC, 2020[11]). This is particularly noteworthy given that SOEs play an important role on the Romanian equity market. Indeed, four of the five largest IPOs in the past two decades in Romania were SOE listings (see Chapter 4).

Even so, there is still a large potential to expand public equity markets by publicly listing minority stakes of financially significant SOEs. This could play an important role in improving the profile of the Romanian stock market, and would have the double benefit of significantly increasing the size of the market while also offering an opportunity to set high standards with regard to corporate governance and possibly improve financial performance. Of the 279 large unlisted companies described above, 42 have been identified as SOEs (defined as a company where the state owns at least 20%). Splitting the group of large unlisted companies into SOEs and non-SOEs, and replicating the analysis provided in Figure 2.3 shows that while the median SOE is slightly larger than the median non-SOE in terms of asset size, SOEs underperform rather significantly both in terms of sales and profitability (Figure 2.5). To the extent that SOEs provide services that the private sector will not, or is not suited to, due to an inherently low profitability in the specific industry, this is natural and not necessarily cause for concern. However, in the

Romanian case the gap between SOEs and non-SOEs is very pronounced, and SOE performance has been deteriorating in recent years, as noted by the European Commission.

Figure 2.5. Financial indicators for large unlisted companies, split by SOEs and non-SOEs



Source: OECD-ORBIS Corporate Finance dataset; see Annex for details.

Still, in absolute terms the median SOE is both mature and profitable, with an age of 19 years and a return on equity of 6.4%. 38 out of the 42 identified companies fulfil the minimum equity value criteria to list on the Main Market of the BVB. A flagship listing which is bound to generate investor interest and significantly expand the equity market is the state-owned power producer Hidroelectrica. The process of floating a minority share of Hidroelectrica was well underway in 2020, but was put on hold after a parliamentary bill was passed in June 2020 prohibiting the listing of state-owned companies for a period of two years (Romanian Parliament, 2020[12]). A parliamentary initiative to abrogate the bill is pending, and the current ambition is to publicly list a minority share of the power producer when possible, ideally by 2022. Another good candidate for public listing is the Compania Naţională Aeroporturi Bucureşti (CNAB), which manages Romania's largest airport, the Henri Coandă International Airport. Just like Hidroelectrica, CNAB would have significant positive impact on the profile and size of the stock market, and has long been a candidate for listing. In addition to benefitting the equity market, the company itself could also benefit significantly from having access to equity capital, especially in the wake of the COVID-19 crisis which has hit the travel industry particularly hard. This would also free up fiscal space for the central government, which has implemented substantial support programmes for airports around the country during the pandemic (see Chapter 3, Section 3.8).

There are also a number of SOEs that are already-listed, but that have low free-float ratios. A complementary measure to issuing minority shares in financially significant unlisted SOEs would therefore be to increase the free-float of currently listed SOEs by reducing the government's holdings. Currently, 18 companies listed on the BVB are identified as SOEs. Of these, nine are listed on the Main Market (three on the Standard Tier and six on the Premium Tier) and nine on the AeRO Market (all on the Standard Tier). As shown in Table 2.2, the average free-float of currently listed SOEs on the Main Market is rather low at 30%. Increasing the free-float ratios of these companies would contribute to increasing stock market activity. Further, endeavours to move SOEs listed on the alternative AeRO Market to the Main Market instead would help grow the core segment. It would also carry the additional benefit of showing that movement from the alternative to the Main Market is a natural path as a company matures.

Table 2.2. Free-float and distribution of currently listed SOEs

	Free-float			Number with free-float below…		
	No. of firms	Average	Median	10%	25%	50%
Standard	3	22%	24%	1	2	3
Premium	6	34%	34%	0	1	6
Main Market	***9***	***30%***	***34%***	***1***	***3***	***9***
AeRO Standard	9	23%	19%	3	5	8
AeRO Market	***9***	***23%***	***19%***	***3***	***5***	***8***
Total	**18**	**27%**	**30%**	**4**	**8**	**17***

Note: SOEs are defined as companies with at least 20% state ownership. Free-float ratios are calculated based on ownership data in the OECD Capital Markets Dataset. When unavailable, data have been complemented with information from Thomson Reuters-Eikon and, if no other data are available, from company prospectuses and financial reports. Free-float data are missing for one company listed on the AeRO Market – the asterisk (*) indicates that 17 represents the entire sample for which free-float data are available, i.e. there are no companies with free-float ratios above 50%.
Source: OECD-ORBIS Corporate Finance dataset (see Annex for details), Bucharest Stock Exchange Website, Company filings.

Another way of increasing the size of the investable universe in Romania would be to promote the establishment of a number of publicly listed investment companies that are actively focused on investing in unlisted companies. This would have the benefit of establishing a link between unlisted companies and the public equity market, allowing stock market participants to indirectly invest in a universe of companies that is currently unavailable to them. In particular, this would offer a good investment venue for investors who want to increase local investment but who are currently limited to investing abroad due to limited opportunities domestically. In addition, since investment companies by definition hold a portfolio of many different companies, they offer an easy and accessible way for retail investors to diversify their exposure and thus reduce their investment risk.

In order to promote the listing of unlisted companies, other markets have launched programmes/campaigns to provide companies with information, support, guidance and connections to potential investors. For example, the ELITE programme by the London Stock Exchange offers mentoring, advice and access to finance to help ambitious companies to improve access to more sophisticated skill-sets, networks and a diversified capital pool. Another example is the Hungarian mentoring programme run by the Budapest Stock Exchange that targets SMEs and is split into two stages. The first stage focuses on further improving and professionalising mentee company operations, by e.g. improving financial literacy, assisting in accessing international markets and providing training for raising third party financing independently. The second one focuses on helping companies prepare for listing on the stock exchange. A similar SME Pre-Listing pilot programme was implemented in 2018 in Slovenia as a collaboration between the EBRD and the Ljubljana Stock Exchange, focusing on preparing SMEs for IPOs or issuing bonds.

Finally, in terms of market infrastructure more generally, the establishment of a central clearing counterparty (CCP) is a welcome development. CCPs reduce counterparty risk and the cost of trade processing as well as contagion risks during financial instability. They can thus increase the trust in and efficiency of capital markets. The establishment of a CCP will also play an important role in developing a functioning derivatives market in Romania.

On 28 October 2021, Romania's National Recovery and Resilience Plan following the COVID-19 crisis was approved by the EU Council. The plan includes a section specifically focusing on aid schemes for the private sector, which is targeted at companies that want to list publicly and diversify their financing sources (MFE, 2021[13]).

Recommendations

To improve conditions for stock market listing, Romania could/should:

- Review the capital raising procedure both for initial listings and secondary public offerings/follow-on offerings;
- Provide direct or indirect financial support for advisory fees associated with the equity listing process to companies for which such costs constitute a barrier to public listing;
- Improve corporate governance standards;
- List minority shares of financially significant SOEs and increase the free-float ratios of currently listed SOEs;
- Introduce a *national public-private campaign* to encourage companies to use market-based financing;
- Support the establishment of publicly listed investment companies or funds that focus on investing in unlisted firms that are not yet ready to go public;
- Prioritise the authorisation and establishment of a Central Clearing Counterparty (CCP);
- Develop a regulatory framework for investment vehicles such as REITs.

The Romanian equity market is characterised by a loss of firms and a general lack of activity. Strong equity markets enable innovative firms to access capital and play an important role in improving the productive capacity of the economy at large. They are also a means to give households an opportunity to share in corporate wealth creation. A well-functioning capital market landscape that can mobilise funds and allocate them productively will be particularly important in the recovery period following the COVID-19 crisis. A number of possible policy initiatives to improve the state of Romanian equity markets are outlined below.

The capital raising procedure should be reviewed from a regulatory perspective, both with regard to initial listings but also for secondary public offerings/follow-on offerings. The regulator may assess its internal processes, with a focus on simplifying procedures and shortening the time needed to raise equity capital. To the extent that advisory fees associated with listing represent a barrier to the further development of the equity markets, aside from measures such as alternative markets, the government may consider offering direct or indirect financial support to concerned companies. EU funds provided in the context of the Resilience and Recovery Plan could be used to this end. Frameworks for alternative listing arrangements, such as direct listings and special purpose acquisition companies, could also be considered. Developing a regulatory framework for investment vehicles such as REITs could support the developments of important sectors in the economy by providing access to market-based financing.

Corporate governance standards should be improved. Specifically, disclosure of the number of audit committee meetings and the activity during the meetings should be promoted. Further, listed SOEs should ensure equitable treatment of shareholders.

In order to expand the size of the currently limited investable universe, which is hampering the development of equity markets, the government may consider the listing of financially significant SOEs, along with increasing the low free-float ratios of currently listed SOEs. The power producer Hidroelectrica and the airport company CNAB are two important candidates for public listing. Given their size and the existing institutional investor interest, a minority listing of these companies could be an important catalyst for the Romanian stock market. It is crucial that the process is handled with great transparency in line with international best practices and that the rationale is clearly communicated. Further, in order to promote transparency as well as to set an example for the rest of the market, these companies should adhere to the highest corporate governance standards, with reference to both the *G20/OECD Principles of Corporate*

Governance and the *OECD Guidelines on Corporate Governance of State-Owned Enterprises*. Efforts should also be made to move SOEs currently listed on the alternative AeRO Market to the Main Market.

In order to improve the general corporate knowledge of and interest in the capital market, several stakeholders could come together in a *national public-private campaign* to encourage companies to use market-based financing. The ASF and the stock exchange, in co-operation with business and financial market associations, should engage in a dedicated and targeted awareness campaign to inform corporate executives and other relevant actors about the many opportunities of market-based financing. The initiative could also help promote investments in the Romanian capital market by foreign investors. It could be built from the existing platform "Made in Romania", which is managed by the stock exchange. This platform could be used for information exchange and for guiding companies in their journey to start using market-based financing. As a way to measure progress, an annual target number of new listings could be set.

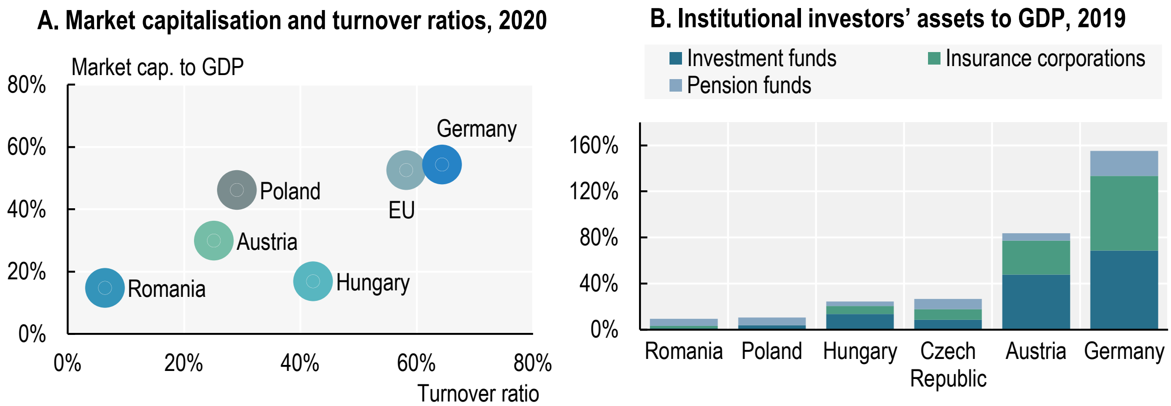
In parallel to encouraging companies to go public, the government may consider supporting the establishment of publicly listed investment companies or funds that focus on investing in unlisted firms that are not yet ready to go public. This would make a wider range of securities available to prospective investors through the stock market. Having a professional investment firm as an owner could also help unlisted companies prepare for adhering to the standards that are associated with a possible subsequent public listing. Support to this end could include the creation of a platform to match investors with private companies (the agreement between the BVB and equity crowdfunding platform SeedBlink could be an example to build from), and/or financial incentives through tax credits for newly-established such investment companies in the first years. Importantly, because of its effect on the trust in and efficiency of capital markets, the completion of the establishment of a Central Clearing Counterparty (CCP) should be a priority. The private entities that are shareholders in the CCP should continue the process of finalising the documentation and the necessary steps for authorising the entity, and continue the collaboration with the ASF, which acknowledges the importance of the project.

2.2. Increasing secondary stock market liquidity

Well-developed capital markets are highly dependent on active secondary markets where securities are exchanged frequently enabling an efficient price formation process (World Bank, 2019[14]). Empirical evidence suggests that there is a positive link between secondary market liquidity and the size of the stock market (Bayraktar, 2014[15]; Garcia and Liu, 1999[16]). Panel A of Figure 2.6 shows the market capitalisation to GDP and turnover ratios[1] for Romania, its peer countries and the European Union. In general, there is a positive correlation between the size of the stock market and the liquidity. Romania shows the lowest level for both measures among peer countries.

Capital market development is also contingent on a well-functioning financial sector, including a deep and diversified institutional investor base which can both channel savings towards capital markets and contribute to stability and liquidity in the market (World Bank, 2019[14]; BIS, 2019[17]). In particular, given the nature of their investment horizon, pension funds provide a long-term supply of funds to the capital markets. However, as pension funds mostly follow buy-and-hold investment strategies, they may provide less liquidity to the market compared to mutual funds (Moleko and Ikhide, 2017[18]). Romanian institutional investors' assets have the lowest share of GDP compared to peer countries (Figure 2.6, Panel B). Importantly, investment funds and insurance corporations' assets amounted to just 1.1% and 2.1% of Romanian GDP. Another important observation concerning Romanian institutional investors is that they own just 15% Romanian company stocks, much lower than in other countries (see Figure 4.10 for more details).

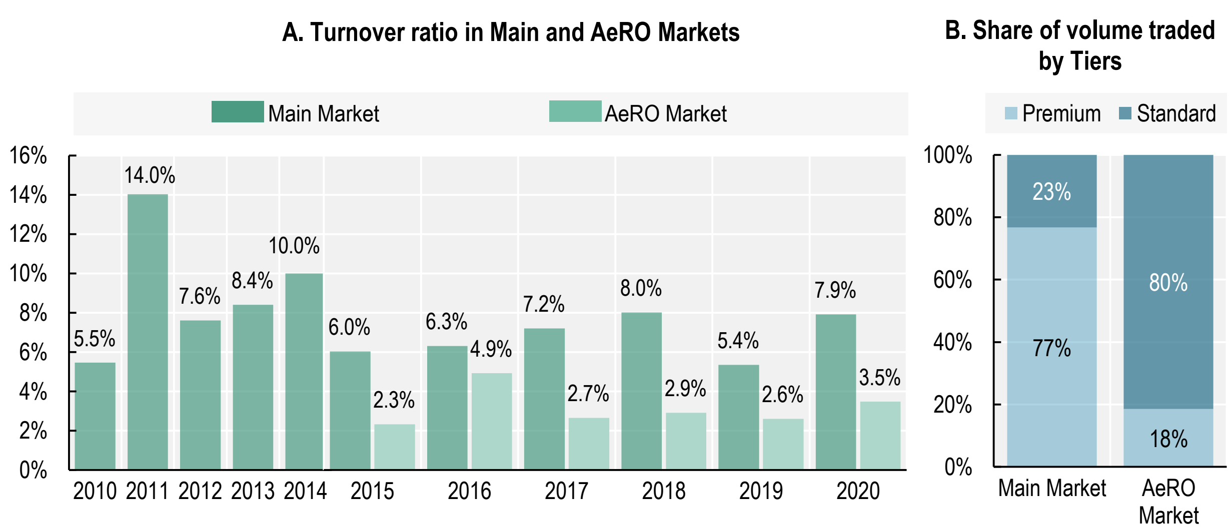
Figure 2.6. Market capitalisation, institutional investors and liquidity



Note: In Panel A, the ratios for Austria and Germany are as of end 2019, and for European Union it is as of end 2018.
Source: ECB, Bucharest Stock Exchange, Warsaw Stock Exchange, Budapest Stock Exchange, WFE, ASF.

A more detailed analysis of the Romanian stock market shows that both the Main and AeRO Markets are characterised by low levels of liquidity. Since 2015, the annual average turnover ratio was 7% in the main segment of the market, and less than half (3%) that level in the AeRO Market (Figure 2.7, Panel A). The overall turnover ratio of the stock market in 2020 was 8%, which is considerably lower than the levels in the European Union and peer countries. In the main segment of the stock market, the Premium Tier accounted for 77% of the total volume traded during the one-year period between May 2020 and April 2021, while in the AeRO Market, the Standard Tier accounted for 80% of the total trading volume (Figure 2.7, Panel B).

Figure 2.7. Turnover ratios in the stock market



Note: For Panel B, volumes traded are the cumulative amounts corresponding to the trading activity of the last one year as of 29.04.2021.
Source: Bucharest Stock Exchange.

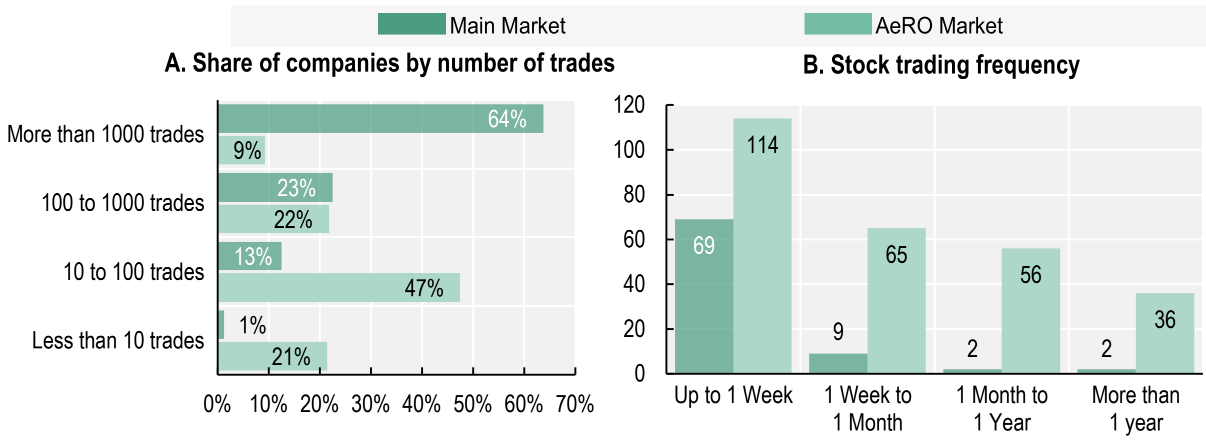
Liquidity on the BVB is mainly dominated by trades in a few individual stocks. By number of trades, the top ten traded stocks during the one-year period between May 2020 and April 2021 account for 62% of the total number of trades on the Main Market, and 70% on the AeRO Market. An important observation concerning the number of trades during that period is that 64% of the stocks traded on the Main Market had traded more than 1 000 times, while on the AeRO Market most of the stocks traded less than 100 times (Figure 2.8, Panel A). Based on 249 trading sessions in a year, 17 companies on the Main Market and 196 companies on the AeRO Market have traded less than one time in each session on average.

Low liquidity on the BVB, especially in the AeRO Market, is also driven by many inactive stocks. As of 29 April 2021, almost 58% of the stocks in the AeRO Market had not been traded in the past week (16% of the stocks in the Main Market) and 36 stocks (two stocks in the Main Market) had not been traded at all in the past year (Figure 2.8, Panel B). To a certain extent, this could be explained by the difference in free-float levels. The level of free-float together with the size of the company, are seen as preconditions for a stock to be liquid. Higher free-float levels, other than increasing the number of stocks available for trading, are generally associated with better shareholder protection, as dispersed ownership improves minority shareholders' rights (World Bank and IFC, 2013[19]). In the Main Market of the BVB, the average free-float level of the stocks that did not trade in the past one week is almost half the free-float level of the stocks traded during the past one week, at 23% and 43%, respectively. Generally, higher free-float levels will lead to more frequent trading. In the main segment, the average free-float level of the Premium Tier is almost twice that of the Standard Tier and the number of trades in Premium Tier is seven times that of the Standard Tier.

Follow-on offerings are not only a key sources of new capital for companies but they also allow companies to increase the free-float levels whenever new shares are issued. Currently, Regulation (EU) 2017/1129 on the prospectus to be published when securities are offered to the public or admitted to trading on a regulated market allows a simplified prospectus for secondary public offerings, and increases the threshold for issuing equity without a prospectus (EU, 2017[20]). While the prospectus remains a key document for investors as it provides with qualitative and comprehensive information, for secondary public offerings it could be burdensome since companies are already disclosing information to the market regularly. According to the EU regulation, issuances of securities of a total up to EUR 1 million – EUR 8 million are exempted from publishing a prospectus. Countries are given the option to adapt their national thresholds (ESMA, 2020[21]). This exemption has the potential to encourage both smaller company listings and secondary public offerings. However, Romania has not modified the threshold yet. In addition, Article 14 of the same legislation allows for a simplified disclosure regime for secondary issuances. The regulation states that a distinct simplified prospectus should be available for use in cases of secondary issuances and its content should be alleviated compared to the normal regime, taking into account the information already disclosed.

One possible reason for the inactivity in some stocks in the Romanian market is the passive retail accounts holding the shares given to citizens during the Mass Privatization Program in 1995-96. Most of these shares correspond to listed companies and around 9 million of these accounts in the records of the Central Securities Depository (CSD) are inactive and therefore not trading on the exchange. As of end 2018, the total value of these accounts amounts to approximately EUR 2.2 billion, corresponding to 7% of the BVB market capitalisation as of end 2018 (Fluent in Finante, 2021[22]; World Bank and IMF, 2018[23]). The lack of activity by the owners of these shares not only affects the liquidity in the market, but also brokers, the BVB and the CSD, who are missing an opportunity to earn income from otherwise possible transactions. Additionally, certain companies, in particular financial investment funds, claim to face problems in taking important decisions during general shareholder meetings as a result of inactive shareholders. In recent years, the BVB and the CSD have put forward awareness programmes to reach out to inactive shareholders, but the situation has not improved significantly (Wall-Street, 2021[24]).

Figure 2.8. Liquidity indicators of the Romanian stock market



Note: For Panel A, number of trades correspond to the trading activity of the last one year as of 29 April 2021. In Panel B, stocks are assigned to each time period based on the difference in the number of days between their last trading date and 29 April 2021.
Source: Bucharest Stock Exchange.

The gap between the number of trades, turnover ratios and trading frequencies between the Main Market and the AeRO Market can partially be explained by the large informational gaps. The availability of market research for companies provides them with visibility to investors and helps generate more information that supports efficient capital markets as well as informed trading. However, there is evidence that at the European level, including country specific analysis from France, market research covering smaller companies has declined in recent years (AMF, 2020[25]). This is mainly the result of the regulatory changes introduced by MiFID II in 2018, aiming at separating research costs from execution costs (unbundling). The directive requires that the research cost be separated from trading commissions paid to brokers, which has substantially reduced asset managers' demand for research. This regulatory change has had a particular impact on smaller listed companies (CFA Institute, 2019[26]). In February 2021, within the Capital Markets Recovery Package approved as a response to the COVID-19, the European Commission approved an exemption to the MiFID II framework to drop the unbundling rules for equity research on companies with a market capitalisation of less than EUR 1 billion during the preceding 36 months (EU, 2021[27]). This exemption aims at supporting liquidity and increasing the visibility of small and mid-cap companies during a time where financing may be needed. In Romania, out of 332 companies listed in the BVB at the end of 2020, almost 90% were concerned by the unbundling rules. A regional initiative by the EBRD has already been introduced to provide publicly available research on SMEs free of charge in six countries including Romania. However, only four companies in Romania will be covered by the programme (BVB, 2020[28]). In response to the research unbundling rules, many countries including Croatia, Hungary and Spain created mechanisms for providing research on smaller companies to the market at no cost. For example, in Hungary, the BSE subsidises the research activity of brokerage companies as part of market development (BSE, 2021[29]).[2] In 2021, the BVB also launched a programme – BVB Research Hub – aimed at increasing research coverage for small to mid-cap companies. The programme currently covers 15 companies from the Main Market, with plans to increase coverage in the future (BVB Research Hub, 2021[30]).

In order to encourage intermediaries and raise awareness of liquidity in the market, the BVB organises an annual award ceremony to recognise the successes of capital market participants. In the ceremony, liquidity-related performances are acknowledged in the categories "the issuers with the largest increase in liquidity", "the most active broker to increase liquidity", and "the most traded share on BVB" (BVB, 2020[31]). Market-making is another mechanism that supports liquidity in stock exchanges. In 2020, the BVB introduced a pilot market-maker programme that further improves the already existing mechanism to enhance liquidity. With this programme, the BVB aims to increase the share of market making activity to at least 15% of the total trading activity, but there is no specific timeline proposed to achieve this target (BVB, 2019[32]). Currently, the Main Market of the BVB only has five active market-makers providing liquidity for 20 stocks, most of which belong to Romanian companies, and the MTS segment only has one active market-maker supporting liquidity of 15 stocks, none of which is a Romanian company stock. Following the improvement of the market-making mechanism, a comparison between the turnover ratios of 2019 and 2020 shows that there has been an improvement in the liquidity of the Main Market of the Romanian stock exchange (see Figure 2.7), which could also be explained by the liquidity boost induced by the upgrade of Romania's status from frontier to secondary emerging market in the FTSE Russell indices in September 2020.

Moreover, in an effort to make the market more accessible to investors, trading fees in Romania were decreased in 2014. The ASF decreased the fees on the buy side of the trades by 25%, and the BVB decreased its trading fees as well by approximately 15% (BVB, 2016[33]). Currently, the BVB charges 9.5 bps on the sell side and 3.5 bps on the buy side, and a fixed fee of RON 0.95 per executed order for regular trades on the equity market. Moreover, the Central Securities Depository (CSD) charges 0.85 bps for each side of the trade, which is applied on a net basis for clearing and settlement. Moreover, brokers also set up their own additional fees on a case-by-case basis. On top of that, the ASF charges another 6 bps fee for the buy side of each trade (BVB, 2018[34]). All taken into account, the total cost for buy and sell sides account for 11.3 bps, adding up to 22.6 bps for a full trade, and the fees charged by the ASF mentioned above (6 bps) made up 53% of total buy side fees. By the end of 2019, trading fees only accounted to a very small part (3%) of the ASF's total income (ASF, 2020[35]). According to the *OECD Corporate Governance Factbook 202*, among 50 jurisdictions surveyed, more than two-thirds of regulators are funded fully or partially by fees from regulated entities, while 21% of regulators are fully financed by the government budget (OECD, 2021[9]). The *OECD Best Practice Principles for Regulatory Policy 2014* recommend that the fees from regulated entities and the scope of activities subject to fees "should be in accordance with the policy objectives and fees guidance set by government" (OECD, 2014[36]). While the ASF receives the fee on trading to perform its activities regarding the supervision of trading systems, the supervisory authorities in many countries do not apply a fee on trading, including Romanian peer countries Hungary, Poland and the Czech Republic.

Moreover, fees charged in Romania for trading shares are higher than in Poland and Hungary. In particular, in the Warsaw Stock Exchange, a trading fee ranges between 1.0 bps and 2.9 bps of the traded value depending on the amount traded.[3] In addition, a fixed amount of PLN 0.15 (EUR 0.03[4]) is charged for every transaction and 0 35 bps of clearing fee on traded value is added, however total trading fee is capped at PLN 880 (EUR 191) regardless of the traded value (Warsaw Stock Exchange, 2019[37]; Interactive Brokers, 2021[38]). In the Budapest Stock Exchange a single trading fee of 1.5 bps with a minimum of HUF 70 (EUR 0.2) and a maximum of HUF 45 000 (EUR 125) is charged on the traded value (BSE, 2021[39]).

In Romania, capital gains earned by resident or non-resident individuals are subject to a 10% tax rate (Article 64 – (Romanian Parliament, 2015[40])). Regardless of a gain or loss for the entire year, the respective amount must be declared to the Romanian tax authorities (ANAF) by the 25 of May of the following year (Article 122/3 – (Romanian Parliament, 2015[40])). In a case where a Romanian broker is included in the transaction as an intermediary, the brokerage firm has the legal obligation to provide a report containing all gains or losses registered during the previous year from all sale transactions at the end of each tax year (Article 96/3 – (Romanian Parliament, 2015[40])). Although the reports taken from the intermediaries are beneficial to complete the declaration, market participants have indicated that the process is burdensome. This might discourage investors from investing in capital markets, and therefore result in lower liquidity. In most countries, for practical purposes, a fixed withholding tax is applied on intermediaries immediately upon the selling of securities. In Turkey, for instance, individuals using a domestic financial institution or bank as intermediaries, pay a 10% withholding tax on capital gains for certain[5] portfolio investment income under a temporary act introduced in 2006 that is valid until 2025. This means the gains generated do not need to be declared in an income tax return (PwC, 2021[41]). In addition to the simplicity of the declaration and payment of the capital gains tax, market participants in Romania mentioned that fiscal incentives on capital gains tax could serve to encourage investors to trade more regularly in the secondary market.

The primary purpose of derivative markets is providing instruments for risk management for borrowers and investors. On top of that, derivative markets complement the development of capital markets, play a prominent role in price discovery and improve the liquidity of the underlying instruments. Moreover, a well-functioning derivative market can also facilitate the participation of foreign investors by allowing them to diversify their portfolios while managing some unwanted risks such as currency risk (Ilyna, 2004[42]). Up until 2018, the Sibiu Stock Exchange (SIBEX) was the market operator and administrator of the derivatives market in Romania. It was also the operator of a cash regulated market and an alternative trading system. Trading of derivative financial instruments within the regulated derivative market of the BVB was also possible between 2007 and 2013 (BVB, 2007[43]). However, in September 2013, BVB announced the termination of trading in derivatives following the maturing of existing derivatives (BVB, 2013[44]).

In January 2018, the BVB acquired SIBEX and following its acquisition, the BVB announced its intention to extend its operations by relaunching the derivatives market to contribute to increasing the liquidity of the local capital market, and in particular to reach its target of doubling the average daily trading value over a ten year period (BVB, 2019[45]). In order to do so, as a first step, in November 2019, the BVB, together with eight other shareholders, established a company that will have the role of a Central Counterparty and will provide clearing services for Romania's capital and energy markets. The company has obtained authorisation to operate from the ASF and it is expected to become operational by the end of 2022 (BVB, 2019[46]). The first phase of the roadmap for the derivative market includes the launch of single stock futures, index futures and energy futures. Additionally, centralised clearing services for forward contracts will be also introduced on Romanian gas and electricity operator – OPCOM.

In the CEE region, the Budapest, Warsaw and Prague stock exchanges have derivative markets, with the Warsaw Stock Exchange dominating trading in the region. With the exception of the Warsaw exchange, these derivative markets suffer from low levels of liquidity and lack of international recognition (Vozianov, 2015[47]). In line with the situation in the CEE region, there are significant concerns about the functioning and depth of the derivate markets in emerging market economies. According to a survey by the Bank for International Settlement (BIS), there is a positive correlation between the degree of market participants' concerns about derivatives market depth and liquidity in the spot market (BIS, 2019[17]). Moreover, evidence suggests that a lower level of financial development, less integration into the global economy, underdeveloped markets for underlying instruments including less issuance by non-residents in domestic markets, and weak/inadequate legal and market infrastructure, are issues that limit the development of local derivative markets (Upper and Valli, 2016[48]; Ilyna, 2004[42]).

Long-term investors can also use derivatives to manage their portfolio risk exposures. However, in many countries, pension regulations constrain investment in derivatives (IOPS, 2011[49]). In Romania, investment in derivatives is allowed only to the extent that it contributes to the reduction of investment risks exclusively by lowering the currency risk or interest rate risk (Romanian Parliament, 2020[50]; ASF, 2020[51]). At the end of 2020, derivatives were almost non-existent in the total value of the assets of the pension funds of Pillar II, and completely inexistent in the financial assets of Pillar III funds (ASF, 2021[52]). However, the share of foreign currency denominated assets in total assets of the Romanian privately managed funds is around 11.5%, most of which is denominated in euros (ASF, 2021[52]). While currency risks are managed in line with the pension funds' risk management strategy, the limited usage of currency derivatives to hedge currency exposures could be a consequence of the lack of a well-functioning derivative market in Romania.

Currency derivatives become increasingly important when investors and corporations in the market are highly exposed to foreign currency risks. Romanian pension funds are still in a developing phase and it is expected that in the future a higher share of their assets under management will be allocated to foreign investments for portfolio diversification purposes, for which a well-functioning derivative markets would be needed. This has been the case with Chilean pension funds which increased progressively their foreign assets allocation, creating a natural demand for derivatives to manage foreign currency exposure, and played an important role in the rapid expansion of the Chilean derivative markets (BIS, 2013[53]). In addition, the increased use of derivatives by corporations also supported the development of the Chilean derivative market (IFC, 2012[54]). Similarly, in Romania, it is expected that there will be a greater demand for currency derivatives from non-financial companies as they are highly dependent on foreign currency financing (see Chapter 3, Section 3.5 for more details). In addition to supporting the risk management of domestic investors, developed currency derivative markets also create investment opportunities for foreign investors who do not want exposure to local currency risk. This will increase the attractiveness of investing in local currency instruments.

Other than the existence of well-functioning market-making mechanisms and derivative markets, measures that can further support the liquidity in the stock markets include improved trading and settlement infrastructure, securities lending and borrowing, and the wide availability of trade and price data (World Bank, 2019[55]). Currently, the BVB publishes pre trade and post-trade data publicly in line with the MiFID II transparency requirements on its website. Additionally, since 2014, there has been a broad transformation in legislative frameworks for capital markets, and short selling, trading on margin, and lending and borrowing techniques were made available to market participants in 2016 (BVB, 2019[32]). Still Romania has to take steps further to support development of the securities lending and borrowing. The necessity of established mechanisms for collateral management in securities lending and borrowing are stressed as further steps to be taken by the World Bank-IMF Financial Sector Assessment Program in 2018 (World Bank and IMF, 2018[23]). Collateral management is one important aspect not only for securities lending and borrowing operations but also for derivative transactions used to minimise credit exposures and, when developed enough, secures efficiently the resilience of the operations. Currently, in Europe, there exists an initiative that defines common rules for managing collateral called as the Single Collateral Management Rulebook for Europe (SCoRE). The initiative introduced in December 2017 will improve the efficiency of collateral management and harmonise applications in Europe. In May, July and August 2019 the Advisory Group on Market Infrastructures for Securities and Collateral (AMI-SeCo) endorsed the first set of AMI-SeCo Standards relating to three of the ten activities namely Triparty Collateral Management, Corporate Actions and Billing Processes (ECB, 2020[56]). Adaptation Plans have been provided by the majority of AMI-SeCo markets each of which have expressed strong support and commitment to the implementation of the standards. While Romania expressed commitment to provide adaptation plans, as of March 2021, no plans were provided to adapt the standards (ECB, 2021[57]).

In order to increase the liquidity of the BVB market and to attract new categories of retail investors, it is advisable to implement an open-end investment fund trading system through the BVB system. This can be done in a similar way to that offered by Euronext Fund Services which is a trading system at NAV.

Recommendations

To increase secondary stock market liquidity, Romania could/should:

- Establish a mechanism that provides independent quantitative research on smaller companies to market participants;
- Create a country wide campaign to reach out to the inactive shareholders linked to the privatisation programme of the 1990s for the liquidation of their shares;
- If there is a market-wide benefit, consider eventually reducing the trading fee charged by the ASF from the buy side to further ease the cost of trading and ultimately increase secondary market liquidity;
- Simplify the capital gains declaration and payment methods to boost investor participation in the stock market;
- Consider a fiscal credit or a temporary tax exemption on capital gains in the secondary market to make the stock market more attractive;
- Assess the regulatory and market conditions of follow-on offerings to encourage companies to increase their free-float levels, and consider providing support to partially or fully cover the cost of the offerings;
- Increase efforts to develop a well-managed derivatives market and develop oversight systems for the possible vulnerabilities that derivatives market could create;
- Improve the efficiency of collateral management to support the development of securities lending and borrowing and derivatives market operations;
- The BVB should consider increasing the number of financial instruments traded on the exchange by introducing the possibility to trade open-end investment funds (UCITS) through its systems;
- Provide clarification with respect to the categories of tax-deductible and non-deductible expenses related to financial activities.

Well-functioning primary capital markets are dependent on a certain level of activity in the secondary markets that facilitates efficient price discovery and increases the resilience of the market. The Romanian secondary public equity market is characterised by low levels of liquidity, driven by a large number of inactive stocks, in particular in the AeRO Market. Liquidity in the market is dominated by shares of a few large companies.

In order to support secondary market liquidity of small companies, the Romanian authorities may consider establishing a mechanism that provides independent quantitative research on smaller companies to market participants at no cost or by subsidising brokerage companies for providing research to the market. Alternatively, the authorities may consider supporting the recent programme launched by the stock exchange aimed at increasing research coverage of small to mid-cap companies. The BVB could also consider expanding the coverage of the programme to include companies from the AeRO Market. Another strategically important issue, that Romanian policy makers have begun to address, is the dissolution of the inactive shareholders linked to the privatisation programme of the 1990s in the stock market. Such an initiative would stimulate liquidity in the market. Authorities may also consider creating a country-wide campaign to reach out to investors for the liquidation of the shares. Within the campaign, a one-time capital gains tax exemption could be offered to encourage investors to go through the process of claiming their shares and selling them. Alternatively, investors could be offered to transfer their shares to an active account from where they can sell in the future. The government may also appoint a brokerage company to support investors through the process at a pre-set fee negotiated by the authorities.

The cost of trading in the stock market has already decreased significantly thanks to efforts by the stock exchange and the ASF. However, the ASF should consider whether there would be a market-wide benefit from reducing the trading fee it charges to the buy side to further ease the cost of trading and ultimately increase secondary market liquidity. Additionally, a burdensome payment and declaration process of the capital gains tax could be discouraging investors from participating in the capital markets to a certain extent. Therefore, a simplification of the capital gains tax declaration and payment methods may boost investors' participation in the stock market. In addition, greater clarity with respect to the categories of tax-deductible and non-deductible expenses for financial firms would be beneficial to industry participants. Authorities may also consider introducing a withholding tax system for capital gains to facilitate the tax collection system. In addition, to make the stock market more attractive, providing a fiscal credit or a temporary tax exemption on capital gains in the secondary market could be considered.

The free-float level of the companies in the stock market is an essential component to ensure liquidity. The current low levels of free-float on the Romanian stock market and the limited number of companies with higher free-float levels pose a challenge to the overall liquidity of the market. In this respect, and in addition to efforts to bring large companies to the public equity markets, authorities may consider measures to increase the free-float levels of already-listed companies. One step could be assessing the regulatory and market conditions for follow-on offerings, and providing companies with support to partially or fully cover the cost of such offerings. To this end, EU funds provided in the context of the Romanian Recovery and Resilience Plan could be used. On top of this, in order to increase the number of financial instruments traded on the BVB, the exchange should consider introducing the possibility of trading open-ended investment funds (UCITS) through its systems, similar to the services provided by Euronext Fund Services.

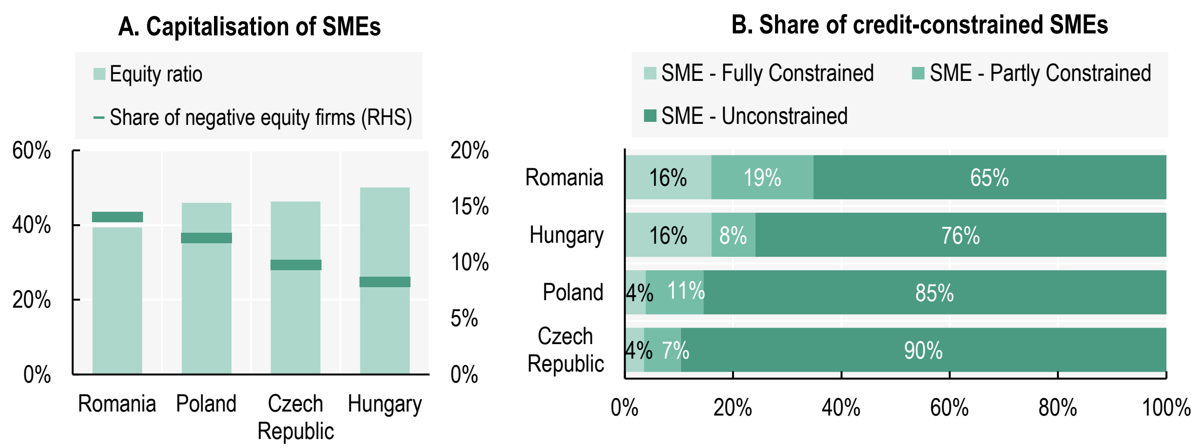
Additionally, a well-functioning derivatives market enhances investors' ability to hedge their risks, complements the development of capital markets and provides opportunities to increase the liquidity of the underlying instruments. In particular, having a well-functioning currency derivatives market would allow institutional investors to hedge their current and future investments and, importantly, would also increase the attractiveness of the Romanian market for foreign investors. The Romanian authorities and relevant private stakeholders should increase their efforts to develop a well-managed derivatives market in Romania, including developing oversight systems for the possible vulnerabilities that a derivatives market could create. Another important measure that would also support the development of securities lending and borrowing operations is if the Central Depository would increase its efforts in preparing adaptation plans for the AMI-SeCo Standards, to improve the efficiency of collateral management in Romania.

2.3. Nurturing a vibrant SMEs growth market

SMEs contribute substantially to economic growth and job creation in Romania. They account for more than nine out of ten enterprises, employ two-thirds of the workforce and generate 54% of total value added. Currently, SMEs' productivity in Romania is still well below peer countries (see Chapter 3, Figure 3.9) and they face substantial challenges, particularly with regard to access to finance. A strong SME sector would not only boost long-term sustainable growth, but would also support the recovery from the COVID-19 crisis.

SMEs in Romania show low levels of capitalisation and a significant share of these companies are credit-constrained. The equity ratio[6] in Romanian SMEs stands at 39%, which is significantly lower than the equity ratio of SMEs in Hungary (50%) and in the Czech Republic (46%). Within the universe of SMEs, Romania has almost twice the share of companies with negative equity[7] compared to Hungary. Moreover, as shown in Panel B of Figure 2.9, according to a survey conducted by the IFC, around 16% of SMEs in Romania are credit constrained. They have either been rejected fully when applying for external financing, or were discouraged from applying due to unfavourable terms and conditions, including unfavourable interest rates and high collateral requirements among others. Another 19% were partially granted the credit they applied for and 65% of SMEs either had no difficulties accessing credit or did not need it. The share of firms not facing any constraint to access credit is significantly lower than in peer countries such as Poland (85%) and the Czech Republic (90%). Credit constraints certainly represent an obstacle to continue growing and investing. During the period from 2015 to 2019, around 64% of SMEs in Romania conducted investment activity, compared to 80% in the Czech Republic and 72% in Hungary.[8]

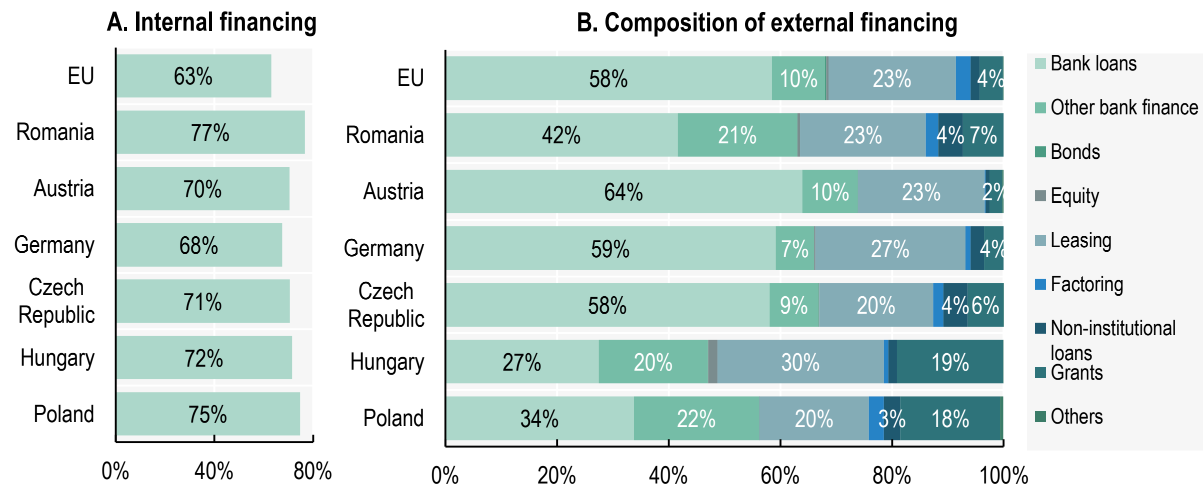
Figure 2.9. SME financing situation by the end of 2018



Source: OECD-ORBIS database, IFC MSME Finance Gap Database.

When it comes to their financing structure, SMEs are generally more dependent on internal financing and bank loans compared to larger firms. The higher risk profile of SMEs and the larger information asymmetries involved make them less suitable for external financing. This financing structure makes SMEs financially vulnerable, particularly in times of crisis when the availability of credit, especially bank loans, tends to contract rapidly leaving them with fewer financing options. In the investment survey conducted by the EIB, SMEs were asked what proportion of their investment was financed by different sources. Figure 2.10 shows an average of the responses for the 2015-19 period. In Romania, 77% of SME financing came from internal financing, significantly higher than the EU average of 63% (Panel A). With respect to external financing sources, bank lending is the most common source accounting for 42% of SME financing in Romania and other bank financing for another 21%. Leasing accounts for another 23% of external financing, the same as the EU level. Importantly, 7% of Romanian SMEs' external funds are grants, which is significantly lower than Hungary (19%) and Poland (18%). Market-based financing sources, such as equity and bonds are negligible for SMEs in Romania and other peer countries. The only exception is Hungary, where equity financing represents 2% of external financing.

