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FOREIGN BANKS - DRIVERS OF EFFICIENT DEVELOPMENT OR YET ANOTHER PROBLEM?

Tamara Vesić*,
Nikola Radić

Faculty of Business Economics and Entrepreneurship,
Belgrade, Serbia

Abstract:

Other than their capital, foreign banks also brought their paradigm of efficient business into our economic system, thus strengthening Serbia's banking system. The aim of this paper is to point out the efficiency trends of the observed banks within the period from 2010 to 2017 using efficiency indicator ratios. The criterion for selecting banks is the amount of net balance sheet assets. By comparing the financial statements of the selected banks, as well as comparing the changes in the number of banks, the employees and the amount of balance sheet assets, with the achieved results, we gain insight into the overall banking image of our country, as the obtained values approximate an image of the entire Serbian banking system. They have been empirically calculated, graphically presented and commented upon in order to create, in a clearer way, an image of the efficient business operation of the banks in Serbia.

Keywords:

banking sector, foreign banks, efficiency indicator ratio, balance sheet, income statement

INTRODUCTORY CONSIDERATIONS

The subject of the research in this paper is a comparative analysis of the publicly published regular annual income statements of the 10 largest banks operating in the Republic of Serbia, using efficiency indicator ratios. The criterion by which the banks were selected is the amount of net balance sheet assets, and as such, we used the data from the balance sheets of the following banks:

- Banca Intesa a.d. Belgrade
- Komercijalna banka a.d. Belgrade
- Unicredit Bank Serbia a.d. Belgrade
- Raiffeisen Bank a.d. Belgrade
- Societe Generale bank Serbia a.d. Belgrade
- AIK banka a.d. Belgrade
- Eurobank a.d. Belgrade
- Erste Bank a.d. Novi Sad
- Banka Postanska stedionica a.d. Belgrade
- Vojvodjanska banka a.d. Novi Sad

As the balance sheet assets of the observed banks amount to about 75% of the total balance sheet assets, the obtained values approximate the performance of the entire banking sector of the Republic of Serbia to a good extent. According to this criterion, the largest bank in Serbia is Banca Intesa a.d. Belgrade with a market share of around 15%. The survey was done on the basis of comparing the balance positions using the program Microsoft Excel. The aim of the research is to

Correspondence:
Tamara Vesić

e-mail:
tamara.vesic@vspep.edu.rs

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indicate the significance of the relations of the positions in the financial statements, so that the obtained results are usable in terms of entering into future business and financial relations.

LITERATURE REVIEW

There is a continuing dilemma regarding which banks are more successful - those that put emphasis on efficiency and permanently, carefully control their operating expenses in order to lower them as much as possible or those that place emphasis on profitability and strive to achieve the best possible returns on invested funds for their owners. To this moment, there is still no consensus on which performance assessment system is better, and whether the highest priority should be given to the concept of profitability or efficiency. Addressing this question Berger et al. (2017) inform the current debate about the efficacy of different ways of intervening and dealing with distressed banks and help fill in a gap in the literature that lacks empirical evidence on whether regulatory interventions and capital support are beneficial. Ljumovic et al. (2015) consider that in the 21st century, a good banker is the one who can provide the client with a service or advice in the right moment, i.e. the one who can satisfy the financial appetites of his clients. According to Kalas and Rakita (2017), when it comes to the efficient operation of banking organizations, the principles of liquidity and profitability are imposed as one of the most important principles of their operation. Mirkovic et al. (2016) say that when it comes to regulatory requirements, it is necessary to emphasize that the main goal of introducing Basel standards (especially Basel III), and improve the quality of regulatory capital and strengthen capital requirements, as well as to shift the focus to share capital and stricter requirements. In order to understand business performance more precisely, experts from the banking sector have developed and designed many indicators. According to Dasic (2015), besides the achievement of the profits, the goal of a bank is to provide a continuous growth and development the market. As the nature of the operation of banks differs fundamentally from the operation of companies in the non-financial sector, financial statements are also different, and their structure and content must reflect all of the specifics of banking business operations. Mishkin and Eakind (2012) say that deteriorating balance sheets and tougher business conditions lead some financial institutions into insolvency, when net worth becomes negative. Andjelic and Vesic (2016) confirm that a large number of studies related to the assessment of bank performance are focused on indicator ratios. The same author believes that when considering the decision of whether to provide credit financing, a commercial bank is most interested in first finding out the liquidity indicators of the company.

