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THE PROBLEMS AND PERSPECTIVES OF THE BANKING SYSTEM DEVELOPMENT: A GLANCE INTO THE FUTURE

Financial industry is one of the most dynamic developing industries since the Second World War. The banks as institutions are also evolving. The financial innovation has increased the competitive environment for the banking industry and is causing fundamental changes in it. Although institutions have grown in size, competition has substantially increased. This was caused by regulators, who have relaxed their rules and have allowed banks to offer new products, and, over the same period of time, to enter new markets and new business activities. Many risks arise from the fact that today's banks are engaged in a wide range of activities. They trade with all types of cash instruments, as well as derivates such as swaps, forward contracts, and options – either for their own account or facilitate customer transactions.

After the Great depression, the banking system was highly regulated and there was no room for profit and funds for the industries. The banking system faced a significant change in its focus by 1972 – from social and conservative, to more risk taking and profit – oriented. The process of liberalization begun with Walter Riston, head of the "First National City Bank". His highly educated professionals brought unprecedented profit by the more entrepreneurial usage of the financial capital. It was by that time, when new innovative financial instruments were introduced into the banking system. Attracted by heavy profits, the bankers reached, what was then considered to be the limit of the safe leverage. This led to a total abandoning of the fundamental social role of the banks. Genetically implemented in the early banking institutions in Italy. The Federal Reserve Bank estimates that in 1996, US banks possessed over 37 trillion of off-balance-sheet assets and liabilities, compared to approximately only 1 trillion dollars only 10 years earlier.

Current a crisis began in the USA with their housing bubble, which peaked approximately 2005-2006. High default rates on "subprime" and "adjustable rate" mortgages began to increase quickly thereafter. Lax regulation, deregulation of government policies and investment from the private sector had greatly increased Wall Street's involvement in higher-risk lending. Subprime mortgages increased 292 %, from 2003 to 2007. An increase in loan incentives such as easy initial terms and a long-term trend of rising housing prices encouraged borrowers to assume difficult mortgages in the belief they would be able to quickly refinance at more favorable terms.

At the moment, the banking system has liquidity problems and central banks are too busy with issuing money and they can not see the long-term effect of this

activity. One of the most important decisions from FDIC was the bailout plan in which central banks saving falling business and financial institutions. At the moment, “The Bear Stearns Companies”, “Fannie Mae” and “Freddie Mac”, “American International Group”, “Citigroup”, “Bank of America”, “Fortis bank” and many other companies have already received a bailout. The effect of this process is nationalization and more money in cash. Thus, an acute part of crisis will become quiet, but secondary effects from it, from now on, will appear. Other decision is to become bankrupt. This leads to restructuring of the banking system.

In future banks have to reconsider the trade with high – risk instruments by diversification of the risk to their portfolios. If the risk, which banks undertake was lower against lower profit, they wouldn’t have these liquid problems. Banks should be highly regulated from regulators. Banks must generate a profit from treasure bonds and the difference between the level of interest they pay for deposits and other sources of funds and the loan interest rate. This difference is referred to as the spread between the cost of funds and the loan interest rate. They shouldn’t trade with shares, derivates, forwards, options, swaps. These activities must be split between other institutions – funds, investment corporations, insurance corporations.

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