Abstract:
The banking industry, as well as the entire financial services industry, has experienced significant changes due to the development of new technologies, government deregulation and globalization, generating both opportunities and risks. The range of financial products and services offered by the banks expanded by adding new ones previously offered by other types of entities in the financial services industry. At the same time, competition continuously increased, from both banks and from other segments of the financial industry. Thus, from risk management under traditional financial intermediation, it was reached a dynamic, active and complex risk management in terms of reduced government regulations and in an environment with higher risks. Moreover, the economic crisis triggered in 2007 brought new challenges for the banking system, revealing many weaknesses in banks' risk management practices. By using appropriate research methods, such as document analysis, interpretative methods, this paper aims to identify the challenges of risk management in banking institutions in the current context of globalization and economic crisis, when the banks should focus on a better understanding of risk and on development of new best practices to ensure efficiency of risk management and better adaptation to dynamic changes of the economic environment.

Keywords: risk management, banks, crisis, regulation, efficiency

JEL Code: G32, G21, G28

1. Introduction

The banking industry registered significant changes since ‘80s, as a result of innovation and accelerated growth in financial markets and the internationalization of financial flows.

The profits achieved by the banks as a result of traditional intermediation activities, consisting of attracting of deposits and granting of loans began to eroding more and more towards the end of the 1980s, while increasing capital adequacy requirements. Meanwhile, the competitive pressure increased in the banking market from both the banking institutions, and non-banking financial ones. To meet these challenges, banks have focused their attention to expanding the business based on superior information and knowledge management capabilities, taking advantages of the opportunities offered by technological progresses and deregulation.

Currently, these activities based on information and financial innovation are the main source of profit, while traditional bank intermediation activity is less profitable.

Internationalization and deregulation facilitated the interaction between different types of risk, both inside banking entities and to the level of the banking system, as well as favoured worsening the contagion and this way the global rapid expanding of the financial crisis through banking systems.

In this way, the financial crisis started initially in the United States in 2007 spread soon after in the EU and worldwide. The entire banking sector globally registered significant losses. However, the banking performance recorded major variations, even among banks headquartered in the same country, but also there were differences between the performances achieved by different countries’ banking systems.

Analyzing the causes which determined these differences in bank performances it was found that one of the preconditions identified for superior performance during the crisis was the adoption of the pre-crisis prudent risk management practices.
Following the detection of serious weaknesses in the banking risk management, this has become a priority of the authorities involved in the regulation and supervision both of banking systems and banking institutions.

2. Methodology of research

The aim of the present work is to present main challenges and perspectives of the banking risk management in the context of the globalization and of the actual economic crisis.

Having a predominant theoretical character, the study is using as research methodology: document analysis, interpretative methods, nonparticipative observation.

In order to achieve the research’s objective, we resorted to fundamental research by approaching the theory on issues related to risk, specificity of banking risks, banking risk management; finally a number of challenges faced by banking system during the present period are exposed.

Although it is theoretical, the paper is formulating practical conclusions applicable by the entities interested in, consisting of potential strategic and operational objectives whose implementation would bring major competitive benefit to the respective banking institutions.

3. Risks in banking activity: concept; specificity; typology

3.1. Risk concept; specificity of banking risk

In general the risk is regarded as the possibility of an event with adverse consequences towards the topic.

Legal approach delineates risk situations to situations where the losses are related to the fault of the counterparties; in this regard, the risk is seen as an external phenomenon that is impossible to be influenced by the partners.

Based on probability theory, risk can be defined in relation to instability of the expected effects, respectively as being the possibility that the results to be different from those expected. However, in ordinary language, the risk connotation is negative, risk managers being interested only in the effects that are lower than expected. Therefore, the risk can be addressed both as threat and as an opportunity to improve the initial objectives proposed to be made (Ducu CM, 2014, pp.13)

Credit risk can be defined as a negative impact of various uncertainty sources on the profitability of the bank.

Although there is no universally accepted definition for banking risk, there are three main features of banking risks recognized by specialists: the risk comes from economic instability which is prevalent in all processes of economic life; the critical point for manifestation of bank risk is dependent on the objectives of the bank; banking risk is the possibility of failure in achieving the bank’s objectives.

The most common meanings defining risk in banking are based on traditional function of banks, respectively the intermediation. From this point of view, risk is seen as a unexpected loss recorded in the banks' asset caused by the market conditions, respectively the credit or liquidity risks. In fact, banking risks are not represented only by risks specific for the traditional banking activity, but by all the risks that banks face in the current activity.

Other approaches are those related risks in terms of potential or actual losses. From this perspective, risks are seen as phenomena that occur in banking activities, causing negative effects manifested as either deterioration in the quality of business, or as a reduction of profits, or by recording losses that may affect the proper functioning of the bank.