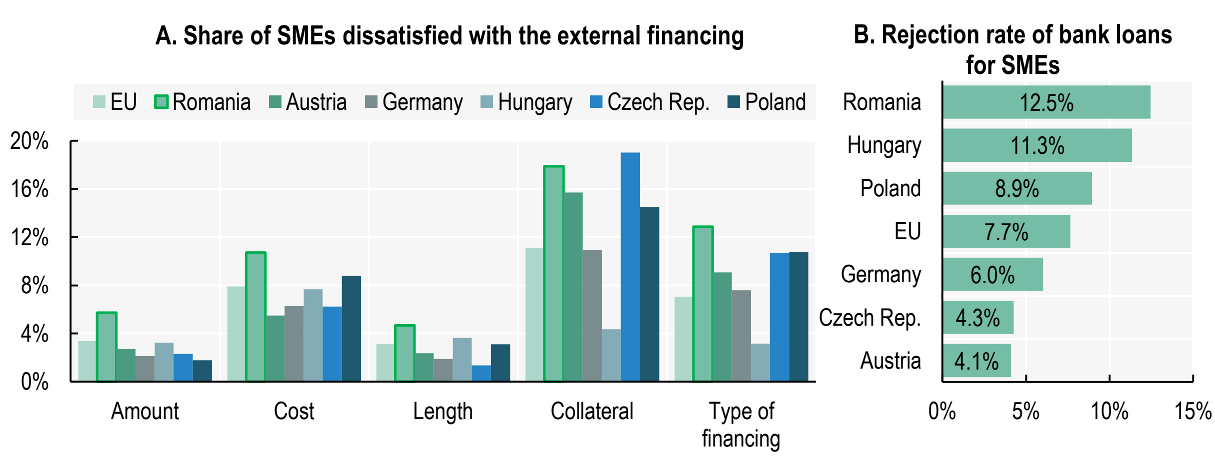
Figure 2.10. Composition of financing sources, 2015-19



Note: The statistics is based on the survey question "What proportion of your investment was financed by each of the following?" The calculation is based on the average for the period 2015-19.
Source: EIB Investment Survey.

SMEs in Romania are much more dissatisfied with the conditions of external financing than in peer countries. Around 6% of firms are not satisfied with the amount they received, twice the EU average. Moreover, when it comes to borrowing costs and collateral used to access financing, 11% and 18% of firms are not satisfied respectively (Panel A of Figure 2.11). Additionally, the rejection rate of bank loans in Romania is high, with 12.5% of firms reporting a rejected loan application or loan offers whose conditions were deemed unacceptable. This number is significantly higher than in peer countries such as the Czech Republic (4.3%) and Poland (8.9%). One reason for the high rejection rate could be the relatively low level of loan guarantees for SMEs. Romania has a low outstanding loan guarantee relative to GDP and low number of SMEs benefiting from guarantees. By the end of 2019, Romania had outstanding guarantees to SME loans of only EUR 0.4 billion, which amounts to merely 0.2% of GDP, compared to Hungary (2.0%) and Poland (0.6%).[9]

Figure 2.11. External financing of SMEs in Romania

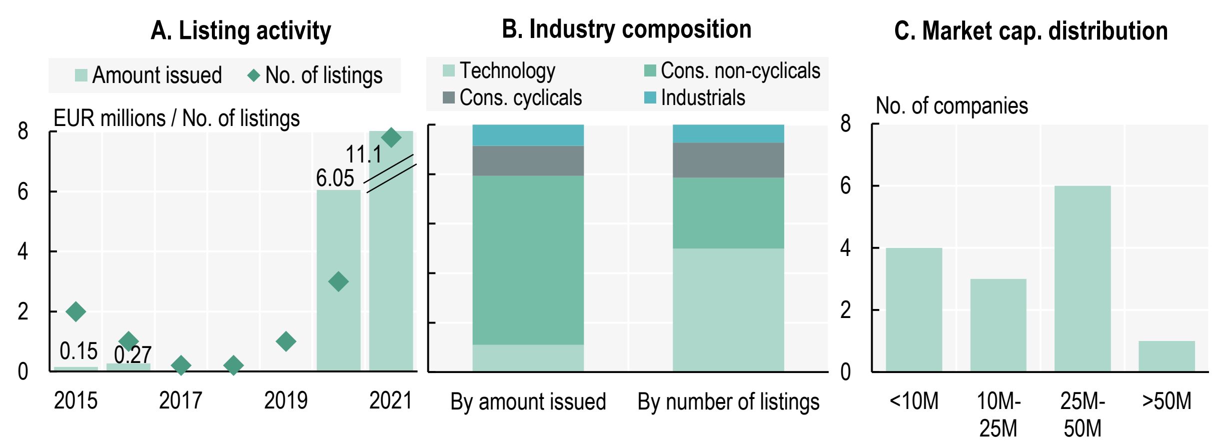


Source: EIB Investment Survey, SBA Factsheet.

SMEs financing has been long recognised as a barrier to growth and innovation. Following international experiences, Romania has already put in place some initiatives to provide SMEs with access to more sources of financing, including public equity as well as other forms of market-based financing such as corporate bonds. In 2015, the Bucharest Stock Exchange launched an alternative trading platform, the AeRO Market, that serves the financing needs of SMEs. The AeRO Market is composed of both an equity segment and a corporate bond segment. Compared to the Main Market, the AeRO Market has less demanding standards for issuers. For example, for the AeRO equity segment, companies are not required to submit quarterly reports and companies are only required to have a minimum free-float of 10%, compared to 25% for the main market. For the AeRO bond segment, there are no prospectus requirements and there is no minimum issue amount.

From the launch of the AeRO Market until the end of May 2021, 11 companies have issued shares through private placements on the MTF, raising a total of EUR 17.6 million. Another three companies chose to list their shares without raising any funds. During the first five years, the amount raised was negligible. In 2015 and 2016, only three companies issued shares, raising a total of EUR 0.5 million. In the following three years, there was only one listing (in 2019) and no capital was raised. Most of the issuances happened in 2020 and during the first half of 2021, when ten companies raised a total of EUR 17.1 million (Panel A of Figure 2.12). The industry composition of these firms shows that half of the listings correspond to technology firms, although they only account for 11% of total proceeds. At the same time, four consumer non-cyclicals companies raised a total of EUR 12 million, representing almost 70% of the total amount raised.

Figure 2.12. AeRO equity market



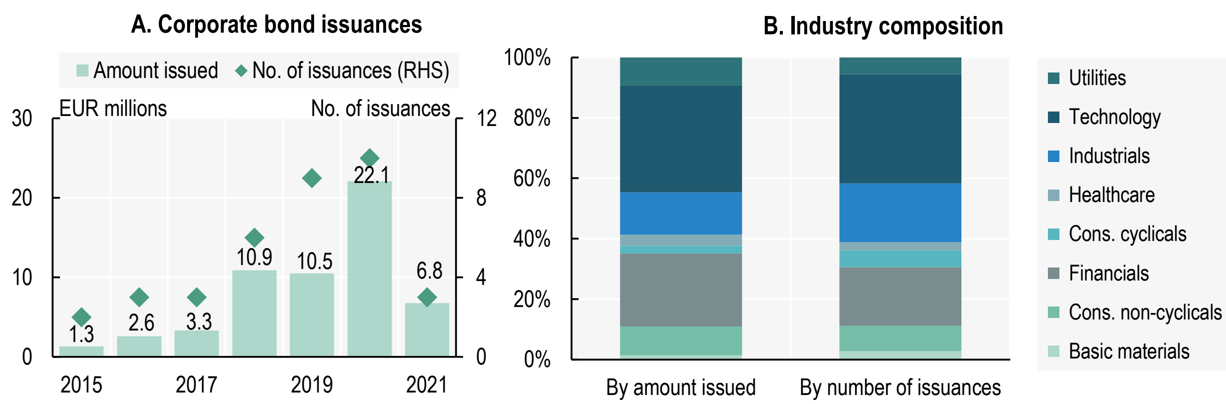
Note: Investment funds and REITs are excluded. The equity issuances in 2021 correspond to issuances taken place before May 2021.
Source: Bucharest Stock Exchange.

Up until now, no company has chosen to issue shares through initial public offerings on the AeRO Market, as the Capital Markets Law requires the preparation of a prospectus that has to be approved by the ASF. All companies listed on the AeRO Market either chose to directly[10] list the shares without raising any funds or conduct private placements. Private placements can limit the pool of investors the listed company can reach compared to a listing conducted through an initial public offering. According to the EU legislation, public offerings of securities below EUR 8 million can be exempted from the obligation to publish a prospectus (EU, 2017[20]). Several countries in Europe such as Croatia, the Netherlands and France have taken advantage of this legislation and exempted companies from the obligation to publish a prospectus if the public offer is below EUR 5 million or EUR 8 million. In Romania, only issuances below EUR 1 million can be exempt from the prospectus requirement, which is a significantly lower threshold compared to other countries (ESMA, 2020[21]).

By the end of May 2021, the AeRO equity market had a total market capitalisation of EUR 334 million. In terms of size distribution, there were six companies listed with a market capitalisation between EUR 25-50 million, and one company with over EUR 50 million. Since the establishment of the AeRO Market, no company has graduated from it to the Main Market. As the AeRO Market targets SMEs that need financing for growth, it would also be natural for these SMEs to transfer to the main market after they have grown to reach a certain size.

The AeRO Market for corporate bonds has seen a much higher activity than the equity market. Since the launch of the market in 2015, there have been 36 bond issuances by 29 companies, raising a total of EUR 58 million (Panel A of Figure 2.13). Four companies have returned to the market several times to continue to raise funds. It is also important to point out that there have been six bond issuances conducted by companies listed on the AeRO equity market. Regarding the industry composition, technology and financial companies together account for over half of the total issuances both in terms of the number of issues and amount issued. Although only two issuances correspond to utility companies, they represent a quarter of the total amounts issued (Panel B of Figure 2.13).

Figure 2.13. AeRO bond market



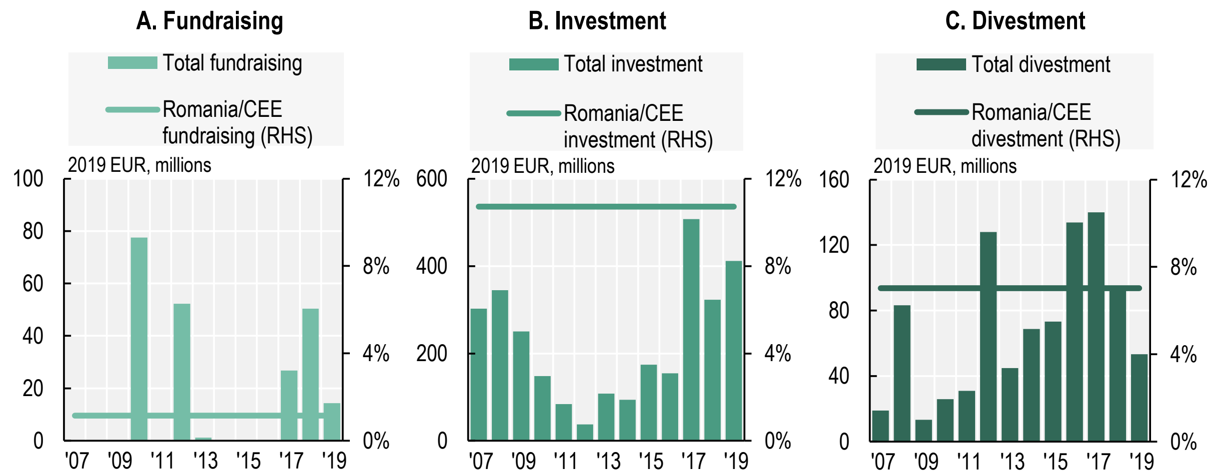
Note: The bond issuances in 2021 are for issuance activities that took place before May 2021.
Source: Bucharest Stock Exchange.

In addition to the AeRO Market, the BVB has also signed a memorandum with Romania's largest crowdfunding platform, SeedBlink, to support the financing of Romanian entrepreneurs. The memorandum stipulates that promising tech start-ups from SeedBlink's portfolio will be offered help from the stock exchange to access the public equity market. The partnership is seeing as an incubator for new listings and a viable alternative to channel resources to innovative ventures. This is a welcome development that certainly will help modernise and develop the Romanian capital market, providing companies with access to multiple financing sources, helping them get listed on the stock exchange, and increasing the base of capital market investors (BVB, 2021[58]). Moreover, the Regulation on European Crowdfunding Service Providers for business will enter in force on 10 November 2021, building a unified framework for all European countries and enforcing cross-border passporting for crowdfunding. As a result, more crowdfunding activities are expected to take place both domestically and across borders.

Private equity (PE) is also an important tool for financing SMEs. It can not only provide financing for the company, but also bring expertise to improve management practices and operational efficiency. Private equity investments are playing an increasingly important role for companies in Romania. During the period 2007-19, private equity funds have invested a total of EUR 2.9 billion in Romanian companies, which accounts for 10.7% of the total investment in the CEE region, almost the same level as Romania's share of GDP in the region (11.7%). In the last decade, PE investment in Romania has grown, reaching almost

EUR 500 million in 2017 and fluctuating around this amount since then. However, Romania's share of fundraising is only 1.1% in the CEE region, much less than its share in GDP. Divestment accounts for 7.0% of the total divestment in the CEE region.

Figure 2.14. Private equity activity in Romania, 2007-19



Source: Invest Europe / EDC.

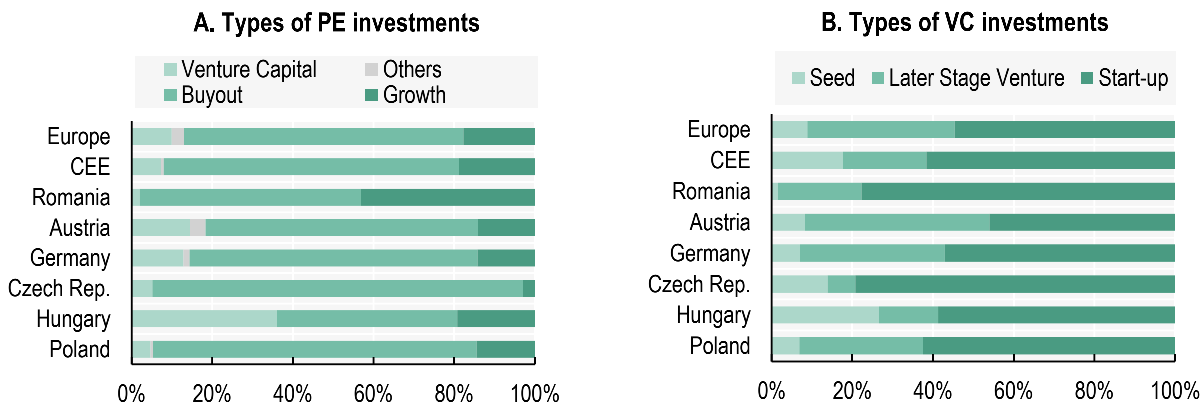
Fundraising in Romania has been highly concentrated in the public sector and sovereign wealth funds, making up more than 60% of total funds raised (see Figure 6.5). Almost no funds have been raised from insurance corporations, funds of funds or pension funds, while in Europe, these three categories represent 45% of total funds raised. Moreover, difficulties to attract and incentivise private investors to the funds is the main cause of the lack of interest in private equity (MFE, 2015[59]). Meanwhile, the Joint European Resources for Micro to Medium Enterprises (JEREMIE) scheme, a joint initiative established by the European Commission in co-operation with the European Investment Bank and other financial institutions to deploy EU Structural Funds, has continued to be the crucial source of private equity. The Venture Capital (VC) fund Catalyst Romania II, which targets expansion stage information and communication technology and technology enabled services companies, was launched at the end of 2020. The fund has raised EUR 40 million, of which EUR 15 million has been committed by the European Investment Fund through JEREMIE Romania Reflows and EUR 25 million from other private investors.

The EU in response to the COVID-19 crisis has also implemented several initiatives to support SME financing. The funds provided by the EU in the context of the Romanian Recovery and Resilience Plan shall be used to increase private equity financing through a dedicated financial instrument to be implemented by the European Investment Fund by 2026. Another EU programme, centrally managed by the European Commission is the InvestEU Programme (Regulation EU 2021/523) that has, among other things, the role of facilitating investments in IPOs for SMEs that are seeking to raise growth capital. Under the InvestEU Fund, the SME IPO Fund will seek to support SMEs through channelling more private and public equity (EU, 2021[60]). Within the main features, the SME IPO Fund can take different structures (Intermediated Equity Investment, Fund-of-Funds, Special Purpose Vehicle), and can invest in SMEs at different IPO stages and across all EU member countries (EU, 2021[60]).

To promote fundraising for PE funds, a number of countries have established schemes to incentivise investors to invest in such funds. The United Kingdom's Venture Capital Trust (VCT) scheme offers an upfront tax relief in the form of a grant of 30% of the investment sum as well as relief on gains for investors. The VCT scheme is a public traded private equity and has been actively used by investors since its introduction in 1995 through the legislation of the UK Finance Act 1995. During the last three years, an average of around GBP 700 million has been raised every year through this scheme (HMRC, 2021[61]), providing risk capital to smaller companies with growth potential.

Although PE investments in Romania have grown in recent years, the amount of venture capital investments in 2015-19 was merely EUR 31 million, accounting for 2.0% of total PE investments, which is relatively low compared to the CEE region level of 7.2% (Figure 2.15). Further, within venture capital investment, the seed stage investment only constitutes 1.5% of the total VC investment, which is much lower than in peer countries such as the Czech Republic (14%) and Poland (27%).

Figure 2.15. Composition of PE investments, 2015-19



Source: Invest Europe / EDC.

This lack of investment in venture capital, along with other deficiencies such as the lack of adequate links between business sectors and research institutes and insufficient public R&D funding, can be tied to the low R&D intensity in Romania. In 2019, Romania ranked last in the EU with total R&D expenditure accounting for no more than 0.5% of GDP (EC, 2020[11]). To boost innovation and economic growth, the Romanian Smart Specialisation Strategy (S3) for 2016-20 has identified four national S3 priorities including: 1) Bioeconomy; 2) Information and communication technology; 3) Space and security; 4) Energy, environment and climate change, eco-nano-technologies and advanced materials. Developing a research and innovation strategy for these industries will require support from market-based financing. Moreover, it requires more links between business sectors and research institutes.

The lack of specialised investment vehicles that invest in SMEs could also be a barrier to SME financing while preventing retail investors from accessing this segment. In this respect, the European Long-Term Investment Funds (ELTIFs) can be a suitable tool to bridge the gap between SMEs and retail investors. ELTIFs are closed-end funds that are required to invest at least 70% of their capital in eligible investment assets including SMEs with a market capitalisation below EUR 500 million listed on regulated markets or MTFs. ELTIFs are subject to strict disclosure requirements, which require ELTIFs to provide retail investors with a key information document in addition to a prospectus. Moreover, as retail investors can only invest up to 10% of their total portfolio in ELTIFs, and the framework for ELTIFs allows retail investors to redeem their investment earlier than the end of life of the ELTIF under certain conditions, it could be used as a vehicle for retail investors to invest in SMEs.

Recommendations

To nurture a vibrant SMEs growth market, Romania could/should:

- Establish a co-operation between the BVB and the Chamber of Commerce and Industry of Romania to promote the use of market-based financing among SMEs;
- Assess the adequacy of the threshold below which public offers of securities are exempt from the requirement to publish a prospectus;
- Subsidise brokerage companies to help smaller companies prepare a relevant and accurate assessment of their financial prospects;
- Design a mechanism for companies listed on the AeRO Market to transfer to the Main Market;
- Create a personal income tax benefit for households investing in private equity funds;
- Support SMEs in taking advantage of the financing available via the SME IPO Fund;
- Promote the use of the ELTIF framework as an investment vehicle for SMEs to further improve access to funding.

SMEs in Romania face significant barriers to access financing. Low capitalisation levels, significant credit constraints and limited sources of external financing have prevented them from grasping growth opportunities. Well-functioning public equity markets targeting SMEs, as well as private equity markets, can play an important role in supporting their growth.

A high degree of reliance on internal financing and bank loans could indicate that SME entrepreneurs lack knowledge about other sources of financing. One useful initiative could be establishing a co-operation between the stock exchange and the Chamber of Commerce and Industry of Romania (CCIR) to promote the use of market-based financing among SMEs. As the CCIR represents over 15 000 companies in the country, it could play a key role in reaching SMEs that have the potential to grow but lack the necessary financing. Within the scope of the *national public-private campaign*, experts from the stock exchange could offer seminars and training sessions on market-based financing to selected SMEs, especially those operating in the areas identified in the Romanian Smart Specialisation Strategy. Such programmes may help to increase awareness among SMEs about the benefits of market-based financing and relevant procedures.

Despite the establishment of the AeRO equity market in 2015, equity offerings have been limited and almost all offerings have been carried out as private placements. Regulation (EU 2017/1129) has granted EU member states the flexibility to waive the prospectus requirement if the issuance is below EUR 8 million. In Romania, the current threshold is only EUR 1 million, which is significantly lower than other member countries. In order to encourage SMEs to undertake public offerings to reach a larger pool of investors, the government may consider increasing this threshold. This could facilitate the use of public offerings and enable firms to reach a wider pool of investors. In addition, in order to support smaller companies in the process of being admitted to trading on the AeRO Market, the Romanian authorities may consider subsidising brokerage companies to help them prepare a relevant and accurate assessment of their financial prospects. In doing so, market trust and confidence can be increased for new AeRO Market issuers. Funds provided by the EU in the context of the Romanian Recovery and Resilience Plan could be used to this end.

Moreover, as the AeRO equity market grows, a number of companies have shown significant growth and could start planning, with the help of the stock exchange, for a future transfer to the Main Market. It is important to design a mechanism for the companies listed on the AeRO Market to eventually transfer to the main market and not stay listed on the alternative market indefinitely. Aside from helping position the

AeRO Market as a marketplace for smaller companies, the prospect of graduating to the Main Market could also be seen as an incentive for some SMEs to list on this market.

Private equity, in particular venture capital and growth capital, can be an important source of alternative financing for SMEs. This is particularly important for growth companies that lack collateral or a stable stream of cash flows. The Romanian private equity industry lags behind those in peer countries, particularly in terms of fundraising. The government and a relevant industry association could join forces to increase the visibility of the Romanian private equity and venture capital market to traditional government agencies, funds-of-funds and other asset managers. To promote the development of the Romanian private equity market, the government may encourage fundraising by establishing a personal income tax benefit, such as the VCT scheme in the United Kingdom. Such a scheme would allow investors to deduct taxes when investing in private equity funds and encourage more participation from retail investors. In addition, the Romanian authorities could evaluate the possibility to support SMEs to take advantage of the financing available via the SME IPO Fund that will provide financing during the pre-IPO, IPO and post-IPO stages. For example, the authorities and/or business associations could group a number of SMEs in search of financing, provide support via information sessions and help these companies meet with fund managers. It is also worth considering that within the portfolio of unlisted SOEs, there are many companies that would benefit from having a private equity fund as an investor.

The Romanian Smart Specialisation Strategy (S3) has identified four clusters of specialisation with innovation potential that could contribute to the country’s transition towards a knowledge-based economy. These selected clusters should be given priority when it comes to support with market-based financing, co-operation programmes and growth strategies, as well as other financial support in the form of grants and research funding. Moreover, a collaboration programme could be established to create more links between the business sector and research institutions.

The framework for ELTIFs in Europe can be used as an investment vehicle to bridge the gap between retail investors and SMEs. The ELTIF regulation not only requires that ELTIF funds provide retail investors with a key information document in addition to the prospectus, it also grants retail investors more flexibility when selling assets to incentivise their participation. With the recent review of the ELTIFs framework, there is an opportunity to engage retail investors in investing in SMEs and further support SME financing in Romania.

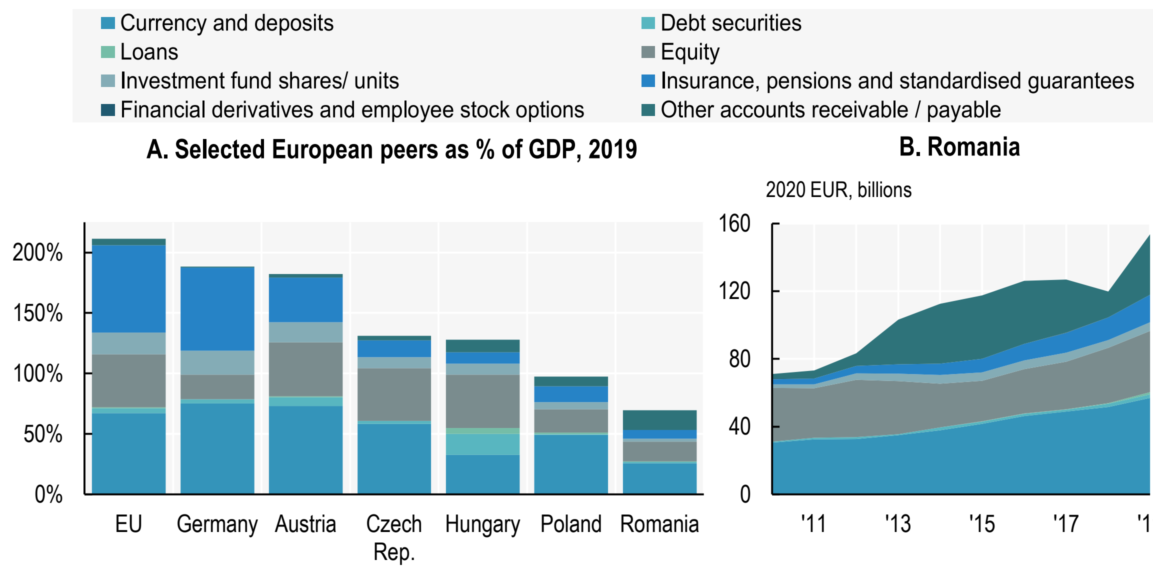
2.4. Promoting household savings

Household savings play an important role in a country’s economic development process. Besides being an instrument to smooth households’ consumption over time, their savings can be an important source of capital that can be channelled to finance the real sector and can contribute to higher levels of investment, job creation and growth. In general, the level of household savings can be influenced by macroeconomic factors such as the fiscal environment or financial markets regulation, but also by income levels, individuals’ risk aversion and financial education, among others (Anghel and Străchinaru, 2020[62]).

Romanian households’ financial assets more than doubled from EUR 71 billion in 2010 to EUR 154 billion in 2019 (Figure 2.16, Panel B). It is worth noting that although the amount of currency and deposits holdings doubled during that period (EUR 57 billion in 2019), equity holdings remained almost unchanged with a modest 14% increase. Despite the growth in the absolute amount of financial assets, there is still a significant gap compared with peer countries and EU averages. In Romania, households’ financial assets amount to 70% of Romanian GDP. This number is the lowest among European peers, with the share ranging from 98% of GDP in Poland to 189% in Germany and 211% in the European Union as a whole (Figure 2.16, Panel A). Regarding the composition of these financial assets, currency and deposits account for 26% of GDP in Romania whereas in the European Union they account for 67% of GDP and in Germany and Austria for more than 70%.

In line with low levels of financial assets, Romanian households' participation in the stock market is limited with equity representing 16% of GDP, investment fund shares only 2% and debt securities only 1%. In comparison, equity holdings account for more than 40% of GDP in Austria, the Czech Republic and Hungary, investment fund shares for more than 15% in Germany and Austria and, although the allocation to debt securities is relatively small on average in Europe in a global context, in some countries such as Hungary it represents a higher share (18% of GDP).

Figure 2.16. Households' financial assets composition



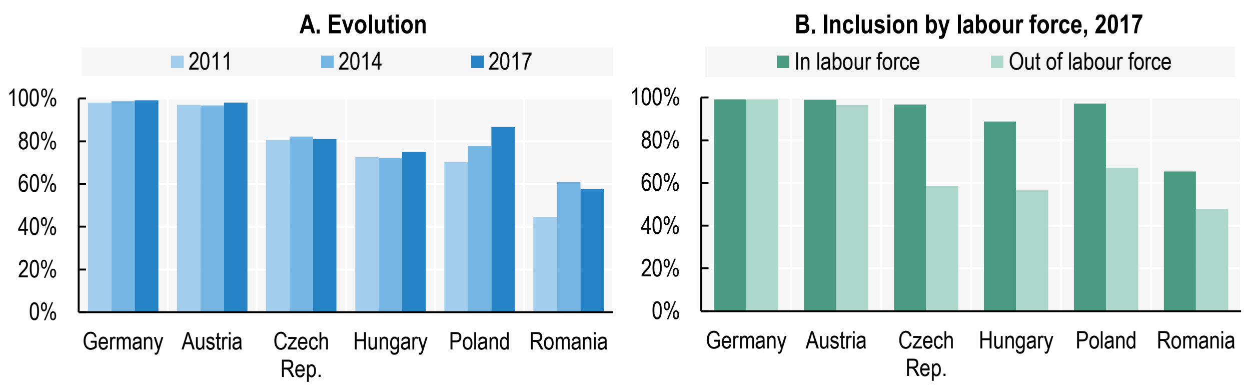
Source: Eurostat.

Some developing countries have developed innovative policies to allow more people to save. In Chile for example, a saving account separated from the mandatory savings (Pillar II) and the voluntary savings (Pillar III) was created. Every person with an account with a pension fund management company can open this saving account and is entitled to deposit any amount of money, on a regular basis or not, and can withdraw it at any point in time with a limit of 24 annual withdrawals. The person can choose one or a mix of the funds offered by the pension fund management company. The fees charged for the management of the savings vary between 0.16% and 0.95% of the balance in the account. The benefit of such an account is that the person choses between options of diversified portfolios managed at a greater scale in the same way the pension funds are invested. The number of accounts with a positive balance represented 13% of the number of accounts in the mandatory accounts in 2021 (Superintendencia de Pensiones, 2021[63]).

Aiming to increase the individual investor base, several countries have implemented individual savings accounts offering a favourable tax status. In recent years, Nordic European countries such as Sweden, Norway, Denmark and Finland introduced share savings accounts for listed shares and units in mutual funds that are either tax-free or taxed at a reduced rate on dividends and on capital gains. Similarly, in France, the *Plan d'Epargne en Actions* (PEA) is a saving instrument allowing households to invest in listed companies and collective investments with a deposit limit of EUR 150 000 and a tax exemption if there is no withdrawal during a minimum of five years. Moreover, in 2015, Russia introduced an individual investment account for private investors managed by brokers or management companies. The account holder can choose between a 13% tax deduction on its contributions to the account or a tax-free withdrawal on the account closure, with a minimum of three years. The singularity of this type of account is that the broker or management company can invest the clients' contributions in stocks, government bonds and foreign securities traded on the Russian stock market (Devlet-Geldy and Armidonova, 2016[64]). By the end of 2019, 1.6 million of this type of account were active, with a total market value of RUB 67.7 trillion (Bank of Russia, 2020[65]).

The modest levels of household savings relative to GDP and in absolute terms can partly be explained by the limited levels of both financial literacy and financial inclusion of Romanian households. Notably, Romania's GDP per capita accounted for less than EUR 10 000 in 2020, compared to EUR 22 400 in the European Union and more than EUR 34 000 in Germany and Austria. Although financial inclusion – measured as the percentage of the population with access to a bank account – increased from 45% in 2011 to 58% in 2017, Romania still lags behind its peers. The same ratio is 75% in Hungary, 81% in the Czech Republic and almost 100% in Germany and Austria (Figure 2.17, Panel A). When taking a closer look at financial inclusion according to the participation in the country's labour force, individuals that are active in the labour force are more likely to have a bank account. However, the gaps between those two groups are smaller in countries such as Germany and Austria, compared to, for instance, the Czech Republic where 97% of adults in the labour force have a bank account, against 59% for those who are out of the labour force. Remarkably, in Romania only 65% of the labour force participants have a bank account.

Figure 2.17. Financial inclusion in Romania and European peers



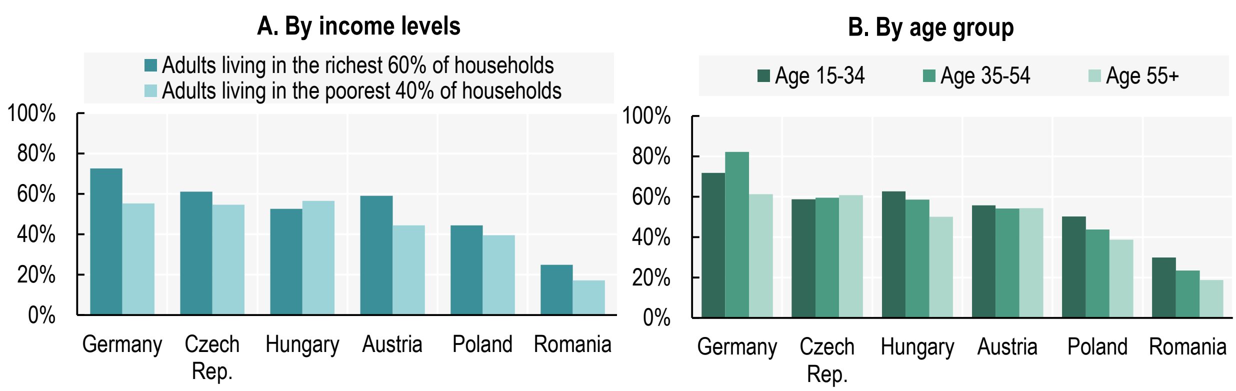
Source: World Bank – Findex database.

In 2017, Romania transposed the EU Directive 92/2014 by passing the Law on Comparability of Payment Account Fees, Change of Payments Accounts and Access to Basic Payment Accounts (EU, 2014[66]; Romanian Parliament, 2017[67]). This legislation introduced zero fee accounts for financially vulnerable consumers, defined as those whose monthly income does not exceed the equivalent of 60% of the country's population average gross earnings. In Romania, vulnerable consumers accounted for half of consumers in 2018 (World Bank and IMF, 2018[23]). In December 2020, the Romanian Association of Banks and the Romanian Institute for Evaluation conducted a study on a sample of 1 500 adults. The survey showed that 67% of Romanians use banking products and services, such as current accounts, cards, loans, deposits and make payments, compared to a 58% level of financial inclusion in 2017 (ARB and IRES, 2021[68]).

According to the Standard & Poor's Ratings Services Global Financial Literacy Survey, Romania presents the lowest rate of financial literacy in the European Union, with 22% of the population being financially literate (Klapper, Lusardi and Oudheusden, 2016[69]). Financially literate individuals have the skills to make informed choices regarding saving, investing and borrowing. This survey measures four fundamental concepts for financial decision-making, namely basic numeracy, interest compounding, inflation and risk diversification. Indeed, low levels of financial literacy can have a detrimental impact on consumers that can end up borrowing more and saving less, but also being less likely to appropriately plan their financial security after retirement (Stango and Zinman, 2009[70]; Lusardi and Mitchell, 2014[71]).

Financial literacy can vary according to the level of education, age group or income levels. Figure 2.18 shows financial literacy levels in Romania and its European peers, first by income levels and second by age group. Overall, except for Hungary, adults living in the richest 60% of households show higher levels of financial literacy compared to the 40% in the poorest households. For example, in Germany, 73% of the richest households are financially literate, compared with 55% for the poorest households. As previously mentioned, Romania ranks last in terms of financial literacy with 25% of the richest households being financially literate, and only 17% of the poorest ones. Regarding differences across different age groups, the Czech Republic and Austria show very similar financial literacy rates among all groups. In Germany, adults between 35 and 54 ranked first, with a rate of 82%. In Romania, financial literacy is the lowest for adults aged 55 and above, with a rate of financial literacy of 19%.

Figure 2.18. Financial literacy in Romania and European peers

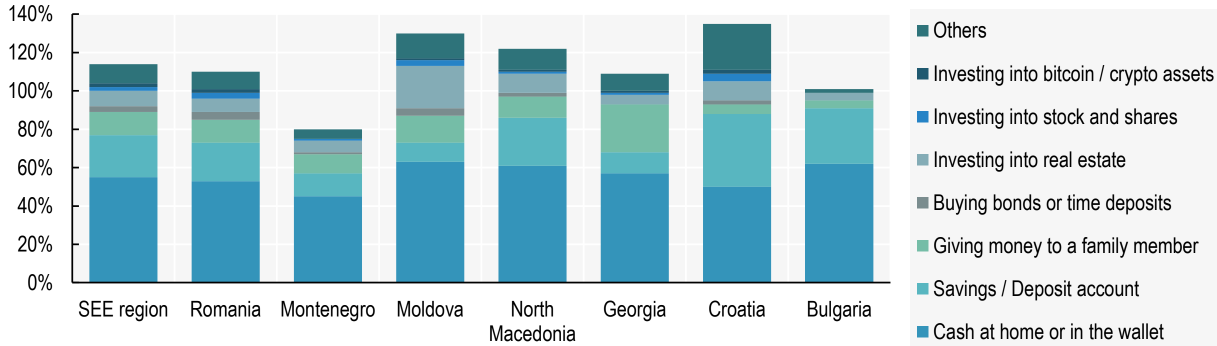


Source: The Standard & Poor's Ratings Services Global Financial Literacy Survey – 2015.

In 2019, the OECD conducted a survey of financial literacy levels in South East Europe gathering information on each of the elements of financial literacy, namely knowledge, behaviour and attitude. Romania's financial literacy score is 11.2 points out of a maximum of 21, with 3.5 out of 7 points in financial knowledge, five out of nine in financial behaviour and 2.7 out of 5 in financial attitude. Romania's scores for financial behaviour and financial attitude are comparable to the rest of the region, but its score for financial knowledge is the lowest (OECD, 2020[72]). Specifically, concerning households' financial attitude, when asked about the methods used for saving and investing in the last 12 months, overall, more than 50% of the respondents reported holding at least some of their savings in cash – in Romania cash is used by 53% of the respondents (Figure 2.19). Moreover, the only notable investment class throughout the region is real estate, with 7% of investments in Romania and more than 22% in Moldova. Other investment classes such as bonds, shares and crypto assets account for 4%, 3% and 2% respectively in Romania.

In July 2015, the Bucharest Stock Exchange launched the "Fluent in Finance" programme. In its initial phase the programme targeted companies interested in providing financial education to their employees, but the project was later extended to private individuals, students and to companies listed on BVB. By 2019, the programme had provided more than 250 seminars reaching more than 16 000 attendees. However only 32 of them were designed for private individual investors (BVB, 2019[73]). Moreover, in March 2018, 21 public and private institutions published the "Practical Manual for the Users of Financial Services", containing for the first time a compendium of information accessible to the general public, in order to promote familiarisation with the concepts of banking, capital markets, insurance, pensions and leasing (ARB, 2018[74]).

Figure 2.19. Methods of saving and investing in the SEE region



Note: Totals are not equal to 100%, as respondents may have given more than one answer.
Source: OECD/INFE Toolkit.

In July 2018, the Ministry for Education and Research, the National Bank of Romania, the Ministry for Public Finance, the Financial Supervisory Authority and the Romanian Association of Banks concluded a collaboration agreement for joint activities in the field of financial education and elaboration of the National Strategy for Financial Education. The initiative is supported by the OECD through a Technical Assistance project implemented through the Constituency Program of the Ministry of Finance in the Netherlands (SNEF, 2021[75]). The financial education platform was launched in March 2021, representing a milestone in the development of the Strategy. This interactive platform encompasses a list of actors engaged in activities or projects aimed at developing the general public's financial knowledge.

Recommendations

To promote household savings, Romania could/should:

- Increase the portion of the population that has access to a bank account through co-operative banks and implement cost-saving digital tools;
- Use the momentum from the National Strategy for Financial Education to reinforce co-operation among all stakeholders involved;
- Introduce a tax-exempt simplified individual savings account tailored to Romanian households.

Well-functioning capital markets provide households with more saving opportunities and allow for diversification and better planning for retirement. However, one of the main obstacles to the expansion of the Romanian capital markets is the limited levels of household savings and their low allocation to capital market securities. Financial inclusion in Romania has improved considerably recently, but still lags behind peer countries.

In order to increase the portion of the population that has access to a bank account, co-operative banks could become a key partner in implementing a low-cost saving digital tool. Under the supervision of the National Bank of Romania, the central body of credit co-operatives – the Banca Centrala Co-operatista Creditco-op – can gain scale by implementing cost-saving digital tools, for example via mobile phone access to services, that could enable them to reach financially excluded households.

Although several programmes to improve financial literacy have already been established, further efforts are needed to reach levels of financial literacy that can help develop a retail investor base in Romania. For this purpose, the Romanian authorities may consider using the momentum from the National Strategy for Financial Education, developed with the support of the OECD, to reinforce co-operation among all relevant stakeholders. Within this framework, seminars and trainings designed specifically to private investors should be implemented, with the aim of raising awareness about the benefits of actively participating in the country's capital markets. The Bucharest Stock Exchange should join this crucial initiative that will enable households to improve their understanding of and confidence in the Romanian capital market. In particular, the fact that the BVB recently established a co-operation programme with a crowdfunding platform, places it in a good position to attract more retail investors to its platforms.

Lastly, following the successful examples of several European countries that have introduced individual savings accounts offering a favourable tax treatment for individual investors, the authorities may consider designing a tax-exempt simplified individual savings account tailored to Romanian households. Either investment firms, pension fund management companies or asset management companies could offer this savings account that invests following similar investment rules as Pillar II funds at a low cost. This would not only increase household participation in the capital market but could also help pension fund management companies reach greater economies of scale.

2.5. Boosting the role of institutional investors

Institutional investors play an important role in developing capital markets in many emerging and developing countries. Owing to the longer-term nature of their liabilities, traditional institutional investors are considered as long-term investors able to channel a significant amount of financing to the real sector for investment and growth. In Romania, asset under management by institutional investors accounted for EUR 28.5 billion by the end of 2020. Within institutional investors, the largest category is pension funds, including mandatory and voluntary funds, with EUR 16 billion in assets under management. Investment funds follow with EUR 8.7 billion in AUM, and insurance corporations ranked last with only EUR 3.8 billion (ASF, 2021[76]).

2.5.1. Pension funds

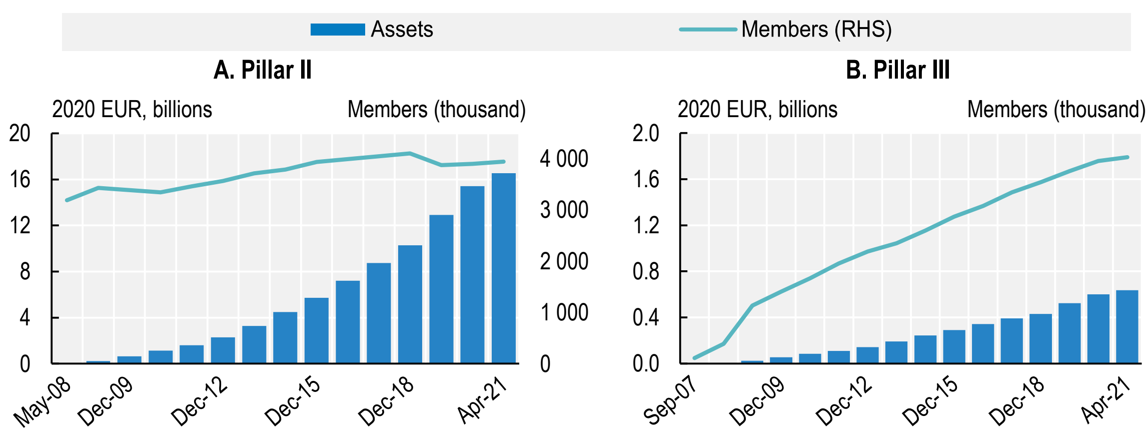
The pension system in Romania consists of three pillars. Pillar I is a pay-as-you-go system managed by the State. Pillar II is a mandatory funded and defined contribution pension scheme where each participant has its own individual account and is designed as a complement to Pillar I. Pillar III is a voluntary saving and defined contribution scheme. The multi-pillar system is new in Romania, since the voluntary savings scheme (Pillar III) was put in place in 2007 and the mandatory scheme (Pillar II) in 2008. Both Pillars II and III are privately managed by pension funds management companies. Women in Romania can currently retire at the age of 61 years and 9 months, but threshold will be gradually increased to 63 in 2030, and men at 65. They are entitled to receive a pension (Pillar I) if they have a minimum contribution of 15 years. However, since 2009, a minimum guaranteed social pension fully covered by the government also exists. Since 2018, around 800 000 people benefit from this minimum guaranteed pension which on average represents around EUR 32 a month.

At the start of the new pension system, 2% of the social contributions paid for those under 35 years old were channelled to the privately managed pension funds (Pillar II). For the employees between 35 and 45, this contribution was optional. The share of the social contributions going into Pillar II was supposed to increase gradually over an eight-year period by 0.5% until they reached 6% according to Law 411/2004 (Romanian Parliament, 2004[77]). However, Law 411/2004 has been modified and currently, the contribution is at 3.75% of the gross monthly income. Pillar III is a voluntary system managed and invested as Pillar II, but contributions are voluntary and are tax-deductible from the monthly average gross salary income. At inception, the maximum amount of the deduction was capped at the equivalent of EUR 200 in one fiscal year and today it stands at EUR 400. The voluntary pension funds' assets are tax-exempt until the benefits are paid to the beneficiaries.

By the end of April 2021, there were seven pension management companies managing in total EUR 16.5 billion for the Pillar II and EUR 638 million for the Pillar III (Figure 2.20). The number of participants[11] in Pillar II has grown from 3.2 million in 2008 to 3.9 million by the end of 2020. Despite the growth in assets under management, since March 2019, the share of members with no contributions in the last month represented over 45% of the total number of members of the system, above its historical average of 39%. Pillar III reached over 500 000 members by the end of April 2021 and only EUR 637 000 in assets under management, around 4% of the Pillar II AUM.