THE CURRENT STATE OF THE BANKING SECTOR IN THE REPUBLIC OF SERBIA

Lin and Wang (2018) say that intensified financial disintermediation, liberalization of interest rates, and development of online banking have reduced the profit margins of the traditional lending business in commercial banks. Although during the financial crisis the banking sector in Serbia was exposed to an intense shock, thanks to the relatively conservative policy of the Central Bank of Serbia, the sector was sufficiently resistant and the accumulated reserves were sufficient for handling all of the current and potential future negative effects of the financial crisis period. Racic and Barjaktarovic (2017) consider that the reaction of the banks that followed in response to the financial crisis, led to the decrease in the volume of placements, the growth of liquidity and a decrease in active and passive interest rates. In order to present and gain a better insight into the current situation of the banking sector in the Republic of Serbia, in this section of the paper an overview of the number of banks, the number of the employees in the banking sector and a review of balance sheet assets are presented. The above-mentioned review is systematized according to the ownership structure of the bank and it was done for the period from 2010 to 2017, according to analyses and reports from the Central Bank of Serbia.

The number of banks in the banking sector

At the beginning of the process of restructuring the financial system in the region of Central and Eastern Europe, the dominance of the banks with majority state ownership has been noted. Dimic and Barjaktarovic (2017) noted that the domestic owners did not take adequate care of their property, which resulted in a change in the ownership structure and an increase in the shares of foreign investors in the financial sector of the region. At the end of 2010, 33 banks operated in the banking system of the Republic of Serbia, as can be seen in Table 1.

Table 1. Overview of the banks in Serbia according to their type of ownership structure for the period of 2010-2017

YEAR / Number of banks	2010	2011	2012	2013	2014	2015	2016	2017
Banks owned by domestic entities	12	12	11	9	8	7	8	9
State-owned	8	8	8	6	6	6	6	6
Privately owned	4	4	3	3	2	1	2	3
Banks owned by foreign entities	21	21	21	21	21	23	22	21
Italy	2	2	2	2	2	2	2	2
Austria	4	4	3	3	3	3	3	3
Greece	4	4	4	4	4	4	4	4
France	3	3	3	3	3	3	3	2
Others	8	8	9	9	9	11	10	10
TOTAL	33	33	32	30	29	30	30	30

Source: Calculations and presentation by the author based on the data provided by the NBS

Of the total number of banks, 12 are owned by domestic entities, while 21 banks are in foreign ownership. Foreign banks come from 11 different countries and with a share of between 70% and 75% in the total assets, capital and the employees prevail in our banking sector. Until 2015, the number of foreign banks remained unchanged, while the total number of banks is slowly decreasing, due to the decrease in the number of banks owned by domestic entities due to the revoking of work permits by the Central Bank of Serbia, because their operations proved inefficient, illiquid and irrational. Thus, at the end of October 2012, the Central Bank of Serbia revoked the license of Nova Agrobanka a.d. Belgrade, on the grounds that within the stipulated deadline of 6 months after obtaining the work permit, it did not perform the harmonization of operations in the area of the capital and indicators of operations with the provisions of the Law on Banks. In April 2013, the Central Bank of Serbia revoked the license of Razvojna banka Vojvodine a.d. Novi Sad. The change in the trend of the number of banks only starts by the end of 2014, when the Central Bank of Serbia granted an operating license to Mirabank a.d. Belgrade, while Bank of China a.d. Belgrade got their operating license in 2016. In 2014, KBC Bank a.d. Belgrade changed its business name to Telenor Bank a.d. Belgrade, and in 2015 Cacanka banka a.d. Cacak changed its business name to Halkbank a.d. Belgrade, further reducing the number of domestic banks.

Number of the employees in the banking sector

By the end of 2010, the banking sector employed a total of 29,887 people. The downward trend in the number of people in the banking sector started in 2009 and continues to this day. From Table 2 we see that the number of the employees is reduced both in domestically owned banks and in foreign-owned banks.

The assets of the banking sector

The total net assets of banks in 2010 amounted to RSD 2,534 billion. From that time onwards, we can see the trend of growth in the assets of the banking sector, as shown in Table 3. Banks owned by foreign entities exhibited faster growth of assets, but despite the decrease in the number of banks, growth in total assets was also present in the banks owned by domestic entities. In terms of shares in the total assets, the banks owned by foreign entities prevail in the observed period, with more than 73% of the net assets of the total assets of the banking sector in Serbia.

The observed period ends with an increase in net balance assets by slightly more than 20% compared to the beginning of the observed period. As for the concentration of the banking sector, given the large number of banks with a small share in the total assets, but also in the total incomes, loans and deposits, it can be said that the sector is largely fragmented. Miljkovic and Ristanovic (2017) consider that the main cause of the growth of balance sheet assets is the increased intensity in lending activity. On the other hand, the highest priority goal of the banks within the Serbian economy, as is the common practice in the modern market, was to achieve a satisfactory profit rate per unit of capital.

