REFERENCE POINTS FOR FINANCIAL INSTABILITY IN THE EURO ZONE CANDIDATES COUNTRIES[1]

Adina CRISTE, PhD[*]

Abstract

The issue of financial instability has been intensely debated over the past few decades both within the academia and by the economy decision-makers. The complexity of the concept and the range of meanings hinder the development of a general, unanimously accepted definition. However, the historical analysis of the episodes of financial instability, which were rather frequent particularly after World War Two, as well as the specific literature, may outline some characteristics of the state if financial instability. Starting from these general aspects, this article aims to identify some traits which define the financial instability in the countries candidate to the Euro zone, taking into account the European integration and all the challenges of this process. The ideas presented in the paper will be used to analyse the actions taken by a national central bank candidate to the Euro zone, to cope with the challenges of the financial instability.

Keywords: banking credits, fragility of the financial system, European integration

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1. Introduction

The long-term deflationist depression of Japan throughout the 1990 and 2000 years, after the prosperous 1980 years, the 1980 and 1990 years currency crises from the Latin America, the Asian

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[*] *Scientific Researcher III, "Victor Slăvescu" Center for Financial and Monetary Research, Romanian Academy.*

financial crisis of the late 1990 years, and more recently, the global financial crisis, started in the USA and propagated in Europe too, are serious examples of financial instability which show the importance of understanding the way in which the functioning of the financial mechanisms may contribute to the production of financial instability.

Although this is a subject intensely studied lately, given the history of the recent global financial crisis which started in 2007, there is enough space for debates on this subject and many questions to be answered. Given the challenges of the process of monetary integration within the candidate countries, it is important to identify markers which define the financial instability in this region.

The paper starts with a brief review of the literature on the financial instability and with some remarks on the manifestation of some episodes of financial instability after World War Two (more precisely, during the period of neoliberal capitalism development), which highlight the main elements which define this concept. The analysis of the financial instability continues with the situation of the emerging European countries, taking into consideration the characteristics entailed by the trends of globalization and by the accession to the European Union (EU). The selected countries are those candidates to the Euro zone: Bulgaria, Lithuania (which will adopt the Euro in 2015), Poland, Czech Republic, Romania and Hungary, as well as Latvia which, although has already adopted the Euro as of January first 2014, is an important case of analysis for the financial instability. The purpose of the analysis is to identify features which describe the financial instability in these countries.

The study leaves from the assumption that the onset of a financial crisis is the most serious consequence of the financial instability, the sign of a deficient functioning of the financial system. The seriousness of the economic, social and politic effects of the financial crisis is enough motivation to identify in time the sources of the financial instability, so that efficient correction measures can be designed, because, usually, the knowledge of the causes which determine the financial instability sketch the directions of prevention and correction.

2. Approaches of the concept of financial instability in the literature

The concept of financial instability doesn’t have a unanimously accepted definition, just like the concept of financial sustainability since an analytical framework for the evaluation of the financial (in)stability is yet to be developed.

According to Crockett (1997), financial instability is the situation in which the economic performance is potentially affected by the price fluctuation of the financial assets or by the incapacity of the financial institutions to meet their contractual duties. Mishkin (1999) also defines the financial instability highlighting the importance of the asymmetric information in its generation, on the basis of its role of intermediary within the banking system which supplies financial resources towards the real economy. Davis (1999, 2002) defines the financial instability as a period of events which amplify the risks of a financial crisis, i.e. the collapse of the financial system which affects the payment services and the allocation of funds for investments. Although the author considers that the volatility of the price for assets should be excluded from this definition, it is known that the systemic risk can manifest by the absence of liquidity from the market and by the jamming of the market infrastructure too. On the other hand, Ferguson (2002), defines the financial instability taking into consideration the element excluded by Davis (1999, 2002), the volatility of the price for the financial assets, considering that if the prices of particular important financial assets deviate significantly from the normal and if there may be distortions in market operation and availability of the credit (internal and international), so that the aggregate expenditure deviates or tend to deviate significantly from the level at which the economy is able to produce, then the conditions for financial instability are met. Ferguson’s definition (2002) also includes the effects of the financial instability on the macroeconomic variables (on the aggregate expenditure).

Chant (2003) considers that the financial instability is determined by the conditions in which the financial markets disturb or threaten to disturb the economic performance through their impact on the operation of the financial system, making distinction between the financial instability and the macroeconomic instability. The author considers that the financial instability also contains different forms of instability (banking crises, crash of the stock market), depending on the segment which is disturbed (banking system or stock market). He draws attention to the dynamic character of the financial markets which leads to permanent changes in the conditions and prices on thee markets, which requires that the definition of the financial instability makes distinction between the “normal” changes and those which have a potential impact on the real economy.