The tax treatment of retirement savings in Romania follows an Exempt-Exempt-Taxed (EET) model. Employee contributions are tax-deductible and investment returns are tax-exempt. Pension benefits paid out during retirement will be subject to a personal income tax rate of 10% above a certain level (EUR 460 in 2018). In OECD countries, the most common tax treatment of retirement savings exempts contributions and returns on investment from taxation while taxing pension benefits and withdrawals as income. It has been suggested that EET regimes encourage participation and contributions to retirement savings plans when personal income tax system is progressive (OECD, 2018[6]).

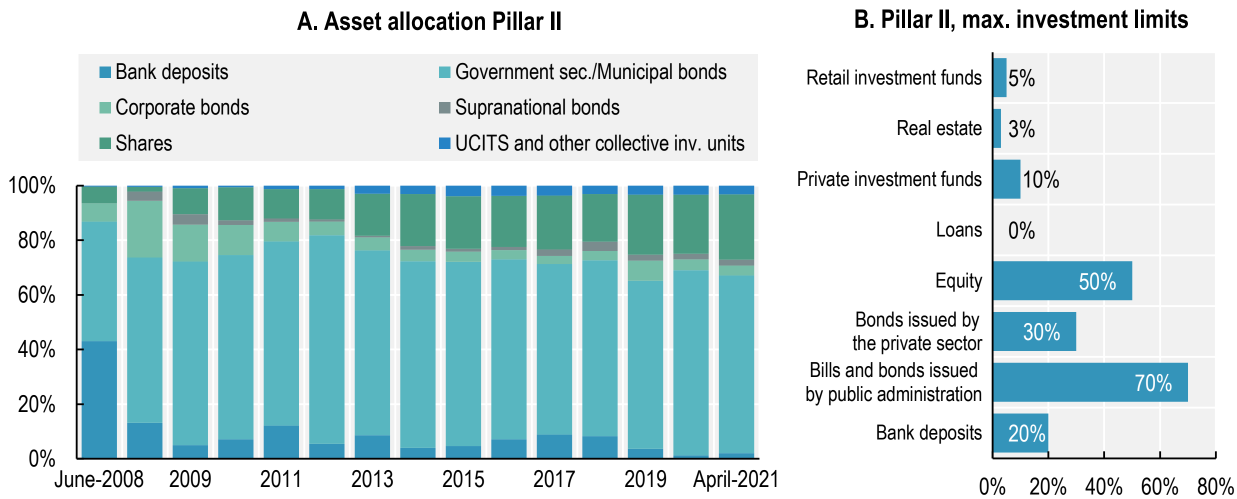
Figure 2.20. Assets under management and participants Pillars II and III



Source: ASF.

Pension funds in Romania follow an overall conservative investment strategy since the vast majority of their assets are invested in fixed income securities (Figure 2.21). At the end of April 2021, 65% of the assets were allocated to government securities, 2% to deposits and another 2% to supranational bonds. Companies' shares make up the second largest investment asset class of the pension system in 2021. Pension funds have been increasingly allocating part of their investment to equity, starting in 2008 with just 6% of the assets invested in equity to reach 24% by the end of April 2021. On the contrary, the importance of corporate bonds in the portfolio allocation of pension funds has declined. The latest available information shows that they represent only 4% of the total pension funds' assets in 2021. Investment in collective investment units is also modest.

Figure 2.21. Asset allocation and maximum limits of Pillar II



Source: Panel A, ASF; Panel B, (OECD, 2020[78])

Pension funds in Romania face investment limits that bound their investments. Pillar II and Pillar III funds are subject to the same limits and there are no different risk category funds defined by law or regulation. However, based on weighting assets according to their risk, pension funds are rated according to different risk profiles (Boon, 2016[79]). Funds are allowed to invest a maximum of 50% of their assets in equity and 30% in bonds issued by the private sector. Both limits for the entire Pillar II funds are far from binding. Not surprisingly, bills and bonds issued by the public administration is the only asset class with a limit that is closed to be reached. Notably, pension funds in Romania are allowed to invest a maximum of only 10% of their assets in private investment funds and only 3% in real estate.

The investment limits are currently not the main effective binding restriction for pension funds. The current regulation in place (ASF Norm No. 11/2011, chapter VII) requires pension funds to classify themselves under a set of pre-defined risk categories (low, medium and high-risk) (ASF, 2011[80]). The regulation provides a formula (shown below) to assess the risk category by weighting the value of assets invested in a particular asset class by their corresponding risk weight. The riskier the asset according to the regulator, the lower the weight in the formula below.

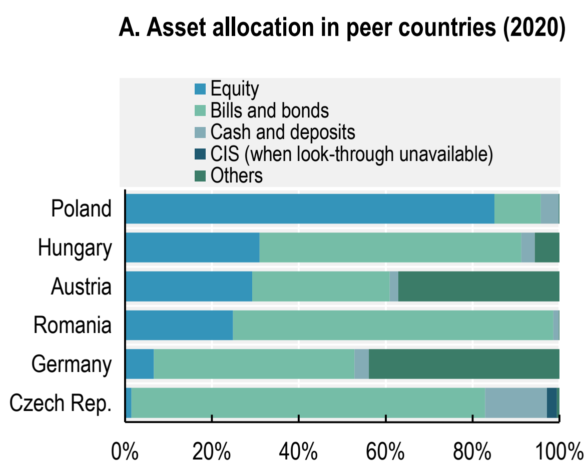
$$Risk\ degree = 100\% - \frac{\sum(Risk\ weighted\ assets)}{Total\ assets - Sum\ of\ assets\ in\ transit}$$

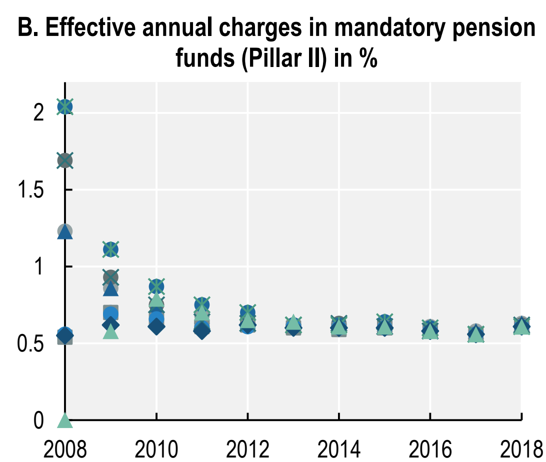
Funds that have a risk degree less than or equal to 10% are considered low-risk pension funds; those with a risk degree greater than 10% and less than or equal to 25% are considered medium-risk; and those with risk degrees greater than 25% and less than or equal to 50% are considered high-risk funds. The current regulation establishes different risk weights to different assets classes. For example, deposits and government securities issued by Romania and EU investment grade countries are assigned a weighting of 100%; a weight of 75% is applied to reverse repo agreements; 25% to shares and rights traded on regulated markets in Romania or in EU/EEA member states. These weightings result in conservative asset allocations by pension funds. For example, a fund that invests only in listed equities and Romanian Governments bonds will be considered low risk only if it invests less than approximately 13% of its portfolio in shares (and thus 87% in government bonds) and medium risk only if it does not surpass one-third of the portfolio allocated to shares (i.e. two-thirds in government bonds). Notably, precious metals (e.g. gold) are assigned a weight of 25%. This means that a hypothetical portfolio holding 65% government bonds and 35% gold, a conservative allocation by any measure, would be classified in the highest possible risk category. There is also no distinction between different types of private equity. All private equity assets are assigned a weight of 0%, without distinguishing between investments in private equity funds that provide diversification (and professional management), and therefore lower risk, and the same amount of money invested directly in the unlisted shares of a single company. The actual risk profile of those two investments would differ significantly.

Despite the increasing amount invested in equity by pension funds in Romania, their participation in the stock market is still relatively modest compared to peer countries, which to an extent probably stems the risk weights that currently apply. For example, pension funds in Poland, Hungary and Austria hold a higher share of their assets in equity. In addition, Romanian pension funds do not invest in any other asset class that could help diversify their portfolios further. For example, pension funds in Germany and Austria hold a significant share of their assets in other assets, including private equity among others.

Pension management companies in Romania charge commissions and fees to beneficiaries in exchange for the management of their retirement savings. The current system charges two types of fees: the management commission, equivalent to 0.5% of each monthly contribution to the fund; and the management fee, a monthly deduction from the total net assets of the funds, varies from 0.02% to 0.07%. In addition, beneficiaries are subject to transfer penalties if they move to another fund before two years – between 3.5% and 5% of the assets in the account of the beneficiary. Panel B in Figure 2.22 shows an estimate of the effective annual charges different pension funds charge their clients. The effective annual charges have become less disperse across funds over time and in 2018 the seven active pension funds were charging almost the same amount.

Figure 2.22. Asset allocation in peer countries in 2020





Note: The “Others” category includes loans, land and buildings, unallocated insurance contracts, hedge funds, private equity funds, structured products, other mutual funds (i.e. not invested in equities, bills and bonds or cash and deposits) and other investments. Data in Panel B correspond to the seven existing pension funds.
Source: OECD Global Pension Statistics, (EU, 2019[81]).

In December 2018, the management commissions charged by pension fund management companies for the monthly contributions to the funds were significantly cut and were further modified in 2020. The reduction in fees has translated into lower revenues for pension management companies impacting negatively their results (EC, 2020[11]). However, these legal provisions were repealed in 2020.

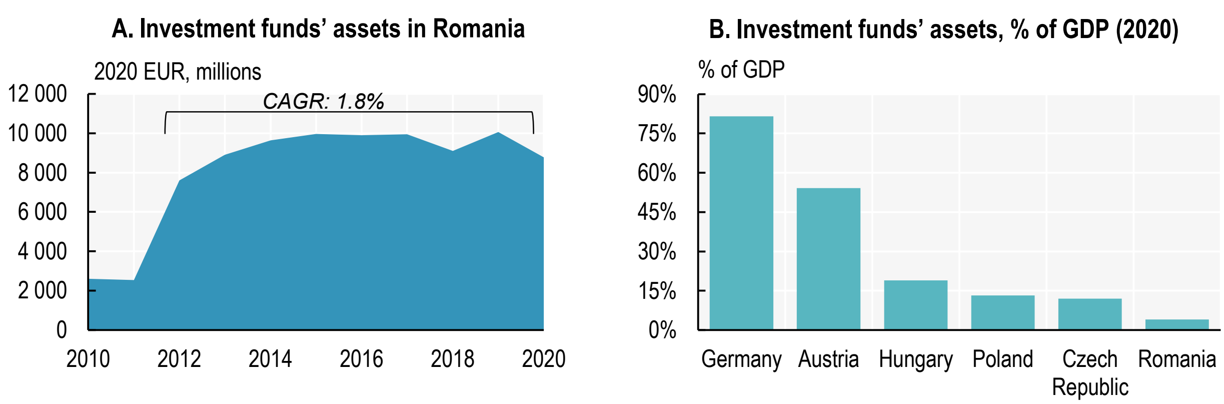
Securities lending is an opportunity for long-term investors to gain an extra premium from their assets by providing liquidity to the market. In the process securities are lent to market participants for a variety of purposes. The borrower of the security pays a fee to the lender, typically monthly, and normally transfer a collateral to reduce the lender’s exposure to the borrower. The process could be delegated to an agent, a custodian in most cases, who carries the responsibility for recording details of the lent securities and ensures that risks are managed by pledging a collateral. According to ESMA, 90% of the equities lending in Europe is done via an agent, either large custodian banks or asset managers (ESMA, 2016[82]). Many funds as part of their efficient portfolio strategy lend securities and, by doing so, generate extra returns for their portfolios. Securities lending can also increase settlement efficiency in financial markets and plays an increasingly important role in addressing the demand for collateral in the system as regulators seek to improve market infrastructure and mitigate systemic risk.

The buy-and-hold nature of pension funds and other long-term investors place them as ideal candidates to lend the assets in their portfolio. This is particularly true for relatively small markets where the presence of large pension funds could result in less available securities for trade. The fact that pension funds do not rotate their portfolios frequently makes them liquidity takers instead of liquidity providers from a market perspective.

2.5.2. Investment funds

Investment funds in Romania are the third largest category of traditional institutional investors with almost EUR 9 billion of assets under management at the end of 2020 (Panel A of Figure 2.23). The industry experienced a rapid increase in assets under management in 2012, but ever since assets have barely increased at an average annual rate of 1.8%. More importantly, their relative size compared to peer countries is modest. For example, in Germany and Austria, investment funds assets account for over 50% of domestic GDP. In Hungary, Poland and the Czech Republic they account for between 12 and 19% of GDP, and in Romania, ranked lowest, only 4% of GDP (Panel B, Figure 2.23).

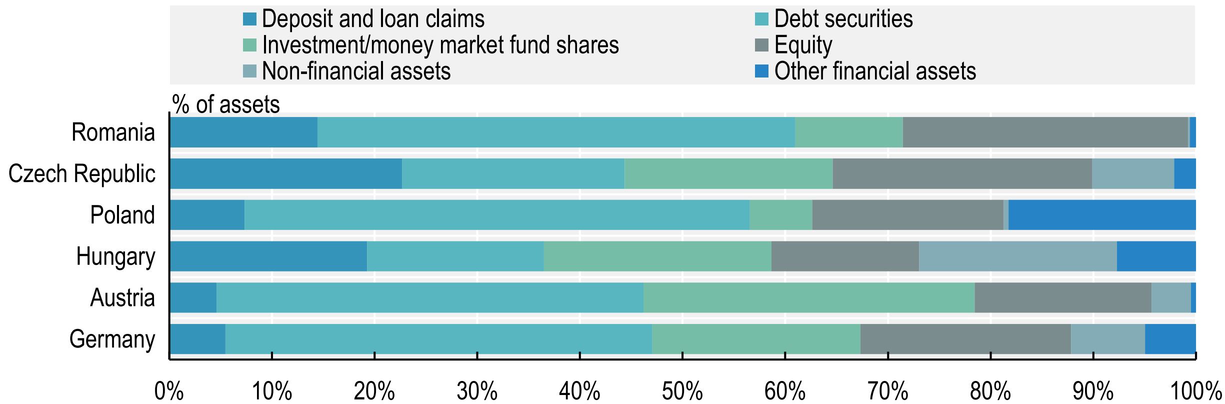
Figure 2.23. Investment funds' assets



Source: ECB Statistical Data Warehouse, Eurostat.

The asset allocation of investment funds in Romania does not differ much from that in other countries. Investment funds in Romania allocate 36% of their assets to debt securities, which is lower than what investment funds allocate to these securities in Poland, Germany and Austria, but still higher than in the Czech Republic and Hungary (Figure 2.24). Investment funds in Romania allocate 43% of their assets to equity, the highest share among peer countries. However, almost half of the equity investment by Romanian investment funds corresponds to the investments by Fondul Proprietatea,[12] representing shares granted to people whose assets were expropriated by the communist regime (especially in cases when restitution in kind would not be possible).

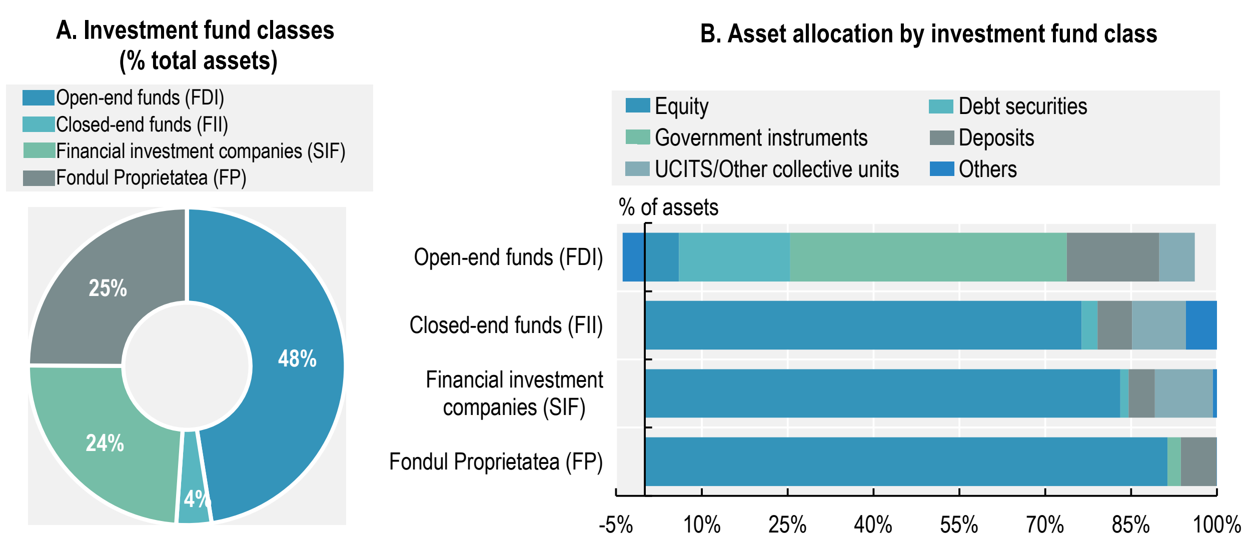
Figure 2.24. Investment funds' asset allocation



Source: ECB Statistical Data Warehouse.

The investment funds industry in Romania has developed around large banking groups. At the end of March 2021, the top 5 investment management companies were related to banks and they concentrated 93% of the total assets related to the investment fund industry. Another characteristic of the industry is the clear dominance of open-end funds (Figure 2.25, Panel A). Of the EUR 8.99 billion in assets under management, almost half correspond to 81 open-end funds that are mostly sold to retail investors. Closed-end funds are smaller in number (26) and in AUM. These types of funds are mostly targeted to qualified investors due to their illiquid nature representing only 4% of the industry assets. In Romania there are five financial investment companies that account for 24% of the assets and Fondul Proprietatea as a separate investment company that has a size equivalent to 25% of the total industry assets.

Figure 2.25. Investment fund classes and their asset allocation by the end of March 2021



Note: Fondul Proprietatea was set up by the Romanian state in 28 December 2005 to indemnify persons whose assets were expropriated by the communist regime (especially in cases when restitution in kind would not be possible) by granting shares in Fondul Proprietatea to the respective persons proportionate to their loss.
Source: ASF.

The largest category, open-end funds, is the one that invests the lowest share in equity (6%) and the highest share in debt securities (21%) and government instruments (52%) (Figure 2.25, Panel B). All other fund categories invest a much higher share in equity, both listed and unlisted. In the case of closed-end funds and financial investment companies, over 70% of their investments correspond to listed equity, and only 18% in the case of Fondul Proprietatea. Investments in corporate bonds are generally low. Open-end funds are the ones that allocate the highest share to corporate bonds with 18%, whereas closed-end funds and financial companies only invest 1.43% and 0.44% respectively.

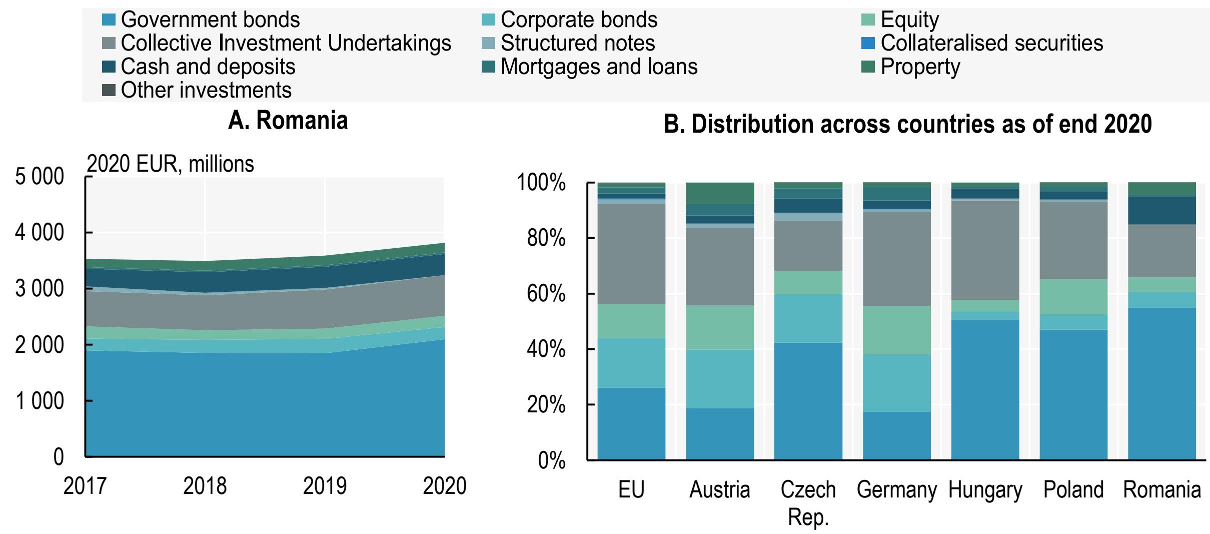
2.5.3. Insurance companies

European Union accession in 2007 led to the internationalisation of the insurance sector in Romania, which translated into increased competition and modifications in the supervisory and legal frameworks. In 2015, the Financial Supervisory Authority, in co-operation with the European Insurance and Occupational Pensions Authority, conducted an assessment of the Romanian insurance sector, in which they concluded that insurance companies were not adequately capitalised and that actions were needed to improve their solvency (ASF, 2015[83]). As a result, market exits and multiple remedial actions took place. The Romanian authorities established a resolution framework for the insurance sector inspired by the EU Bank Recovery and Resolution Directive (World Bank and IMF, 2018[23]). In 2016, the consolidation of the insurance corporations' activities was stimulated by the introduction of the Solvency II European directive aiming at ensuring the integration and unitary functioning of the European insurance market. Following the introduction of the Solvency II regime, insurance companies received a capital injection of more than EUR 130 million by foreign shareholders strengthening their capital positions (Dina, 2018[84]).

In Romania, the property and motor third party liability insurance (MTPL) companies lead the insurance market. With the aim of stabilising the MTPL market, the Romanian Parliament enacted the MTPL Law (Legea 132/2017) introducing reference tariffs and more effective protection of the rights of MTPL policyholders (Romanian Parliament, 2017[85]; ASF, 2017[86]) In 2019, the ASF, together with the Ministry of Public Finance, proposed an amendment to the 2017 MTPL Law to fulfil European obligations under Directive 2009/138/EC and in Article 14 of Directive 2009/103/EC by, among others, eliminating the provisions limiting the administrative expenses and selling the insurance policy that may be included by the insurer in the premium calculation tariff (ASF, 2020[35]).

At the end of 2019, there were 28 insurance corporations in Romania, of which 15 were non-life insurance, seven life insurance and six composites (ASF, 2020[35]). The total assets of Romanian insurance corporations amounted to EUR 3.8 billion in 2020, accounting for less than 2% of Romania's GDP, a modest increase from the 2017 amount of EUR 3.5 billion (Figure 2.26, Panel A). In terms of asset composition, insurance corporations allocate 55% of their assets to government bonds. Government bonds allocation is also high in Hungary, Poland and the Czech Republic, but in Austria and Germany, it represents less than 20%, and in the European Union it amounts to 26% of total asset allocation. Collective investment undertakings are the second largest category in Romania, representing 19% of the assets in 2020, still behind the European Union average at 36%.Furthermore, as Romanian insurance companies are part of international groups, the collective investment undertakings are generally observed in cross border funds rather than in the Romanian capital market. Moreover, insurance companies in Romania only allocate 6% of their assets to corporate bonds compared to, for example, 18% in the Czech Republic. Likewise, the equity allocation is modest with only 5%, compared to 13% of the assets in Poland (Figure 2.26, Panel B).

Figure 2.26. Asset allocation of insurance corporations



Note: Asset allocation is based on the asset exposures statistics.
Source: EIOPA Solvency II statistics.

Recommendations

To boost the role of institutional investors, Romania could/should:

- Consider revising the risk-weighting methodology currently applicable to pension funds aiming to increase the effective investable universe of asset classes;
- Consider allowing pension funds to lend securities to provide an extra return for beneficiaries and support secondary market liquidity;
- Consider increasing the fiscal deductibility of the annual contribution to Pillar III of the pension system and indexing it to a relevant income measure in the country, and increase awareness of the need for a higher saving rate;
- Simplify the approval process for funds, for example by standardising some of the required documents;
- Promote occupational pension schemes within the scope of the *national private-public campaign*.

Romanian institutional investors could help drive the development of capital markets by providing the real sector with long-term capital to invest, innovate and grow. This has been the case in many other countries that have established funded pension systems. However, the system in Romania is still young and many challenges remain. In order to continue boosting the role of institutional investors in capital markets the authorities may consider the policy initiatives outlined below.

As the pension system in Romania matures, the regulator should consider developing a strategic approach to further develop the system. Both Pillars II and III of the pension system currently follow investment limits in different assets classes in order to ensure a balanced diversification of risks and have to apply a risk-weighted assets approach. These restrictions, combined with the very few available securities, will eventually make it harder for pension management companies to deliver an adequate return to their beneficiaries. Therefore, the regulator should consider revising the risk weighting methodology currently applicable to pension funds with a view to effectively increasing the investable universe of asset classes.

Moreover, the authorities should consider allowing pension funds to lend securities, with the aim of providing an extra return for beneficiaries and to support secondary market liquidity given the limited rotation of pension funds' portfolios. Considering the social purpose of pension funds, securities lending will require the completion of the establishment of a Central Clearing Counterparty (CCP) and a well-functioning market that ensures harmonisation and integration of securities settlement, and collateral management as well as the proper execution of guarantees.

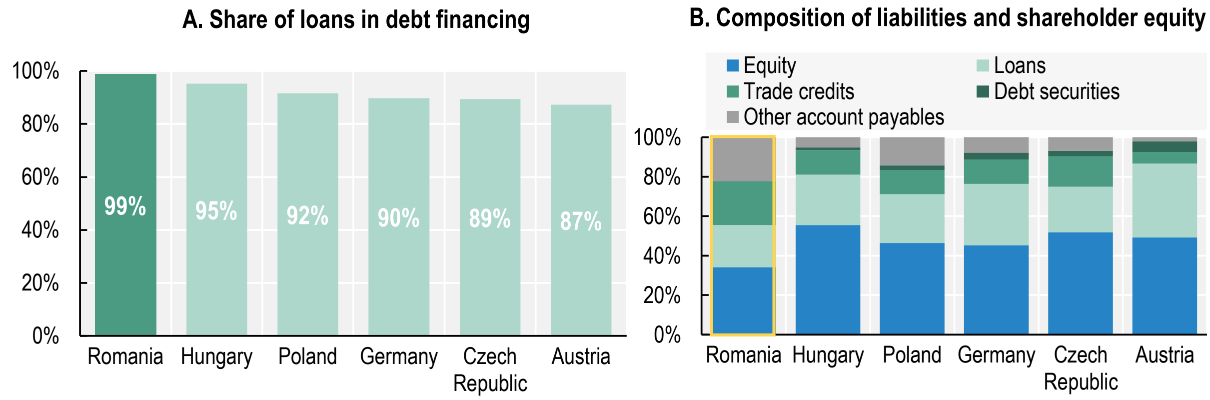
The voluntary saving system has not grown as expected and the balance in each account remains modest. Therefore, the government may consider increasing the fiscal deductibility of the annual contribution and indexing it to a relevant income measure in the country. Romania needs a fiscal system that encourages long-term savings, and fiscal incentives is one among many tools that the government can use to boost savings. In addition, the authorities may prioritise improving communications to the public aiming to increase knowledge and awareness of the need for a higher savings rate. The promotion of long-term investment products targeted to households could also be part of the national private-public campaign mentioned above. Occupational pension schemes should also be promoted within the scope of the *national private-public campaign*, since they represent another alternative to foster long-term savings.

The investment fund industry is still underdeveloped in Romania. Moreover, probably due to the lack of listed securities, investment funds allocate a small share of their assets to these instruments. Similarly, the insurance industry is still immature and further efforts are needed to continue expanding it beyond the property and motor third party liability insurance. The investments of insurance corporations are highly concentrated in government bonds. However, if the industry develops further, it can be expected that insurance companies will increasingly demand other long-term securities that can provide higher returns. Therefore, promoting the participation of more issuers in the capital market, either via listed equity or corporate bonds, could contribute to further developing the entire market. In addition, a simplification of the approval process for funds, for example by standardising some of the required documents, could further support the development of the industry.

2.6. Facilitating market-based long-term debt financing

Corporate access to credit is generally deficient in Romania and the problem is particularly pronounced for market-based financing. Firms are reliant on internal funds to finance their operations and investments. In terms of external financing, bank loans are the dominant form of credit. Even so, in 2018 bank loans to GDP was only 11.7%, about a third of the EU average. Lower still, market-based financing stood at 6.2% in the same year, representing one-eighth of the EU average (EC, 2020[11]). Compared to European peers – which are already heavily bank dependent in a global context – Romania is the country where bank loans make up the largest share in total debt financing, at 99% (Figure 2.27, Panel A). As Panel B of Figure 2.27 shows, the low access to debt financing does not translate into a higher share of equity financing for Romanian non-financial firms, but rather into trade credits and other account payables. Further, Romanian companies are dependent on foreign credit. At the end of 2019, loans from non-resident financial institutions were 20% higher than those from resident ones (see Chapter 3).

Figure 2.27. Composition of non-financial corporations' liabilities as of Q4 2020



Note: In Panel A, bank loans are measured as a share of the sum of bank loans (long-term and short-term) and debt securities (long-term and short-term).
Source: ECB Statistical Data Warehouse.

The general lack of credit access constitutes a barrier to corporate investment and economic growth, and the overreliance on bank loans compared to market-based financing is a potential impediment to corporate resilience and financial stability more generally. Owing to the pro cyclicality of bank financing, when recessions and financial crises coincide, the negative impact on GDP is three times larger in bank-dependent economies compared to economies more oriented towards market-based financing (Gambacorta, Yang and Tsatsaronis, 2014[87]).

The Romanian corporate bond market is still small. Total issuance between 2009 and 2019 amounted to only 0.01% of GDP, significantly lower than regional peers such as Hungary (0.3%) or Poland (0.5%). The Main Market of the BVB is dominated by financial companies, which make up over 90% of all total amount of issuance (see Chapter 5 for more details). The trend is the opposite for the more recently established, SME-focused AeRO Market. In addition, most corporate bonds are not listed on the local stock exchange, which also differs from peer countries where local listings are much more common. Foreign currency borrowing is common, with 94% of all Romanian non-financial corporate bonds issued either in EUR (54%) or USD (40%). This is significantly higher than regional peers, although mainly dominated by a number of large issuances on foreign stock exchanges. Domestic investors are not active in the Romanian corporate bond market, holding only 8% of the outstanding stock of non-financial corporate bonds. Finally, a benefit of bond markets is that bonds typically offer longer maturities compared to bank loans and are therefore better suited to finance longer-term investments. However, owing to the underdevelopment of the Romanian corporate bond market, in the two decades since 2000 there has not been a single Romanian corporate bond issuance with a maturity over ten years (see Chapter 5).

The lack of a well-functioning corporate bond market has not only led to significant restrictions in access to finance for substantial segments of the Romanian corporate sector, but has also resulted in a high exposure to Romanian Government securities among institutional investors. For example, at the end of April 2021 government bonds made up 65% of Pillar II pension funds' portfolios whereas corporate bonds only represented 3.7% (ASF, 2021[88]). In addition, together with insurance companies Romanian pension funds have the lowest share of investment in domestic corporate bonds compared to peer countries. While pension funds and insurance corporations in Hungary, the Czech Republic, and Poland owned 3.5%, 4.2% and 6.6% of the outstanding stock of non-financial corporate bonds respectively at the end of the third quarter of 2020, the share in Romania is almost non-existent. However, Romanian investment funds own 4% of the outstanding stock of corporate bonds. Most of the holdings correspond to open-end funds which by the end March 2021 were allocating 20% of their assets to listed corporate bonds. Closed-end investment funds' portfolio allocation was more conservative at 1.43% (ASF, 2021[76]).

Low levels of investment in corporate bonds by pension funds is partly a regulatory effect. Pension funds are allowed to invest a maximum of 30% of their assets under management in bonds issued by the private sector (OECD, 2020[78]). While the overall limit for pension funds to invest in corporate bonds in Romania is similar to its peer countries, in reality these investments remain modest, representing only around one-eighth of the maximum limit allowed by the end of April 2021. Pension funds in Romania are generally only allowed to invest in debt securities issued by companies in Romania, the EU or the European Economic Area (EEA) which have an investment grade credit rating from at least one of the main three rating agencies (or two investment grade ratings in the case that several agencies rate the bond). Non-investment grade bonds are allowed in their portfolios provided that the rating is no more than one notch below Romania's sovereign rating and that it is no lower than one notch below investment grade from any of the main three rating agencies (ASF, 2011[80]). Pension funds are also allowed to hold unrated bonds (within certain limits) provided that the issuer's shares are traded on a regulated market in Romania, the European Union or the European Economic Area. Unrated and non-investment grade bonds may not make up more than 3% of a fund's portfolio.

Obtaining a credit rating for a bond issuance from the large international rating agencies can be unaffordable for many issuers in Romania, particularly for smaller issuers. This in turn restricts the investable universe for institutional investors and distances these companies from the possibility of market-based financing. Market participants have highlighted that the fixed cost associated with obtaining a credit rating is too high relative to the size of bonds envisioned by smaller issuers. This creates a barrier to access bond financing that ultimately reduces the available liquidity in the market. Under the existing regulatory framework, which only makes reference to the three major rating agencies, the scope for a domestic credit rating agency focused specifically on Romanian companies or a European rating agency is limited. Some markets, in the understanding that the domestic issuance is not targeted to foreign investors but rather to domestic investors, have established alternative credit rating systems. For example, in France the Banque de France provides a credit score on individual firms for a fee, through the FIBEN (*Fichier bancaire des entreprises*) system.

In addition to the limited number of securities available for investment, pension funds face further restrictions that reduce their investment options even further. As a measure to increase diversification, pension funds are not allowed to buy more than 5% (10%) of the total principal of a corporate bond issued by a single issuer (by a group of issuers), which, owing to the modest size of most Romanian bond issuances, limits the range of worthwhile investments.

An issue which may be contributing to the underdevelopment of the corporate bond market is the corporate bond issuance process. As an initial overview, Table 2.3 compares the fees charged by the Bucharest Stock Exchange with different regional peers. The fees are calculated both for a small bond issuance of EUR 3 million and for a large issuance of EUR 48 million, corresponding to the average size of corporate bonds on the Main Market of the BVB. Both have an assumed maturity of five years. While it is relatively expensive to issue small corporate bonds on the Main Market in Romania compared to Hungary and Poland, it should be noted that the alternative AeRO Market offers a more attractive fee structure for smaller companies. When looking at larger issuances, the BVB is competitive when it comes to fees charged by the exchange. The fees for a corporate bond with a principal of EUR 48 million and a maturity of five years are 112% of those charged by the Prague Stock Exchange, 52% of those charged by the Warsaw Stock Exchange and only 14% of those charged by the Budapest Stock Exchange.

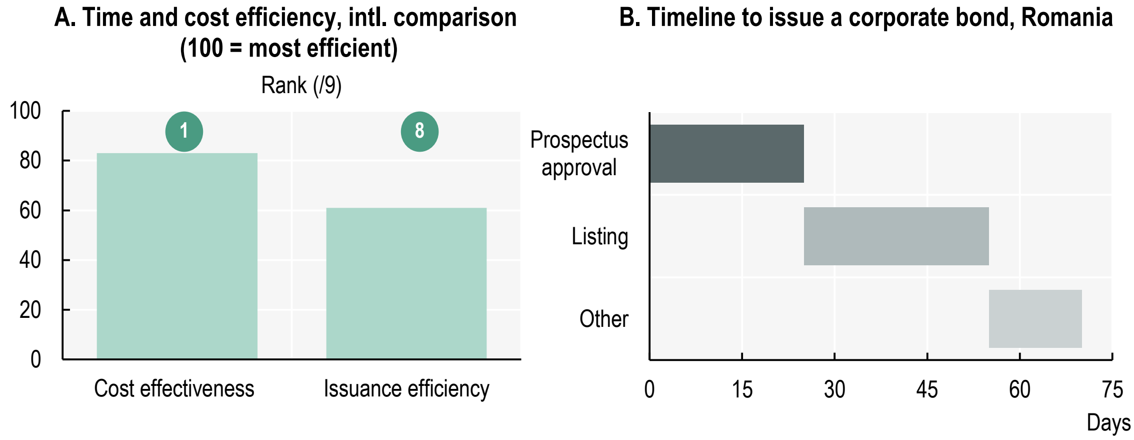
Table 2.3. Corporate bond listing fees, different markets (EUR)

EUR	Bucharest	Prague	Budapest	Warsaw
	Principal: EUR 3 million			
Processing fee (one-off)	240	0	0	0
Admission fee (one-off)	600	1 950	300	330
Maintenance fee (annual)	3 000	1 950	1 710	550
Total (5 years)	**3 840**	**3 900**	**2 010**	**880**
As percentage of amount issued	*0.13%*	*0.13%*	*0.07%*	*0.03%*
	Principal: EUR 48 million			
Processing fee (one-off)	240	0	0	0
Admission fee (one-off)	690	1 950	4 800	3 600
Maintenance fee (annual)	3 450	1 950	27 360	4 800
Total (5 years)	**4 380**	**3 900**	**32 160**	**8 400**
As percentage of amount issued	*0.01%*	*0.01%*	*0.07%*	*0.02%*

Note: Bonds are assumed to be listed on the Standard/Regulated Tier of each market. Maturity is assumed to be five years, and it is assumed that the issuer does not have equity listed on the local exchange. The Prague Stock Exchange applies lower fees to issuances with maturities below 12 months, and the Budapest and Warsaw Exchanges offer discounts for companies that also have equity listed on the exchange.
Source: Bucharest Stock Exchange, Prague Stock Exchange, Budapest Stock Exchange, Warsaw Stock Exchange.

However, as with equity, the main costs associated with listing a corporate bond are not necessarily the exchange fees. In a comparative study of debt markets in nine countries in South-Eastern and Central Europe, the EBRD provides a comparison of costs associated with issuing a bond which, in addition to issuance fees, also includes direct and indirect trading costs, costs for settlement and safekeeping as well as tax costs (EBRD, 2020[89]). Although the group of peer countries differs from Table 2.3, the results are similar. Romania ranks first of the nine countries in terms of cost effectiveness, with a value of 83 out of 100. However, when looking instead at issuance efficiency, a measure based on the time it takes to issue a bond, Romania ranks second to last with a score of 61 (Figure 2.28, Panel A). On average, it takes 70 days to issue a corporate bond in Romania, compared to five days in Bulgaria and 22 days in Montenegro. The most time-consuming part of the issuance process in Romania, with an average of 30 days, is the listing, i.e. agreement in principle and admission. Prospectus approval on average takes 25 days (Figure 2.28, Panel B). It should be noted that the ASF has a maximum ten-day deadline to approve prospectuses, but the EBRD report notes that this conflicts with market participants' experiences of the actual time required for approval. According to the regulator, the delays in many cases occur when an issuer's documentation does not meet the required standard and/or supplementary information is required. In addition, there is a requirement to hold an extraordinary general meeting in order to approve the prospectus to issue a corporate bond, which complicates the process and extends the issuance timeline.

Figure 2.28. Time and cost efficiency for corporate bond issuances



Note: Aside from Romania, the eight reference countries in the study are Bosnia and Herzegovina, Bulgaria, Croatia, Montenegro, North Macedonia, Republika Srpska, Serbia and the Slovak Republic.
Source: (EBRD, 2020[89]).

Fiscal constraints on governments, in particular in developing countries, can make it difficult to provide public financing for large-scale infrastructure needs. As a result, the private sector often plays an important role in financing such projects. A commonly applied model for financing of these projects is public-private partnerships (PPP), in which risk is shared to varying degrees between the public and private sector. Due to their long-term nature, infrastructure projects are well-suited for bond financing. Importantly, infrastructure bonds issued through a PPP project could support the development of local currency bond markets as well as provide investment opportunities for institutional investors with long-term liabilities, such as pension funds and insurers. In general, as recommended in the *OECD Principles for Public Governance of Public-Private Partnerships*, policy makers should ensure that the public governance framework for PPPs is set and monitored at the highest political level, so that a whole of government approach ensures affordability, transparency and value for money (OECD, 2012[90]). In this respect, PPP projects need to be structured carefully to mitigate any possible drawbacks such as the typically higher private sector financing cost relative to governments' own borrowing costs and issues with the quality of the services provided by the private sector. Therefore, contracts have to be designed to include sufficient tools securing both the quality and a reasonable cost (CEB, 2017[91]). In Romania, the quality and reliability of transport infrastructure is still inadequate, below peers countries and the EU average (EC, 2020[11]). Moreover, the country is also lacking investment in sustainable transport, energy and environmental infrastructure (i.e. in waste, wastewater and air pollution). Importantly, the European Commission has noted that insufficient levels of infrastructure investment in Romania constitutes a barrier for its economic convergence with EU levels. Currently, Romanian has a number of PPP projects in progress financed or projected to be financed through loans provided by international financing institutions or by commercial banks (CNP, 2021[92]).

The low levels of market-based financing in Romania are possibly also suggestive of a limited awareness among companies, especially SMEs, about alternative sources of financing and the possibility of external financing in general. In 2018, the BVB and the Romanian Ministry for the Business Environment signed a partnership for promoting financing opportunities through capital markets and organised a series of eight workshops where the BVB provided an overview of the opportunities that market-based financing can offer, both to companies that want to expand and to individual investors who want to use the stock exchange (BVB, 2018[93]). The BVB has also previously conducted workshops and engaged in activities targeting companies, although most of these were short-term programmes (BVB, 2017[94]), (BVB, 2014[95]). Several other countries also have initiatives in place to increase corporate financial literacy, such as the implementation of a national strategy with a committee overseeing the process, training sessions for entrepreneurs, business owners and managers, and the creation of a website where businesses are offered advisory services and networking opportunities.

Government bonds are used as a benchmark in the pricing of financial instruments, including corporate bonds. Empirical evidence suggests that jurisdictions with larger and more active government bond markets generally have more developed corporate bond markets (IOSCO, 2011[96]). However, government bond markets can only support the development of corporate bond markets if they can effectively provide a liquid benchmark yield curve, a transparent auction process, timely announcement of issuance schedules and user-friendly market statistics (BIS, 2006[97]). Romania has already taken many steps to develop a domestic government bond market by supporting advancement in the auction process, establishing a primary dealer mechanism and employing an efficient settlement system. In addition, in line with international best practices, Romania pursues medium-term debt management strategies by setting targets to manage the risks of the government debt stock. However, like in the Romanian corporate bond market, the liquidity in the secondary government bond market is low. Moreover, there is still room to increase the average maturities of the domestic government debt, which was only 4.2 years at the end of 2021 (RMF, 2021[98]). Further, as of December 2021 more than half of the outstanding Romanian Government debt stock was denominated in foreign currency, significantly more than peer countries.

Although government bonds represent a large share of Romanian pension funds' portfolios, they only hold one-fifth of total local currency denominated government bonds. Instead, commercial banks are the main investors in local currency denominated Romanian Government bonds, holding around half of the outstanding stock of bonds according to statistics as of end of December 2021 (RMF, 2021[98]). As a comparison, government bond investments of the Czech and Polish banking sectors represent 32.4% (as of February 2021) and 46.3% (as of end 2020) of their respective domestic government bond stocks (MFCR, 2021[99]; PMF, 2021[100]). In terms of the banking sector balance sheet, general government debt securities amounted to 27% of the Romanian domestic banking sector's total assets at the end of 2018. The corresponding shares were significantly lower in the European Union overall, the Czech Republic and Poland at 8%, 9% and 10%, respectively (ECB, 2021[101]).

The high holdings of government bonds by the Romanian banking sector contrast with its almost non-existent (0.02% as of end 2018) holdings of corporate bonds, which are significantly lower than peers countries and EU levels. The European Union's domestic banking sector allocated a share equivalent to 0.7% of its cumulative total assets to non-financial corporate bonds at the end of 2018. The banking sectors in the Czech Republic and Poland each allocate around 1.2% (as of end 2018) of their assets to non-financial corporate bonds (ECB, 2021[101]).

To support the green transition, many regulators have come up with incentives to stimulate the market for corporate bonds. One notable example is Singapore. The Monetary Authority of Singapore has established a scheme that covers 100% of the costs (up to a cap of SGD 100 000) related to obtaining an external review or rating for bonds within an internationally recognised green, social or sustainability bond framework. The scheme is in place until mid-2023 and certain criteria related to size and maturity apply. Qualifying bonds must be issued and listed in Singapore (MAS, 2021[102]). Such a measure recognises the additional expenses that might be associated with issuing a green bond compared to a regular bond, and can therefore be helpful in the development of green corporate bond markets.

Recommendations

To facilitate market-based long-term debt financing, Romania could/should:

- Undertake a regulatory review to streamline the listing process of corporate bonds;
- Re-evaluate the requirement to hold an extraordinary general meeting to issue a bond;
- Improve the availability of credit ratings;
- Adapt the current pension fund regulatory framework that only recognises credit ratings from the three major international agencies;
- Encourage the creation of collective investment vehicles that invest in diversified products including non-financial corporate bonds;
- Promote investment in non-financial corporate bonds by the banking sector and other institutional investors;
- Design public-private partnerships where a private sector company or entity is created for the purpose of executing infrastructure projects;
- Provide incentives for issuers of and investors in green bonds such as covering the cost related to obtaining an external review or rating for bonds within an internationally recognised green, social or sustainability bond framework.

The Romanian corporate bond market is undersized, but could be further developed by addressing a number of inefficiencies. The general lack of access to market-based credit for many companies has left the Romanian economy over-reliant on bank financing – when available – and on foreign financing in particular. An expansion and deepening of the local bond market would be both an important step towards increasing the resilience of the corporate sector and a way to satisfy the existing demand from local institutional investors to invest in long-term local currency fixed income securities. A number of policy measures can be taken to this end.