Based on these approaches, we consider bank risk as the likelihood of achieving different outcomes from those expected, representing on the one hand a cause for recording of unforeseen negative consequences and on the other hand risk is an effect of known and unknown events.
3.2. Typology of banking risks

Banks face several risks, which may be related to:
- Late payment or non-payment from creditors;
- Depositors request for refund their money faster than the bank has scheduled;
- Changes in market interest rates, which may adversely affect the value of bank loans;
- Loss in value of the investments in securities or private companies;
- Losses due to human error in data entry or fraud on information systems.

Given that a bank faces a variety of risks, but also a variety of situations that they generate in order to respond certain interests both theoretically and practically, it was proved useful to classify these risks according to specific criteria.

The risks identified by the Basel Acords, the most important set of recommendations on the regulatory framework for banking risk at global level and on which banks focus, are as follows:
- credit risk;
- market risk, whose components are: interest rate risk; equity risk; currency risk; risk commodity risk;
- operational risk (including legal risk)

In addition to these three types of risk, there are also identified other types of risks that banks face and need to manage properly, as follows:
- liquidity risk;
- business risk;
- reputational risk.

NBR Regulation no. 5 of 20 December 2013 on prudential requirements for credit institutions defines significant risks as those risks with significant impact on the economic situation and / or reputational credit institutions.

According NBR Regulation no. 5/2013, the main risks identified as being faced by the banking institutions are as follows:
- market risk - caused by adverse movements in market prices (stock prices, interest rates, exchange rates);
- model risk - the effect of errors in the development, implementation and use of internal models that underpin certain decisions;
- credit risk - consequence of failure by debtor of contractual obligations;
- country risk - determined by events occurring in a foreign country;
- transfer risk - resulting from foreign exchange restrictions imposed by the government of the debtor’s country and it is manifested through inability of a debtor to convert local currency into foreign currency and therefore to make debt repayments in the foreign currency;
- liquidity risk - determined by the credit institution's inability to meet its obligations at their maturity;
- legal risk - consequence of the fines, penalties and sanctions which the credit institution is liable in the event of failure or misapplication of legal or contractual provisions, but also of the fact that the contractual rights and obligations of the credit institution and / or its counterparty not are set properly;
- interest rate risk - the result of adverse changes in interest rates;
- risk related to information technology (IT) – led by by inadequacy of IT strategy and IT policy, of information technology and information processing with respect to management capacity, integrity, controllability and continuity or misuse of information technology;
- reputational risk - caused by unfavorable perception of the image of a credit institution by customers, counterparties, shareholders, investors and supervisory authorities;
- strategic risk – caused by changes in the business environment or adverse business decisions, improper implementation of decisions or lack of responsiveness to changes in the business environment.

In terms of risk exposure of a bank, banking risks are classified into pure risks and speculative risks (A. Olteanu, FM Olteanu, L. Badea, 2012).

Pure risks are those risks for that loss is the only possible outcome; they may actually be materialized in losses from banking activities related to events that are beyond the bank’s control and, therefore, a person cannot consciously take on pure risk. The forms of the pure risks are: physical risks (material damage, accidents); financial risks (loss of data, loss settlement tools, destruction of archives); liability risks (nonobservance the rules, errors in operation documents, manage accounts etc.); criminal risk (fraud, theft, embezzlement, etc.)

Speculative risks are the opposite of pure risks and can be materialized in gains or losses as a result of actions taken in order to maximize profits, either as a result of aggressive lending policies (loans not repaid at maturity) or of the losses to the portfolio of securities under their volatility, either due to a defective structure of bank assets (eg shares held in non-bank companies when they do not achieve their goals of profit).

Given allocation in the banking system, we can delineate the banking risks (Nitu I., 2000) into:

- diversifiable risks - which end up being relatively insignificant in their division to a sufficient number of balance sheet items, so the law of large numbers can be activated. For these types of risks is possible to design a specific protection.
- nondiversifiable risks – which cannot be reduced to an insignificant level by internal treatments specific protection.

Depending on the range of banking transactions that may engender risks and on the form of these risks, we identify three main categories of risks which can be grouped under the main types of risk assumed by a universal bank, summarized in Table no. 1:

<table>
<thead>
<tr>
<th>Bank feature</th>
<th>Risk category</th>
<th>Type of risk</th>
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<tbody>
<tr>
<td>Business environment</td>
<td>Environmental</td>
<td>Competitive risk</td>
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<tr>
<td></td>
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<td>Economic risk</td>
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<td>Legal risk</td>
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<td>Risk of fraud</td>
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<td>Provided banking services</td>
<td>Provision</td>
<td>Operational risk</td>
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<td>Technological risk</td>
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<td>Risk of new products</td>
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<td></td>
<td></td>
<td>Strategic risk</td>
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<tr>
<td>Balance sheet management</td>
<td>Financial</td>
<td>Credit risk</td>
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<td></td>
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<td>Liquidity risk</td>
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<td>Interest rate risk</td>
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<td>Currency Risk</td>
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<td>Risk of insolvency</td>
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</tbody>
</table>