Allen and Wood (2006) defined the financial instability from the perspective of the real economy taking into consideration the non-financial sector too (households, companies, governments) which is confronted with financial “crises” too, but the definition is much too general and it includes elements which cannot be directly influenced by the monetary authority in order to promote the financial stability.

Another concept used by the literature, closely tied to the issue of financial instability, refers to the *financial fragility*. Minsky (1995) developed a *theory of the financial market fragility* on the basis of which he explains the appearance and propagation of the financial crises, highlighting that the financial fragility is caused by the build up of debts within the private sector during the economic cycle. According to this theory, during the periods of prosperity, the increase of the cash-flow over the necessary amount for the payment of the debts leads to a phenomenon of speculative euphoria which creates a credit bubble. Gradually, the speculative phenomenon generates the excess growth of the debts, which leads to the contraction of the economy. The formulation of this theory contributes to the understanding of the way in which the financial markets operate and of the relation between the financial system and the real economy, showing that the financial system fluctuates between solidity and fragility, and that these fluctuations are part of the process which generates the economic cycles. Actually, Minsky depicts very well the behaviour of the capitalist financial system which, by definition, is a complex and sophisticated financial system affected by internal processes which generate instability (Minsky, 2011).

Issing (2003), considers that the financial fragility is a characteristic of that economy which neared its critical level, that particular level after which the resources are allocated inefficiently. The fragility of the financial system can be caused by endogenous factors specific to the financial environment (deficient functioning of the financial system components, build up of imbalances determined by particular conjunctural conditions, inadequate regulations which increase the moral hazard, etc.), or by exogenous factors, from the wider macroeconomic environment (lower rate of economic growth, poor foreign payments balance , higher inflation rate, poorer international competitiveness of the economy, deterioration of the exchange rate, etc.). These factors put a specific “pressure” on the financial system, which accumulates vulnerabilities in terms of infrastructure and relations between the entities, thereby wrecking the entire system.

When a financial system is fragile, an insignificant shock may lead, through contagion, to significant effects. A financial system fragile due to its internal structure, with no adequate mechanisms of auto correction, increases the risk that any shock generates internal crises of the financial system, which may expand and lead to financial instability. On the other hand, an endogenous shock, such as the bankruptcy of a bank or a major fluctuation in the price of the assets, cannot always be regarded as a proof of financial instability, but rather as a correction reaction against some abnormalities within the financial system. Issing (2003), stated that the major fluctuations in the price of the assets which may determine the bankruptcy of the financial and monetary institutions due to the propagation of an important real and financial shock, might be a proof of the stability and self-regulation capacity of the system (in agreement with the Schumpeterian vision of “creative destruction”), as long as an efficient financial intermediation and an efficient process of financing can be maintained.

Chant (2003), distinguished the three states of a vulnerable financial system – fragility, instability and crisis, depending on the operational capacity of the particular financial system. Thus, the financial fragility is that state in which the financial system fulfils its functions under the conditions of an obvious vulnerability; the financial instability is that state in which the vulnerabilities start affecting the operation of the financial services, while the financial crisis is the most serious state of financial instability, in which n the normal operation of the financial system ceases. Lupu (2011) concluded that the financial crisis is a manifestation of the financial instability which burdens the real economy with significant costs.

On the basis of Chant’s idea (2003), we consider that the financial instability has a premises the financial fragility and, thus, the markers defining the financial instability are those elements which determine in time the financial instability.

3. Brief history of the episodes of financial instability

David Kotz (2013) depicted the characteristics which define the capitalism after World War Two. He considers that the financial instability which characterizes the period after the 1970 years (as shown by the high frequency of the financial crises) is generated by the major changes in the global capitalist system, the USA and the United Kingdom being the promoters of this process. The changes which actually drafted the neoliberal current (through the Washington consensus) were considered to be the necessary elements to solve the crisis period of the regulated capitalist system, which existed at that time and which had been established after World War Two. Thus, in the early 1980 years, the new form of capitalism was setting the grounds for new institutions, for new policies and ideas, first in the USA and United Kingdom, spreading thereafter to other countries. The neoliberalism, relying on liberalization, privatization and stabilization, meant on the one hand the stimulation of the development of capital and investments by the liberalization of the financial flows and, on the other hand, the reduction of the social programs of the government, restrictive monetary policies oriented towards price stability and additional efforts for budget balancing. Such orientation of the economic development meant the domination of the capital over the work, unlike the regulated capitalism (relying on Keynesianism), which ensured a balance between these two variables. By encouraging the investments in capital, concomitantly with the stagnation of the real wages, this new form of capitalism stimulated overproduction and the maintenance of the economic expansion encouraged consumption in excess of the incomes and the establishment of speculative bubbles. The financial cycles increased in amplitude, and the financial instability became a major concern for the macroeconomic policies.