Several market participants have raised concerns about the time required to issue a bond. A regulatory review should be undertaken with a view to streamlining the listing process. In order to prevent any delays in the approval of prospectuses, the ASF may consider expanding its staff to support companies in ensuring the documentation is submitted in the correct form. Further, the requirement to hold an extraordinary general meeting to issue a bond should be re-evaluated.

To increase activity in corporate fixed income markets, it is important to address the role of credit rating systems. It should be assessed whether any existing authority has the capacities and the required data to provide credit ratings to the market. Alternatively, subsidies for the establishment of a domestic rating agency could be considered. A third option is to simply provide financial support to smaller companies in obtaining credit ratings from an already established credit rating agency. Finally, the current pension fund regulatory framework only recognises credit ratings from the three major players. It should be adapted with a view to including more rating agencies that follow rigorous standards and use solid methodologies.

Investors and their investment policies play a key role in developing the domestic market. Currently, institutional investors' participation in the corporate bond market is very limited. While traditional institutional investors are still at an early stage of development and remain small, diversification of their investments with increasing allocation to corporate bonds could generate increased demand for these instruments and encourage other issuers to make use of the market. This would enable a simultaneous development of institutional investors and corporate bond markets over time. In this respect, the Romanian authorities should encourage collective investment vehicles to create diversified products including non-financial corporate bonds. A special focus could be given to the instruments issued on the

AeRO Market to support the financing of mid-sized companies through corporate bonds. Finally, promoting the investment in non-financial corporate bonds by the banking sector would also create additional demand.

To promote the development of the corporate bond market and to finance Romania's large scale infrastructure needs, the authorities should consider financing these projects via corporate bonds. There are a number of projects in progress, but the financing model used has mostly been bank loans. Romanian authorities could design public-private partnerships where the private sector company or an entity created for the purpose of the execution of the project could issue corporate bonds to fund the investment. This would support an increase in corporate bond activity in Romania, while providing longer-term investment opportunities to institutional investors.

As a combined measure to stimulate the market for corporate bonds and to facilitate Romania's green transition, the government should consider providing incentives for issuers of green bonds such as covering the cost related to obtaining an external review or rating for bonds within an internationally recognised green, social or sustainability bond framework. Such a measure recognises the additional expenses that might be associated with issuing a green bond compared to a regular bond, and can therefore be helpful in the development of green corporate bond markets.

One important step to support the development of the corporate bond market is to ensure a well-functioning government bond market. Therefore, it is crucial that Romanian Government debt managers continue to employ strategies to build a liquid local currency benchmark yield curve while also increasing the average maturity of government bonds.

In line with the objectives stated in the Romanian National Recovery and Resilience Plan to create opportunities for businesses to diversify their financing sources, authorities could consider allocating part of the funds received from the EU to further develop the corporate bond market. In this respect, EU funds could be used to finance the above recommendations to support smaller companies to obtain credit ratings, subsidise the establishment of a domestic rating agency, and/or incentivise the issuance of green bonds.

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Notes

[1] The turnover ratio is measured as the total value of shares traded over market capitalisation.

[2] Find more information about the Hungarian programme, please see: https://www.bse.hu/Issuers/bse-research/BSE-market-development-programme-for-companies-with-small-and-medium-capitalisation.

[3] The amount traded is split into three segments: the first trading segment is above PLN 2 million and the corresponding fee is 1 bps; the second trading segment goes between PLN 100 000 to PLN 2 million and the corresponding fee is 2.4 bps; and the third segment is up to PLN 100 000 with a corresponding fee of 2.9 bps.

[4] Converted using the exchange rate that retrieved from Thomson Reuters as of 30.09.2021 for PLN/EUR 0.2167, and HUF/EUR 0.002779.

[5] Capital gains derived from listed equities acquired after 1 January 2006 or from Turkish local government bonds issued after 1 January 2006.

[6] Equity ratio is measured as equity over total assets.

[7] Companies with negative equity are defined as companies with total liabilities greater than total assets.

[8] The investment data is based on EIB Investment Survey statistics.

[9] The data for outstanding guarantees of SME loans is from EIF (2020) and the GDP data is from IMF statistics.

[10] A direct listing is referred to as a technical listing in the BVB documents.

[11] Members with payment of contributions in current month.

[12] Fondul Proprietatea was set up by the Romanian state on 28 December 2005 to indemnify persons whose assets had been expropriated by the communist regime (especially in cases when restitution in kind would not be possible) by granting them shares in Fondul Proprietatea proportionate to their loss. Until the appointment of a selected administration, the fund was been managed provisionally by the Ministry of Finance through the Board of Supervisors. Following a tender selection process, on 9 June a Selection Commission selected Franklin Templeton Investment Management Ltd as the manager of the fund.

3 The Romanian corporate sector

This chapter provides some key economic indicators and analysis of Romanian non-financial companies' demographics, capital structure, investment and performance. Although some data pre-date the COVID-19 crisis, they still provide useful insights for understanding the underlying structural challenges faced by the corporate sector and the Romanian economy. The chapter also provides an overview of the initial impact of the COVID-19 crisis on the corporate sector and summarises the government relief programmes to the corporate sector.

Romania had a period of strong economic growth in the five years up to 2019, which helped improve living standards and reduce unemployment. However, it has had twin fiscal and current account deficits for the past two decades, and investment growth has lagged general economic growth. Further, competitiveness is held back by shortcomings such as a lack of skills, poor innovation and uncertainty with respect to the regulatory environment. At the same time, the financial system is heavily bank dependent, in particular on foreign-owned banks, while capital markets play a very limited role in providing financing to the non-financial corporate sector.

3.1. Overview of the economy

Economic growth in Romania was on average 4.7% per year between 2015 and 2019, leading to lower unemployment and improved per capita income levels converging towards those of advanced European economies (Table 3.1). However, due to the impact of the COVID-19 pandemic, GDP contracted 3.9% in 2020.

Table 3.1. Key economic indicators for Romania

	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Real GDP growth (%)	(3.9)	1.9	2.0	3.8	3.6	3.0	4.7	7.3	4.5	4.1	(3.9)
Real GDP per capita (EUR, thousands)	12.8	13.3	14.0	14.3	14.8	15.5	16.9	18.7	19.9	21.6	21.4
Unemployment rate (%)	7.0	7.2	6.8	7.1	6.8	6.8	5.9	4.9	4.2	3.9	5.0
Headline inflation (%)	6.1	5.8	3.3	4.0	1.1	(0.6)	(1.6)	1.3	4.6	3.8	2.8
Labour productivity growth (%)	(2.0)	3.9	2.7	4.7	3.4	5.6	4.6	6.0	4.1	3.9	(2.3)
Fiscal balance (% of GDP)	(6.9)	(5.4)	(3.7)	(2.1)	(1.2)	(0.6)	(2.6)	(2.6)	(2.9)	(4.4)	(9.4)
Primary fiscal balance (% of GDP)	(5.6)	(4.0)	(2.3)	(0.7)	0.2	0.7	(1.4)	(1.6)	(2.0)	(3.5)	(7.9)
Gross government debt to GDP (%)	29.6	34.0	37.1	37.6	39.2	37.8	37.4	35.1	34.7	35.3	47.4
Current account balance (% of GDP)	(5.2)	(5.0)	(4.9)	(0.9)	(0.2)	(0.5)	(1.4)	(2.7)	(4.3)	(4.6)	(3.8)
Investment (GFCF, percentage of GDP)	26.1	27.2	27.5	24.7	24.4	24.8	22.9	22.4	21.1	23.6	.
Non-performing loans to total lending (%)	11.9	14.3	18.2	21.9	20.7	13.4	9.7	6.6	5.0	4.3	3.9

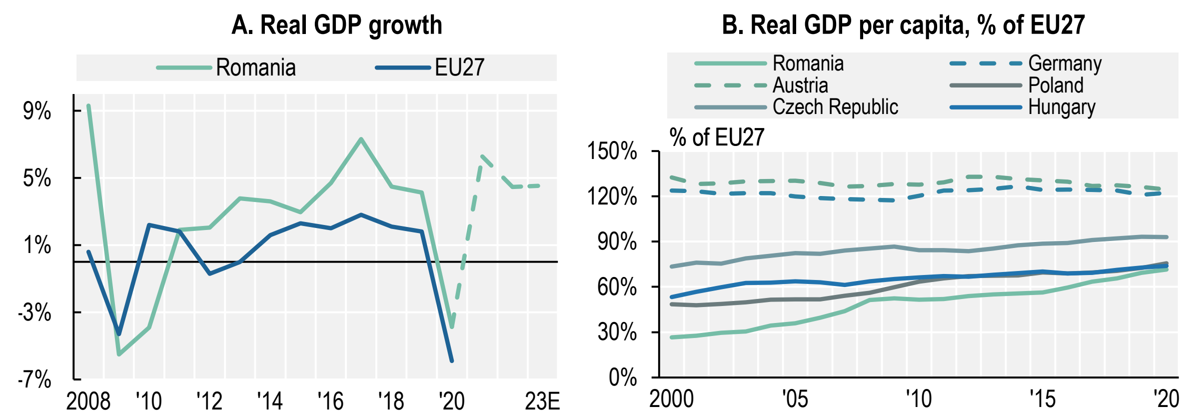
Note: Real GDP per capita is measured in purchasing power standards (PPS).
Source: Romanian National Institute of Statistics, OECD Economic Outlook 110, OECD Productivity Statistics, Eurostat, World Bank.

Even including the global crises of 2008 and 2020, which had significant impacts on Romanian economic growth, the economy has been expanding by an average of 3.7% annually in real terms since 2000, far above the EU average (Figure 3.1, Panel A). The economy grew at 6.1% per annum from 2000 to 2008, followed by a protracted downturn after the 2008 crisis and the subsequent European sovereign debt crisis. It was only in recent years that it began to pick up again, reaching 7.3% in 2017. Prior to the pandemic, this growth appeared set to continue into 2020, as real GDP in Q1 2020 was 2.4% higher than the same quarter in 2019.

However, as an effect of the pandemic induced crisis, Romania's real GDP growth for 2020 was -3.9%. 2021 has surpassed growth expectations and showed strong signs of recovery, as the first three-quarters of 2021 saw a GDP growth of 7.2%.

While Romania's per capita real GDP is still low compared with more advanced European countries and in the lower range of CEE peers, the growth in recent years has led to a convergence towards general EU levels (Figure 3.1, Panel B).

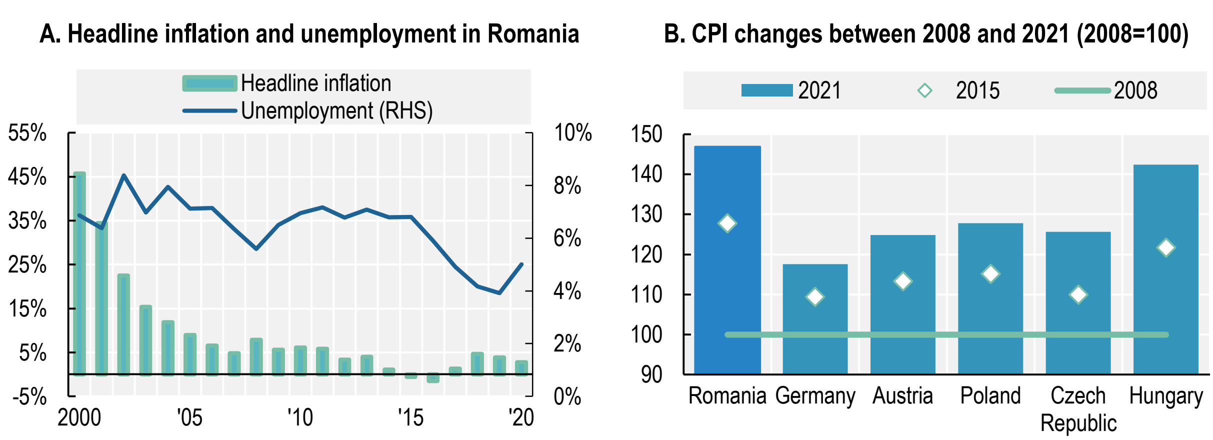
Figure 3.1. GDP growth in Romania and selected European countries



Note: Figures provided in dashed lines in Panel A for 2021, 2022 and 2023 are forecasts from (OECD, 2021[1]).
Source: Romanian National Institute of Statistics, OECD Economic Outlook 110, Eurostat.

After remaining persistently high at around 7% between 2000 and 2015, the Romanian unemployment rate began to decrease gradually in 2016, falling to a record low of 3.9% in 2019. However, this is partly an effect of a sustained decrease in the labour force following a reduction in the working age population coupled with outward migration of skilled labour (EC, 2019[1]; EC, 2020[2]). The current structure of the labour force is seen as leading to challenges in the recruitment process and driving the wage growth in the country (EC, 2019[1]). Further, as a result of the COVID-19 crisis, unemployment has increased markedly, reaching 5.0% in 2020 (Figure 3.2, Panel A).

Figure 3.2. Inflation and unemployment



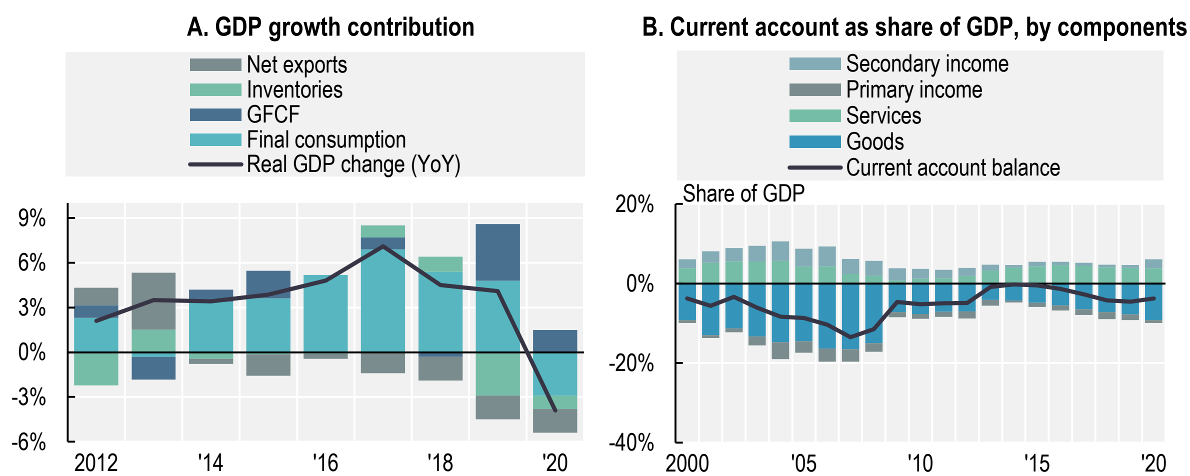
Source: Romanian National Institute of Statistics and OECD Economic Outlook 110 for Panel A; Eurostat for Panel B.

Simultaneously, price inflation in Romania has fallen from high levels in the early 2000s to more subdued levels since the 2008 financial crisis, in line with the more general European pattern of pervasive low inflation (Figure 3.2, Panel A). Still, in 2021 price inflation in Romania was one of the highest among EU countries (Eurostat, 2022[3]). Indeed, between 2008 and 2021 consumer prices saw a cumulative increase of almost 50%, the highest among peer countries (Figure 3.2, Panel B). Despite a period of deflation in 2015 and 2016, in recent years there are signs that inflation has begun to increase again, driven by hikes in food and energy prices as well as internal factors (EC, 2019[1]).

GDP growth in Romania over the past decade was driven by consumption. Of the cumulative real GDP growth contribution between 2012 and 2020, 96% was made up by consumption, with gross fixed capital formation (investment) representing only 24% (inventories and net exports contributed -10% each). This consumption-led growth model has not only led to pressure on the current and fiscal accounts but is also hampering Romania's sustainable economic convergence towards general EU living standards (EC, 2019[1]; EC, 2020[2]). The sustainability of such a growth model is fragile if consumption is financed with debt or driven by a wealth effect resulting from a rise in real house prices, for example. In both cases, future spending may be constrained as a result of deleveraging or a reversal in housing prices (Kharroubi and Kohlscheen, 2017[4]).

The consumption dependent growth is also reflected in the long standing Romanian current account deficit, which is driven primarily by large goods imports, coupled with relatively low export growth (Figure 3.3,Panel B). The net export contribution to GDP growth has been negative in every year since 2014 (Figure 3.3, Panel A). These developments have contributed to the diminishing competitiveness of Romanian corporations in domestic and foreign markets (IMF, 2019[5]). Specifically, the average annual current account deficit since 2000 has been over 5%, with a corresponding goods deficit of almost 10%. This has been slightly offset by an average services export surplus of around 3.6% and an average secondary income surplus of 2.5%.

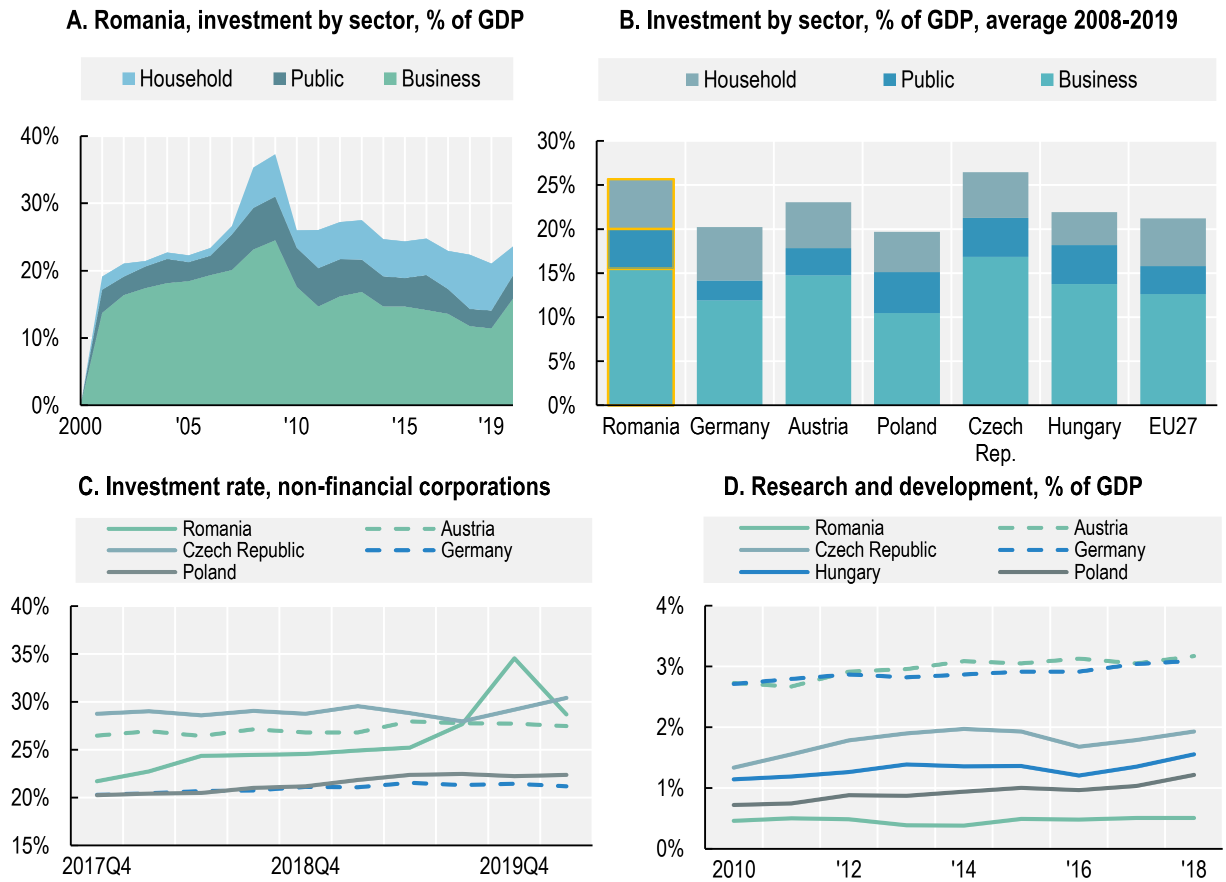
Figure 3.3. GDP growth contribution and current account composition in Romania



Source: Romanian National Institute of Statistics for Panel A; Eurostat for Panel B.

Investment in Romania has been declining since the 2008 financial crisis (Figure 3.4, Panel A). Still, compared to regional peers the headline figures remain favourable, with a split between business, public and household investment similar to that of the EU average (Figure 3.4, Panel B). Non-financial corporate investment has been improving since 2017, both in terms of shares of gross value added and when compared to peer countries. However, it should be noted that the investment rate only reflects fixed investment and as such is typically higher for less advanced economies that have a smaller capital stock to begin with (Figure 3.4, Panel C). Finally, compared to other EU economies, non-financial corporate investment in Romania appears to be concentrated in a much smaller number of firms, as the country has one of the lowest shares of domestic companies investing (Pal et al., 2019[6]).

Figure 3.4. Investment trends in Romania and selected European countries



Note: In Panel B gross fixed capital formation consists of resident producers' acquisitions, less disposals of fixed assets plus certain additions to the value of non-produced assets realised by productive activity, such as improvements to land. In Panel C the gross investment rate is defined as gross fixed capital formation divided by gross value added. Data for Hungary are unavailable in Panel C. Research and development in Panel D covers basic and applied research as well as experimental development.
Source: Eurostat.

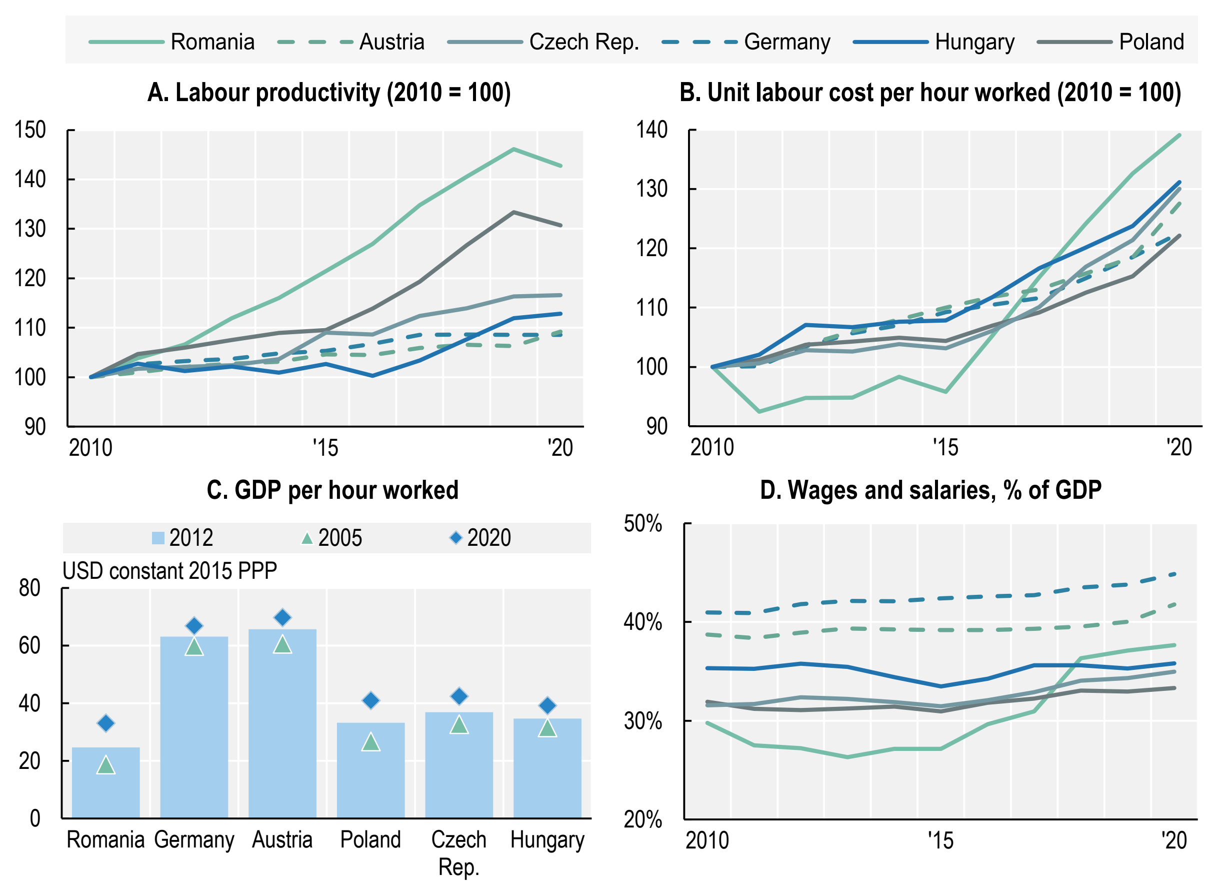
To compare the level of intangible investment across economies, research and development (R&D) expenditure is a relevant indicator. Romania shows by far the lowest level of R&D as a share of GDP among its peers at around 0.5% annually since 2010. This is less than a quarter of the EU average and around one-seventh of Germany and Austria's levels (Figure 3.4, Panel D). Lack of R&D investment may hamper future technological progress, productivity increases and innovation in the economy. It is important to note that in order to support such intangible, relatively riskier investments, some form of market-based financing is often required, which is why underinvestment in intangibles is also a reflection of the state of capital markets.

Moreover, financial soundness is low in the Romanian corporate sector, which has the highest share of companies with negative equity in Europe (see Section 3.6). Together with the closely related phenomenon of higher financing costs, this represents an important factor hindering companies' access to external financing, thereby limiting their investment capacity (EIB, 2019[7]) In addition, according to a survey on companies' views on investment obstacles by the European Investment Bank the level of uncertainty in the economy as well as challenging business and labour market regulations are pointed out as key issues for Romanian firms (EIB, 2019[7]).

Labour productivity growth (measured as GDP per hour worked) in Romania was strong in the past decade, far outpacing regional peers and more advanced European economies (Figure 3.5, Panel A). It should be noted, however, that at the start of the analysed period, labour productivity was significantly lower than that of peer countries (for example, in 2010, USD 23 was produced for every hour worked in Romania, compared to USD 36 in the Czech Republic and USD 61 in Germany). As a result, and despite the growth, it remains low in dollar terms both in a CEE and in a broader European context (Figure 3.5, Panel C). In addition, wages have outgrown productivity in recent years, notably since 2015. The increase in unemployment after the 2008 crisis and the subsequent Euro crisis led to a year on year decrease in Romanian unit labour costs in 2009, 2011 and 2015. However, between 2015 and 2020 unit labour costs increased by 45%, far exceeding the increase in labour productivity of 18% (Figure 3.5, Panels A and B).

Still, while due attention should be paid to the relation between wage and productivity growth over the longer-term, it should be noted that the wage share of GDP has historically been low in Romania (Figure 3.5, Panel D). Since labour productivity/wage comparisons do not account for the initial relation between wages and productivity, cross country comparisons should be contextualised with the wage share of GDP. Wages and salaries as a share of GDP have been rising since the second half of 2015, as a result of increments in public sector wages, minimum wage increases and a tightening labour market. In spite of this, wages in Romania are still low relative to much of the rest of the EU and they are expected to continue growing. One factor to bear in mind is that wage growth in excess of productivity gains could lead to losses in competitiveness. Boosting productivity enhancing investments is therefore key for the Romanian economy.

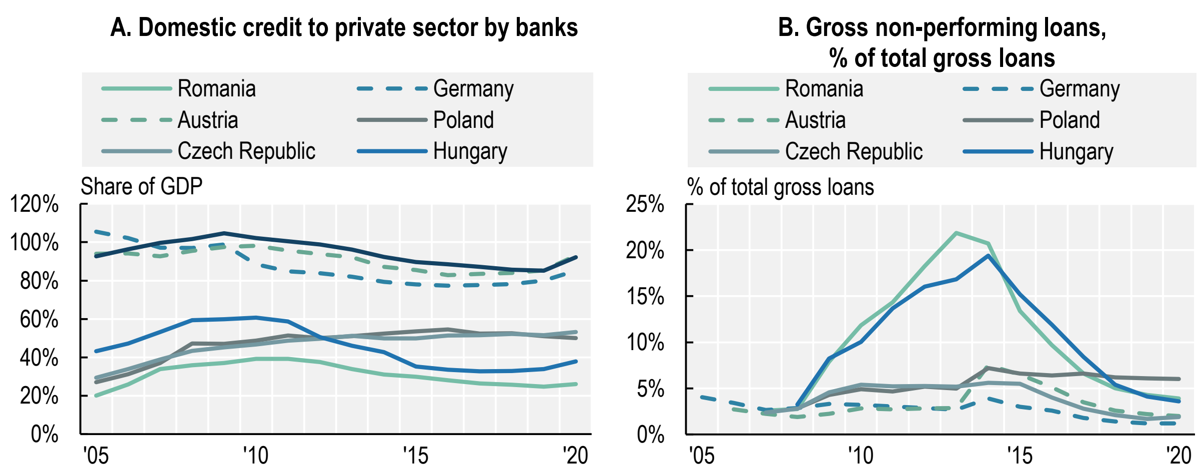
Figure 3.5. Labour productivity and wage share in Romania and selected European countries



Source: OECD Productivity Statistics, OECD Stat Database.

Further, domestic bank credit to the private sector as a share of GDP stood at 26% in Romania at the end of 2020, the lowest among peer countries, and the share has been decreasing since 2011 (Figure 3.6, Panel A). The non-bank financial system is even smaller and does not fill this financing gap. While the banking financial system represented 57% of GDP in Q3 2021, the non-bank financial system represented less than 14% (ASF, 2021[8]). Moreover, Romanian non-financial companies rely heavily on non-resident financial institutions for loan financing, which is a cause for concern in terms of financial stability. At the end of 2019, loans from non-resident financial institutions were 1.2 times higher than loans from resident financial institutions (BNR, 2020[9]). Rather than bank loans or capital markets, Romanian companies' main sources of external financing are overdrafts and credit lines. Together with the lack of bank financing to the corporate sector, the underdevelopment of the capital market is likely to negatively impact economic growth (EC, 2020[2]). Both the bank and non-bank financial sectors are instead heavily exposed to Romanian Government securities, raising risks of excessive interdependence between banks and the state (World Bank and IMF, 2018[10]; ASF, 2020[11]) As of November 2021, government bonds made up 61% of assets both for mandatory pension funds and optional pension funds (ASF, 2021[8]).

Figure 3.6. Banking sector loan trends in Romania and selected European countries



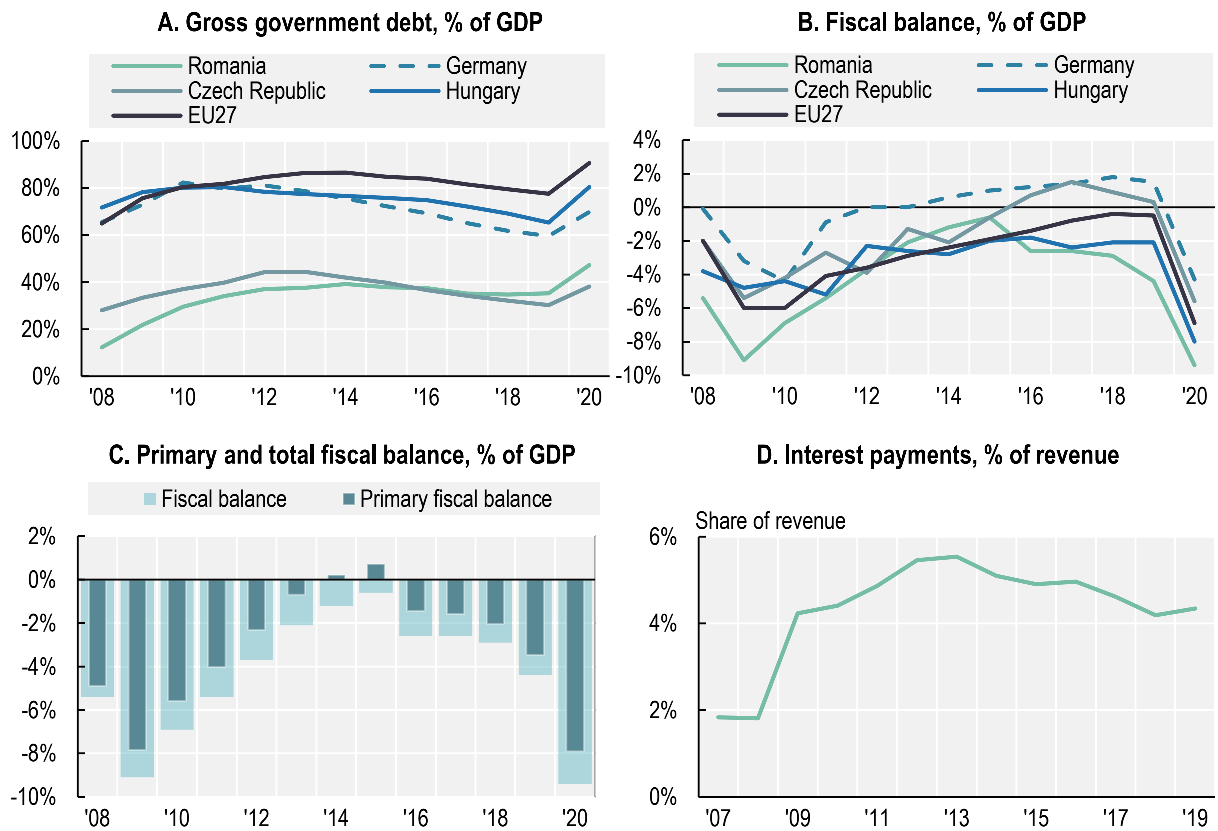
Note: For Panel B data from 2014 onwards comes from Eurostat (except for the Czech Republic, 2014-15). Prior years use World Bank data.
Source: Eurostat, World Bank.

Despite low levels of credit to the private sector, Romania had the highest share of non-performing loans (NPLs) among peer countries after the 2008 financial crisis and the subsequent Euro crisis (Figure 3.6, Panel B). In 2014, it had the fifth-highest share in the European Union (Eurostat, 2022[12]). Since then, the National Bank of Romania (BNR) has pursued a number of initiatives in order to reduce pressure on banks' balance sheets with respect to NPLs, including more prudent provisioning, disposal of NPLs and annual bank by bank supervisory targets for NPL reductions (World Bank and IMF, 2018[10]). In addition to the significant decrease in the NPL ratio between 2015 and 2020 (more than 9 percentage points), at the end of 2019, the non-performing loan coverage ratio in Romania exceeded 60% which is far above the EU average of 44.6% (BNR, 2020[9]). Despite the COVID-19 crisis, the NPL ratio continued to fall in 2020, reaching 3.9%, while the coverage ratio increased to 63.3% (BNR, 2021[13]). According to the National Bank of Romania, the probability of default estimated for non-financial corporations during September 2021 – September 2022 will further decline to an average of 2.7% (BNR, 2021[14]). In addition, the Romanian economy has a significant level of overdue payments, amounting to 9% of GDP at the end of 2018 (BNR, 2020[9]).

In spite of sustained fiscal deficits over the past decade and the additional pressure from the COVID-19 crisis, Romanian sovereign indebtedness remains well below the threshold stipulated in the Stability and

Growth Pact (S&G) of the European Union,[1] and modest compared with many other European countries (ECB, 2020[15]). Still, gross government debt almost tripled as a share of GDP between 2008 and 2019 (from 12% to 35%), and further rose to 47.4% in 2020 and reached 48.9% in 2021 (RMF, 2022[16]). The fiscal deficit has remained larger than the 3% laid out in the S&G Pact for many years (Figure 3.7, Panel B). Moreover, according to the European Commission, the debt-to-GDP ratio is projected to exceed 90% by 2030, mainly driven by a projected significant increase in pension spending (EC, 2020[2]).

Figure 3.7. Fiscal balance and gross public debt



Source: Eurostat, OECD Economic Outlook 108, World Bank.

It should be noted that the primary and total fiscal balances differ markedly in Romania (Figure 3.7, Panel C). While the average fiscal deficit over the 2008-20 period was over 4% of GDP, the primary deficit was around 3%, meaning interest payments make up a significant part of the Romanian deficit. Indeed, interest payments as a share of total revenue has increased substantially since 2008, even as interest rates have fallen to historical lows in Romania (BNR, 2021[17]) and around the world (Figure 3.7, Panel D). This was a joint effect of falling government revenue in 2009 and a sharp increase in borrowing from 12% of GDP in 2008 to 22% in 2009 (Eurostat, 2022[18]). For this reason, it should also be noted that even if debt levels are modest, there is lower “tolerance” for debt in emerging economies compared to advanced economies. Therefore, the sustainable level of sovereign borrowing for Romania is likely to be lower than in advanced economies.

3.2. Business demographics

In 2021, small and medium enterprises (SMEs) accounted for 99.8% of all firms in the non-financial business sector in the European Union, employing 65.2% of the total workforce (EC, 2021[19]). Similarly, in Romania, SMEs made up 99.7% of total non-financial corporations at the end of 2019 (Table 3.2). Although the share of SMEs is very similar across peer countries, the composition of subcategories within SMEs varies considerably. For instance, the share of micro firms in the Czech Republic, Hungary and Poland averages 95%, whereas in Germany and Austria micro firms account for only around 85% and small firms for over 10%. Romania stands in the middle with micro firms (1 to 9 employees) representing 89.5%, small firms (10 to 49 employees) 8.6%, and medium sized firms (50 to 249 employees) 1.6%. Large firms (over 250 employees) represent 0.3% of all Romanian non-financial companies. Notably, the share of large non-financial companies is larger than in the Czech Republic, Hungary or Poland, but lower than in Austria and Germany, where large firms constitute 0.4% and 0.5% of all firms, respectively.

The distribution of Romanian companies remained quite stable between 2010 and 2019, with the share of micro firms growing from 88.9% in 2010 to 89.5% in 2019. The total number of non-financial firms grew from 440 000 in 2010 to over 500 000 in 2018, a 16% increase. This increase exceeds those in Austria, the Czech Republic and Hungary but is smaller than those in Germany and Poland, which saw their total number of non-financial firms increase by 25% and 37% respectively from 2010 to 2019.

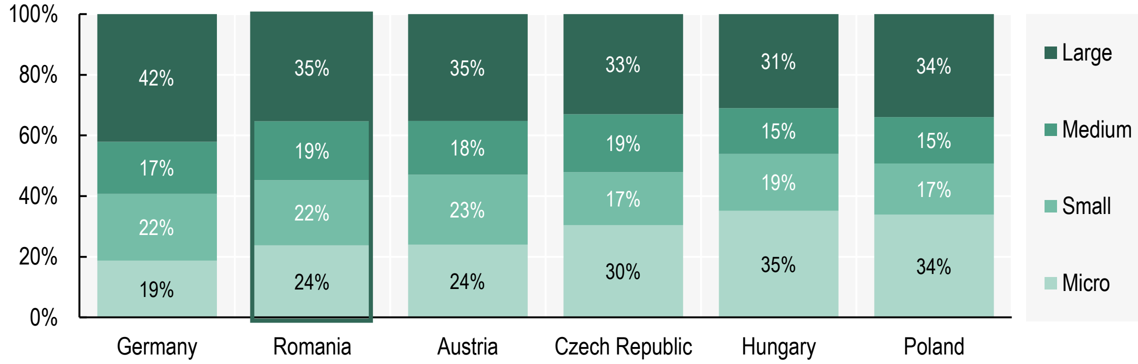
Table 3.2. Company distribution by firm size

	2010					2019				
	Micro	**Small**	**Medium**	**Large**	**No. of firms**	**Micro**	**Small**	**Medium**	**Large**	**No. of firms**
Romania	88.9%	9.0%	1.7%	0.3%	**443 736**	89.5%	8.6%	1.5%	0.3%	**512 762**
Austria	87.4%	10.7%	1.6%	0.3%	**300 252**	87.2%	10.8%	1.6%	0.4%	**329 680**
Czech Republic	95.7%	3.4%	0.7%	0.1%	**968 539**	96.0%	3.1%	0.7%	0.2%	**1 050 650**
Germany	82.2%	14.8%	2.6%	0.5%	**2 063 310**	83.2%	14.2%	2.2%	0.5%	**2 580 300**
Hungary	94.6%	4.5%	0.7%	0.1%	**547 724**	94.7%	4.5%	0.7%	0.1%	**639 635**
Poland	95.3%	3.4%	1.1%	0.2%	**1 460 288**	94.8%	4.3%	0.7%	0.2%	**2 002 550**

Note: In accordance with the International Standard Industrial Classification of All Economic Activities (ISIC) Rev. 4, the total corresponds to the Business economy, except financial and insurance activities.
Source: OECD SDBS Structural Business Statistics.

In Romania, the non-financial business sector employs 21% of the total population (4.1 million workers) compared to 33% on average in Austria, the Czech Republic and Hungary. In Poland and Germany, the shares are 26% (10 million employees) and 38% (31 million employees) of the total population, respectively. SMEs in Romania account for 65% of total employment, similar to its peer countries with the exception of Germany, where SMEs represent 58% of total employment (Figure 3.8). Moreover, while in terms of the number of firms, large firms account for the smallest portion of non-financial companies in all the selected countries, they employ the largest share of workers. In Romania, 35% of the labour force is employed by large firms.

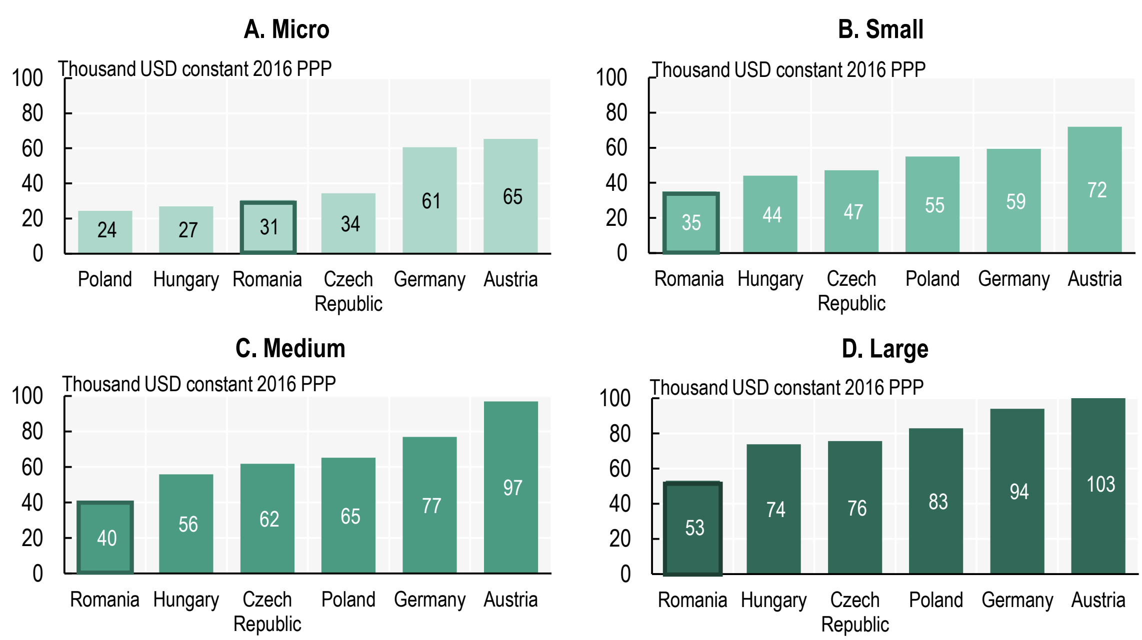
Figure 3.8. Employment distribution by firm size in 2019



Note: The figure corresponds to the sector "Business economy, except financial and insurance activities" according to the International Standard Industrial Classification of All Economic Activities (ISIC) Rev. 4.
Source: OECD SDBS Structural Business Statistics.

In general, labour productivity levels tend to be higher for large firms than for smaller ones. For instance, in Romania, labour productivity of micro firms is USD 31 thousand (2016 PPP) per person employed, and USD 53 thousand for large firms (Figure 3.9). German and Austrian firms are the most productive among peer countries, with over USD 60 thousand per person employed across firm size categories. In particular, large German and Austrian firms generate USD 94 thousand and USD 103 thousand respectively per person employed annually. In contrast, Romanian companies rank the lowest in terms of labour productivity when compared to their peers, with the exception of micro firms, where Romanian firms are more productive than Polish and Hungarian firms.

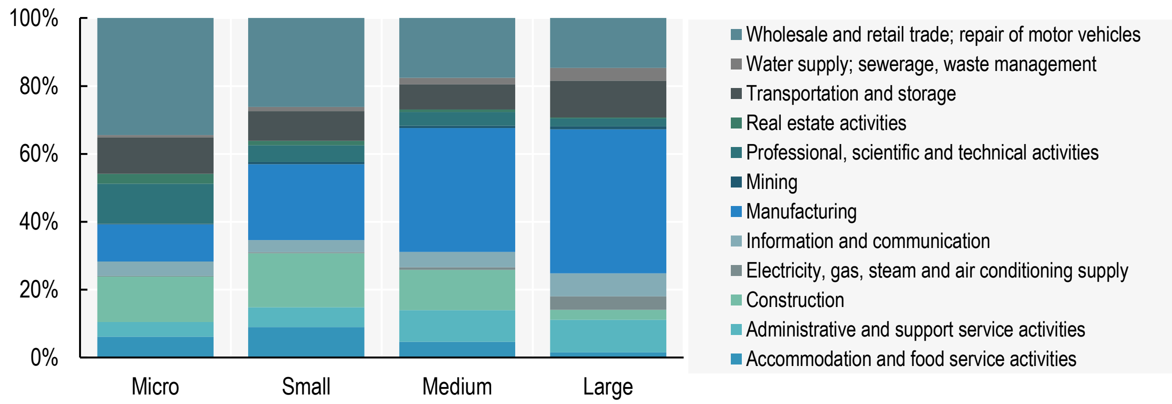
Figure 3.9. Labour productivity by firm size in 2016



Note: The figures correspond to the sector "Business economy, except financial and insurance activities" according to the International Standard Industrial Classification of All Economic Activities (ISIC) Rev. 4. The numbers are form 2016 due to the lack of updated information for Germany and Hungary.
Source: OECD SDBS Structural Business Statistics.