Source: Synthesis conducted by author

Of all the financial risks are in permanent interaction. Therefore, excessive exposure to credit risk may generate liquidity risk in a situation where the bank liquid assets, decreased as a result of default loans, are not sufficient to fund operations and cover its outstanding obligations. In turn, liquidity risk may pose a risk of insolvency, if the bank is unable to quickly obtain scarce resources. Moreover, due to the banking market integration and the high degree of interconnection issues faced by a bank may negatively affect the partner banks generating systemic risk and enhancing contagion effects.
4. Banking Risk Management: basic elements; process; regulatory

Bank risk management is the entire set of processes and models used by banks to implement risk-based policies and practices, whose common goal is to enhance the risk-return profile of the bank.

Given that any present potential risk may be a certain loss in the future, the objective of the risk management function is that each bank risk can be identified before the event effects, even when designing or promoting a product or service, in order to be then monitored and controlled at all levels of banks and for all activities. However, taking into account that the risks are not as visible and tangible as income or costs, one of the challenges of risk management which affects the credibility of the measures is the measure of risk.

This is why during the latest approximately two decades were dominated by the emergence of numerous models and risk management tools designed to quantify and monitor risks. Adoption of risk-based practices has accelerated and expanded to the entire banking industry, the main reasons being: strong incentives on banks to act in this direction; guidelines issued by regulators regarding the risk measurement and the defining risk-based capital; risk management modeling tools were significantly enriched for all types of risks.

With regard to the regulatory framework for risk management in Europe, this has experienced changes over the past two years. The recent developments are contained in the following documents:
- Directive 2013/36 / EU of the European Parliament and of the Council - contains provisions on reiteration of the principle of proportionality and risk-based provisions regarding the treatment of risks, including clearly specifying the risk management function, its coordinator and risk management committee, duties and responsibilities of the management body in relation to risks;
- Regulation U.E. No. 575/2013 - contains additional disclosure requirements with respect to the objectives and risk management policies.

At national level, NBR Regulation no. 5 of 20 December 2013 regarding prudential requirements for credit institutions regulates the administration frame of credit institutions in Romania, the internal assessment process of capital adequacy and conditions of outsourcing activities of credit institutions.

Regarding the administration framework of the activity, the Regulation provides that credit institutions are responsible for the existence of a such a framework rigorously designed, adapted to the nature, scale and complexity of the risks inherent in the business model and activities developed by them.

Responsibility for implementing such a framework to ensure the effective and prudent management of the credit institution belongs to management body.

This framework should include at least the following:
  a) organizational structure and organization;
  b) the governing body of the credit institution, namely: roles and responsibilities, composition and functioning, general framework for the activity;
  c) risk management;
  d) internal control;
  e) information systems and business continuity;
  f) transparency requirements.

It is also provided that risk management within a credit institution means:
  a) the existence of a culture of risk;
  b) the existence of a risk management framework;
  c) the existence of a policy for the approval of new products.

Regarding the risk management function, NBR Regulation no. 5/2003 provides that credit institutions to dispose of such a distinct function which fulfills the following conditions:
- to be independent from operational functions, with sufficient authority, importance, resources and access to the governing body;
- to be a central component in the credit institution and structured so that it can implement risk policies able to control the risk management;
- to ensure that all significant risks are identified, measured and properly reported.

The role of the risk management function within the credit institution is extremely important, ensuring that it has effective risk management processes, involved in:

a) developing and reviewing strategies and decision-making;
b) analysis of related party transactions;
c) identifying the risks of complex legal structure of credit institutions;
d) assessment of significant changes;
e) internal risk measurement and evaluation;
f) monitoring of risks;
g) issues of unapproved exposures.

The overall risk management model in any banking institution includes the following steps:

- Identifying potential risks in product / specific banking activities;
- Assessment / risk measurement, which involves expressing the equivalent value of potential losses that generate credit risk events;
- Monitoring and controlling risks, which aims extent to which banking activities are carried out according to regulations as well as continuous updating of risk profile related to each product;
- Mitigation of risks, namely the implementation of action plans established as a result of the risk assessment and the measures taken in case of risk indicators that exceeded the acceptable level of risk;
- Documenting and reporting risks to the bank structures responsible for monitoring and control and / or to the banking supervisor (BNR) or other institutions that manage credit risk information (Credit Bureau, National Office for Prevention and Control of Money Laundering, etc.).