The economic and financial history of the past 30 years, which passed under the sign of neoliberalism, confirms the endogenous character of the financial instability specific to the market-oriented capitalist system. Through the 1980-2000 years, many regions of the world were confronted with periods of financial instability, both in developed countries (New Zealand, Australia and the Scandinavian states, Japan, USA), and in emerging countries (the Latin America countries, the Asian countries, Russia).

The deregulations in the financial-banking system and the removal of the control of the capital which were produced within favourable financial conditions in various parts of the world in the 1980 and 1990 years, produced resembling local effects, of financial stability, by the excessive stimulation of the credits and by increasing the price of assets on various markets (real estate, stock exchange). The financial instability which we consider as an aggravating for of the financial fragility started to show up together with the propagation of shocks within the financial system (oil shock, change of the monetary or fiscal policy behaviour, etc.), which generated the burst of the speculative bubble which had formed in time. Table 1 shows the stages of financial instability, with their characteristics, in several countries.

Table 1

Characteristics of the stages of financial instability in different countries (1980-1990)

Country	Period of the financial fragility (the 1980 years)		Period of the financial instability (end of the 1980 years - the 1990 years)		
	Changes in the macroeconomic policies	Effects (formation of the speculative bubble)	Shocks	Effects during stage I (burst of the speculative bubble)	Effects during stage II
Japan	Capital inflows Relaxed monetary policy	Stimulation of the credit Higher price of the assets	Changed behaviour of the monetary policy (restrictive policy) to curb inflation	Higher interest rates Decreasing price of the assets, including the real estate price.	Payment incapacity Lower prices Long deflating phenomenon
Norway	Capital inflows Real negative interest rates for the debts of the private sector	Stimulation of the credit Extreme financing of the demand for credits Higher price of the assets	Oil shock (falling oil price)	Deterioration ratio of the high wages and production Currency speculations to the detriment of the national currency	Banking crisis Economic recession
Finland	Capital inflows Budgetary expansion	Effervescence of the credit Higher real estate prices	Restrictive monetary policy (higher interest	Lower growth of the credits Shrinking commercial activity	No prolonged effects because the banking system was

			rates and reserves requirements) Fall of the Soviet Union	Strong decrease of the price of assets	supported by the government
Sweden	Capital inflows	Stimulation of the credit Effervescence of the real estate market	Restricted credits Higher interest rates	Problems within the banking system (some banks had major difficulties based on overestimated values of the assets)	Recession
Mexico	Privatization of the local banks Capital inflows Cancellation of the reserves requirements	Stimulation of the credit for companies Development of the stock exchange market	Political shock (assassination of a candidate to the Presidency)	The political instability crashed the prices of the stock exchange and of other financial assets	Crises of the financial system (banking and currency crises)

Source: author's diagram

The above observations support the idea of a pattern of the financial instability manifestation, at least for the period 1980-1990. A shock which occurred on the background of the financial system fragility marked the beginning of the period of financial instability.

Although the financial instability became more complex after the 2000 years, as it was shown many times during the recent debates on the causes of the global financial crisis, its pattern maintains and is like a prolongation of the episodes of financial instability of the 1990 years. The financial deregulation, accompanies by the strong development of the financial system (financial innovations, globalization and technological development) determined the strong increase of the credit and the boost of consumption and investment using borrowed resources, which created the conditions for the development of speculative bubbles. The subsequent burst of that speculative bubble generated several adverse effects on the financial market and within the real economy.

It is interesting to see whether such a pattern maintains in the specific case of the countries candidate to the Euro zone. The concern of the decision-making factors for the liberalization of the capital account, which meant the possibility of making free transactions in the form of direct foreign investments or the purchase of extreme securities, had different motivations in different countries. Thus, while for the USA and the United Kingdom, the liberalization of the capital account was largely motivated by the fact that they had the statute of issuers of global reserve money, and by the fact that they were international financial centres, for Europe, the liberalization was motivated particularly by the objective of European integration and establishment of the common market.