In terms of employment distribution across industries, manufacturing companies dominate and employ 31% of the Romanian workforce (Figure 3.10). Moreover, the share of employment in the manufacturing industry increases with company size, representing 11% of the employment in micro firms, 22% in small firms, 38% in medium firms and 43% in large firms. Wholesale and retail trade companies rank second in total employment in Romania with a share of 22%. This industry represents on average 35% of employment in micro and small companies, 17% in medium firms and 14% in large firms. The transportation and storage industry ranks third representing 10% of total employment, followed by the construction industry, which is important among SMEs.

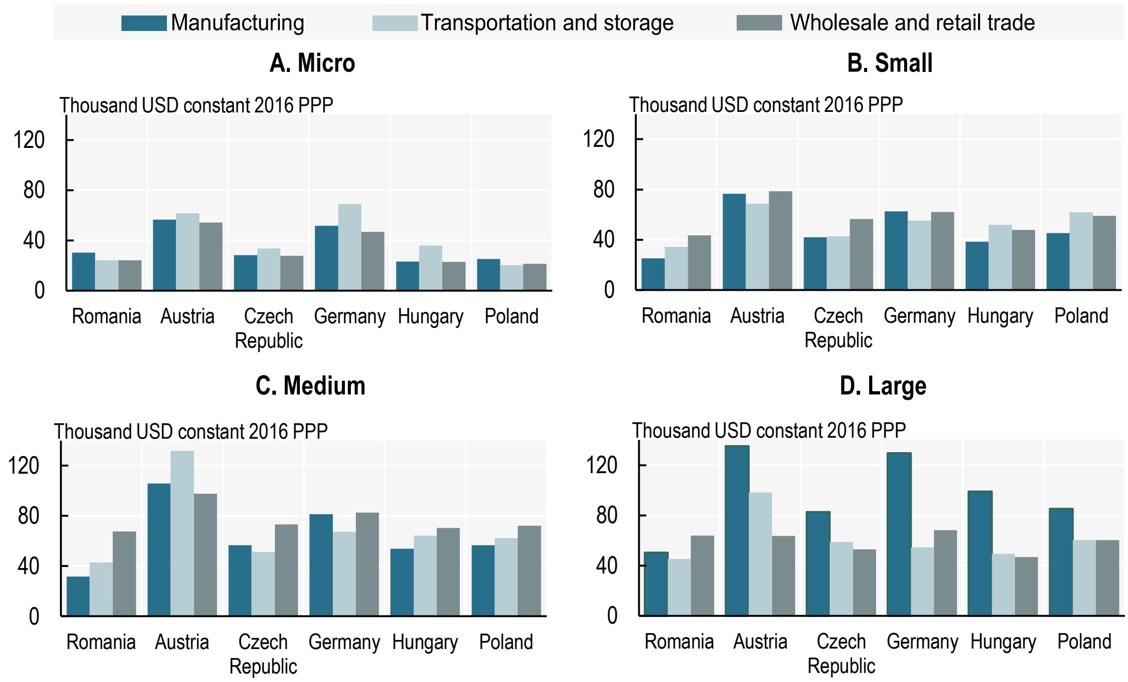
Figure 3.10. Employment distribution in Romania by company size and industry in 2019



Note: In accordance with the International Standard Industrial Classification of All Economic Activities (ISIC) Rev. 4, the total corresponds to the Business economy, except financial and insurance activities.
Source: OECD SDBS Structural Business Statistics.

Manufacturing, wholesale and retail trade, and transportation and storage account for a significant share of employment in Romania. A detailed analysis of labour productivity for these three industries is shown by firm size in Figure 3.11. Austrian manufacturing large firms have the highest level of productivity with USD 135 thousand (2016 PPP) per person employed against only USD 50 thousand (2016 PPP) for large Romanian companies in the same industry (Figure 3.11, Panel D). Among micro firms, Romanian manufacturing firms have a labour productivity of USD 30 thousand, greater than firms in the Czech Republic, Hungary or Poland. In the rest of the firm category sizes – small, medium and large – wholesale and retail trade companies in Romania appear to be the most productive ones when compared to the other two industries. Notably, large Romanian wholesale and trade firms rank second with USD 64 thousand per person employed just behind German wholesale and trade large firms.

Figure 3.11. Labour productivity by firm size for selected industries in 2016



Note: Sectors classification is in accordance with the International Standard Industrial Classification of All Economic Activities (ISIC) Rev. 4.
Source: OECD SDBS Structural Business Statistics.

3.3. Company categories in Romania

This section describes how companies are classified and grouped for the analysis in the following sections of this part the report. Using financial and ownership information from the ORBIS database, Sections 3.4 to 3.6 present an analysis of the business dynamics in Romania, including comparisons with selected European peer countries. The analysis is limited to non-financial companies with more than ten employees. The rationale for choosing a size threshold of ten employees is twofold: first, data coverage typically increases with firm size which means that the coverage for smaller firms is less reliable, hampering comparability. Second, the focus of this report is market-based financing and micro firms are generally unlikely to tap capital markets.

The OECD-ORBIS Corporate Finance dataset includes financial and ownership information for non-financial companies between 2005 and 2018. To evaluate the representativeness of the data against the official statistics, Table 3.3 compares the coverage of the OECD ORBIS Corporate Finance dataset with the Eurostat business statistics. The OECD-ORBIS dataset generally has similar coverage as Eurostat for small firms and a higher coverage for medium and large firms. Moreover, the distribution of firms across different size groups is also similar for both datasets. For Romania, the total coverage is almost identical in both datasets.

Large companies are defined as having 250 or more employees, medium sized companies as having between 50 and 249 employees, and small companies as having less than 50 employees. When employment figures are unavailable, companies are classified based on their asset size. The asset size thresholds used are: above EUR 20 million for large firms, between EUR 4 million and EUR 20 million for medium firms, and less than EUR 4 million (but larger than EUR 350 000) for small firms.

Table 3.3. Comparison of the OECD-ORBIS Corporate Finance dataset and the Eurostat universe

	Large	*Share of total*	Medium	*Share of total*	Small	*Share of total*
Romania – Eurostat	1 662	3%	7 955	15%	43 643	82%
Romania – ORBIS	1 693	3%	7 918	15%	44 424	82%
Czech Rep. – Eurostat	1 654	4%	7 057	17%	32 763	79%
Czech Rep. – ORBIS	1 372	6%	4 869	20%	17 551	74%
Germany – Eurostat	12 139	3%	61 634	14%	375 504	84%
Germany – ORBIS	9 804	4%	47 335	20%	175 057	75%
Hungary – Eurostat	941	3%	4 515	13%	28 033	84%
Hungary – ORBIS	1 208	3%	5 838	15%	32 909	82%
Poland – Eurostat	3 364	3%	15 474	15%	82 709	81%
Poland – ORBIS	3 819	6%	14 548	23%	45 139	71%

Note: All data are as of end-2018, with the exception of Germany, for which 2017 data are used due to limited availability in 2018 from both ORBIS and Eurostat.
Source: OECD-ORBIS Corporate Finance dataset and Eurostat; see Annex for details.

One potential weakness of analysing the investment and financing structure of the business sector in an economy is treating the whole non-financial corporate sector as one entity without taking into account differences with respect to key characteristics, such as size, listing status and industry. From a corporate finance perspective, it may also be important to know if a company is part of a larger company group. To overcome these shortcomings, non-financial companies in Romania and peer countries are divided into four categories:

Category 1: Listed companies

This category includes, on average, 287 non-financial listed corporations per year with median assets of around EUR 8.3 million. Since being listed on a stock exchange requires the adoption of certain transparency and disclosure standards as well as other corporate governance practices, listing status may have a strong impact on a corporation's financing conditions. A listed company typically passes a certain threshold in terms of its formal and institutional structure, which may make outside investors more willing to provide funds and which facilitates access to a wider range of financing options, including private equity as well as public and private debt markets. This category includes corporations that were listed on multilateral trading facilities (MTFs). Companies that were listed on the discontinued (since 2015) alternative equity market Rasdaq were excluded. As presented in Figure 3.12, in 2018 listed companies accounted for 3% of employment in the economy and generated 5% of aggregate sales.

Category 2: Large unlisted companies

This category includes, on average, 216 non-financial corporations with assets larger than EUR 89 million (USD 100 million) in 2019 real terms. Their median asset size was EUR 166 million in 2018, which is significantly larger than that of listed companies. This is mainly a result of the inclusion of smaller MTF listed companies in the listed company category.[2] Compared with publicly listed companies, less information is available for large unlisted companies, reducing their available financing options or potentially resulting in less favourable financing conditions. However, companies in this category can generally be classified as professionally managed, formal companies. In 2018, large unlisted companies represented around 35% of total sales and 15% of employment in the economy.

Category 3: Small and mid-sized companies that are part of a group

This category includes all small and mid-sized enterprises controlled by a listed (Category 1) or a large unlisted corporation (Category 2). SMEs based in Romania but controlled by a non-Romanian company are also included in this category. Category 3 contains, on average, 1964 companies per year with median assets of EUR 4.5 million. Since the financial results of SMEs that are part of a group are consolidated into a parent company, unconsolidated accounts are used in the analysis to identify their own structure. In general, the information available for SMEs is relatively limited, but being part of a group can help them access financing on better conditions compared with independent SMEs. By creating an internal capital market, an economic group can also improve the available financing options for group companies.

Category 4: Independent small and mid-sized companies

The last category includes all SMEs identified to be controlled by individuals and those with no available ownership information. For this category, only unconsolidated accounts are available. The group of Independent SMEs is the largest in terms of number of companies (an average of 40 540 companies per year), but the smallest in terms of size (median assets of around EUR 0.39 million). The information available for these companies is limited and unlike SMEs that are part of a group, Independent SMEs do not benefit from the financing advantages related to a group structure. As of end-2018, independent SMEs made up more than half of the total employment in the economy, but only 33% of total sales.

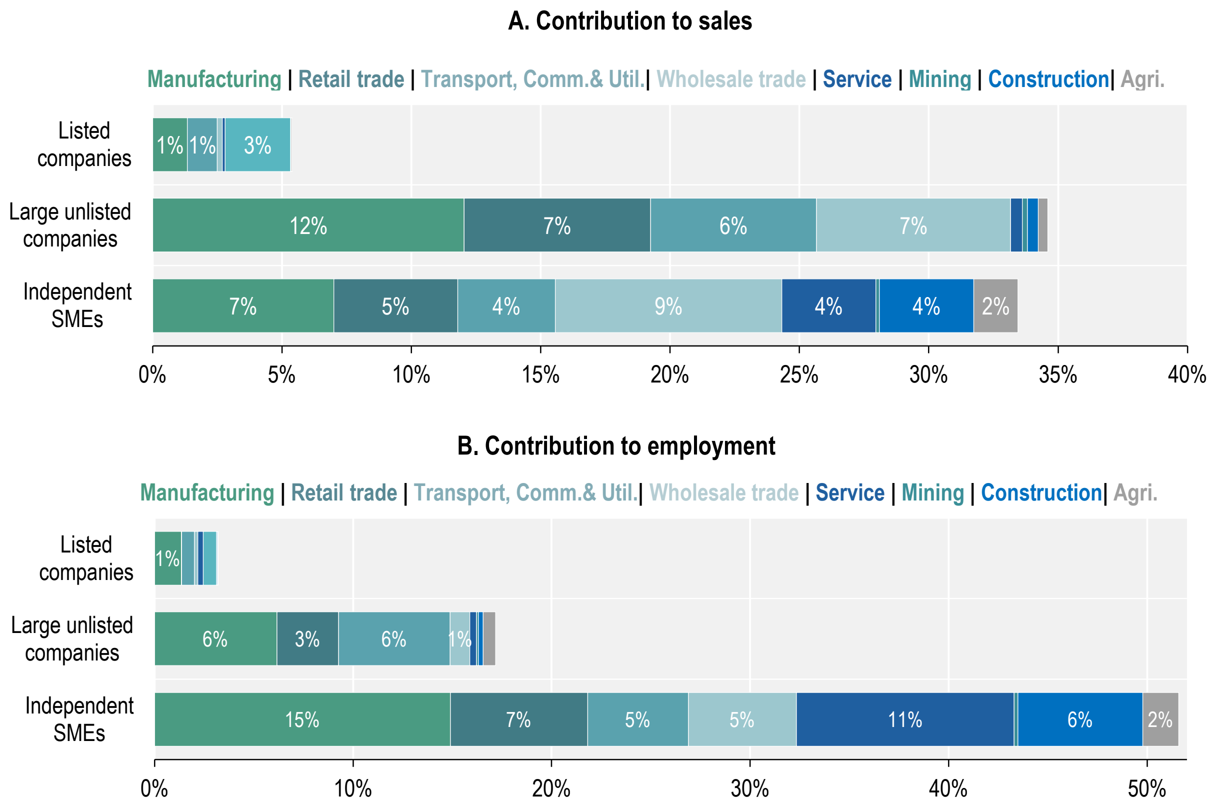
Table 3.4 below shows the distribution of these four categories of non-financial companies in Romania with respect to their number and their median assets.

Table 3.4. Company categories of the non-financial business sector in Romania.

	Category 1: Listed companies		Category 2: Large unlisted companies		Category 3: SMEs part of a group		Category 4: Independent SMEs	
	No. of companies	*Median assets (EUR K)*	*No. of companies*	*Median assets (EUR K)*	*No. of companies*	*Median assets (EUR K)*	*No. of companies*	*Median assets (EUR K)*
2005	325	5 113	104	207 801	1 546	3 024	32 745	271
2006	320	6 213	142	181 782	1 587	3 842	35 923	338
2007	318	8 087	191	172 845	1 696	4 399	39 303	383
2008	315	8 157	208	171 499	1 832	4 419	39 909	399
2009	305	8 181	206	163 619	1 820	4 402	35 188	419
2010	296	8 641	221	171 535	1 876	4 524	34 945	430
2011	288	8 640	221	172 637	2 032	4 663	38 951	394
2012	294	8 729	219	190 497	2 083	4 572	41 116	382
2013	288	8 945	213	173 276	2 084	4 587	42 341	370
2014	281	8 538	226	168 614	2 162	4 761	43 193	385
2015	270	8 804	256	157 895	2 268	4 723	44 952	395
2016	245	8 747	266	151 430	2 167	4 939	46 262	397
2017	246	8 883	268	158 618	2 239	5 094	46 225	411
2018	232	9 905	279	165 573	2 098	5 538	46 509	445
Avg.	**287**	**8 256**	**216**	**171 973**	**1 964**	**4 535**	**40 540**	**387**

Source: OECD-ORBIS Corporate Finance dataset; see Annex for details.

Figure 3.12. Company categories' contribution to sales and employment by industry in 2018

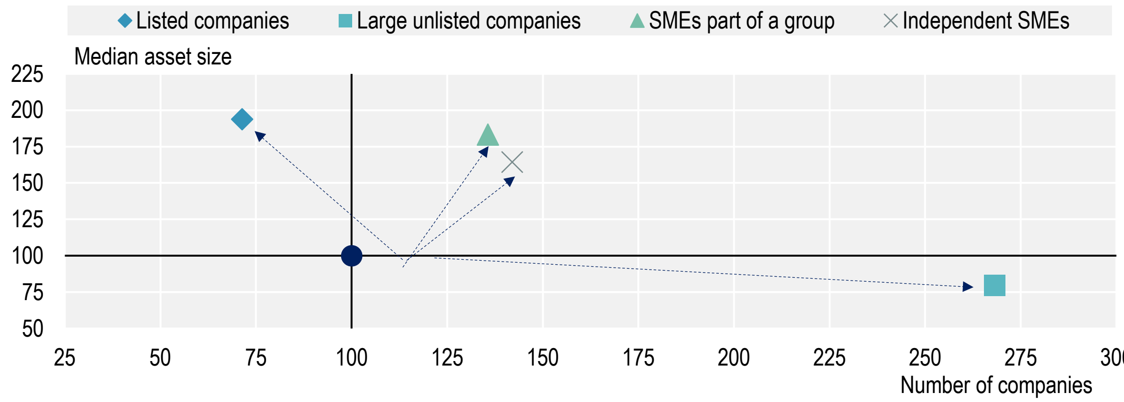


Note: For each category, sales and employment numbers are presented as shares of economy totals. Calculations for the total economy take into account the group structure of companies and avoid considering companies that are already consolidated in the accounts of domestic non-financial parent companies. The figure does not show the category SMEs part of a group as these companies are accounted for in the financial statements of their parent company. The categories in this figure are subsamples of the economy constructed for characterisation and comparison purposes and do not consider parent companies with less than EUR 89 (USD 100) million in assets. As a result, they do not add up to 100%.
Source: OECD-ORBIS Corporate Finance dataset, see Annex for details.

3.4. Non-financial company performance and profitability

In Romania, the number of companies in all four categories has grown since 2005, except for the number of listed companies, which is now significantly lower than it was in 2005. In parallel, the median asset size of listed companies has increased substantially, resulting in fewer but larger listed companies. Asset size has also increased for SMEs that are part of a group and independent SMEs, while it has decreased somewhat among large unlisted companies. Figure 3.13 illustrates the evolution in the number of companies and median asset size for each category between 2005 and 2018, where 2005 is indexed to a baseline value of 100.

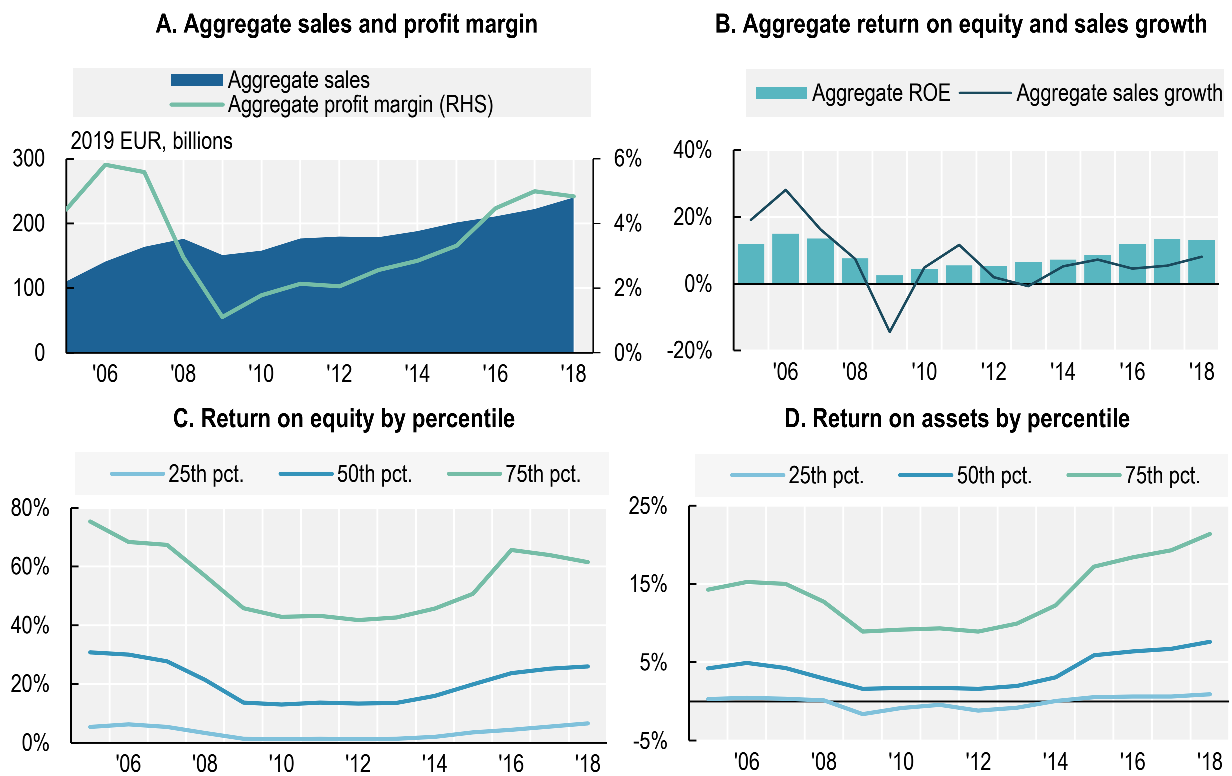
Figure 3.13. Growth in the number of companies and median asset size, 2005-18 (2005 = 100)



Note: Median assets are inflation adjusted per 2019, thus the change in median assets size reflects real change.
Source: OECD-ORBIS Corporate Finance dataset; see Annex for details.

The corporate sector in Romania was severely hit by the 2008 financial crisis. Sales dropped by 14% in 2009, profit margins fell from 3% to 1% and aggregate ROE from 8% to 3% (Figure 3.14, Panels A and B). This decline is observed for both high and low-performing firms in terms of return on equity (ROE) and return on assets (ROA) (Figure 3.14, Panels C and D). After remaining at lower levels for a number of years, the aggregate profitability ratios started to pick up gradually in 2013. While sales growth has remained subdued compared to pre-2008 levels, the aggregate profit margin reached pre-crisis levels in 2018. It should be noted that there is a marked difference in performance between the top and bottom groups of non-financial corporations in Romania, as illustrated in Panels C and D below. While the differences between the 75th and the 25th percentiles in terms of both ROE and ROA were actually decreasing during the period between 2005 and 2012, the gap has been widening again since 2013.

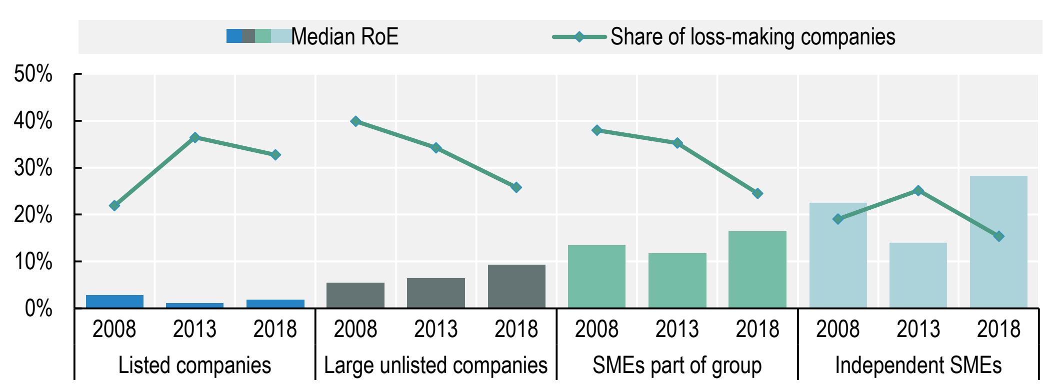
Figure 3.14. Profitability and sales of Romanian non-financial companies



Source: OECD-ORBIS Corporate Finance dataset; see Annex for details.

Financial performance, measured as ROE and the share of loss making companies,[3] differs significantly across company categories (Figure 3.15). Generally, the lower the share of loss making companies, the higher the median ROE. Independent SMEs exhibit by far the highest median ROE and the lowest share of loss making companies, while the reverse is true for listed companies.

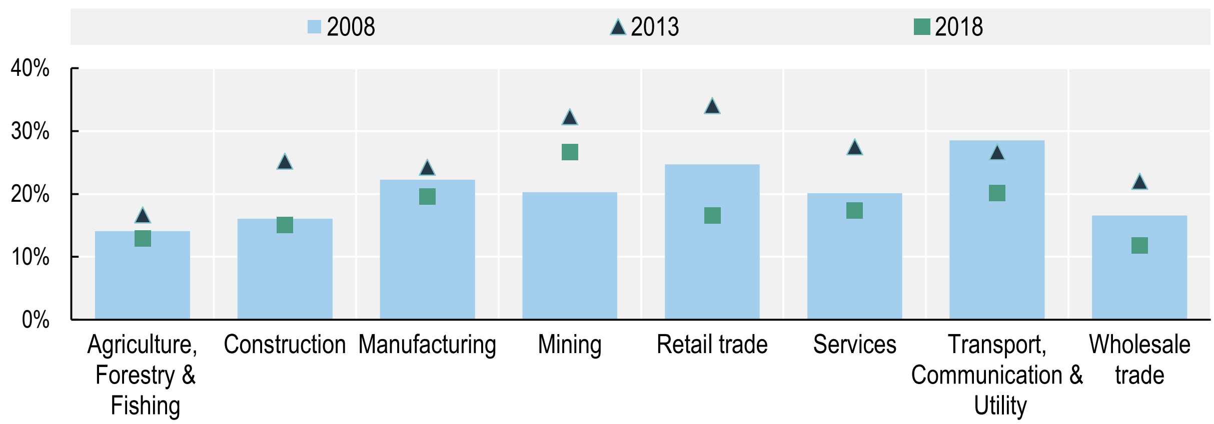
Figure 3.15. Median ROE and share of loss-making companies by category



Source: OECD-ORBIS Corporate Finance dataset; see Annex for details.

In 2018 the mining industry had the highest share of loss making companies in Romania, followed by the transport, communication and utility industry (Figure 3.16). The mining industry is also the only one that had a larger share of loss making companies in 2018 than it did in 2008. Wholesale trade had the lowest share in 2018 with 12% of all the companies in the industry. A general observation is that the share of loss making companies has declined for all industries since 2013, although to varying degrees.

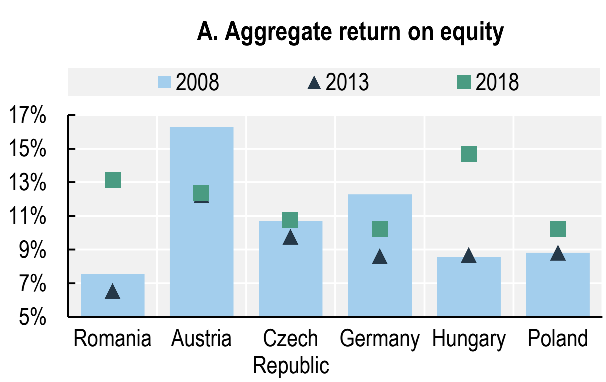
Figure 3.16. Share of loss-making companies by industry

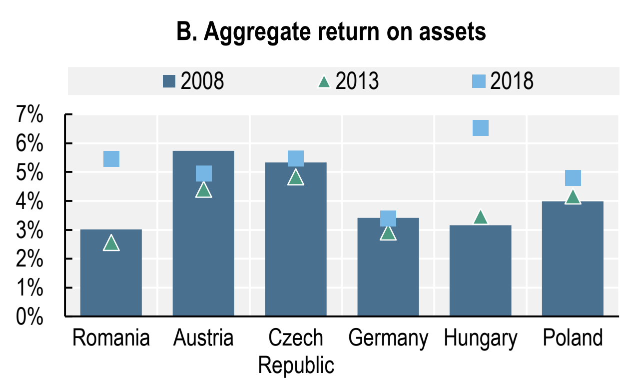


Source: OECD-ORBIS Corporate Finance dataset; see Annex for details.

A comparison with peer countries reveals that Romanian non-financial companies' profitability ranked second highest in terms of return on equity and close third in terms of return on assets in 2018 (Figure 3.17). This is a significant improvement from both 2008 and 2013, when Romania ranked last for both metrics.

Figure 3.17. Profitability of non-financial companies for Romania and selected European countries



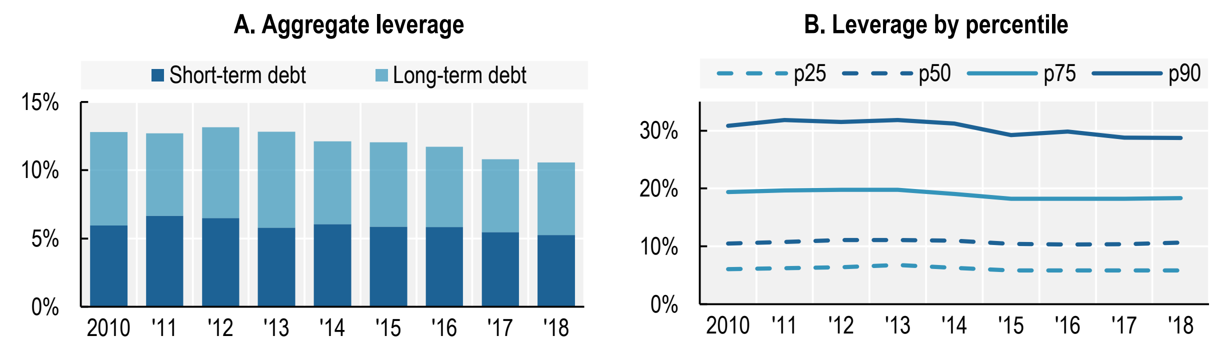


Source: OECD-ORBIS Corporate Finance dataset; see Annex for details.

3.5. Leverage levels

Romanian non-financial companies have seen a slight decrease in leverage ratios (financial debt over total assets) over the past decade, which is mainly a result of the decline in long-term debt from 7% in 2010 to 5% in 2018. This drop can be primarily attributed to highly leveraged companies lowering their indebtedness. Specifically, companies in the 90th percentiles saw a 2 percentage point decline in 2015.

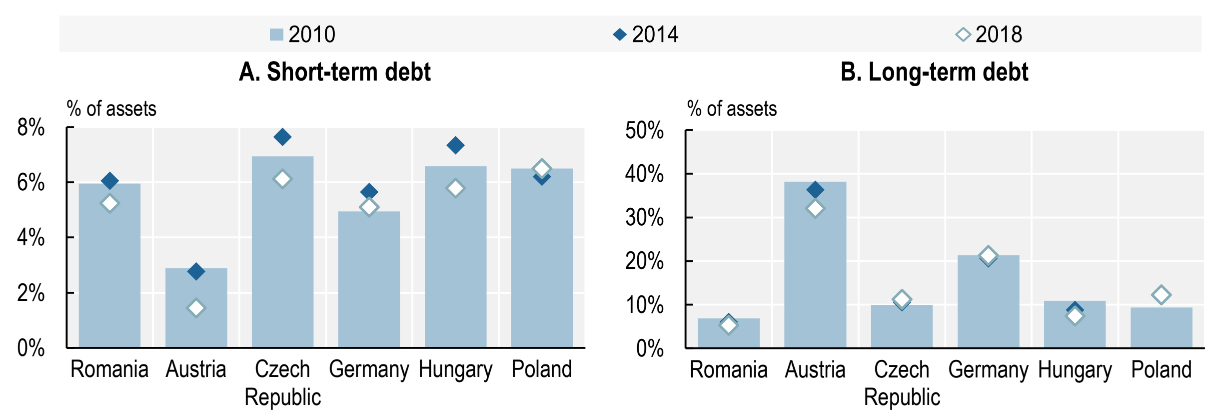
Figure 3.18. Leverage of Romanian non-financial companies



Source: OECD-ORBIS Corporate Finance dataset; see Annex for details.

A comparison with peer countries shows that the Romanian corporate sector has a relatively low level of indebtedness, particularly with regards to long-term debt (Figure 3.19, Panel B). This is consistent with the fact that the bank credit stock to the corporate sector in Romania has remained one of the lowest in the region at around 26% of GDP (see Figure 3.6, Panel A). Notably, Romanian corporations have since 2005 always been the ones with the lowest level of long-term debt. The opposite is true for Austrian and German firms, which have lower levels of short-term debt, as they instead rely mainly on long-term debt. High reliance on short-term debt can expose companies to economic downturns and is not considered appropriate for financing strategic productivity enhancing investments.

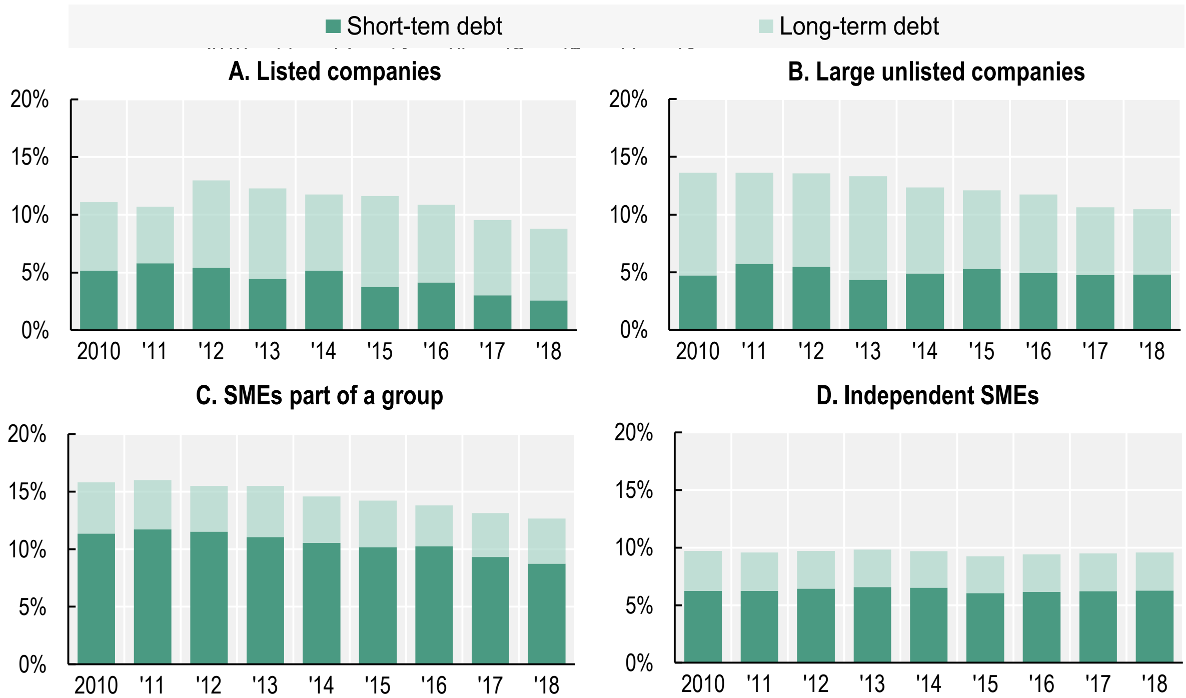
Figure 3.19. Debt of non-financial companies in Romania and selected European countries



Source: OECD-ORBIS Corporate Finance dataset; see Annex for details.

Among the four categories of non-financial companies in Romania, independent SMEs are the ones with the lowest leverage levels, remaining at around 10% throughout the period (Figure 3.20, Panel D). SMEs that are part of a group have the highest aggregate leverage levels, with short-term debt almost 5 percentage points higher than independent SMEs (Figure 3.20, Panel C).

Figure 3.20. Aggregate leverage levels by company categories in Romania



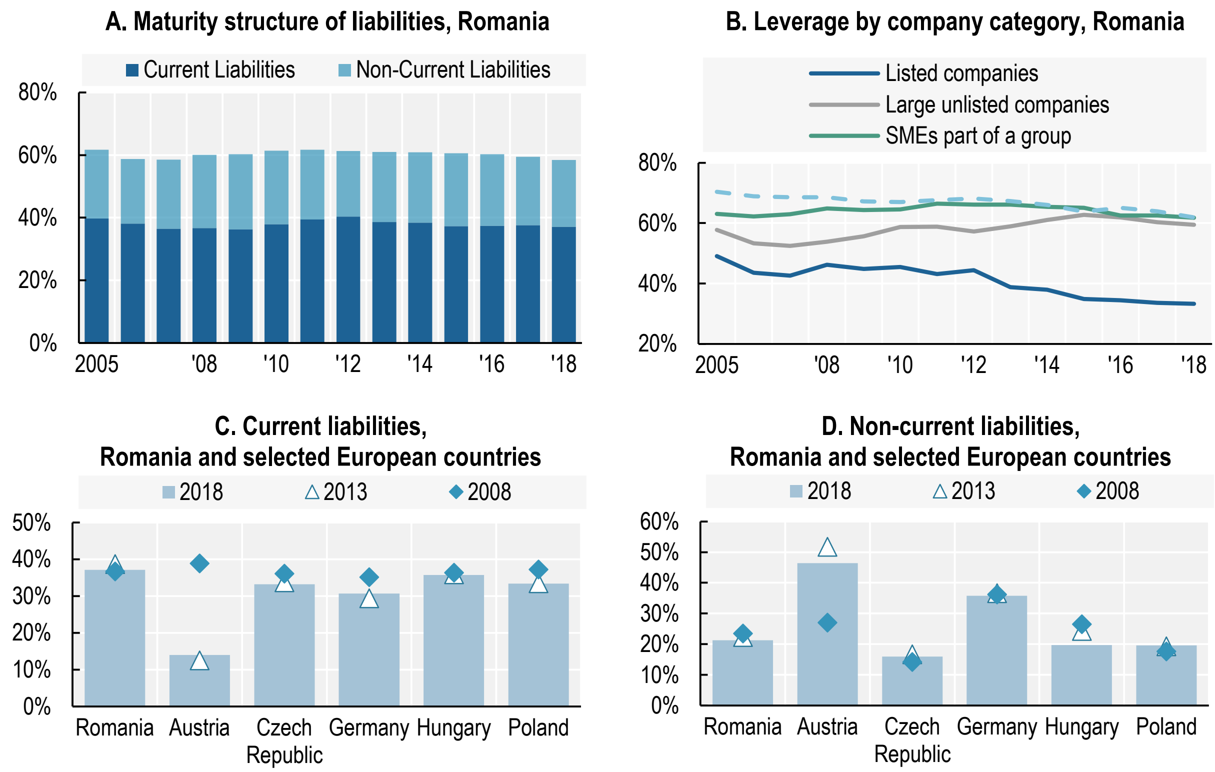
Source: OECD-ORBIS Corporate Finance dataset; see Annex for details.

Listed companies, which typically have higher levels of capitalisation, are much less dependent on debt financing. As Panel A of Figure 3.20 shows, in 2012 listed companies increased their average debt level rather sharply from 11% to 13%, which may be a result of companies raising funds to cope with the crisis. Since then, leverage in listed companies saw a stable decrease from 13% in 2012 to 9% in 2018. The same trend can be observed in large unlisted companies, where average leverage decreased from 14% in 2012 to 10% in 2018 (Figure 3.20, Panel B). It is also important to point out that these two groups of companies have a higher ratio of long-term debt to total debt compared to SMEs.

Only a small share of the total number of companies in Romania reported that they had any financial debt on their balance sheets. Therefore, in order to improve the comparability of the analysis, Figure 3.21 shows an alternative leverage measure which also includes non-financial liabilities (e.g. trade payables). Total liabilities over total assets was around 60% throughout the period for Romanian companies, with current liabilities accounting for almost two-thirds of the total liabilities (Figure 3.21, Panel A). However, there is heterogeneity across company categories and over time. The alternative leverage ratio for listed companies was significantly lower compared with the other three categories at 49% in 2005 and 33% in 2018. While the leverage level for the independent SMEs category was the lowest when only financial debt is considered, it is the highest when total liabilities are taken into account. However, they also saw a decline in leverage from 70% in 2005 to 62% in 2018 (Figure 3.21, Panel B). The two other groups, large unlisted companies and SMEs part of a group, had relatively stable levels of liabilities as a share of total assets over the period.

Companies in the CEE region are typically more heavily reliant on short-term liabilities in their financing structure than European peers. In 2018, the average share of current liabilities to total liabilities for Romania, the Czech Republic, Hungary and Poland was 65%, compared to 23% in Austria and 46% in Germany (Figure 3.21, Panels C and D).

Figure 3.21. Leverage measured as total liabilities as a share of total assets

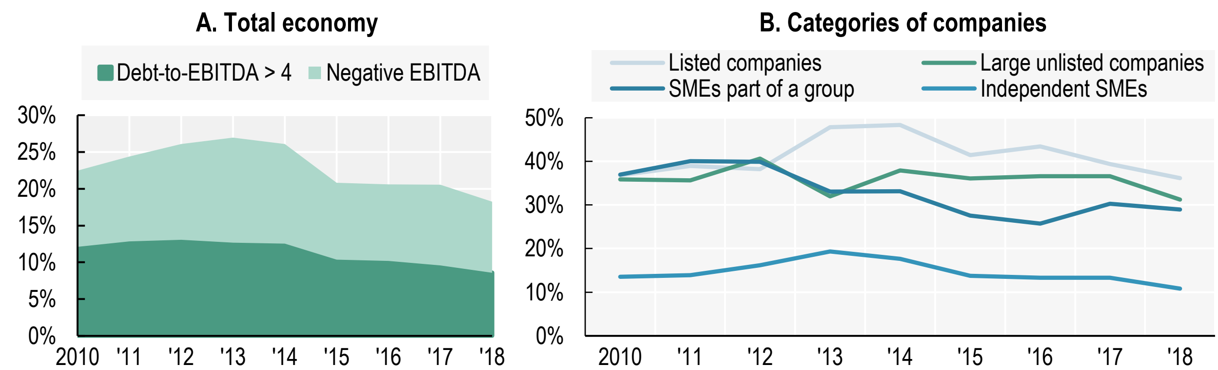


Source: OECD-ORBIS Corporate Finance dataset; see Annex for details.

One important indicator to measure a company's ability to service its debt is the debt-to-EBITDA ratio, which shows the indebtedness level against the operational profit generating capacity of the company. This measure provides a proxy for debt sustainability: a higher value reflects a lower debt service capacity. It is typically considered that a ratio over four puts a company in a higher risk category (Standard & Poor's Global, 2013[20]). Panel A of Figure 3.22 shows that the share of Romanian firms with a high debt-to-EBITDA ratio (>4) increased significantly after the 2008 crisis and during the European sovereign debt crisis, as profitability decreased. As the economy has recovered gradually in recent years and indebtedness has decreased, the share of firms with high debt-to-EBITDA ratios has since dropped significantly.[4] In 2018, around 9% of companies in Romania had a debt-to-EBITDA ratio over four, which is significantly lower than in Poland (17%) and the Czech Republic (14%).

Among the different categories of companies, listed companies have the largest share of companies in the higher risk category at around 40%, while the independent SMEs category has the smallest portion (Figure 3.22, Panel B). Large unlisted companies and SMEs that are part of a group reached 40% in 2012 during the crisis, after which the portion of companies with high debt-to-EBITDA ratios declined gradually, reaching around 29% in 2018.

Figure 3.22. Share of firms with high debt-to-EBITDA ratio



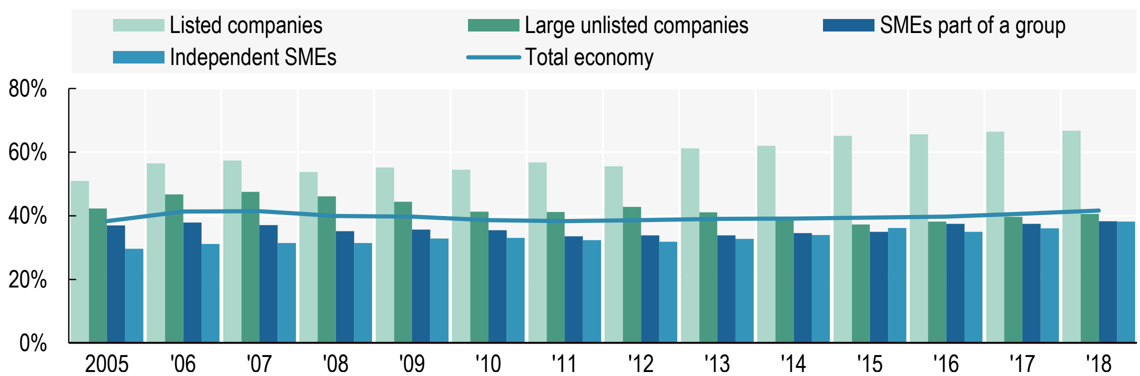
Note: In Panel A, companies that reported both financial debt and negative EBITDA are included in the high-leverage companies to reflect their incapacity to generate operational profit to be used towards repaying debt.
Source: OECD-ORBIS Corporate Finance dataset; see Annex for details.

An issue of great importance with respect to corporate leverage is the structure of the debt, in particular the currency composition. Non-financial companies in Romania are heavily dependent on non-resident creditors and foreign currency debt, which has financial stability implications. Foreign direct investment in the form of loans and direct loans from non-resident financial institutions make up more than half of all non-financial corporate debt in Romania. At the end of 2019, foreign financing was 1.2 times higher than financing from resident financial institutions. More importantly, loans from non-resident entities make up 72% of total foreign currency debt (BNR, 2020[9]). This reliance on foreign creditors and currencies carries potential financial stability risks, including spill overs from macroeconomic fluctuations in the currency issuing country, especially to the extent that there is a mismatch between the debtor companies' revenues (local currency) and their debt service (foreign currency). Overall, the debt composition of Romanian non-financial corporations add to the already strong rationale for developing domestic capital markets.

3.6. Capitalisation and equity capital misallocation

During the 2008 financial crisis, Romanian non-financial companies saw a sharp drop in their capitalisation levels (total shareholders' equity as a share of total assets). The aggregate equity capital as a share of total assets declined by 3 percentage points, from 41% in 2007 to 38% in 2011 (Figure 3.23). Listed companies have had the highest capitalisation level since 2008, and following the initial drop in capitalisation they also managed to increase their equity capital significantly from 56% in 2012 to 67% in 2018. Large unlisted companies, however, saw a continued decrease in capitalisation over the same period. SMEs that are part of a group experienced a decline from 37% to 34% from 2007 to 2011. After remaining at this level for a number of years, their equity levels began to improve, reaching 38% in 2018. The capitalisation level of independent SMEs has risen modestly since 2005.