Table 2. Overview of the banks in Serbia according to their number of their employees for the period of 2010-2017

YEAR	2010		2011		2012		2013		2014		2015		2016		2017	
Number of the employees	Number	Share (%)	Number	Share (%)	Number	Share (%)	Number	Share (%)	Number	Share (%)	Number	Share (%)	Number	Share (%)	Number	Share (%)
Banks owned by domestic entities	8750	29.3	8705	29.8	8002	28.2	7031	26.7	6383	25.4	5752	23.7	6056	25.2	6297	29,0
State-owned	7305	24.4	7216	24.7	6930	24.4	5924	22.5	5621	22.4	5142	21.2	5259	21.9	5240	22,4
Privately owned	1445	4.8	1489	5.1	1072	3.8	1107	4.2	762	3.0	610	2.5	797	3.3	1521	6,5
Banks owned by foreign entities	21137	70.7	20523	70.2	20392	71.8	19349	73.3	18723	74.6	18505	76.3	17965	74.8	16581	71,0
Italy	4015	13.4	4177	14.3	4142	14.6	4085	15.5	4114	16.4	4155	17.1	4279	17.8	4182	17,9
Austria	4260	14.3	4227	14.5	3656	12.9	3514	13.3	3396	13.5	3397	14.0	3239	13.5	2601	11,1
Greece	5934	19.9	5364	18.4	5267	18.5	5116	19.4	4894	19.5	4412	18.2	4223	17.6	3392	14,5
Franca	2525	8.4	25888	8.9	2698	9.5	2637	10.0	2596	10.3	2558	10.5	2557	10.6	2285	9,8
Others	4403	14.7	4167	14.3	4629	16.3	3997	15.2	3723	14.8	3983	16.4	3667	15.3	4121	17,7
TOTAL	29887	100	29228	100	28394	100	26380	100	25106	100	24257	100	24021	100	23342	100

Source: Calculations and presentation by the author based on the data provided by the NBS

Table 3. Overview of the net balance sheet assets in the banking sector of Serbia for the period of 2010-2017.

YEAR	2010		2011		2012		2013		2014		2015		2016		2017	
Assets of the bank expressed in billions of RSD	billions	Share(%)	billions	Share(%)	billions	Share(%)	Billions	Share(%)	billions	Share(%)	billions	Share(%)	billions	Share(%)	billions	Share(%)
Banks owned by domestic entities	671	26	685	26	716	25	730	25,6	758	25,6	729	23,9	756	23,3	795	24,2
State-owned	454	18	472	18	522	18	534	18,8	571	19,3	550	18,0	561	17,3	539	16,4
Privately owned	217	,9	213	,8	194	,7	196	6,9	187	6,3	179	5,9	195	.6,0	256	7,8
Banks owned by foreign entities	1862	74	1965	74	2163	75	2117	74,4	2210	74,5	2319	76,1	2486	76,7	2498	75,8
Italy	526	21	591	22	657	23	679	23,8	738	24,9	796	76,1	884	27,3	919	27,9
Austria	469	18	493	19	449	15	429	15,1	440	14,8	453	14,9	494	15,2	411	12,5
Greece	427	17	393	15	426	15	409	14.4	418	14,1	395	13,0	403	12,4	328	9,9
France	202	8	263	,10	287	10	299	10,5	304	10,2	316	10,4	327	10,1	350	10,6
Others	238	,9	225	8	345	12	301	10,6	310	10,4	359	11,8	378	11,7	490	14,9
TOTAL	2534	100	2650	100	2880	100	2846	100	2969	100	3048	100	3242	100	3293	1100

Source: Calculations and presentation by the author based on the data provided by the NBS

EMPIRICAL ANALYSIS OF EFFICIENCY, RESULTS AND DISCUSSION

The analysis of our banking sector was carried out for the period from 2010 to 2017, on the basis of the financial statements, i.e. the reports on the financial position and reports of the total achieved result of the banks collected from the website of the Central Bank of Serbia. It is a known rule that when calculating indicator ratios, the calculation of the average of the items from the balance sheet is done based on the values from the beginning and the end of the year. By using the average value in the analysis of a longer period of time the movement dynamics of the indicator are ironed out. In our analysis, average values were not taken for the indicators that use items from the balance sheet because the analysis was done for 7 years and the basic idea was to make the movement dynamics of the indicator more pronounced. According to Laeven, Ratnovski and Tong (2016), we find strong evidence that systemic risk increases with a bank size. Ljumovic and Knezevic (2011) say for the analysis of the efficiency of a bank's operations, numerous indicators that are classified into two groups are used: indicators of noninterest expenses and indicators of noninterest income.

Natoi and Spulbar (2016) belive that the results show that an increase in the non-interest income or changes in the structure of income will reduce the operating stability of the banking industry.