4. Premises of the financial fragility in the countries candidate to the Euro zone

In the early 1990 years, the European emerging countries were encouraged, by the evolution of the financial markets and by the direct or indirect suggestions of the international institutions, to remove the barriers to the cross-border transactions and to start a broad process of financial liberalization. The opening towards the exterior of the economies from these countries was done in the hope for foreign capital and for its efficient allocation within the economy, as productive investments, which would have long-term beneficial effects on the economic growth. However, the process of liberalization didn’t take into account the structure of the internal financial system of these countries, which was insufficiently adapted to such opening. The financial liberalization implanted within an insufficiently developed institutional framework created favourable conditions for the build up of systemic risk factors.

Although the episodes of financial instability at that time were testimonies to the risks of financial liberalization in the form of excessive assumption of risks, high macroeconomic volatility and strong exposure of the economy to the episodes of financial crisis and instability, it was considered that the advantages of the financial liberalization would outmatch the adverse effects.

The inflows of foreign capital were drawn to these countries in a period of optimism, with global liquidity, with low interest rates and with high rates of economic growth in this region (particularly during the 2000 years, up to the start of the global financial crisis). Besides the worldwide favourable conditions, there also was a positive perception of their accession to the EU. The fulfilment of the pre-accession conditions increased the confidence that there is a favourable internal climate and that the economies will have a convergent evolution with the evolution of the older EU member states. Such expectations determined the reduction of the risk premium for the new EU member states and created attractive conditions for investment for the foreign banks. These, particularly the banks from the Euro zone, invested massively in the region, as shown by the significant increase of their assets within the total assets of the banking system from these countries. Theoretically, the investments of the foreign banks within the national banking system should improve the quality of the financial services and the efficiency of the process of financial intermediation (Prasad and Rajan, 2008). Actually, the higher attractiveness of this region increased the number of banks from the national markets and thus, the competition, within the national banking system. Under these conditions, many of these institutions adopted aggressive strategies of gaining an as large as possible market share, by orienting their activity mainly towards the financing of economy through credits. However, the insufficiently developed financial systems of the analysed countries could not absorb the massive financial flows, and they reoriented towards non-tradables (such as real estate), with more simple and accessible collaterals. The pressure on the market of the non-tradable increased their price and the value of the collaterals, which increased further the activity of crediting (Evans et al., 2000). The accelerated increase of the bank credits generated by the competitional pressure reflected in the deterioration of the credit quality by the assumption of increasing risks, this effect being very difficult to manage by the monetary authority, because usually, during the periods of effervescence, the accelerated dynamics of the financial system make it difficult the short-term increase of the analytical and monitoring capacity.

The liberalization of the banking sector also favoured the expansion of the non-banking financial institutions and of the securities market. These trends amplified the access to foreign capital and the range of investment possibilities, thus increasing the level of investments while reducing the internal saving.

The structural reforms, the opening of the capital and financial account, the financial liberalization and the domination of the foreign banks, with easy access to financing from the mother-banks, were the factors which generated financial instability before the onset of the global financial crisis, because they decreased rapidly the cost of borrowing, particularly in hard currency, and amplified very much the credits to the private sector. The effervescence of the credit before the onset of the crisis consolidated the bond between the financial intermediators and the real economy. Thus, on the one hand, the excessive increase of credits disturbed the macroeconomic stability by the higher aggregate demand in excess of the potential capacity of the economy. This deteriorated the foreign balance by increasing the current account deficit of the foreign payment balance and impacted on the foreign debt of the private sector. On the other hand, the massive inflows of capital within a poorly developed financial system put pressure on the price of the financial assets (shares, exchange rate) and of the real estate assets, generating speculative bubbles which intensified the credits.

5. Elements of the financial fragility in the countries candidate to the Euro zone

Analysing by country the elements which generated financial instability before the onset of the global financial crisis, one can notice a fast increase of the credit towards the private sector in the Baltic states, Bulgaria, Poland, Hungary and Romania, which deepened the current account deficit by stimulating consumption (trough indebting), thus favouring a higher financial instability. Also in these countries, one may notice the preference for hard currency credits (Euro, mainly), because the hard currency risk was perceived as being very low in the countries whose national currency was anchored to the Euro (Bulgaria and the two Baltic states), while in the countries with a flexible exchange rate (Poland, Romania and Hungary), the national currency was expected to appreciate in relation to the Euro.