Figure 3.23. Capitalisation levels for different categories of Romanian companies

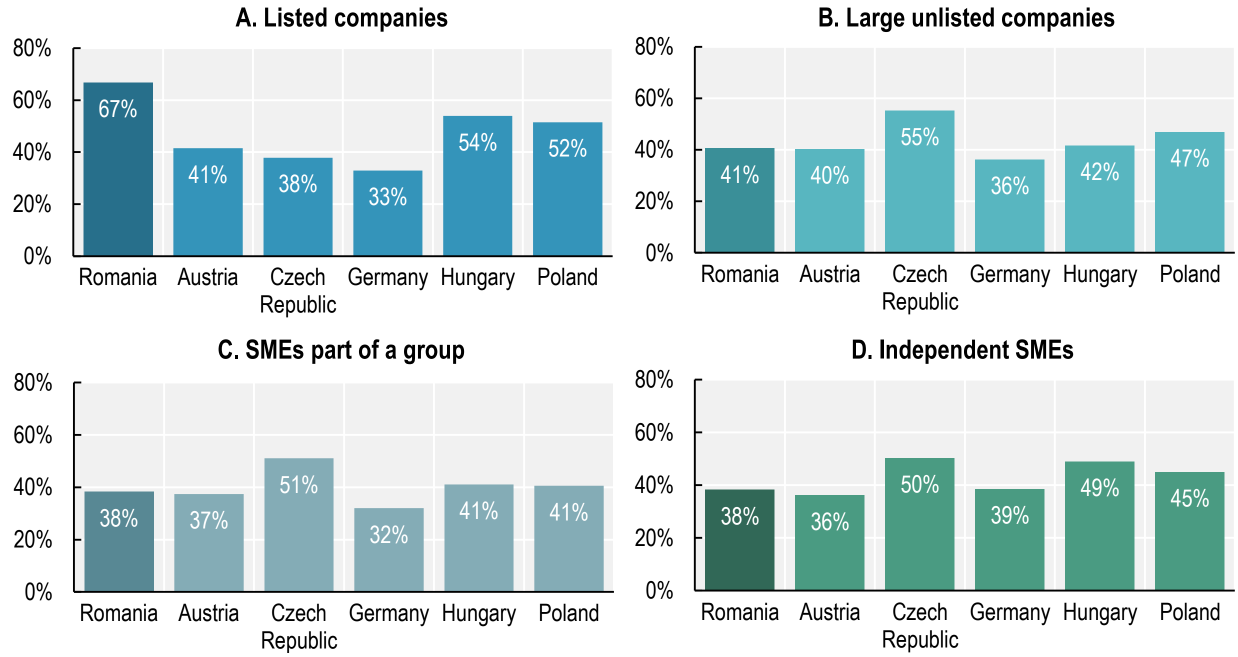


Source: OECD-ORBIS Corporate Finance dataset; see Annex for details.

A comparison between Romania and peer countries shows that Romanian listed companies have a much higher aggregate capitalisation level (Figure 3.24, Panel A). This generally holds across the distribution of capitalisation (i.e. both for high and low-capitalisation companies) and over time. However, large unlisted companies have a lower level of capitalisation (41%) compared with countries such as the Czech Republic (55%) and Poland (47%) (Figure 3.24, Panel B). In addition, both groups of SMEs have relatively low capitalisation levels compared to regional peers (Figure 3.24, Panels C and D).

In recent years, there has been an increasing concern worldwide about companies that do not even generate enough profits to service their debt, so called zombie companies. In addition, some companies have suffered an erosion of their equity capital over time as a result of continued low profitability and are currently in a situation where they have negative equity. While zombie companies are defined as those that are incapable of covering their interest payments with operating income, negative equity firms are those firms for which liabilities exceed assets.[5] These two groups of companies are still alive either due to the protection of creditors or because they are related to a more solvent economic group or parent company. Having a large share of zombie and negative equity companies can pose a threat to the resilience of the corporate sector as a whole (Banerjee and Hofmann, 2018[21]). Importantly, it may not only be detrimental to the individual company but to the economy as a whole, since zombie companies are locking in resources that could be allocated to more productive activities. Continued support for zombie companies distorts market functioning and hinders economic recovery and reallocation (Scope, 2019[22]).

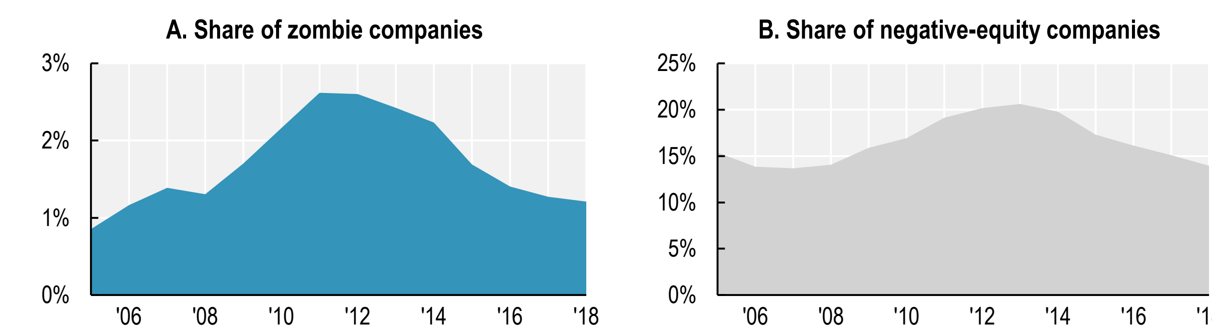
Figure 3.24. Company capitalisation for Romania and selected European countries in 2018



Source: OECD-ORBIS Corporate Finance dataset; see Annex for details.

In Romania, the share of zombie firms is relatively small. This is to some extent driven by the fact that smaller companies have low levels of financial debt. In 2015, out of 460 000 enterprises active in the country, less than 28% fell within banks' minimum financial criteria (World Bank and IMF, 2018[10]). Panel A of Figure 3.25 shows that the share of zombie firms increased significantly in the build up and aftermath of the 2008 crisis, after which it began decreasing in 2012. Romanian companies have also experienced an increase in firms with negative equity. The share of firms with negative equity peaked in 2014 at 20% of all companies and then declined to 14% in 2018 (Figure 3.25, Panel B).

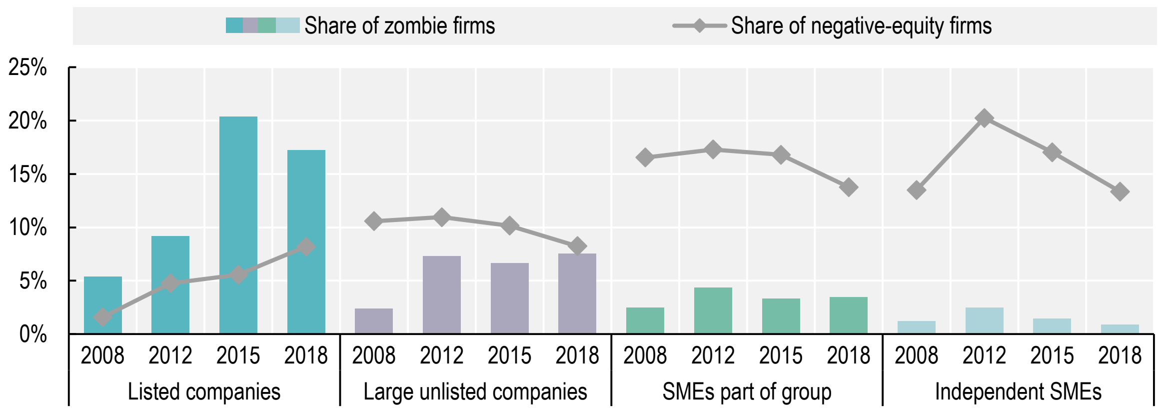
Figure 3.25. Share of zombie and negative-equity companies in Romania



Source: OECD-ORBIS Corporate Finance dataset; see Annex for details.

The share of zombie and negative equity companies differs considerably between different groups of companies. Importantly, the portion of listed zombie companies more than tripled between 2008 and 2018 (Figure 3.26). Similar to listed companies, large unlisted companies also saw a significant increase in zombie companies in the aftermath of the 2008 financial crisis and during the European sovereign debt crisis, reaching 7% in 2012; a level at which it remained in 2018. Both groups of SMEs, particularly independent SMEs, have rather low share of zombie firms. However, they have the highest ratio of negative equity companies. Independent SMEs saw an important increase in negative equity companies from 13% in 2008 to 20% in 2012.

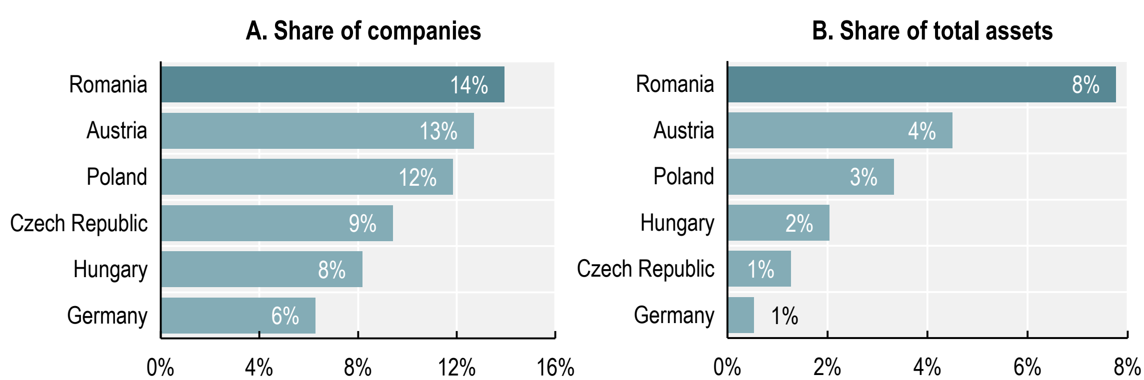
Figure 3.26. Share of zombie and negative-equity companies across different groups



Source: OECD-ORBIS Corporate Finance dataset; see Annex for details.

Both zombie and negative equity firms can reduce the efficiency of capital allocation in the economy as capital locked up in such firms could potentially be used by more productive companies. Despite having a modest share of zombie firms, Romania was the country with the highest ratio of negative equity firms in 2018 among peer countries (Figure 3.27). The share of companies and assets associated with negative equity companies are 14% and 8% respectively, which is higher than in peer countries. According to the National Bank of Romania, by the end of 2019, the capital needs of non-financial companies with negative equity amounted to 16.8% of Romanian GDP. Moreover, negative equity companies accounted for 67% of overdue payments in the economy and around 35% of non-performing loans from local credit institutions. The NPL ratio of those firms was 20% at the end of 2019 (BNR, 2020[9]).

Figure 3.27. Companies with negative equity in Romania and selected European countries in 2018



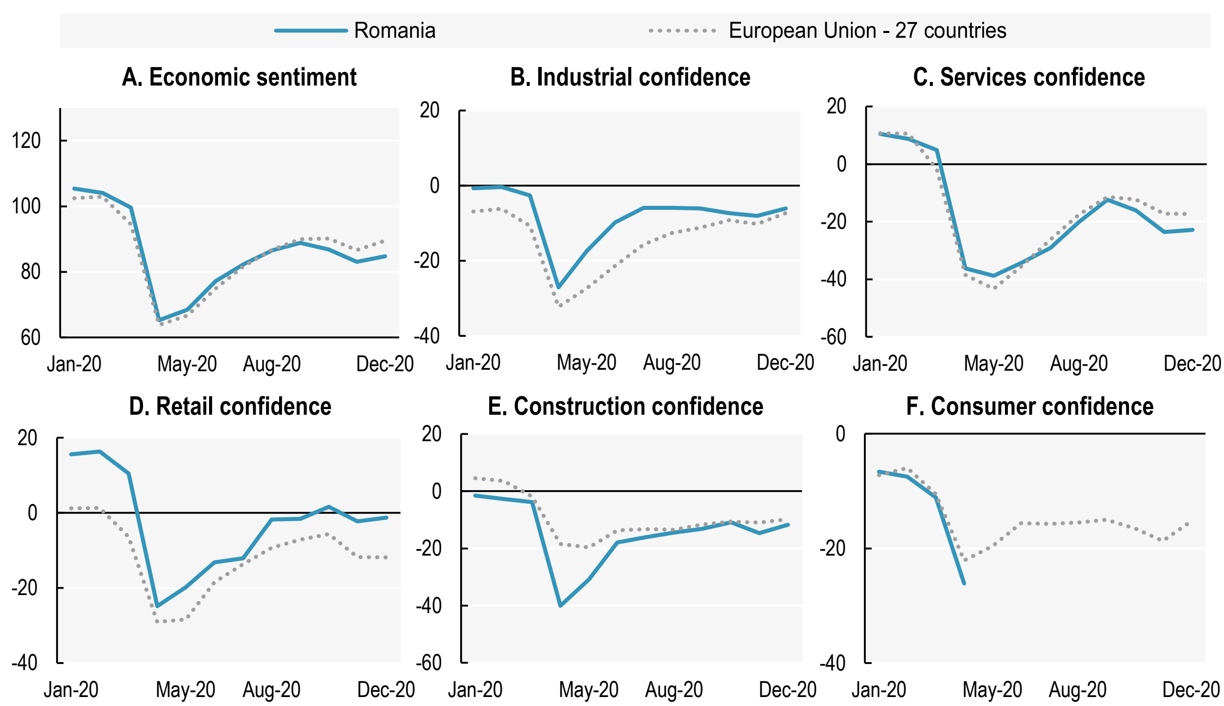
Source: OECD-ORBIS Corporate Finance dataset; see Annex for details.

3.7. The impact of COVID-19 on the corporate sector

The COVID-19 pandemic is having an unprecedented impact on economies around the world. Measures such as social distancing, travel restrictions and prohibitions to engage in social activities implemented to contain the transmission of the virus led to a widespread shutdown of businesses during the initial and subsequent waves of the pandemic. As a result, the world economy has seen a record slowdown in activity. The OECD expects a 3.4% contraction in global GDP in 2020 (OECD, 2021[23]). The sharp drop in sales experienced by the corporate sector has also caused acute liquidity pressures and growing insolvency concerns in many economies and industries. The estimated decline in profits is sizeable, amounting to on average between 40% and 50% of normal time profits according to OECD research. In such a scenario, around 7-9% of otherwise viable European companies could become distressed and around one-third of the companies may not be able to cover their interest expenses (Demmou et al., 2021[24]). It is forecasted that as the crisis evolves, some existing businesses will recover after a temporary downturn while others will be phased out. Importantly, this shock came at a time when there was already widespread concerns about the high levels of debt in the corporate sector and the declining quality of the outstanding stock of debt around the world.

In the third quarter of 2020, global activity recovered in some sectors as a result of significant measures taken by governments and central banks. Government interventions have played an important role in helping firms address the liquidity shortfall (Demmou et al., 2021[25]). However, some service activities remain limited due to physical distancing. The collapse in employment observed at the start of the pandemic has partially reversed, but a large number of people still remain unemployed. Most firms have survived, but are in many cases financially weak. Vaccination programmes, health policies and government financial support are expected to lift global GDP by 5.6% in 2021 (OECD, 2021[23]).

Figure 3.28. Economic sentiment and confidence across industries in Romania and EU-27

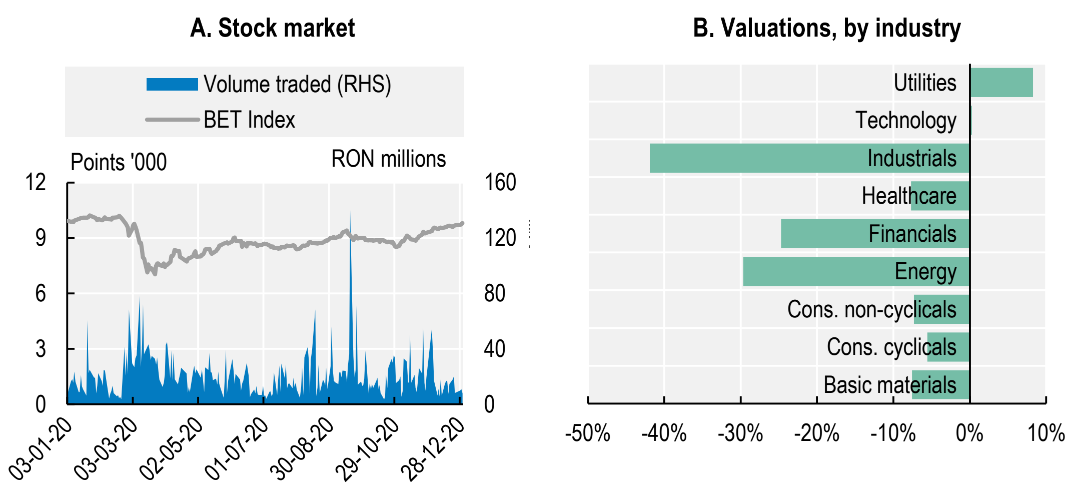


Note: The Economic Sentiment Indicator is scaled to a long-term mean of 100 and a standard deviation of 10. Values above 100 indicate above-average economic sentiment and vice versa. The confidence indicators are published as the difference between positive and negative answers (in percentage points of total answers).
Source: European Commission - DG ECFIN.

As in all other countries, the uncertainty about the future developments of the COVID-19 pandemic has significantly weakened expectations about economic growth and business sector confidence in Romania. The economic sentiment indicator in Romania saw a sharp decline during the initial phase of the pandemic, much in line with the EU 27 (Figure 3.28, Panel A). After May 2020, expectations started to pick up. Still, uncertainties kept expectations lower than at the beginning of 2020 and the economic sentiment in Romania was lower than the average EU 27 by the end of 2020. The confidence indicator across industries reached its lowest level in April 2020. Confidence loss was particularly strong in the Services and Construction industries. Similar to economic sentiment, confidence levels have not yet recovered, and perceptions at the industry level remain overall pessimistic. Confidence in the retail industry has recovered faster in Romania than in the EU 27 overall (Figure 3.28, Panel D).

The listed corporate sector in Romania has also suffered a large contraction in valuations while volatility in financial markets has increased. As a result of the pandemic, current and forecasted corporate revenues have declined significantly. The local index of the Bucharest Stock Exchange experienced a sharp contraction of 30% from the end of 2019 to its lowest index value in March 2020. By the end of 2020 the domestic index had almost recovered its value compared to the start of the year, recovering more quickly than the stock market indices in Hungary and the Czech Republic (Figure 3.29, Panel A). The contraction in stock market valuations varied across industries. For example, industrials companies had seen a 42% contraction by October 2020, followed by energy companies and the financial sector, which fell by 30% and 25%, respectively. Technology companies in Romania did not experience any change in their valuations, whereas utilities companies showed an 8% increase (Figure 3.29, Panel B).

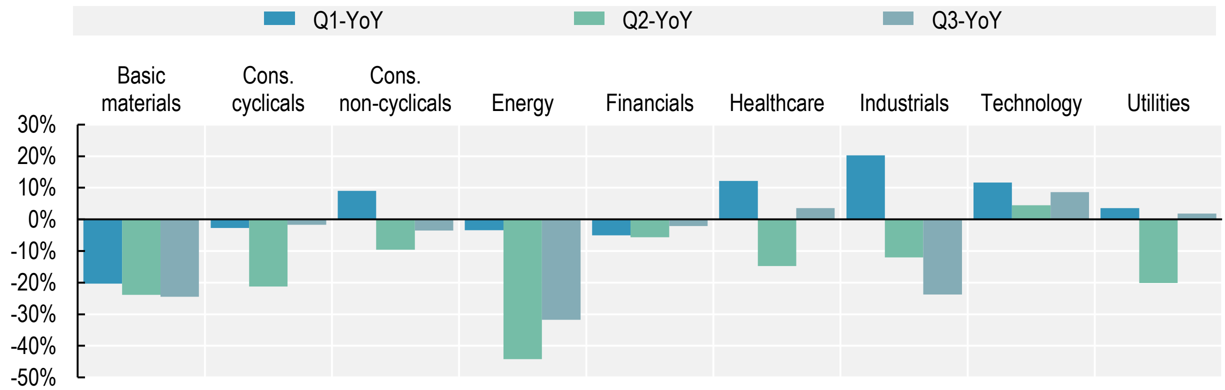
Figure 3.29. Financial market indicators in Romania



Note: Panel B compares stock market values between end-October and the beginning of 2020.
Source: Thomson Reuters Eikon, Bucharest Stock Exchange, BNR.

In the first quarter of 2020, among the listed companies on the Bucharest Stock Exchange, five industries saw an increase in total sales compared to the same quarter in 2019 (Figure 3.30). However, in the second quarter all industries experienced a drop in reported sales compared to the second quarter of 2019, with the exception of technology companies. Energy, basic materials and industrials saw sharp falls in total sales in the third quarter of 2020. At the same time, health care, technology and utilities companies experienced higher sales.

Figure 3.30. Quarterly sales YoY changes 2019-20



Source: Thomson Reuters Datastream.

3.8. Government relief programmes to the corporate sector

In response to the COVID-19 pandemic, the Romanian Government has implemented a range of measures to support households, jobs and businesses. The authorities have also implemented measures to support specific industries affected by the pandemic.

To *help companies maintain their workforce*, the government started partially covering the wages of the self-employed and partially subsidising the wages of workers with reduced working hours at the beginning of the pandemic. Subsidies were allocated to workers returning to work. Later, the government established a job retention scheme (with a compensation for employees at 75% of their gross salary), a 3-months wage subsidy for the resumption of activity, and an allowance for the self-employed. Subsidies were also provided for hiring jobseekers aged over 50 or below 30, and to Romanian citizens returning to the country. These measures amounted to RON 8.0 billion in 2020 and RON 1.9 billion in 2021 (OECD, 2022[26]).

To *alleviate the liquidity needs of corporations*, the government has introduced a deferral of utilities payments for SMEs. Other measures include faster reimbursement of VAT, suspending foreclosures on overdue debtors, discounts on corporate income taxes, postponement of the property tax, and exempting hospitality companies from the industry specific tax. In addition, the government has issued legislation that requires banks to defer loan repayments for households and businesses affected by the crisis by up to nine months (in place until March 2021). In October 2020, a EUR 103 million Romanian guarantee scheme was established to support the trade credit insurance market with a view to secure the continuity of the trade credit insurance to all companies, to avoid the need for buyers of goods or services to pay in advance, therefore reducing their immediate liquidity needs. In November 2020, another EUR 216 million scheme was introduced to support SME liquidity through guarantees of the factoring products. The scheme applies only to factoring products with recourse against the seller. The support was offered in the form of direct grants. The government also introduced the possibility to cancel interest and penalties on outstanding corporate tax liabilities (in place until January 2022) and to reschedule corporate tax liabilities for 12 months (in place until September 2021) (OECD, 2022[26]).

To *help companies access financing*, in 2020 the government enabled a state aid scheme under the Temporary Framework developed by the European Commission to support the economy in the context of the coronavirus outbreak. The aid was provided in the form of state guarantees for loans (the guarantee ceiling in 2020 was RON 20 billion) and direct grants to cover interest and some related fees. The aim of the scheme is to help businesses cover their immediate working capital or investment needs, thus ensuring the continuation of their activities. By the end of September 2021, the total amount of guarantees issued amounted to RON 19.09 billion. A guarantee scheme of about RON 1.5 billion (0.15% of GDP) was also adopted to support the procurement of work equipment by SMEs. In July 2020, the EC approved an additional RON 4 billion (approximately EUR 800 million) Romanian scheme to support companies affected by the coronavirus outbreak. The scheme offered subsidised loans and state guarantees on loans to SMEs with a turnover over RON 20 million (approximately EUR 4 million) in 2019 and to large companies. The scheme is managed by the development bank arm of Export Import Bank of Romania ("EximBank"), acting on behalf of the Romanian state. In August, another EUR 935 million was made available to support SMEs active in specific sectors and certain large companies related to the eligible SMEs. The help was provided in the form of direct grants for working capital and productive investments and was co-financed by the European Regional Development Fund. Grants to microenterprises, SMEs and firms in the tourism, accommodation and food sectors were also introduced in 2021.

To *help the airline industry*, a EUR 1 million scheme was established to support airlines resuming or starting flights to and from Oradea airport in Romania. The aid was in the form of direct grants and was accessible to all interested airlines, with a limit of EUR 800 000 per company. An additional EUR 1.7 million scheme was approved to support airlines resuming or starting flights to and from Sibiu airport in Romania. In addition, in August 2020, the EC approved a Romanian direct grant of approximately EUR 1 million (RON 4.8 million) to compensate the Timișoara Airport for the high operating losses incurred in the context of the coronavirus outbreak. In November, another EUR 4.4 million was assigned to compensate regional airport operators for the damage suffered due to the COVID-19 pandemic. The scheme was targeted at operators of Romanian airports with an annual traffic turnover of between 200 000 to 3 million passengers, which are to be compensated with direct grants for net losses incurred between 16 March and 30 June 2020. Two airline companies have also received direct aid. In October 2020, a loan guarantee of EUR 62 million was granted to the Romanian airline Blue Air, and in December the Romanian state owned airline TAROM, received a loan guarantee of EUR 19.3 million.

To *help companies active in the pig and poultry breeding sectors, as well as wine producers*, two schemes with a total budget of EUR 47.4 million were established in September 2020. The support will be provided in the form of direct grants. The aim of the schemes is to help companies address their liquidity needs and continue their operations in order to ultimately secure food and feed materials for the food industry and to maintain jobs. For each of the sectors, the schemes are expected to benefit over 1 000 companies. On November 2020, the EC authorised a EUR 12.4 million scheme to support wine producers. The support is offered in the form of direct grants and is also expected to benefit over 1 000 producers (IMF, 2021[27]).

In addition to the above-mentioned measures, on April 2020 the Romanian Financial Supervisory Authority (ASF) increased the threshold for private pension funds to invest in government securities. In particular, private pension funds were allowed to invest up to 70% of the total value of the fund's assets in government securities issued by the Romanian state or by other EU countries. In addition, in March 2020, the ASF lowered the notification threshold for net short positions in relation to shares traded on the regulated market to 0.1% of the issuer's share capital (Schonherr, 2020[28]). The ASF has also established a 25% discount on all tariffs, taxes, quotas and contributions collected from regulated entities during the state of emergency (ASF, 2020[29]).

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Notes

[1] The Stability & Growth Pact limits the debt to GDP ratio to 60% and fiscal deficits to 3% annually.

[2] Around 75% of listed companies in the sample are listed on the AeRO Market, which is the MTS Market run by Bucharest Stock Exchange.

[3] The share of firms with negative net income in the total number of firms.

[4] Note that debt here refers to financial debt, not total liabilities.

[5] More specifically, in the following analysis zombie companies are defined as companies that are more than nine-years old and which have had interest payments in excess of EBIT during at least the last three years.

4 The Romanian public equity market

This chapter describes the equity market landscape in Romania, including the market infrastructure and recent developments. It provides an overview of the listed corporate sector and the main trends in the use of equity markets with respect to both initial public offerings (IPOs) and secondary public offerings (SPOs) as well as delistings from the stock market. It also illustrates the ownership structure of listed companies in Romania.

Equity capital plays an important role in financing long-term investments with uncertain outcomes, including research, development and innovation. Equity is particularly well-suited to finance investments in intangible assets without strict collateral requirements compared to loan financing. Equity capital also plays an important role in providing companies with the financial soundness and flexibility needed to endure crises and meet financial obligations. For example, following the outbreak of the COVID-19 pandemic in 2020, both listed and new listed companies raised significantly higher amounts of equity capital through the public markets worldwide compared with previous years.

4.1. Stock market developments in Romania

After a long period of inactivity, the Bucharest Stock Exchange (BVB) was re-established as a public interest institution in 1995 and later that year the first trading session took place. In 1997, the exchange listed the first companies of national importance and created the first stock market index BET. The exchange was demutualised and became a joint stock company in 2005. The BVB also merged with Rasdaq, the Electronic Exchange of Securities from Bucharest that same year. In 2010, the BVB became a listed company with its shares trading on the Regulated Market. In 2015, the exchange launched the AeRO Market, a multilateral trading system (MTS) dedicated to serving SMEs. By the end of 2020, 72.17% of BVB's share capital was in the hands of Romanian institutional investors, 5.25% was owned by foreign institutional investors and 19.96% by Romanian private individuals (BVB, 2021[1]).

Developing the capital market has been one of the Financial Supervisory Authority (FSA)'s main objectives since 2014. An important milestone for the Romanian capital market was the upgrade from Frontier to Secondary Emerging market status by the global index provider FTSE Russell. The decision was made in 2019 after Romania had been on the monitoring list for three years and it took effect in September 2019. The reclassification as Secondary Emerging market increases the visibility of the Romanian stock market and decreases the country risk premium since the new status places Romania in the investable universe of a wider range of investors. In addition, a series of measures were adopted to increase transparency and ease market access overall, raising the attractiveness of the local capital market.

Table 4.1. Key dates and developments for the Bucharest Stock Exchange

2020	EBRD launched an analysis and research programme to develop medium sized listed companies.
2019	FTSE Russell promoted Romania to the status of Secondary Emerging Market from Frontier Market.
2016	FTSE Russell included Romania in the list of countries with potential to be upgraded to Emerging Market.
	Launch of the Issuers Reporting Information System (IRIS).
	Launch of the new version of the ArenaXT Web trading platform.
2015	Launch of AeRO Market.
	BVB became a partner exchange to the United Nations Sustainable Stock Exchanges Initiative.
	BVB became a member of the United Nations Sustainable Stock Exchanges Initiative.
2014	BVB organised the first forum for retail investors and adopted the 10 Steps towards civic shareholding.
	Implementation of changes to trading system and practices, and measures targeting issuers.
	Legislative measures supported by the Great Barriers Shift Task Force.
2010	On 8 June, the Bucharest Stock Exchange listed its own shares on the Regulated Market.
2007	Romania became a member of the European Union.
	BVB became an affiliated member of the World Federation of Exchanges (WFE).
2006	The Central Securities Depository was established.
	BVB became a member of the World Federation of Exchanges.

2005	BVB became a joint stock company.
	The merger with Rasdaq market was finalised.
2003	Introduction of the new trading system Arena.
	BVB became a full member of the Federation of Euro Asian Stock Exchanges (FEAS).
2002	BVB became a correspondent member of the Federation of the European Securities Exchanges (FESE).
1997	Launch of the first market index: BET.
1995	BVB was re-established as a public interest institution.
1882	BVB was officially established.

Source: Bucharest Stock Exchange.

4.2. Stock market infrastructure

The reform process that took place in Romania during the 1990s provided the legal and regulatory framework for the creation and operation of private corporations. The enterprise reform of 1990 (Romanian Parliament, 1990[2]) gave birth to commercial companies and Romania also adopted the Commercial Companies Law to regulate the functioning of these entities. The process was accompanied by market reforms, including a competition law and price liberalisation. As part of the reform process, the capital market in Romania was fully recreated in 1994 with Law No. 52/1994 (Romanian Parliament, 1994[3]) on the functioning of securities and stock exchanges (OECD, 2001[4]).

In April 1995, the Bucharest Stock Exchange was re-established as a public interest institution. In 2006, the Central Securities Depository (CSD) was established, with the mission to ensure the clearing and settlement of transactions. This institution keeps records of the issuers' shareholder registries. Today, the BVB remains the major shareholder of the CSD with a 69% stake, the rest being in the hands of other private entities.

As in other countries, the central securities depository in Romania is a key institution for the functioning of the capital market. It provides and maintains securities accounts at the top tier level in the RoClear system ('central maintenance service') and provides the initial recording of securities in the RoClear system ('notary service'). It facilitates the transfer of financial instruments and money between the seller and the buyer. Settlement is done using the delivery versus payment (DVP) principle and takes place two days after the transaction date. The CSD updates and keeps the shareholders' register of the financial instruments safe. The institution provides a large number of auxiliary services to participants, issuers and financial instrument holders. Currently, a Central Counterpart clearinghouse (CCP) is not yet in place in the Romanian market. However, the FSA is committed to supporting its establishment in accordance with best practices.

4.3. Segments of the regulated market in the exchange

The Bucharest Stock Exchange operates two markets: the Main Market, which is the regulated market, and the alternative trading system, the AeRO Market. The Main Market targets large mature companies, whereas the AeRO Market is designed for SMEs. To become listed on the Main Market companies are required to be legally structured as a joint stock company and to have a minimum market capitalisation of EUR 1 million. In addition, companies are required to have at least a 25% free-float and a minimum of three years of financial reporting history. There are specific requirements for the three tiers of the Main Market: Premium, Standard and International (Table 4.2).

Table 4.2. Main Market admission requirements

<table>
<tr><th rowspan="2">Premium Tier</th><th rowspan="2">Standard Tier</th><th colspan="2">International Tier</th></tr>
<tr><th>Member of the EU</th><th>Non-member of the EU</th></tr>
<tr><td colspan="2" rowspan="2">Registered with the FSA. Transferable, book entry, fully paid for, issued in a dematerialised form and registered into an account.</td><td>Meet the following 3 conditions:</td><td>Comply with the following 3 requirements:</td></tr>
<tr><td colspan="2">1) Registered with the FSA.
2) Transferable, book entry, fully paid for, issued in a dematerialised form and registered into an account.
3) Classified as belonging to the same class, and free-float of at least EUR 40 million.</td></tr>
<tr><td>Same share class with free-float of at least EUR 40 million.</td><td>Same share class with free-float of at least 25%.</td><td>Request to be admitted to trade.</td><td>Represent the object of a request for admission to trade.</td></tr>
<tr><td colspan="4">Be a company that has concluded a public offer for the sale of shares, for admission to trading, based on a prospectus approved by the relevant competent authority or which has approved by the relevant competent authority a prospectus prepared for admission to trading.</td></tr>
<tr><td colspan="4">Nominate 2 persons to liaise with the BVB.</td></tr>
<tr><td colspan="4">Comply with the terms and conditions of the Admission and Maintenance to Trade Arrangement.</td></tr>
<tr><td colspan="4">Comply with one of the following alternative conditions:</td></tr>
<tr><td colspan="2">For issuers whose financial instruments have not been traded within a trading venue authorised by ASF or by other competent authority during the last 3 years:
1) Last 3 annual financial statements and proof of submission to the tax authorities, last 3 reports of the financial auditors certifying the annual financial statement.
2) Last half yearly financial report.</td><td colspan="2" rowspan="2">1) The last 3 annual financial statements accompanied by the legal annexes from the issuer’s state of origin, as well as the last 3 annual reports;
2) The last semi-annual financial report together with the legal appendixes and the last semi-annual report.</td></tr>
<tr><td colspan="2">For issuers whose financial instruments have been traded within a trading spot authorised by ASF or by other competent authority during the last 3 years:
(a) Last 3 issuer’s annual reports and the last 3 AGM decisions regarding the approval of the annual financial reports.
(b) Issuer’s semi-annual report.</td></tr>
</table>

Note: Extract from the Rulebook, for more details see BVB Rulebook.
Source: Bucharest Stock Exchange Rulebook – Regulated Market Operator.

The AeRO Market is designed to serve the needs of SMEs that do not yet meet the size or the time of operation criteria necessary for listing on the Main Market. In order for a company to be listed on AeRO, it needs to have an anticipated market value of at least EUR 250 000 and a minimum of 10% free-float or at least 30 shareholders. Companies seeking to raise capital on the AeRO Market have to be established as a joint stock company (SA) prior to the listing. A summary of the main requirements are listed in Table 4.3 below.

Table 4.3. AeRO Market admission requirements

<table>
<tr><th>Premium Tier</th><th>Standard Tier</th><th>MTS International</th></tr>
<tr><td colspan="2">Registered with the ASF. Request the trade within MTS.</td><td rowspan="3">Confirmation of Central Depository regarding the fulfilment of clearing settlement and registration conditions, or performed by another central depository of another state.</td></tr>
<tr><td colspan="2">Be freely transferable, fully paid, issued in dematerialised form and evidenced by registration in the account.</td></tr>
<tr><td colspan="2">Free-float to be at least 10% of the issued shares or the number of shareholders to be at least 30.</td></tr>
<tr><td colspan="2">Foreseeable capitalisation of at least the EUR 250 000.</td><td rowspan="2">A request from a participant who assumes the obligations of market maker.</td></tr>
<tr><td colspan="2">The company must have a contract with an Authorised Advisor and to remain in it at least 12 months after the admission to trading.</td></tr>
<tr><td colspan="2">Have an agreement with the Central Depository or, to have the confirmation of the Central Depository regarding the fulfilment of conditions of clearing, settlement and registration necessary for the trading of the respective financial instruments.</td><td rowspan="2">Financial Instruments issued in a third country and traded on a market equivalent to a regulated market in that country can be introduced to trading on MTS International only if they are “share” type.</td></tr>
<tr><td colspan="2">Sign the Contract between BVB and Issuer provided in Appendix.</td></tr>
</table>

Note: Extract from the Rulebook, for more details see BVB Rulebook.
Source: Bucharest Stock Exchange Rulebook – Multilateral Trading System.

In 2008, the Bucharest Stock Exchange (BVB) adopted a Corporate Governance Code to be implemented by listed companies on a comply-or-explain basis. The code was most recently revised in 2015 and entered into force in January 2016 (BSE, 2015[5]). The BVB also provides a manual and a compendium of Corporate Governance Practices to help companies implement the code.

All companies listed on the Main Market are supposed to implement the Corporate Governance Code. They shall include a corporate governance statement in their annual report containing a self-assessment on how the "provisions to comply with" are observed and include the measures taken to comply with provisions that are not fully met. The code establishes some specific requirements for the companies listed on the Standard and Premium Tiers. For example, companies listed on the Standard Tier should have at least one independent board member in their board of directors or in the supervisory board. For companies listed on the Premium Tier, no less than two non-executive members of the board of directors or supervisory board should be independent. In addition, these companies are required to set up a nomination committee formed of non-executives, which will lead the process for board appointments and make recommendations to the board. Additionally, the majority of the members of the nomination committee of the Board of Premium tier companies should be independent. Moreover, regarding the risk management and internal control system the boards of companies listed on any of the three tiers of the Main Market should set up an audit committee with at least one independent non-executive member. In the case of Premium Tier companies, the audit committee should be composed of at least three members and the majority should be independent.

Table 4.4. Post-listing requirements

	Main Market	AeRO Market
Initial promises fulfilment	Investors need to be informed if the funds raised were spent in line with the company's prospectus.	
Mandatory reporting obligations	Investors need to be updated and informed regarding important events in the company's life. Major contracts, acquisitions, new product releases, litigations or other major developments should be communicated to the market, this also includes negative information.	
	Companies listed on the Main Market have to submit financial reports on a quarterly basis and it is recommended to do so in both Romanian and English.	AeRO listed companies have to submit annual reports, half year reports and current reports. Quarterly reports are not mandatory, but highly recommended.
Financial Reporting	Best practices suggest that quarterly financial reports should be accompanied by conference calls or meetings with analysts and investors.	
	The Main Market requires financial reporting in line with IFRS standards.	
Investor Relations	A contact point has to be established after a company lists its shares or bonds in order to carry out communication between the company and its investors, both current and potential.	
Corporate Governance	Companies listed on the Main Market have to adhere to the highest standards of governance, as defined in the Bucharest Stock Exchange's Code of Corporate Governance (in force since January 2016).	Companies listed on AeRO have no obligation to adhere to the BVB's Code of Corporate Governance. Instead, the BVB has developed a specific set of Principles of Corporate Governance for companies listed on AeRO.

Source: Bucharest Stock Exchange.

In addition to the fees paid to the investment banks for underwriting their securities and to the auditors, companies also pay listing fees to the exchange and to the ASF (a percentage of the offering) as well as a prospectus fee and a registration fee (both also to the ASF). There are also fees related to the central depository functions. The fees paid to the exchange are comprised of a fixed processing fee, a variable admission fee and a maintenance fee (Table 4.5).

Table 4.5. Fees in the Bucharest Stock Exchange as of December 2020

	Processing Fee	Admissions Fee	Maintenance Fee
Premium Tier	RON 1 200 *~ EUR 246*	RON 11 100 – 21 000 *~ EUR 2 275 – 4 303*	RON 25 000 – 50 000 *~ EUR 5 123 – 10 246*
Standard Tier		RON 3 600 – 7 500 *~ EUR 738 – 1 537*	RON 12 000 – 25 000 *~ EUR 2 459 – 5 123*
International Shares Tier		RON 3 600 – 7 500 *~ EUR 738 – 1 537*	RON 25 000 – 50 000 *~ EUR 5 123 – 10 246*

Source: Bucharest Stock Exchange.

4.4. Overview of the listed corporate sector

The Bucharest Stock Exchange has two segments, the Main Market – which is split into three tiers: Standard, Premium and International – and the Multilateral Trading System (MTS) AeRO which includes the AeRO Base, AeRO Standard and AeRO Premium. The Main Market has 76 listed companies (as of end 2020), of which 54 (71%) are listed on the Standard Tier (Table 4.6). The market capitalisation of the Main Market totals EUR 28.8 billion, with EUR 1.7 billion in the Standard Tier, EUR 15.6 billion in the Premium and EUR 11.5 billion in the International Tier. The AeRO Market has 242 listed companies of which 222 (92%) are in the Standard Tier. The market capitalisation of this segment totals EUR 1.2 billion.

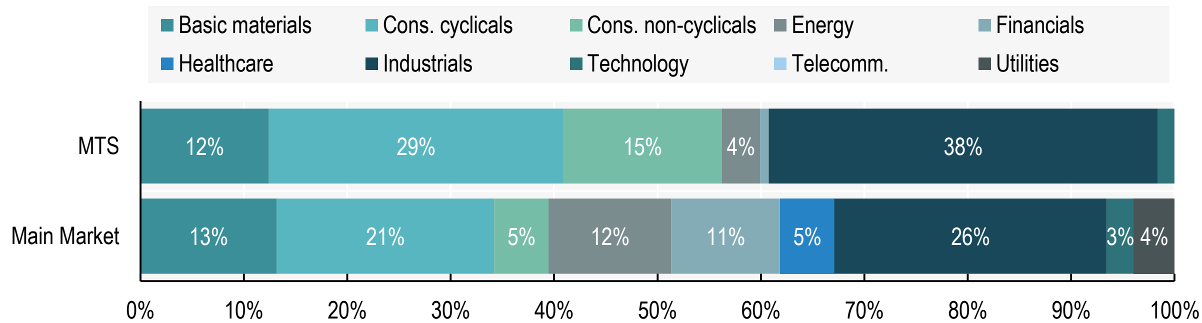
Table 4.6. Number of listed companies as of end 2020

Segment	Tier	No. of companies	Market capitalisation (EUR M)
Main Market	Standard	54	1 727
	Premium	19	15 551
	International	3	11 523
MTS	AeRO Base	3	3
	AeRO Standard	222	1 021
	AeRO Premium	17	159

Note: Excluding investment funds and REITs.
Source: Bucharest Stock Exchange.

With respect to the industry distribution of the listed companies of the BVB, Industrials accounts for 26% and 38% of the number of listed companies on the Main Market and the AeRO Market, respectively (Figure 4.1). Companies from the consumer cyclicals are also important issuers on the BVB, representing more than 20% of the listed companies on both segments. While 11% of the companies listed on the Main Market are financials (8 companies), their share on the AeRO Market is 1% (2 companies). Eight percent of the companies on the Main Market are technology and health care companies and in the AeRO Market their share totals only 2%.

Figure 4.1. Industry composition, by number of companies as of December 2020

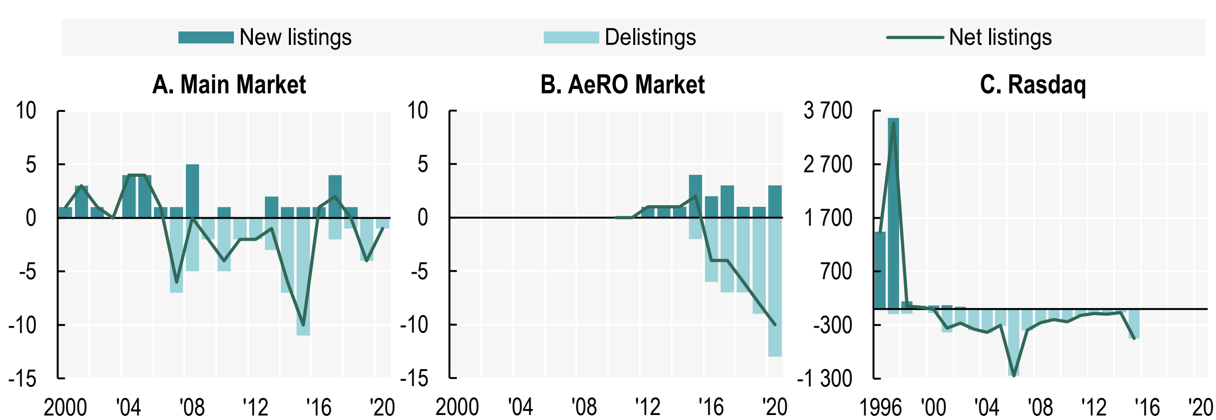


Note: Excluding investment funds and REITs.
Source: Bucharest Stock Exchange.

Since 2000, 31 new listings and 52 delistings have taken place on the Main Market of the Bucharest Stock Exchange (Figure 4.2, Panel A). Net listings were positive until 2007, a period when not a single company delisted from the market. However, since then, delistings have mostly surpassed new listings and since 2018 no new listings have taken place on the Main Market. Since its inception in 2010, the MTS Market – AeRO – had 17 new company listings (Figure 4.2, Panel B). Regarding delistings, which started in 2015, a total of 31 companies delisted until 2019. In 2020, net listings on the AeRO Market were at a historical low level with only three new company listings and 13 delistings.