5. Challenges and perspectives of banking risk management in the context of globalization and the current economic crisis

During the crisis, and especially in recent years significant changes have been recorded in the affairs of the banking institutions, which were manifested by activity shrinking due to a contraction of the market and to an increased competition, as well as by reducing revenue margins; in addition to these challenges banks face difficulties related to the implementation of new regulations on risk management requirements, quantitative and qualitative extended capital requirements, requirements on liquidity, as well as conditions on credit risk of the counterparty. There are opinions that the new requirements introduced by Basel III Capital Accord would lead to reduced interest on financing of the credit institutions, and that a challenge will be represented including by the banking industry's ability to achieve profit.

In front of these challenges banks' leadership reacted by placing the risk management as top priority. The focus of the risk teams transferred nowadays from measurement, compliance and control to the mitigation of problems in the areas of lending, allocation of capital, liquidity and funding.

Reviewing the issues encountered by banks this period and analyzing the factors considered by various analysts that have contributed to this situation, we summarize the challenges faced by the banks management, representing also potential strategic and operational objectives, as follows:
Developing an effective risk culture
Initially, especially among emerging countries, it was not given proper attention to cultivating a culture in terms of risk among employees, since developing a risk culture takes time and involves more stakeholders.

The situation changed in the current economic and banking environment in which credit institutions are compelled to deal promptly with existing and emerging risks. Under these circumstances, it is important to involve actively in risk assessment the functions of business, of risk and of control, with clear definition of the responsibilities of all parties involved and their commitment to action to develop the culture of risk across banks. This requires from all interested parties, among other things, better communication: from the specialists needed to present aspects of risk in a language and in terms that can be understood by all those involved and from others functions increased efforts are needed to understand the risk issues.

Improve the collection of receivables
Losses from bad loans rose continuously and significantly during the current economic crisis, affecting this way the results of the banks and even their proper functioning. The solution to this problem involves on the one hand, the identification and implementation of actions regarding the bad loans that may have an immediate impact on bank performance, on the other hand supporting the implementation of improvements in the management of credit on the recovery strategy, on structures and organizational processes as well as on systems.

Developing innovative and effective risk models
Lending decision is needed to be much better supported with information about the client, which means that banking institutions to develop their own risk models incorporating quantitative and qualitative factors as relevant for taking a decision.

Rethinking the capital allocation
Bank capital is a scarce resource and more and more insufficient. To support business growth and achieve the potential profit, banks must effectively use the capital resource and understand very well what the current capital consumption is and optimize its use.

Develop an overview on risk exposure and focus on the significant risks
Given the multitude of risks which a bank faces, as well as their different relevance at different points in time, it is important the bank to be aware of major categories of risk namely credit risks, market risks and operational risks, and within them to pursue different types of risks, such that there is a general, comprehensive picture over the risk. Given that banks often lack the tools and the refinement needed to keep pace with the rapid changes taking place in the banking products, it is important to continually following their risk framework and to monitor developments the various risks in real-time in order to be able to pay the necessary attention and act effectively.

Centralization of key processes and their coordination at the top level, with clear definition of roles and responsibilities
Effectiveness of risk management can be achieved only if its application is consistently across banks, in accordance with policies and procedures developed by the risk experts with relevant experience in the country, industry, type of client; however, the decision is in conformity with the developed risk management framework that provides protection against unwanted risks.

Risk management is the responsibility of everyone, not just of risk department, but this requires a clear assignment of roles and responsibilities to each member of the organization. Furthermore, the organization's leaders themselves must be an example to employees regarding conduct prudent to risk management, which is key to success.
Assessment the risk exposure as well as benefit versus cost related to the risks management

A good example in this regard is represented by the risk of derivatives on credit risk which has not been seriously assessed; if it had been adequately assessed and were quantified benefits of such risks, probably the acquisitions volume of such securities would have been much lower, and the problem would have been limited to the original source, meaning mortgage market overheating in the USA. Lesson to be retained by banks after what happened is that risk transactions involve consistent and rigorous assessment of the potential disadvantages and in any case can not be assumed a risk based only on the potential benefits that may result.

Implementation of IT systems to support the risk management process

IT systems represent critical assets for delivering necessary information to decision makers. Value of IT systems is justified and realized only if they are designed starting from the needs of users such as to ensure the technology necessary to the controlling and compliance monitoring, database market research instruments, industry analysis tools and means of communication as well.

6. Conclusions

Core business of a bank is risk management, which involves taking over the risks, their transformation and their incorporation into products and services, with the ultimate aim of offering to shareholders a better return as compared to the risk profile supported. This is also why risk sensitivity is extremely important for risk management.

Unfortunately, the credit crisis followed by global recession indicated a failure of the banking sector in developing its basic business, respectively risk management. Approaching the presented strategic and operational objectives involves effort and time, but the banks which will be able to implement them will have significant competitive benefits.

Besides superior financial performance and improved strategic management, many banks will achieve a competitive advantage because the higher capabilities they will get will implicitly lead to a higher level in terms of risk selection and price risk assessing as well as a better risk management.

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