Furthermore, in Bulgaria, Latvia and Lithuania, the high level of Euro use, the poor development of the financial sector and the presence of the foreign banks with fast access to foreign financing, were important factors which generated financial instability because they affected the adequate functioning of the mechanisms for monetary policy transmission, thus hampering the implementation of the monetary authority measures.

The amplification of the trend of foreign financing of the credits also generated balance mismatch for the currencies (credits to the private sector in national currency, from currency funds borrowed from abroad). Even in the situation in which the currency exposure remained within acceptable limits, the currency credits became risky due to the mismatch between the sources denominated in hard currency and the sources in the national currency. Such risks occurred throughout 2002-2005 in Latvia, Lithuania, Bulgaria, Romania and Hungary.

The deterioration of the credit conditions because of the higher competition on the market was stronger in Bulgaria, Hungary and the Baltic states. The credit risk also increased in Latvia and Lithuania because the credits concentrated in the non-tradable sector (mortgages) and in household consumption.

The stable macroeconomic and financial evolution from Czech Republic, in this period, didn’t lead to the build up of distortion within the financial system which was robust in Czech Republic, not fragile like in the other countries. In Czech Republic, before the start of the financial crisis, the low internal interest rates and the stable macroeconomic environment didn’t encourage the excessive use of the Euro or the development of major speculative bubbles, and the need for foreign financing was limited. Thus, the banking sector (dominant within the financial sector, like in the other analysed countries), was characterized by a conservative balance structure, meaning that it was predominated by deposits and credits of the residents in the local currency (Czech crown)[2]. Furthermore, the banking sector was net external creditor, the credits being granted mainly using the deposits of the population. There also was a low level of indebting, both of the public sector, and of the private sector, with currency equilibrium of the balance sheets. The exchange rate flexibility and the high credibility of the central bank policy also played an important role in the positive evolution of the Czech banking system.

Synthesizing the results of this analysis, we may identify several common elements which weakened the national financial systems before the onset of the crisis, and which had different intensities, as shown in Table 2.

[2] *According to a study by the International Monetary Fund (IMF, 2012), just 20% of the volume of credits are denominated in hard currency, and all were given to companies, which limits the indirect currency risk.*

Table 2

Specific elements of weakening of the national financial system in the countries candidate to the Euro zone before the start of the global crisis

Elements of the financial fragility	Countries						
	BG	CZ	LV	LT	PL	RO	HU
Higher indebtedness of the private sector, particularly in hard currency	■	□	■	■	■	■	■
Excessive use of the Euro within the economy	■	□	■	■	▨	▨	▨
Higher foreign debt of the banks	■	□	■	■	■	■	■
Development of the real estate market by increasing the price of real estate assets (formation of the speculative bubble)	■	□	■	■	▨	▨	■
Deterioration of the credit conditions	■	□	■	■	▨	▨	■
Currency mismatch	■	□	■	■	▨	▨	▨
Level of financial fragility	■	□	■	■	▨	▨	▨

Source: author's representation based on the information from the ECB reports on the financial stability (ECB, 2012 and ECB, 2014) and in Ötker-Robe et al. (2007)
Notes: The characteristics of the financial fragility are shown in different colours function of the seriousness of their manifestation within the economy – from darker colours (strong manifestation) to lighter colours (less strong, even insignificant manifestation); BG - Bulgaria; Czech Republic - CZ; LV - Latvia; LT - Lithuania; PL - Poland; RO - Romania; HU - Hungary.

On the basis of Table 2, we may group the analysed countries in three groups, for the period before the start of the global financial crisis, depending on the intensity of the factors which generate financial instability. Thus, the countries with the most fragile weakened system, with the highest risks towards the financial stability (direct and indirect exposure of the banks to the currency risk, exposure to the liquidity and refinancing risk due to currency mismatch, relaxed credit conditions, exposure to the market risk and to the credit risk) are Bulgaria, Latvia and Lithuania. Hungary, Poland and Romania form the group of the countries with a medium fragility, while Czech Republic is the only country which has a robust financial system, the least exposed to the episodes of financial instability.

After the start of the global financial crisis, the already weakened national financial systems have been submitted to episodes of instability and incertitude which affected their financial market and their real economy: slower economic growth, sudden corrections of the current account deficits and of the real estate prices (burst of the speculative bubble), particularly in Bulgaria, Latvia, Lithuania and Romania, and to a lesser extent in Poland and Hungary. The exchange rate volatility increased in the countries with a flexible exchange rate, especially the depreciation, which affected the payback capacity of the credits in foreign currency. This generated a higher volume of non-performing credits within the banking system and a higher risk of withdrawal of the foreign banks from the national markets (by limiting the exposure of the foreign banks on the local markets). Furthermore, the Baltic states, with a fixed currency regime, were confronted with the unemployment problem, low wages and a high level of governmental indebtedness.