In November 1996, the Rasdaq market was launched as an alternative equity exchange in which around 5 000 Romanian companies – following the Mass Privatisation Programme – were listed. Similar to experiences in other transition economies, many of the listed companies were not able to meet the listing requirements and were subsequently forced to delist from the market (Pop, Georgescu and Balint, 2014[6]). In December 2005, the Bucharest Stock Exchange acquired Rasdaq and converted it into an over the counter electronic stock market. During the 1996-2000 period Rasdaq's reputation was plagued by share theft, price manipulation and severe opacity. In addition, since 2010, the absence of a legal status for Rasdaq as a trading platform added to existing reputational concerns, leading to a decline in the trading volume from 2012. Thus, after the BVB's acquisition, only eight new listings took place, coupled with more than 3 000 delistings until its dissolution in 2015, when almost 300 companies were transferred to the AeRO Market (Figure 4.2, Panel C).[1]

Figure 4.2. Newly listed and delisted companies



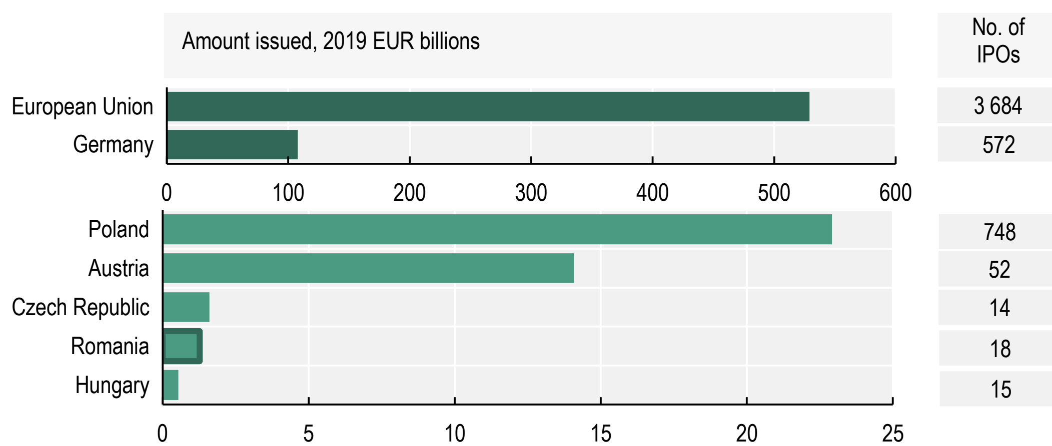
Note: Excluding investment funds and REITs.
Source: Bucharest Stock Exchange.

4.5. Trends in initial public offerings

A company wishing to raise equity can do so by listing its shares on one or more stock exchanges by conducting an initial public offering (IPO). This section describes IPO activity in Romania and selected European peer countries during the last 20 years. Since 2000, 18 Romanian companies have conducted an IPO and together raised EUR 1.3 billion in proceeds. While from 2000 to 2009, 11 companies went public, the proceeds accounted for only 14% of the amount raised over the entire 2000-19 period. During the 2010-17 period, seven companies raised 86% of the total proceeds (EUR 1.1 billion). No companies went public in 2018 and 2019.

Although IPO activity was more dynamic in Romania in the last 10 years compared to the early 2000s, the market has not yet fully developed and the number of companies making use of public equity markets remains limited and still lags behind regional peers such as the Czech Republic, Austria, Poland and Germany. It only surpassed the IPO activity in Hungary, where a total of 15 IPOs have raised a modest EUR 544 million since 2000 (Figure 4.3). Romanian IPOs accounted for only 0.24% of the total funds raised by EU companies through IPOs over the entire period.

Figure 4.3. Initial public offerings, 2000-19



Source: OECD Capital Market Series dataset; see Annex for details.

The largest IPO by a Romanian company took place in 2014 when the electricity distribution and supply company Electrica SA raised a record amount of EUR 460 million, with a primary listing on the Bucharest Stock Exchange and a secondary listing on the London Stock Exchange (Table 4.7). The natural gas production company SNGN Romgaz SA raised almost EUR 400 million in its IPO in 2013 with its primary listing on the BVB and secondary listing on the London Stock Exchange. Five out of the 18 Romanian IPOs were conducted by a state owned company, representing almost 90% of the total proceeds raised since 2000. The three most recent Romanian IPOs took place in 2017, when Sphera Franchise Group SA raised EUR 64 million, Transilvania Broker de Asigurare SA EUR 2 million and SC AAGES SA EUR 1.2 million.

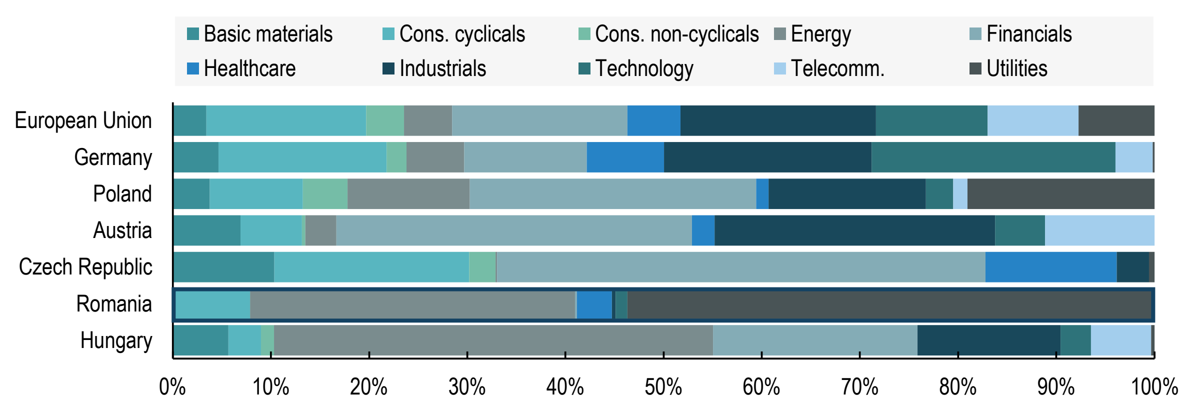
Utilities company IPOs in Romania accounted for more than half of the total proceeds raised over the 2000-19 period, followed by energy companies which raised 33% of the total proceeds (Figure 4.4). This trend differs from European peers where utilities IPOs are much less common, representing only 19% of the proceeds in Poland and being almost non-existent in Austria, Germany, Hungary and the Czech Republic. While consumer cyclicals IPOs make up 20% and 17% of the funds raised in the Czech Republic and Germany, respectively, in Romania their share was only 8%. Importantly, the technology and health care industries together account for only 5% of the Romanian IPOs, whereas in the European Union they make up 17% of total proceeds.

Table 4.7. Romanian IPOs

Issuer name	Economic sector	SOE	Year	Proceeds (EUR K)
Electrica SA	Utilities	Yes	2014	456 234
SNGN Romgaz SA	Energy	Yes	2013	398 928
Societatae Nationala Nuclearelectrica SA	Utilities	Yes	2013	75 717
Transgaz SA	Utilities	Yes	2007	69 112
Sphera Franchise Group SA	Cons. cyclicals	No	2017	63 999
MedLife SA	Healthcare	No	2016	43 388
Transelectrica SA	Utilities	Yes	2006	34 380
SC Teraplast SA	Cons. cyclicals	No	2008	14 938
Flamingo International SA	Technology	No	2005	12 288
Alumil Rom Industry SA	Cons. cyclicals	No	2006	8 892
Contor Group	Industrials	No	2008	3 258
Casa de Bucovina Club de Munte SA	Cons. cyclicals	No	2007	2 747
Transilvania Broker de Asigurare SA	Financials	No	2017	1 961
M.J. Maillis Romania SA	Basic materials	No	2001	1 579
SC AAGES SA	Industrials	No	2017	1 210
Vrancart SA	Basic materials	No	2005	712
BRD Groupe Societe Generale SA	Financials	No	2002	31
SSIF BRK Financial Group SA	Cons. non-cyclicals	No	2005	3

Note: A company is considered as an SOE if the Public sector (see Section 4.8) holds over 20% of the equity capital.
Source: OECD Capital Market Series dataset; see Annex for details.

Figure 4.4. Industry distribution of IPOs by total proceeds, 2000-19



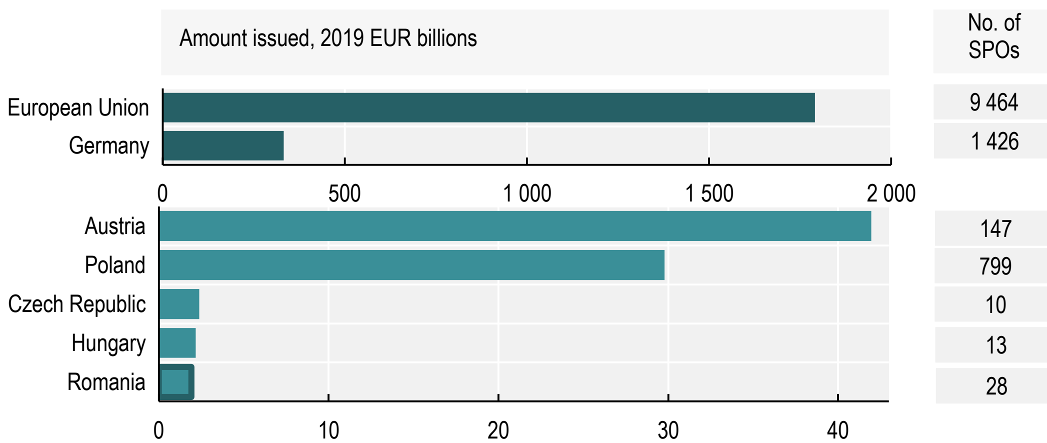
Source: OECD Capital Market Series dataset; see Annex for details.

4.6. Trends in secondary public offerings

Companies that are already listed can raise additional equity on the primary public equity markets through secondary public offerings (SPOs or follow-on offerings). A company can make use of this recapitalisation source several times depending on its funding needs. The proceeds from the SPOs may be used for a variety of purposes and can also help fundamentally sound companies bridge a temporary downturn in economic activity. SPOs played an important role in providing the corporate sector with equity capital in the wake of the 2008 financial crisis and through the 2020 COVID-19 crisis.

In the European Union, companies made extensive use of SPOs, raising almost EUR 2 trillion over the last 20 years (Figure 4.5). German firms alone raised almost 20% of the EU's total proceeds. Austrian and Polish companies also tapped the SPO market regularly over the 2000-19 period, with proceeds of EUR 42 billion and EUR 30 billion respectively. However, companies in the Czech Republic, Hungary and Romania together accounted for only 0.36% of the total EU proceeds, amounting to EUR 6.4 billion.

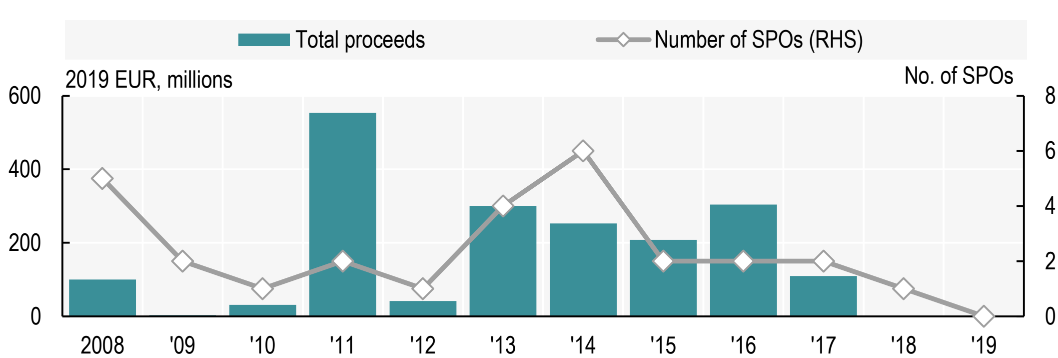
Figure 4.5. Secondary public offerings, 2000-19



Source: OECD Capital Market Series dataset; see Annex for details.

Since 2000, Romanian companies have conducted 28 SPOs raising a total of EUR 1.9 billion, the lowest amount among European peer countries (Figure 4.6). Indeed, until 2008, SPO activity in Romania was non-existent, with the exception of one consumer cyclicals company back in 1996. Since 2008, an average of two SPOs have taken place annually. In terms of proceeds raised, 2011 saw a record amount of EUR 554 million to a large extent driven by the state controlled energy company OMV Petrom SA's first SPO. In 2016, the SPO activity in Romania was driven by the second SPO of OMV Petrom SA and the offering by another state controlled energy company SNGN Romgaz SA which together raised a total amount of EUR 305 million. Importantly, in 2018 and 2019 only one company conducted an SPO.

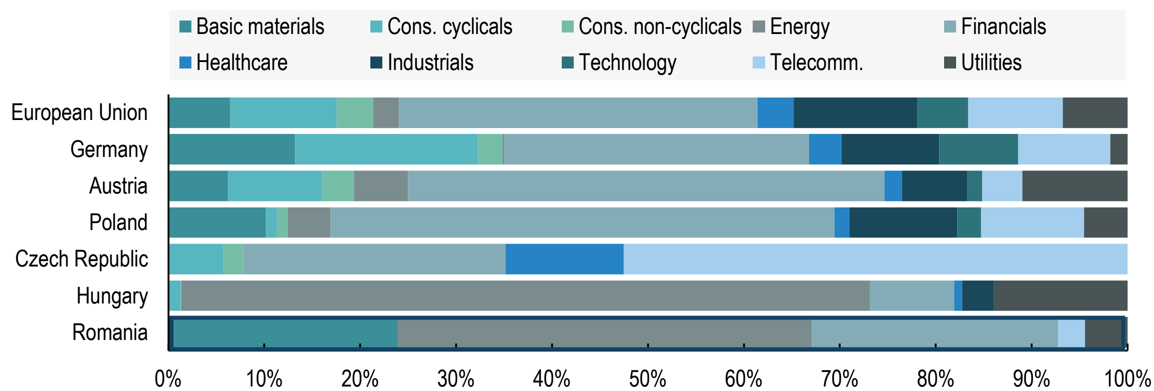
Figure 4.6. Romanian SPOs



Source: OECD Capital Market Series dataset; see Annex for details.

Financial companies are usually frequent users of secondary offerings. In the European Union, financials account for 37% of the total proceeds raised through SPOs since 2000 (Figure 4.7). In Poland and Austria, financial companies accounted for more than half of the total proceeds raised. In Germany, financials represented 32%, in the Czech Republic 27% and in Romania for 26% of the proceeds raised. In Hungary, Financials are less prominent, representing only 9% of the total proceeds. Apart from financials, energy and basic materials companies have been important users of SPOs in Romania, accounting for 43% and 24% of the amount raised, respectively. While in the European Union, technology and health care SPOs together represent 9% of the funds raised, in Romania companies from those two industries have never conducted an SPO.

Figure 4.7. Industry distribution of SPOs by total proceeds, 2000-19



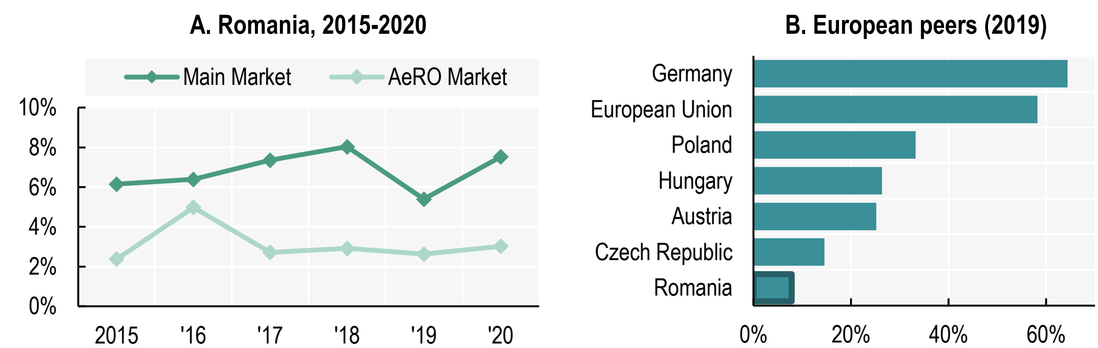
Source: OECD Capital Market Series dataset; see Annex for details.

4.7. Trends in secondary stock market activity

The level of liquidity in the secondary stock market is an important factor influencing investors' demand for stocks, as greater liquidity reduces the risk premium of holding stocks and increases the efficiency of the price discovery mechanism. A liquid market may also help attract more issuers, who would expect the market to price their securities more accurately. Importantly, empirical evidence shows that low liquidity levels can increase the cost of equity for companies wanting to raise capital as investors require a higher expected return to compensate for the extra risk of reduced liquidity (IMF, 2016[7]).

In recent years, liquidity measured as the turnover ratio has been low in Romania, averaging 6.8% since 2015 on the Main Market of the BVB. The situation is identical on the alternative AeRO Market, where the average turnover ratio has been 3.1% (Figure 4.8, Panel A). Other markets in the CEE region such as the Czech Republic, Austria, Hungary and Poland also had liquidity levels well below the EU average of 58%, but Romania ranked by far the lowest as shown in Panel B of Figure 4.8.

Figure 4.8. Stock market turnover ratio

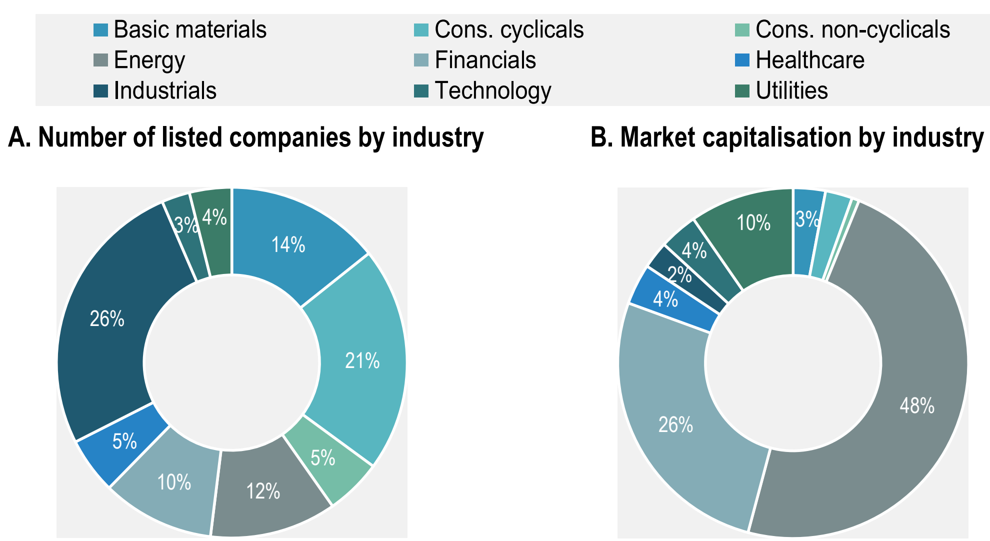


Note: Turnover ratio in Panel A corresponds to the total value traded over the market capitalisation. In Panel B, the turnover ratio is the value of domestic shares traded divided by their market capitalisation. The value is annualised by multiplying the monthly average by 12.
Source: Bucharest Stock Exchange, World Federation of Exchanges.

4.8. Investors and ownership structure in the Romanian stock market

By the end of 2019, there were 77 companies listed on the regulated market of the Bucharest Stock Exchange. Industrials companies accounted for 26% of the total, followed by consumer cyclicals companies accounting for 21%. However, by market capitalisation, energy companies account for almost half of the total listed equity with financial companies representing another 26%.

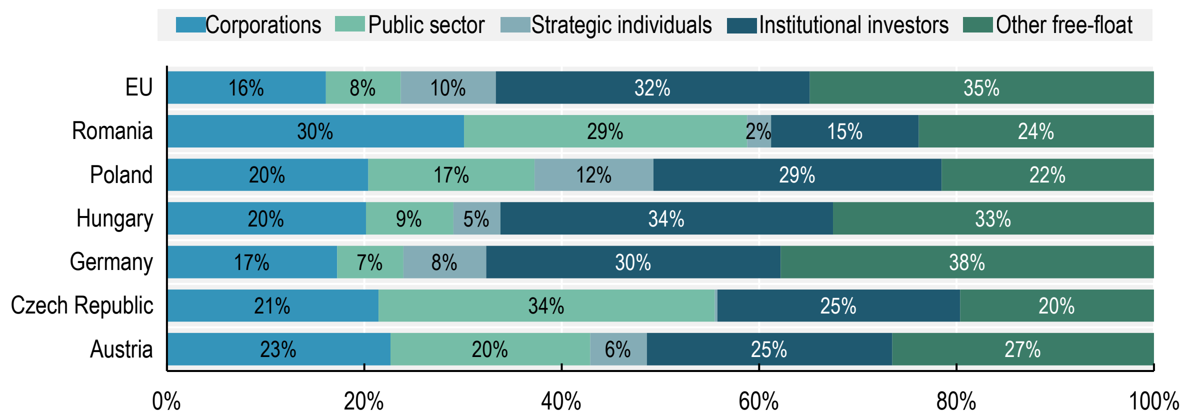
Figure 4.9. Industry composition of listed companies in Romania



Source: OECD Capital Market Series dataset, FactSet, Thomson Reuters, Bloomberg; see Annex for details.

Ownership information was available for 59 of the listed companies on the regulated market of the exchange. To identify the ownership structure, investors were classified into the following categories of investors: corporations, public sector, strategic individuals, institutional investors and other free-float (De La Cruz, Medina and Tang, 2019[8]). At the market level, private corporations and holding companies is the largest investor category holding 30% of the listed equity (Figure 4.10). Their relative importance as owners in the equity market is much higher compared with other European peer countries and the EU. The public sector ranks second owning 29% of the total market capitalisation. Institutional investors are not large investors in the Romanian market compared with their importance in other European markets such as Germany, Hungary and Poland where they own around 30% of the listed equity.

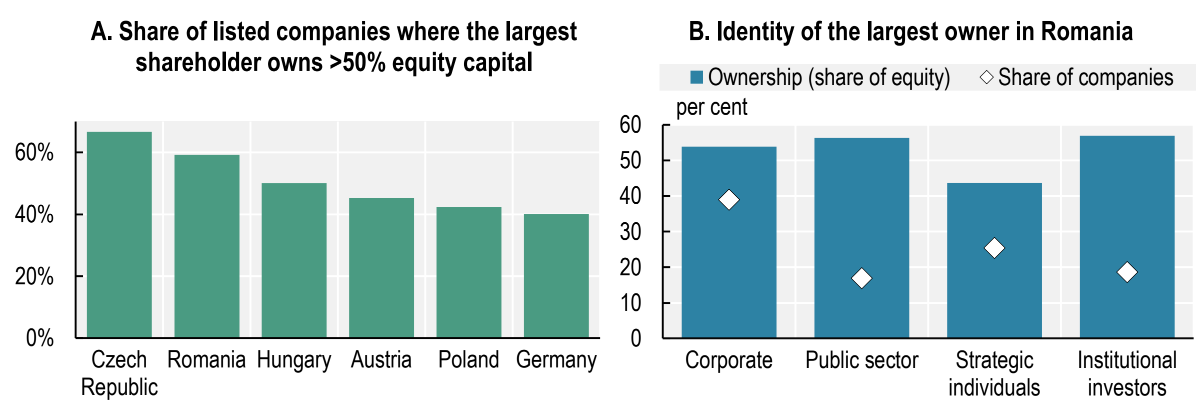
Figure 4.10. Ownership landscape at the country level as of end 2019



Source: OECD Capital Market Series dataset, FactSet, Thomson Reuters, Bloomberg; see Annex for details.

The ownership structure in the Romanian stock market is fairly concentrated (Figure 4.11, Panel A). In six of every ten listed companies the largest single shareholder holds over 50% of the equity capital. This level of control and concentration is much higher than in other European countries. More importantly, corporations and holding companies are not only the largest owners at the aggregate level, they are also the most common largest shareholders at the company level as they own on average 54% of the equity in almost 40% of the listed companies (Figure 4.11, Panel B). The public sector is also an important owner, but in fewer companies. It holds an average of 56% of the listed equity in 17% of the listed companies. The institutional investors that are the largest owners in 19% of the companies are predominantly mutual funds and investment advisors.

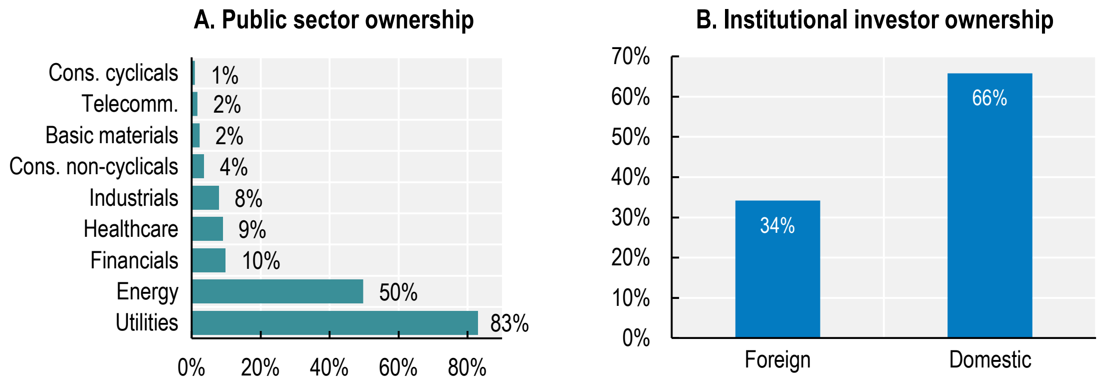
Figure 4.11. Ownership concentration as of end 2019



Source: OECD Capital Market Series dataset, FactSet, Thomson Reuters, Bloomberg; see Annex for details.

The public sector plays an important role in the Romanian economy and Romania has the largest number of SOEs in Europe (Statecapture, 2018[9]). At the end of 2016 Romanian SOEs accounted for a high share in total employment and contribution to the total value added compared to SOEs in many countries in the region (IMF, 2019[10]). The government is also a majority shareholder in ten listed companies. At the industry level, public sector holdings are concentrated in Utilities and Energy companies (Figure 4.12, Panel A). At the end of 2020, almost half of the market capitalisation of the energy industry, the largest industry in the stock market, was held by the public sector. With respect to ownership by institutional investors, two-thirds were in the hands of domestic institutional investors and one-third was held by foreign institutions (Figure 4.12, Panel B).

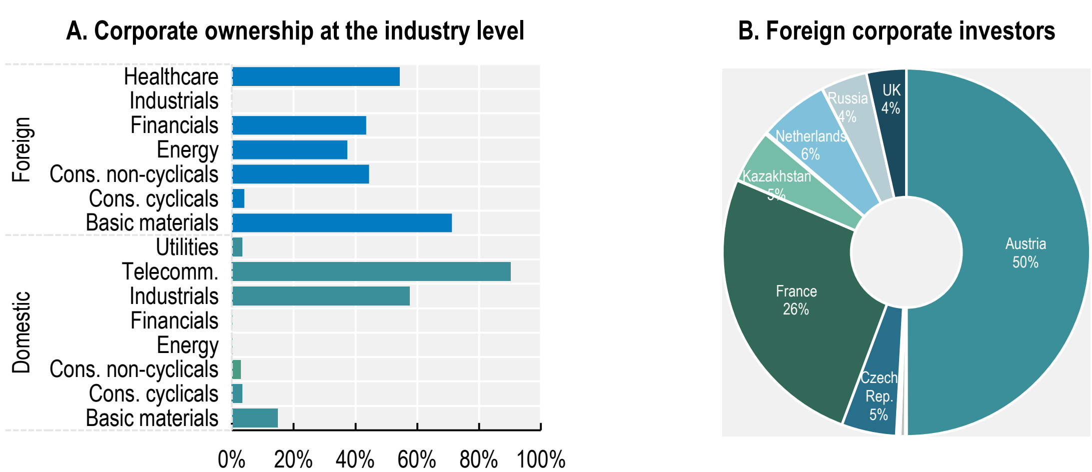
Figure 4.12. Public sector and institutional investor ownership in Romania as of end 2019



Source: OECD Capital Market Series dataset, FactSet, Thomson Reuters, Bloomberg; see Annex for details.

As mentioned above, private corporations and holding companies is the largest category of investors in the Romanian stock market holding 30% of the listed equity. Domestic corporate investors concentrate their holdings in telecommunications and industrials companies, while foreign corporate investors hold significant stakes in the healthcare, financials, energy, consumer non-cyclicals and basic materials industries (Figure 4.13, Panel A). Foreign corporate investors account for 87% of corporate investors' total holdings in Romania. Half of the foreign corporations and holding companies that invest in the Romanian equity market are from Austria, 26% are from France, and 6% are from the Netherlands (Figure 4.13, Panel B).

Figure 4.13. Corporate ownership in Romania as of end 2019



Source: OECD Capital Market Series dataset, FactSet, Thomson Reuters, Bloomberg; see Annex for details.

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Notes

[1] These 300 companies transferred to the AeRO Market were not considered as new listings.

5 The Romanian corporate bond market

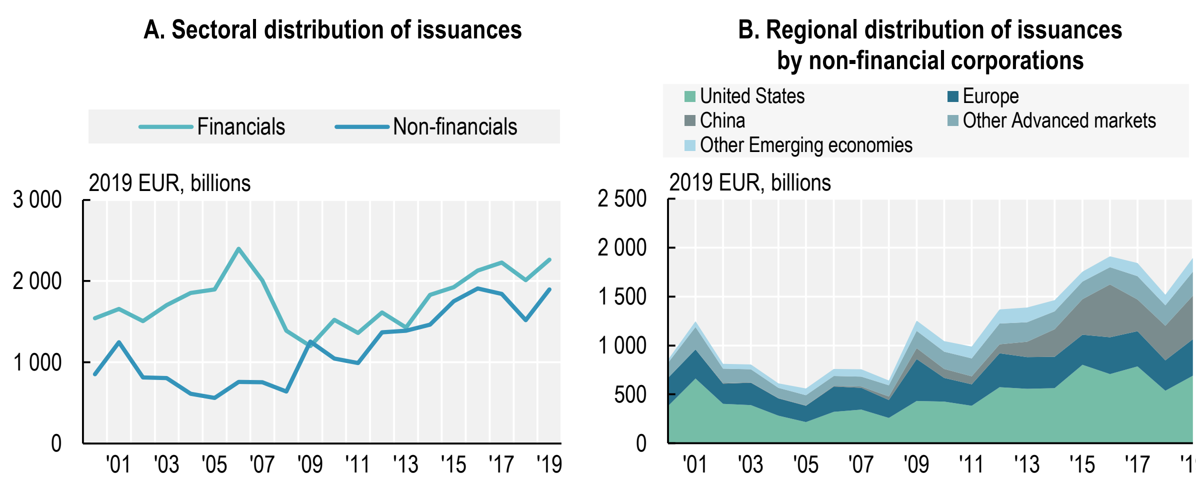
This chapter provides an overview of the trends in corporate bond markets both in Romania and at the global level. It also presents selected features, such as the maturity structure, currency composition and listing market, of corporate bonds issued by companies from Romania and peer countries.

Corporate bond markets have become an increasingly important source of financing for non-financial corporations over the past decade. They played a crucial role when banks tightened credit conditions after the 2008 financial crisis and during the market contraction in 2020. During these two periods, many companies around the world were able to tap the corporate bond market to roll over their existing debt, create a financial buffer to overcome an economic downturn or immediately use the proceeds to meet their obligations to employees, suppliers and customers. At the same time, since corporate bonds typically allow the borrower to issue debt at longer maturities compared to bank loans, they are also well-suited to finance long-term investments.

5.1. Trends in corporate bond issuance

The last two decades have seen a remarkable increase in global debt levels, and corporate bonds are no exception to this trend. Particularly, non-financial companies have seen a stable increase in bond issuances. With the significant contraction of bank lending to non-financial companies during and after the global financial crisis, non-financial companies resorted to corporate bonds as an alternative source of financing. As shown in Panel A of Figure 5.1, non-financial corporations have raised an average of EUR 1.4 trillion annually between 2008 and 2019, which is almost twice the annual amount of EUR 801 billion that they raised between 2000 and 2007. A look into the regional distribution indicates that each region has seen a different evolution of the corporate bond market (Figure 5.1, Panel B). Europe has experienced a relatively slow nominal increase compared to other regions, and thus its share of proceeds decreased from around 30% of the global amount issued before the 2008 crisis to 20% in 2019.

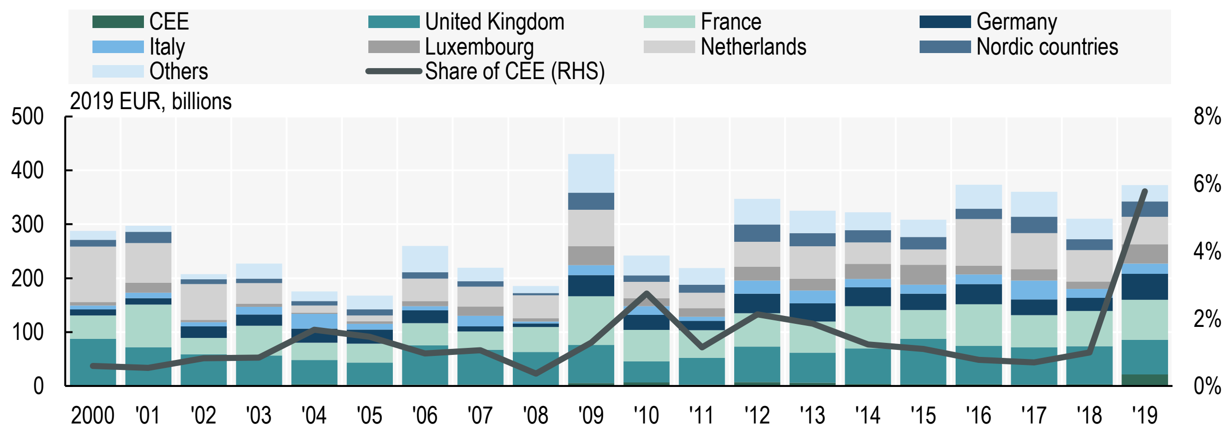
Figure 5.1. Global corporate bond issuances



Source: OECD Capital Market Series dataset, Thomson Reuters Eikon; see Annex for details.

Within Europe, companies from the United Kingdom, France and the Netherlands have been the largest users of corporate bonds, together accounting for over half of total European proceeds. Corporate bonds issued by CEE companies represent only about 1-2% of the European proceeds, which is much lower than the CEE region share in European GDP (Figure 5.2). 2019 was an exception, as corporate bond issuances by non-financial companies from CEE countries reached EUR 22 billion amounting to 6% of the European total proceeds. However, this was mainly driven by one large bond issue carried out by a Polish construction company.

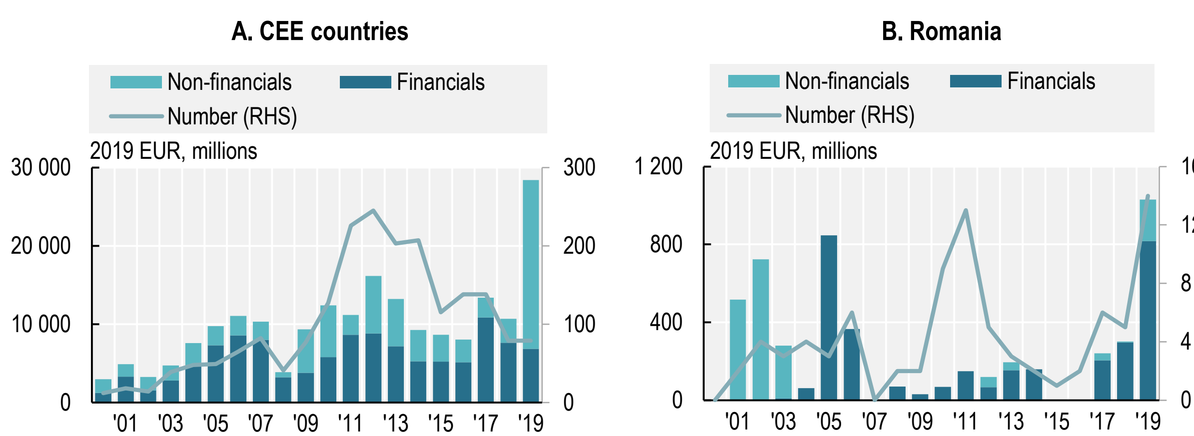
Figure 5.2. Corporate bond issuances by non-financial European companies



Note: Nordic countries include Denmark, Finland, Norway and Sweden.
Source: OECD Capital Market Series dataset, Thomson Reuters Eikon; see Annex for details.

A closer look at bond issuances by CEE companies shows an increasing use of corporate bonds after the financial crisis when banks strengthened borrowing requirements. As shown in Panel A of Figure 5.3, in 2012, corporate bond issuances reached a total of more than EUR 16 billion, issued by 332 companies, the second highest amount over the period analysed. Meanwhile, corporate bond activity has remained relatively low in Romania, where non-financial companies raised only EUR 349 million over the last decade (Figure 5.3, Panel B). The number of companies issuing corporate bonds decreased significantly after 2011, and only one company issued bonds in 2015. However, since the launch of the AeRO Market in 2015, which targets SME financing, the number of issues have seen a significant increase (Figure 5.3, Panel B).

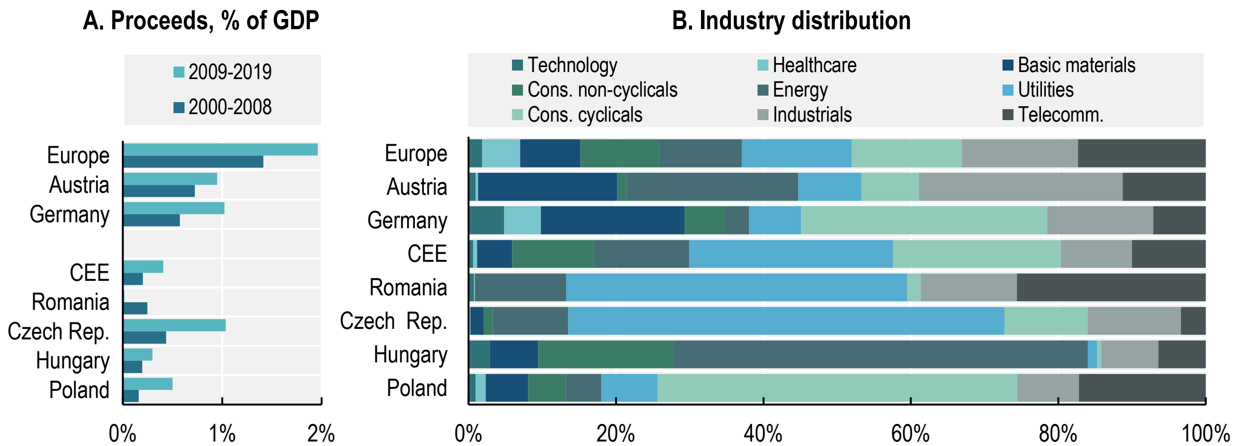
Figure 5.3. Corporate bond issuances by companies from CEE countries and Romania



Source: OECD Capital Market Series dataset, Thomson Reuters Eikon; see Annex for details.

Corporate bond activity in CEE countries still lags behind the rest of Europe. The average proceeds of non-financial companies during the 2009-19 period amounted to 0.4% of GDP, which is well below the European level of 2% (Figure 5.4, Panel A). In Romania, the value of corporate bond issuances between 2009 and 2019 represented only around 0.01% of GDP, compared with 0.3% in Hungary and 0.5% in Poland.

Figure 5.4. Corporate bonds issued by non-financial companies in Romania and selected European countries



Source: OECD Capital Market Series dataset, Thomson Reuters Eikon; see Annex for details.

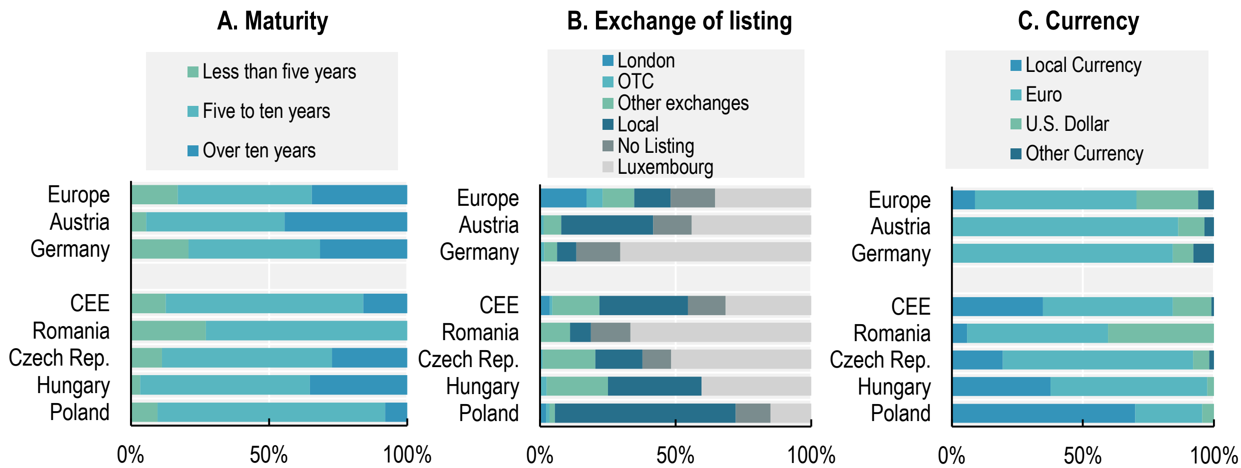
The industry composition of European non-financial companies issuing corporate bonds is more evenly distributed across industries compared to the bonds issued by companies from the CEE region, where around 63% of the proceeds come from three industries: utilities, consumer cyclicals and energy (Figure 5.4, Panel B). In the case of Romania, almost 72% of proceeds are from companies in the utilities and telecommunications services industries. Moreover, with the recent launch of the AeRO Market targeting SMEs, there has been a few technology companies issuing corporate bonds, although the amounts are relatively small.

One of the main advantages of corporate bonds is that they can offer the issuer longer maturities. Corporate bonds have about four to five years longer maturity than syndicated loans in developed countries and one to two years longer in developing countries (Cortina Lorente, Didier and Schmukler, 2016[1]). In recent years, as a result of the general low level of interest rates, companies have been lengthening the maturity of their issuances (Çelik, Demirtaş and Isaksson, 2020[2]). In Europe, most of the volume issued has a maturity of between 5 to 10 years. Bonds issued by non-financial companies from the CEE region represent an even higher share of the volume issued with maturities in that range (Figure 5.5, Panel A). However, the share of the volume issued with maturities over ten years is higher for European issuers than for issuers from the CEE region. In particular, over 35% of the amount raised by European companies via corporate bonds has a maturity longer than ten years, compared to 16% for issuers from the CEE region. Indeed, 27% of bond issuances by Romanian companies have a maturity of less than five years, compared to 3% and 10% for Hungarian and Polish companies. Notably, during the entire period, there was no single Romanian corporate bond issuance with a maturity over ten years.

Only 8% of the total number of corporate bonds issued by Romanian non-financial companies are listed on the Bucharest Stock Exchange (Figure 5.5, Panel B). This is much less than in Hungary and Poland where 34% and 67% of non-financial corporate bonds are listed on the local stock exchanges.

As most Romanian corporate bonds issued are listed on non-domestic exchanges they are also issued in foreign currencies. Indeed, as shown in Panel C of Figure 5.5, Romania is the country with the lowest ratio (6%) of corporate bonds denominated in the local currency (Romanian Leu). The rest is denominated either in EUR (54%) or in USD (40%). In contrast, in Poland and Hungary 70% and 38% of the corporate bonds are issued in local currency, respectively. It is also important to note that no issuances denominated in Romanian Leu have been listed on foreign exchanges, whereas for all other CEE peer countries, between 2-3% of corporate bonds denominated in local currency are issued on foreign exchanges.

Figure 5.5. Characteristics of corporate bonds by total proceeds, 2000-19



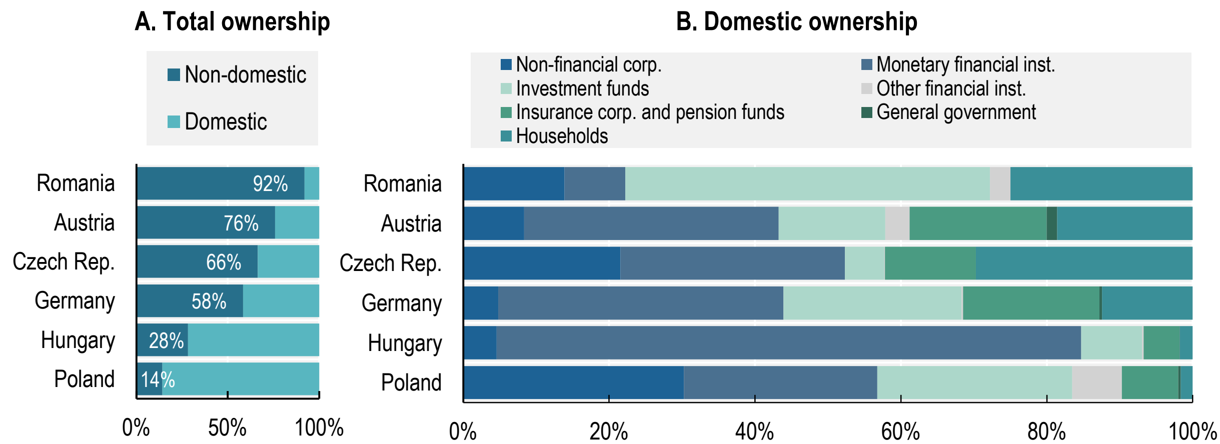
Source: OECD Capital Market Series dataset, Thomson Reuters Eikon; see Annex for details.

5.2. Investors in non-financial corporate bonds

Romania has a very low presence of domestic investors in the corporate bond market. Only 8% of the outstanding stock of non-financial corporate bonds are held by domestic investors, compared to 86% in Poland and 72% in Hungary (Figure 5.6, Panel A). Generally, there is a significant heterogeneity in the domestic ownership of corporate bonds across countries. Typically, the financial sector (including monetary financial institutions, investment funds, insurance corporations and pension funds, and other financial institutions) plays a significant role as owner of corporate bonds. Particularly, two categories of financial investors – monetary financial institutions and insurance corporations and pension funds – hold a large share of corporate bonds issued by non-financial corporations in most countries. They make up 85% of domestic bond ownership in Hungary, 58% in Germany and 54% in Austria (Figure 5.6, Panel B). This differs sharply for Romania, where their holdings are much smaller. Domestic monetary financial institutions hold only 8% of the outstanding stock of domestic non-financial corporate bonds, whereas domestic insurance corporations and pension funds do not to hold any of the outstanding stock. Instead, investment funds hold 50% of the non-financial corporate bond stock in Romania.