The experiences highlight the role of the financial system fragility in the generation of the episodes of instability. Also, the experience of Czech Republic, the only country among the surveyed countries which was not directly affected by the crisis, confirms the importance of not having financial fragility in the prevention of the episodes of financial instability. Actually, the onset of the global financial crisis practically blocked any factor which could have activated the speculations on the Czech real estate market. The monetary authority (Czech National Bank) played an important role since it has warn the public, even before the financial crisis had actually started (in the 2006 report on the financial stability), on the overoptimistic expectations specific to the peak stages of the economic cycles and on the build up of risks on the real estate market.

The characteristic elements identified in relation with the fragility of the financial system in the countries candidate to the Euro zone are sources that generate financial instability and premises for the more detailed study of the relation between the seriousness of the financial instability and the seriousness of the financial instability manifested through the adverse effects of the initial shock of the global financial shock.

6. Conclusions

The adverse effects of the financial crisis which occurred in the real economy and in the financial economy, shown in many papers of the literature and in the reports of the national and international institutions, confirm the idea that the financial instability is started by the propagation of a shock, on the background of previous accumulation of macroeconomic and financial imbalances which make the financial system become frail.

Theoretically, the financial fragility accumulated in time can be generated either by the promotion and implementation of internal macroeconomic policies inadequate to the structure of the financial system and to its environment, which allows the build up of imbalances within the system (endogenous causes), or by the propagation of shocks within the financial system which affect sufficiently important elements of the system ("contagious" character) to affect the functionality of the whole (exogenous causes), or by the unsustainable relation of the system with the outer environment (penetration of imbalance-generating factors - factors of accumulation), situation specific particularly to a formerly closed system which opens up (mixt causes).

The financial instability of the 1980-1990 years had endogenous causes: the neoliberal ideology adopted by the developed countries and transposed in the internal macroeconomic policies stimulated speculative behaviours which generated financial instability.

The countries candidate to the Euro zone, surveyed in this paper, and which went through the specific conditions of the process of accession to the EU and of adopting the Euro, passed from a closed, restricted financial system, to a liberalized one. This characteristic favoured the financial instability because the fragility of the acquired financial systems resulted from the accumulation of imbalances generated by the regional wave of changes. Although it seems that the nature of the changes is endogenous, the transition from one regime to another was much more complex and it involved both internal and external factors, at least under the form of the recommendations formulated by the international institutions and of the external influence which generated an adaptive behaviour by ***imitation***. Furthermore, the structure of the internal financial system of these countries was not adapted to such opening – the lack or insufficient development of the financial sector didn't allow the absorption of the large volume of financial capital. The financial liberalization applied to an insufficiently developed institutional framework created favourable conditions to the accumulation of factors with systemic risk. The massive inflows of capital on the national market and the predominant presence of the foreign banks which adopted aggressive strategies of increasing their market share generated the excessive increase of the credit, particularly of the hard currency credits. This trend was encouraged by the direct relation of these institutions with the mother-banks abroad, which ensured a fast access to liquidity.

The specific elements which made more fragile the financial systems from the countries candidate to the Euro zone and which represent sources generating financial instability refer to the increasing foreign indebtedness of the economy (particularly of the private sector) through the banking system and of the proportion of the debts in relation with the revenues, but the internal conditions of these countries generated different nuances of the financial fragility. A strong fragility was noticed in the case of the Baltic States and of Bulgaria, a medium fragility was noticed in Romania, Poland and Hungary, while no fragility (robust financial system) was observed in Czechia.

The identification of the elements which define the financial instability is important to the monetary authority if it has available the special instruments needed to correct the possible fragility of the financial system. One of the conditions necessary for the management of the financial instability is the collaboration of the central bank with the other financial institutions and authorities for the exchange of information of mutual interest (Criste, Lupu, 2014). On the other hand, however, given the direct relation between the national economies of the countries candidate to the Euro zone and the activity of the foreign banks in these countries, the financial instability acquires a broader meaning than that circumscribed to the responsibilities of national central bank. The financial instability from EU member states crossed the national borders. It must be seen through the prism of the link between the interest of the foreign banks and the interest of the national economy in which the foreign banks operate, and one of the conditions for the management of the financial instability within the European Union is the cooperation between countries and between the private institutions (the large commercial banks) and the national public authorities.

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