Non-financial corporations and households hold only a modest share of the outstanding stock of corporate bonds in most countries, except for the Czech Republic where households and non-financial corporations together hold 51% of the corporate bond stock. In Romania, households and non-financial corporations also own a relatively large share of corporate bonds, representing 25% and 14% of total domestic bonds, respectively.

Figure 5.6. Ownership of outstanding non-financial corporate bonds in Q3-2020



Source: ECB Statistical Data Warehouse.

5.3. Market segments for corporate bond listing in Romania

The Bucharest Stock Exchange offers two segments for listing corporate bonds: the regulated Main Market and the alternative trading system, the AeRO Market. Companies can list bonds for trading on both segments, but the Main Market targets larger companies and the AeRO Market targets small and medium sized enterprises. The AeRO Market is only regulated by the BVB's rules and obligations, and was established in order to provide issuers a market with less stringent reporting obligations while maintaining a good level of transparency for investors. As there is no minimum issuance value and no prospectus requirement, the AeRO Market offers smaller companies an easier way of accessing the corporate bond market.

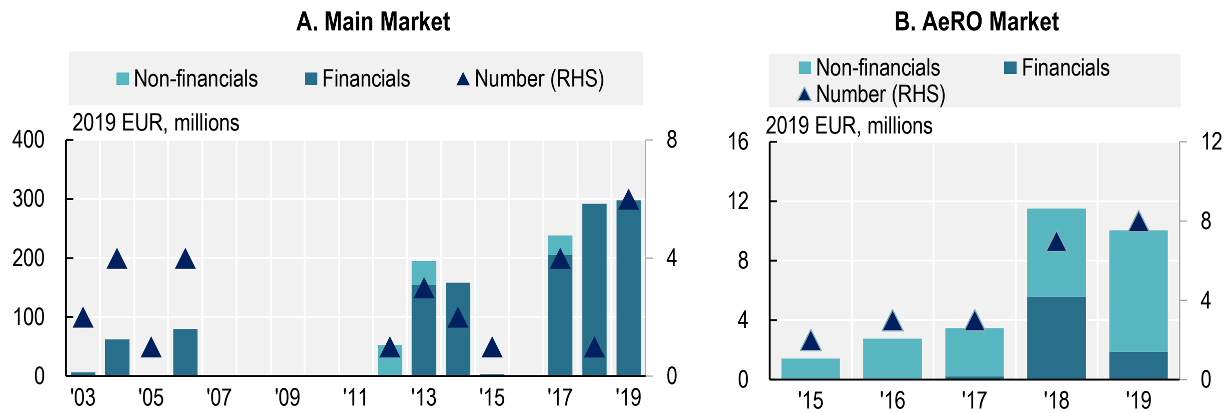
Table 5.1. Listing requirements and targeted investors

	Main Market	AeRO Market
Listing requirement	The minimum value of the issuance must be the RON equivalent of EUR 200 000. If the value is lower, ASF may issue a special approval for listing. Prospectus is required.	No minimum value for issuances. No prospectus is required.
Targeted investors	Local and foreign institutional investors, local and foreign individual investors.	Specialised and smaller investment funds targeting SMEs, individual investors.

Source: Bucharest Stock Exchange.

Since the creation of the AeRO Market in 2015, there have been 23 issuances raising a total of EUR 29.2 million (Figure 5.7, Panel B). Non-financial companies make up 74% of issuances on the AeRO Market. In fact, almost all bond issuances by non-financial companies in Romania are listed on the AeRO Market. In contrast to the AeRO Market, most issuances on the Main Market are done by financial companies and only 9.2% of issuances by non-financial companies. Over the last five years, a total of 12 issuances raised EUR 831 million on the Main Market (Figure 5.7, Panel A). Of these, only one in 2017 was by a non-financial company. The proceeds raised on the Main Market are typically much larger than those on the AeRO Market. While the average proceeds per deal raised on the Main Market is EUR 47.8 million, it is only EUR 1.27 million on the AeRO Market.

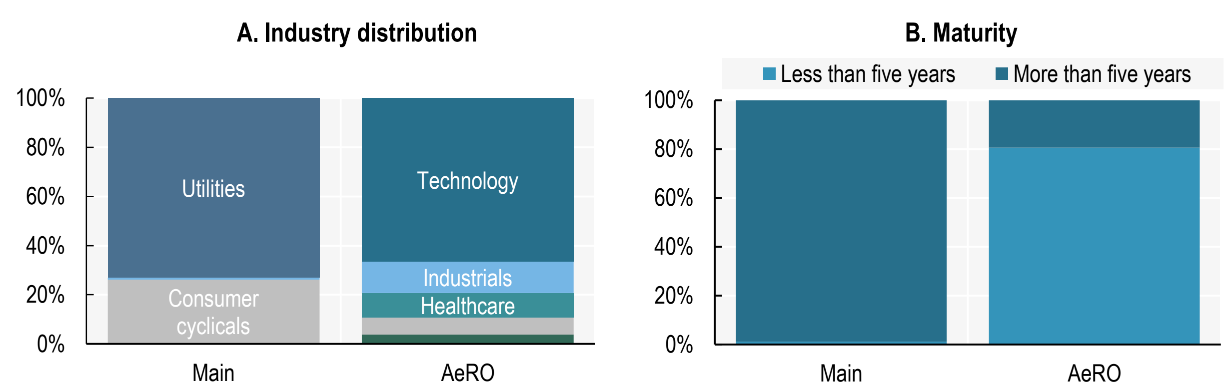
Figure 5.7. Corporate bond issuance in the Romanian market



Note: Issuance below EUR 1 million have also been included in the above figures.
Source: OECD Capital Market Series dataset, Thomson Reuters Eikon; see Annex for details.

In 2016, Bittnet Systems became the first technology company in Romania to ever issue a corporate bond. Since then, six technology companies have made ten issuances, raising a total of EUR 14 million. At the end of 2019, more than half of the corporate bonds listed on the AeRO Market were issued by Technology companies (Figure 5.8, Panel A). Apart from technology companies, companies from industrials, health care and consumer cyclicals have also been using the AeRO Market to raise funds. Meanwhile, the Main Market has hosted a handful of companies from utilities and consumer cyclicals, apart from financial companies. Regarding the length of maturity, nearly all issuances on the Main Market have a maturity over five years, whereas on the AeRO Market almost 81% of issuances have a maturity of less than five years (Figure 5.8, Panel B).

Figure 5.8. Characteristics of non-financial corporate bonds, 2000-19



Note: The figure shows the distribution by proceeds. Issuance below EUR 1 million have also been included in the above figures.
Source: OECD Capital Market Series dataset, Thomson Reuters Eikon; see Annex for details.

References

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Cortina Lorente, J., T. Didier and S. Schmukler (2016), "How Long Is the Maturity of Corporate Borrowing?", https://openknowledge.worldbank.org/handle/10986/25060. [1]

6 The Romanian private equity market

This chapter provides an overview of private equity trends in Romania and offers a comparison with selected peer European countries. It presents a detailed analysis of the three main stages of private equity activity: fundraising, investment and divestment. The analysis addresses, among other things, issues relevant to the geographical and institutional source of fundraising, the industry distribution of investments and divestment forms.

Private capital markets have grown significantly in recent years. By the end of June 2019, total assets in private capital markets reached USD 6.5 trillion globally. In private capital markets, private equity (PE) is by far the largest asset class. Its global net asset value has increased eight fold since 2000 and assets under management (AUM) of PE funds reached USD 3.9 trillion by the end of June 2019 (McKinsey, 2020[1]). Private equity and venture capital serve as an alternative source of financing for non-financial corporations especially for start-up firms, private medium-sized firms, firms in financial distress and public firms seeking buyout financing.

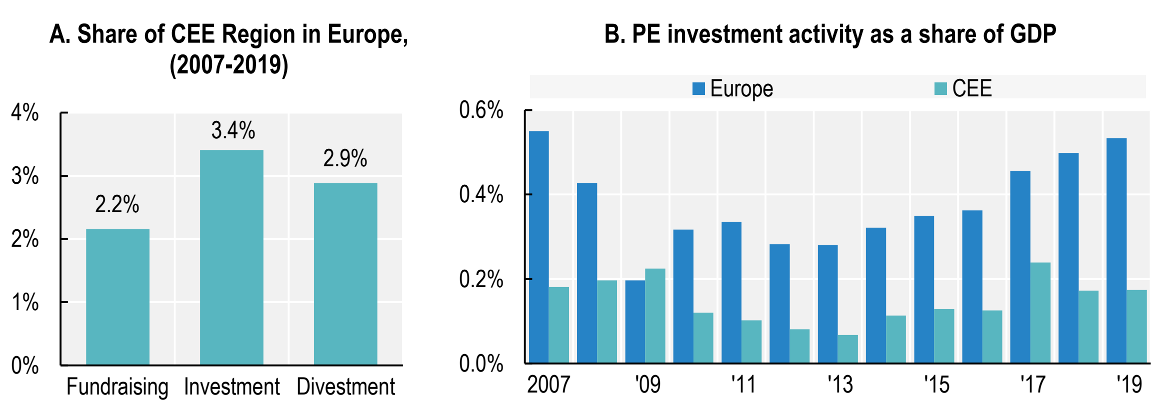
6.1. Overview of private equity activity in Romania

There are three main stages in the private equity investment process. The initial stage is fundraising where general partners of the private equity firms raise funds from investors, including institutional investors and high-net-worth individuals. In the second stage of the process, funds are invested in companies at different stages of their lifecycle. Private equity funds generally have a defined investment horizon within which they are expected to exit their investments. Divestment, the third stage of the process, occurs when private equity firms sell their stake in investee companies. There are a number of options for PE funds to divest their holdings, including initial public offerings and sales to other private equity firms.

During the 2007-19 period, EUR 20 billion was raised by private equity firms in the Central and Eastern Europe (CEE) region. This amount represented only 2.2% of the total private equity capital raised in Europe (Figure 6.1, Panel A). In the CEE region,[1] PE investment and divestment activity is slightly higher than the fundraising activity as a share in European investment and divestment volumes. CEE private equity firms invested EUR 28 billion and divested EUR 13 billion between 2007 and 2019. This represented 3.4% and 2.9% of the total European investment and divestment activity, respectively (Figure 6.1, Panel A).

Another comparison with Europe reveals that PE activity in the CEE region is also far below European levels. PE activity measured as the volume of PE investment to GDP represented 0.53% of European GDP in 2019, and only 0.17% in CEE. In every year between 2007 and 2019, except 2009, PE investment activity in CEE has been less than a half of PE investment activity in Europe (Figure 6.1, Panel B). A similar trend can be seen for the CEE PE fundraising and divestment activity. The volume of funds raised in Europe in 2019 was 0.62% of European GDP, while the corresponding share was very modest for the CEE region at only 0.08% of the CEE GDP. PE divestment as a share of GDP represented 0.18% of European GDP in 2019, while for the CEE region, the corresponding share was 0.06%.

Figure 6.1. Private equity activity in CEE region and Europe

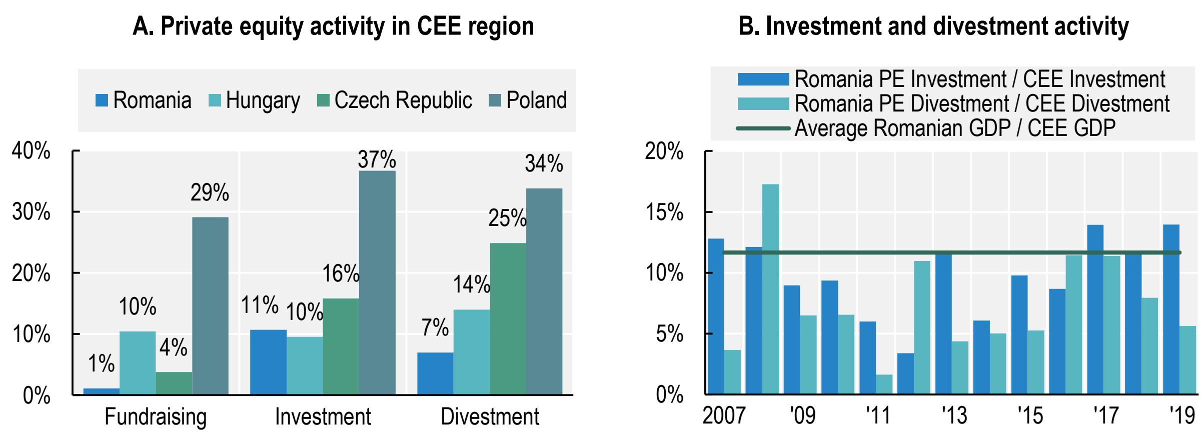


Source: Invest Europe / EDC.

The private equity market in Romania is still in a development phase. Between 2007 and 2019 private equity firms in Romania raised EUR 222 million. This represented only 1% of the total amount of private equity capital raised in the CEE region and was well below Romania's average annual share in CEE GDP for the same period (11.7%). In fact, during this period, fundraising activity in Romania was concentrated in only six years. Yet, during the last three years, PE firms were able to raise an annual average of EUR 31 million. Poland and Hungary ranked first and second in the CEE fundraising activity and together accounted for almost 40% of all the funds raised in the region.

Compared to fundraising, Romania's share in PE investment in the CEE region volume was significantly higher. Between 2007 and 2019, PE investment in Romania was, on average, EUR 226 million per year. This means that Romania's investments are equivalent to 11% of the regional total and close to its share in CEE GDP (Figure 6.2, Panel A). PE investment activity in Romania has increased since 2012 (Figure 6.2, Panel B). Romanian divestments between 2007 and 2019 amounted to EUR 909 million, representing 7% of divestment in CEE countries. Poland and the Czech Republic ranked first and second, respectively, in PE investment and divestment in the CEE region. Together their activity represented 53% of PE investment and 59% of PE divestment of the regional total.

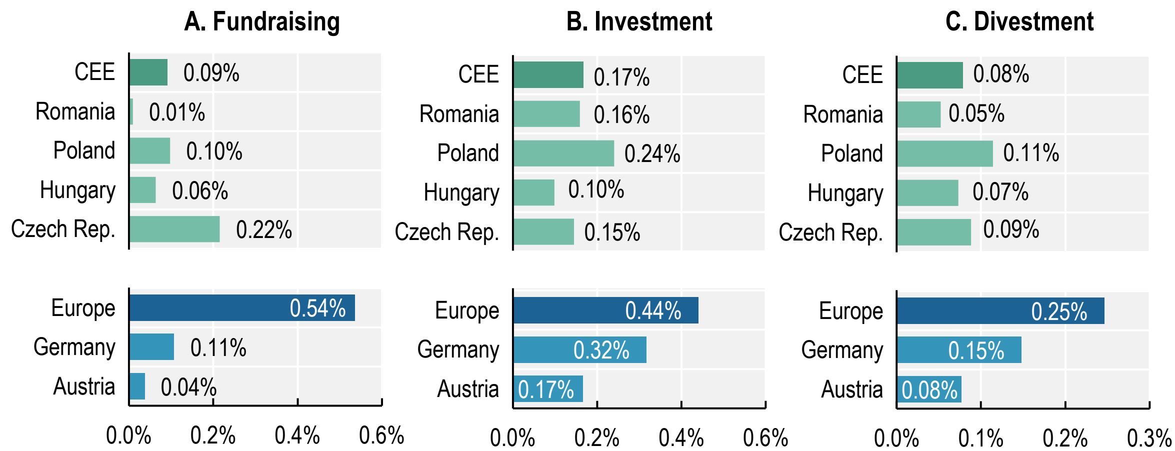
Figure 6.2. Private equity activity in Romania as share in CEE region, 2007-19



Note: In Panel A, CEE region includes EUR 8 billon of funds raised of which the target country information not specified.
Source: Invest Europe / EDC.

Compared to the selected peer countries, Romania has lagged behind in PE activity over the last five years, particularly in fundraising and divestment (Figure 6.3). In the Czech Republic and Poland, PE fundraising between 2015 and 2019 represented on average 0.22% and 0.10% of their respective GDP, while the corresponding figure for Romania was only 0.01%. Moreover, PE divestments over the same period accounted for only 0.05% of Romania's GDP, which is also below the CEE average of 0.08%. The exception is PE investment to GDP, for which Romania, with 0.16%, is almost at the same level as the CEE average of 0.17% of GDP.

Figure 6.3. Private equity activity in Romania and selected European countries, percentage of GDP



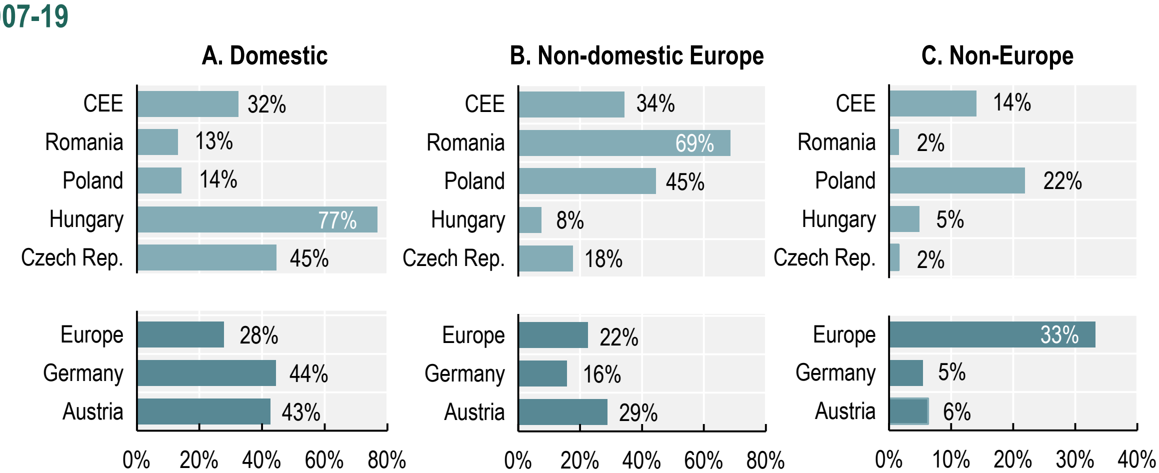
Note: The shares represent the five-year average between 2015 and 2019, in Panel A, CEE region includes EUR 8 billon fundraising of which the target country information not specified.
Source: Invest Europe / EDC.

6.2. Fundraising, investment and divestment trends

PE fundraising activity in Romania is modest compared to CEE regional volumes. Romanian private equity firms mostly rely on foreign investors when raising funds. Between 2007 and 2019, 69% of the committed capital in Romania was raised from other European investors (Figure 6.4, Panel B). This is almost twice as high as the total CEE non-domestic share of 34%. Moreover, a modest amount of the Romanian funds have been raised from investors outside of Europe, while for the CEE region as a whole, around 14% of funds were raised from non-European investors (Figure 6.4, Panel C).

In Poland, 45% of the funds were raised from other European countries and 22% from non-European countries. However, other CEE countries rely heavily on their domestic market for raising funds, notably in Hungary where 77% of total funds raised come from domestic investors (Figure 6.4, Panel A). Generally, CEE countries depend heavily on the domestic market and on other European markets which together account for 66% of the total funds raised, while for Europe the corresponding share is 50%.

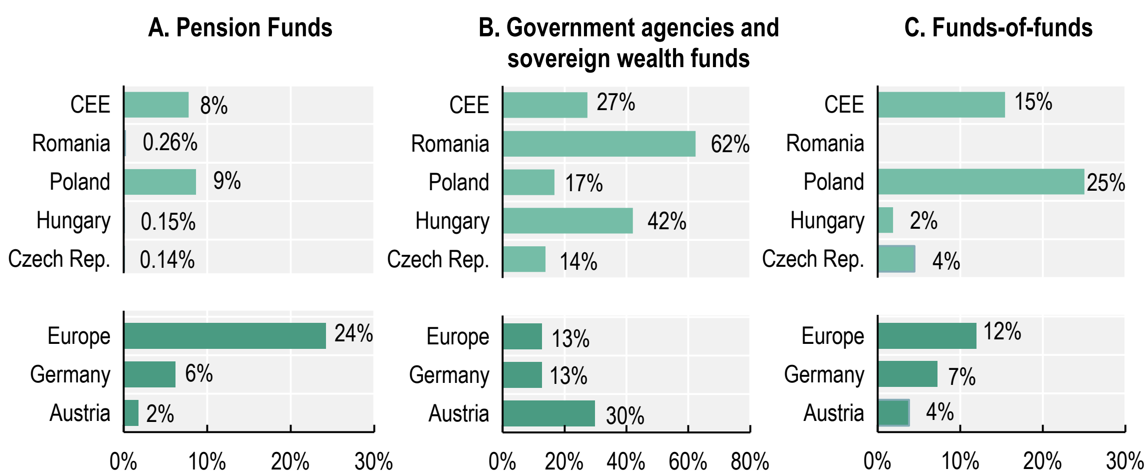
Figure 6.4. PE fundraising by origin of investors in Romania and selected European countries, 2007-19



Note: The analysis only includes funds raised where the origin of the investor is specified.
Source: Invest Europe / EDC.

During the 2007-19 period, pension funds were the largest investors providing 24% of the total funds raised in Europe (Figure 6.5, Panel A). For the CEE region, however, pension funds provided only 8% of total funds raised, while government agencies and sovereign wealth funds was the single largest source of funds, contributing 27% of total funds raised. This situation is even more accentuated in Romania where government agencies[2] account for 62% of all funds raised between 2007 and 2019. (Figure 6.5, Panel B). This is to a large extent the result of increased PE activity by government agencies in Eastern Europe, including Romania, to offset investment outflows in the wake of the 2008 global financial crisis and the 2012 Euro crisis (Mihai, 2015[2]). Additionally, in Romania individual investors and banks represent 10% and 5% of the funds raised, respectively. Importantly, funds-of-funds, which otherwise play a significant role in PE fundraising especially in Europe, were not active in the Romanian PE market.

Figure 6.5. PE fundraising by type of investors in Romania and selected European countries, 2007-19



Note: CEE region includes EUR 8 billon fundraising of which the target country information not specified, as a result, the specific country level data of the capital providers for that amount is not available.
Source: Invest Europe / EDC.

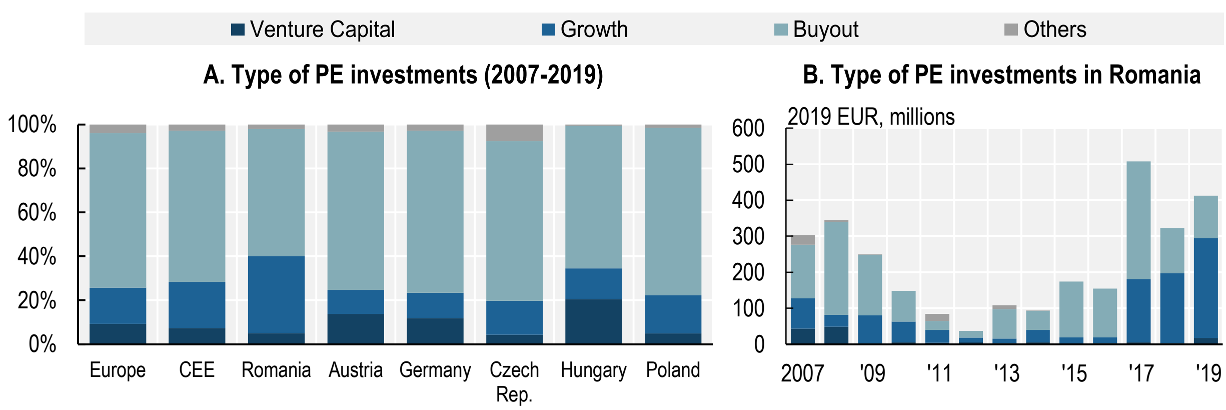
Private equity firms mainly specialise in buyouts, venture capital and growth investment. The AUM of the three account for 54%, 25% and 18% of the total PE AUM, respectively as of June 2019 (McKinsey, 2020[1]). The buyout segment of private equity markets provides funds for the acquisition of more mature companies to improve their operations, thereby enhancing the efficiency and increasing the valuation of the company. Generally, the buyout segment of PE investment focuses on under performing companies, with the investment aiming to foster corporate restructuring and enhance productivity (OECD, 2007[3]). Venture capital investors typically focus on early stage firms, for example companies in technology intensive industries, which may have difficulties raising funds from the banking sector or the primary financial markets. An efficient venture capital market contributes to economic growth, employment creation and long-term competitiveness by enabling access to financing for high-growth firms (ECB, 2005[4]). The growth segment of PE refers to the investment in relatively mature companies that require capital for their growth objectives.

As discussed before, investment activity in Romania, unlike fundraising, shows a level of activity closer to its contribution to GDP in the CEE region. Among different types of PE investments, buyout transactions dominate investment volumes across countries and regions. Buyout transactions typically involve high levels of debt financing, with the aim of acquiring a controlling share of the company to facilitate the restructuring process. In both Europe and the CEE region, buyout deals accounted for almost 70% of the total PE investment value between 2007 and 2019. A cross-country comparison shows that the share of buyout deals in investments (58%) is relatively low in Romania (Figure 6.6, Panel A).

Growth investments accounted for 35% of total PE investments in Romania between 2007 and 2019 (Figure 6.6, Panel A). This investment type represents the highest share of total PE investment compared to peer countries. It was mainly driven by the increase in growth investments during the last three years when the share of growth investment increased from 35% in 2017 to almost 70% of total PE investment in 2019 (Figure 6.6, Panel B). It is also worth mentioning that the share of venture capital stood at 5% of the total investment over the whole period, a modest level compared to 20% in Hungary and 14% in Austria.

Among different reasons for the low level of venture capital activity in Romania, the total R&D intensity measured as the gross R&D expenditure to GDP has been found to be closely linked to early stages of venture capital activity in Romania (Diaconu, 2012[5]). Enterprises create a demand for venture capital for their innovative projects, therefore creating activity in the venture capital market. However, Romania shows by far the lowest level of R&D measured as a share of GDP among its peers (see Chapter 3, Figure 3.4), which could partly explain the low level of venture capital activity in the country.

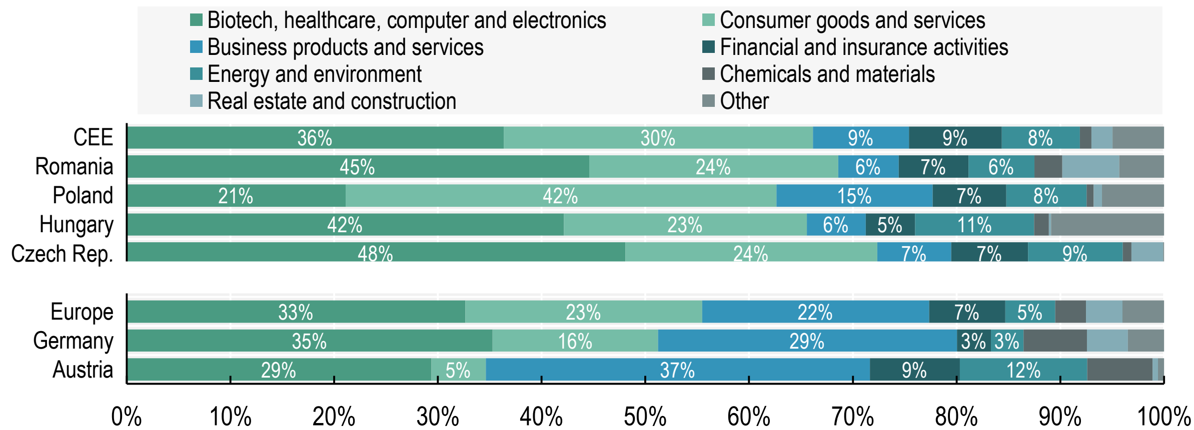
Figure 6.6. PE investment in Romania and selected European countries



Source: Invest Europe / EDC.

During the 2007-19 period, most PE investments in Europe and in the CEE region were concentrated in three industries: technology including biotech, health care, computers and electronics; consumer goods and services; and business products and services. These three industries accounted for more than 75% of total PE investments in Europe as well as in the CEE region, with Europe at large being more focused on the business products and services industry compared to the CEE region (Figure 6.7). In Romania, the largest industry is technology, which attracted 45% of total PE investments over the 2007-19 period.

Figure 6.7. PE investment by industry in Romania and selected European countries, 2007-19

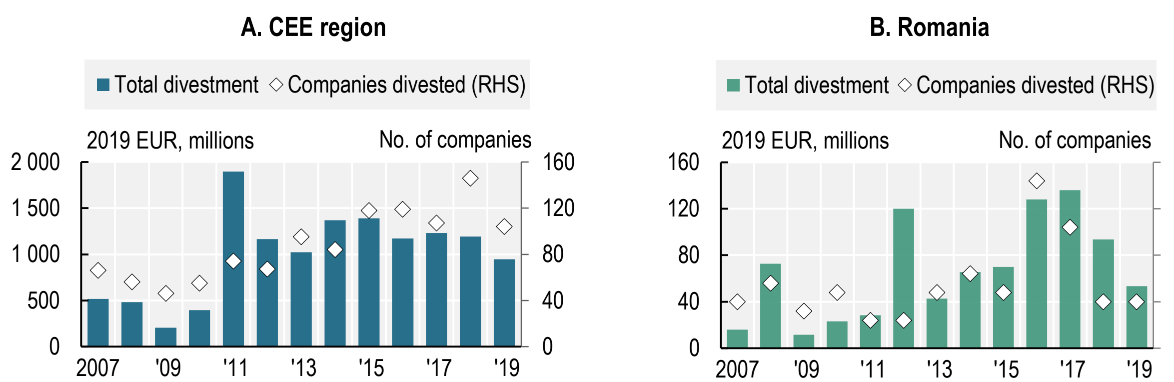


Source: Invest Europe / EDC.

The final stage of private equity investment is divestment, where private equity funds exit their investments at the end of the fund's lifecycle. There are several forms of divestments including sale through public offerings, sale to other private equity firms or financial institutions, buyback by managers or owners, repayment of preference shares/loans and write-offs.

Divestment activity in the CEE region has decreased since 2015 (Figure 6.8, Panel A). In 2019, total divestments in the CEE region amounted to EUR 946 million, a decline of 21% compared to 2018. This decrease is in line with broader European divestment trends, where the total divestment amount decreased by 16% between 2018 and 2019. Divestment by companies from the CEE region in 2019 accounted for 3% of total European divestments. In 2019, Romania recorded its lowest level of divestment since 2013 at EUR 53 million, corresponding to only five companies (Figure 6.8, Panel B). This placed divestment volumes in Romania fourth in the CEE region after Serbia, Poland and the Czech Republic.

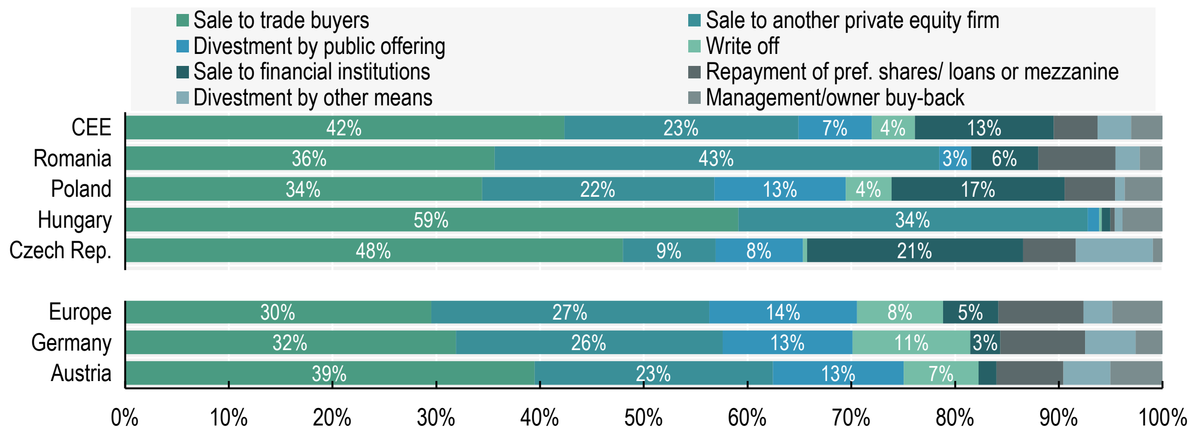
Figure 6.8. PE divestment volume in CEE Region and Romania



Source: Invest Europe / EDC.

Among the different forms of divestment, the sale to another private equity firm and trade buyers are the most common forms accounting for 57% and 65% of the total aggregate divestment value for Europe and the CEE region, respectively (Figure 6.9). In Romania, these two forms of exits account for 79% of all divestments. In particular, exit through the sale to another private equity firm makes up more than 40% of the total exit value. Importantly, while the divestment through a public offering represents 14% and 7% of the total exit value for Europe and the CEE region, respectively, it represents only 3% in Romania.

Figure 6.9. PE divestment by exit forms in Romania and selected European countries, 2007-19



Source: Invest Europe / EDC.

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OECD (2007), "The Private Equity Boom: Causes and Policy Issues", http://www.oecd.org/finance/financial-markets/40973739.pdf. [3]

Notes

[1] CEE countries include: Bosnia Herzegovina, Bulgaria, Croatia, the Czech Republic, Estonia, Hungary, Latvia, Macedonia, Moldova, Montenegro, Poland, Romania, the Slovak Republic, Slovenia, Serbia, Ukraine.

[2] Government agencies refer to the amounts raised by two funds "Balkan Accession Fund" and "Emerging Europe Accession Fund" managed by the private equity firm Access Capital Partners SA. The Balkan Accession Fund targets investment in Bulgaria, Romania and other south east European countries and the lead investors of the fund are Black Sea Trade and Development Bank (BSTDB), the German Investment and Development Society (DEG), EBRD and the Netherlands Development Finance Company (FMO).The Emerging Europe Accession Fund targets companies based in South Eastern Europe and fund's lead investors are BSTDB, DEG, EBRD and European Investment Fund (EIF).

Annex A. Methodology for data collection and classification

A. Company financial and ownership information

The information presented in Chapter 2 is mainly based on the OECD ORBIS Corporate Finance database. The extract of information presented in Chapter 2 includes financial statement and ownership information for non-financial companies between 2005 and 2018.

Company categories construction

Chapter 2 shows the following four non-financial firm categories: Category 1 *"Listed companies"*, Category 2 *"Large unlisted companies"*, Category 3 "Small and mid-sized companies part of a group", and Category 4 *"Independent small and mid-sized companies".* The construction of the company categories is based on the ownership, industry, legal information and financial information tables.

The procedure starts by identifying all listed and unlisted companies with assets over USD 100 million in the entire ORBIS universe. Non-financial listed companies are classified immediately as Category 1 and large unlisted non-financial companies as Category 2. For these groups, the consolidated financial statements are used, if available.

The following steps identify the countries of interest and uses their ownership country year tables to identify companies in Category 3 and Category 4. ORBIS provides many records of owners at different points in time from different sources. Two criteria are used to clean the ownership information and to be left out with only one record for each owner firm year observation: the largest owner is kept and the latest information is prioritised. The largest owner can be either the global ultimate owner at 50%, the global ultimate owner at 25%, or the largest direct owner with over 25% holdings. Once the sample has a unique owner firm year record, owners are classified as corporations or natural persons.

Using the ownership records generated in the previous step, the routine starts by identifying the subsidiaries of the listed and large unlisted companies. Three types of companies are identified: 1) domestic subsidiaries with a local parent, 2) domestic subsidiaries with a foreign parent, and 3) companies controlled by a person. Some companies that are classified as subsidiaries in this step were already identified as large unlisted companies at the beginning. In these cases, since the subsidiary was already consolidated, its data were not used to avoid duplications. The domestic subsidiaries with a local parent in Category 1 or 2, or with foreign parents Category 1 or 2 are classified as Category 3. Please note that this category includes the non-financial domestic subsidiaries of financial domestic parent and foreign parents as these parents are excluded as they do not meet the industry requirement or because they are not incorporated in the domestic market under analysis. The companies where the largest owner is a person (over 25% ownership) are classified as Category 4.

Economy wide calculations take into account the ownership structure of companies and avoid considering companies that are already consolidated in the accounts of domestic non-financial parent companies. Thus, economy wide calculations include companies from Category 1, Category 2, Category 4, companies without ownership information, and companies from Category 3 that had a foreign parent or a financial domestic parent.

Financial information cleaning

The company category classification described in the previous section also incorporates different types of financial reporting (consolidated and unconsolidated reports). Large companies in the universe commonly report consolidated financial statements as well as unconsolidated financial statements. For the listed and large unlisted non-financial company categories, consolidated accounts are considered, if available. For the remaining categories, unconsolidated financial statements are used.

The raw financial dataset contains several firm year observations when a company has multiple consolidation codes or it reports for different purposes. To construct a panel with a unique firm year observation, the following steps are applied:

1. Financial companies are excluded.
2. The fiscal year is recorded as the previous calendar year of the closing date whenever the closing date of the financial statement is before 30 June.
3. Financial statements covering a 12-month period are used, preferably.
4. When multiple observations within the same year exist, accounts with closing dates closer to year-end are preferred to accounts with older closing dates.
5. Published annual reports are preferred to local registry filings. Local Registry filings are preferred to unknown filing types.
6. Accounts using IFRS are preferred to those using GAAP, accounts using GAAP are preferred to those using unknown accounting practices.
7. For companies with multiple consolidation codes, the following criteria apply: for companies that release consolidated financial statements, C1 is preferred when both C1 and C2 exist; for companies that release unconsolidated statements the observation from annual reports are preferred over others.
8. Financial information is adjusted by annual EUR Consumer Price Index changes and information is reported in 2019 constant million EUR.
9. Companies with at least one observation showing negative assets or negative fixed assets are dropped from the sample.
10. Companies with equal or less than 10 employees are dropped from the sample. When employee number is not available companies with total assets below EUR 35 000 are dropped from the sample.
11. Financial statement information is winsorised at 1% for both tails within companies' categories.
12. In the case that there are single year gaps in the financial data, these are populated by interpolation using the average value of the preceding and the succeeding year for major items. Sub items are then calculated using accounting identities. Such interpolation is reserved for single year gaps, and is not applied for data gaps with two or more years.

The OECD ORBIS Corporate Finance uses the 1 digit SIC industry classification.

Table A.1. ORBIS industry classification

Standard Industrial Classification (SIC)
Agriculture, Forestry and Fishing
Mining
Construction
Manufacturing
Transportation, Communications, Electric, Gas and Sanitary service

B. Public equity data

The information on initial public offering (IPOs) and secondary public offerings (SPOs) presented in Chapter 4 is based on transaction and/or firm level data gathered from several financial databases, such as Thomson Reuters Eikon, Thomson Reuters Datastream, FactSet and Bloomberg.

Considerable resources have been committed to ensuring the consistency and quality of the dataset. Different data sources are checked against each other and, whenever necessary, the information is also controlled against original sources, including regulator, stock exchange and company websites and financial statements.

Country coverage and classification

The dataset includes information about all initial public offerings (IPOs) and secondary public offerings (SPOs or follow on offerings) by financial and non-financial companies for six European economies (Romania, Austria, the Czech Republic, Germany, Hungary and Poland) for the period from January 1995 to December 2019.

All public equity listings following an IPO, including the first time listings on an exchange other than the primary exchange, are classified as a SPO. If a company is listed in more than one exchange within 180 days, those transactions are consolidated under one IPO. The country breakdown is carried out based on the domicile country of the issuer. In the dataset, the country of issue classification is also made based on the stock exchange location of the issuer.

It is possible that a company becomes listed in more than one country when going public. The financial databases record a dual listing as multiple transactions for each country where the company is listed. However, there is also a significant number of cases where dual listings are reported as one transaction only based on the primary market of the listing. For this reason, the country breakdown based on the stock exchange is currently carried out based on the primary market of the issuer. Going forward, the objective is to allocate proceeds from an IPO to respective markets where the issuance is listed at the same time.

Currency conversion and inflation adjustment

The IPO and SPO data, and related financial statement data, such as total assets before the offering, are collected on a deal basis via commercial databases in current USD values. The information is aggregated at the annual frequency and, in some tables, presented at the year industry level. Issuance amounts initially collected in USD were adjusted by US Consumer Price Index (CPI) and finally converted to 2019 EUR using the average exchange rate EUR/USD for 2019.

Industry classification

Initial public offering and secondary offerings statistics are presented in this report using the Thomson Reuters Business Classification (TRBC). The economic sectors used in the analysis are the following:

Table A.2. Public offerings industry classification

Thomson Reuters Economic Sector
Basic Materials
Cyclical Consumer Goods / Services
Energy
Financials
Healthcare

Exclusion criteria

With the aim of excluding IPOs and SPOs by trusts, funds and special purpose acquisition companies the following industry categories are excluded:

- Financial companies that conduct trust, fiduciary and custody activities
- Asset management companies such as health and welfare funds, pension funds and their third party administration, as well as other financial vehicles
- Companies that are open-end investment funds
- Companies that are other financial vehicles
- Companies that are grant making foundations
- Asset management companies that deal with trusts, estates and agency accounts
- Special Purpose Acquisition Companies (SPACs)
- Closed-end funds
- Listings on an over the counter (OTC) market
- Security types classified as "units" and "trust"
- Real Estate Investment Trusts
- Transactions with missing or zero proceeds

C. Ownership data

The main source of information is FactSet Ownership database. This dataset covers companies with a market capitalisation of more than USD 50 million and accounts for all positions equal to or larger than 0.1% of the issued shares. Data is collected as of end of 2019 in current USD, thus no currency nor inflation adjustment is needed.

The data is complemented and verified using Thomson Reuters Eikon and Bloomberg. Market information for each company is collected from Thomson Reuters Eikon. For each of the following six economies (Austria, the Czech Republic, Germany, Hungary, Romania and Poland), the information presented in Chapter 4 corresponds to all listed companies in those markets.

Next, the information for all the owners reported as of the end of 2019 is collected for each company. Some companies can have up to 5 000 records in their list of owners. Each record contains the name of the institution, the percentage of outstanding shares owned, the investor type classification, the origin country of the investor, the ultimate parent name, among others. Each owner record is re classified into the following investor classes: Private corporations, Public sector, Strategic individuals, Institutional investors and Other free float. When the ultimate parent was recognised as a Government, the investor record is, by default, classified as Public sector. For example, public pension funds that are regulated under public sector law are classified as government, and sovereign wealth funds are also included in that same category.

D. Corporate bond data

Data shown on corporate bond issuances in Chapter 5 is based on original OECD calculations using data obtained from Thomson Reuters Eikon that provides international deal level data on new issues of corporate bonds, which are underwritten by an investment bank. Corporate bond data from Romania, Hungary, Poland and the Czech Republic also includes the non-underwritten ones retrieved through Thomson Reuters Eikon's Bond Search application. The database provides a detailed set of information for each corporate bond issue, including the identity, nationality and sector of the issuer; the type, interest rate structure, maturity date and rating category of the bond, the amount of and use of proceeds obtained from the issue. For corporate bond data in Romania, information from the Bucharest Stock Exchange is also added to complement the original dataset.

The initial dataset covers observations in the period from 1 January 2000 to 31 December 2019. From this initial set, convertible bonds, deals that were registered but not consummated, preferred shares, sukuk bonds, bonds with an original maturity less than one year or an issue size less than USD 1 million are excluded.

The country breakdown is carried out based on the domicile country of the issuer. Issuance amounts initially collected in USD were adjusted by US Consumer Price Index (CPI) and finally converted to 2019 EUR using the average exchange rate EUR/USD for 2019.

E. Private equity data

The main source of information for the private equity data presented in Chapter 6 is Invest Europe / EDC. The information provided by Invest Europe is made up of firms managing investment vehicles or pools of capital (Funds) and primarily investing equity capital in enterprises not quoted on a stock market. Firms are included in the analysis as long as at least one of the funds they manage qualifies to the inclusion conditions; however, only the activity of the qualifying funds is taken into consideration.

The countries included when referring to Europe statistics are: Austria, Baltic countries (Estonia, Latvia, Lithuania), Belgium, Bulgaria, the Czech Republic, Denmark, Finland, France, Germany, Greece, Hungary, Ireland, Italy, Luxembourg, the Netherlands, Norway, Other CEE (Bosnia Herzegovina, Croatia, Macedonia, Moldova, Montenegro, Serbia, Slovenia, the Slovak Republic), Poland, Portugal, Romania, Spain, Sweden, Switzerland, Ukraine, United Kingdom.

The fundraising activities are classified according to the country that corresponds to the location of the advisory team of the fund. For the CEE region, fundraising activity is the sum of funds managed from the CEE region plus funds that have declared CEE as their target region. The amount reported under investments includes equity, quasi equity, mezzanine, unsecured debt and secured debt. Secured debts amounts within all investments packages are removed, unless the debt originates from private equity funds. Investment activities are recorded according to the location of the portfolio company. Divestment amounts are recorded at cost (i.e. the total amount divested is equal to the total amount invested previously). Private equity statistics are collected in current Euros. Amounts are then adjusted by using Euro CPI to express them in constant 2019 EUR.

The categories of private equity entities that are excluded from the Invest Europe Universe are: Fund of Funds, Hedge Funds, Real Estate, Project Financing/ Infrastructure, Secondary Funds, Distress Debt, Venture Credit, Participative Loans, Incubators, Accelerators, Business Angels and Holding companies.

Capital Market Review of Romania

TOWARDS A NATIONAL STRATEGY

This publication provides a comprehensive overview of capital markets in Romania, focusing on conditions for stock market listing, secondary stock market liquidity, growth markets, modalities for household savings, institutional investors and market-based debt financing. It underlines potential areas for reform and suggests policy actions that could help Romanian authorities improve the legal, regulatory and institutional framework for capital markets and ultimately prepare a national capital market strategy.

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