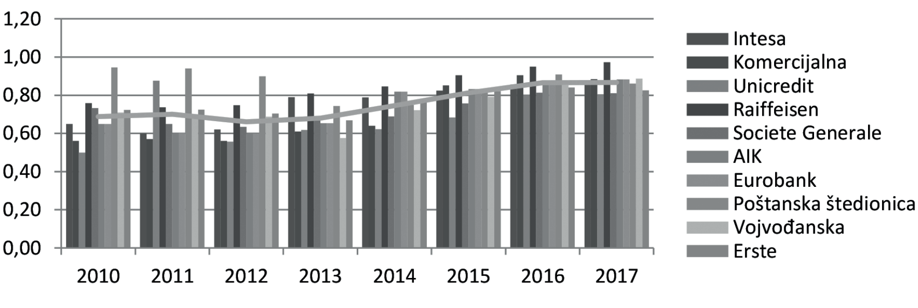
In this part of the paper, a graphical representation of the calculated indicator ratios with comments is given. In order to achieve more clarity, the charts show the values of the indicator ratios for the 10 observed banks. A particular chart is related to the particular indicator ratio and shows a graphical representation of the value of that indicator ratio for those banks within the observed period. In addition to the individual values of the indicator ratios, their average value is also shown, in order to better understand the performance dynamics of banks.

The first indicator of noninterest expenses is shown in Graph 1 and is calculated using the following formula:

$$(\mathrm{I}) = \frac{\text{noninterest expenses}}{\text{total expenses}} \tag{1}$$

From the graph we see that the share of noninterest expenses in the total operating expenses in the observed period shows a slight increase. Since there are no significant deviations from the average, banks have an increasingly smaller share of expenses based on their business, the collection of deposits. The increase in noninterest expenses is a consequence of the expenses on the basis of modern services provided by the bank to its clients, but these costs are for a good part on the rise, also due to the bank's unsecured loans.

Illustration 1. Share of the noninterest expenses in the total operating expenses



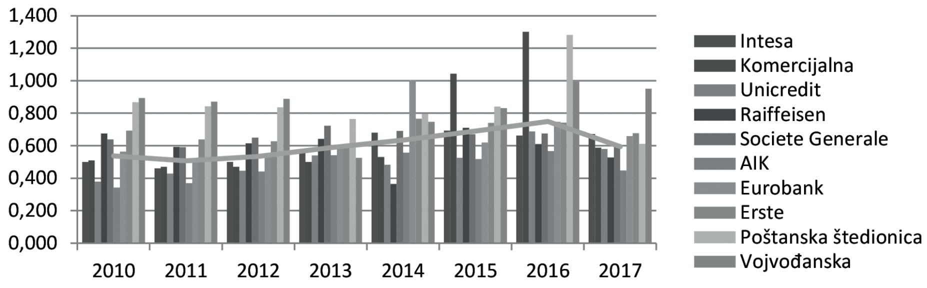
Source: Calculations and presentation by the author based on the data provided by the NBS

The second indicator of noninterest expenses is shown in Graph 2 and is calculated using the following formula:

$$(\mathrm{II}) = \frac{\text{noninterest expenses}}{\text{total income}} \tag{2}$$

On average, about 60% of the total income is spent on noninterest expenses. Given that noninterest expenses represent the value of all of the expenses of the banks, besides interest expenses, we can conclude that banks are not heavily indebted either to each other or to the Central Bank, but also that they are not able to collect new deposits.

Illustration 2. The share of noninterest expenses in the total income

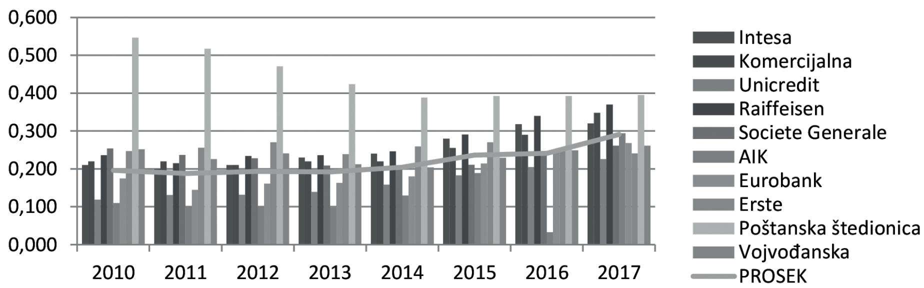


Source: Calculations and presentation by the author based on the data provided by the NBS

Noninterest income indicators are made up by the first ratio as the ratio of noninterest income and the total operating income, and the second ratio as the ratio of noninterest income and average total assets. The first indicator of noninterest income is shown in Graph 3 and shows stable movement, meaning that during the observed period there were no significant changes in the structure of the income of the banks.

In total income, slightly more than 25% is represented by noninterest bearing income, meaning that in most banks, income based on their core activity, loan approval, is dominant. The exception is Postanska stedionica a.d. Belgrade, which in 2010, 2011 and 2017 realized about 45% of the noninterest income.

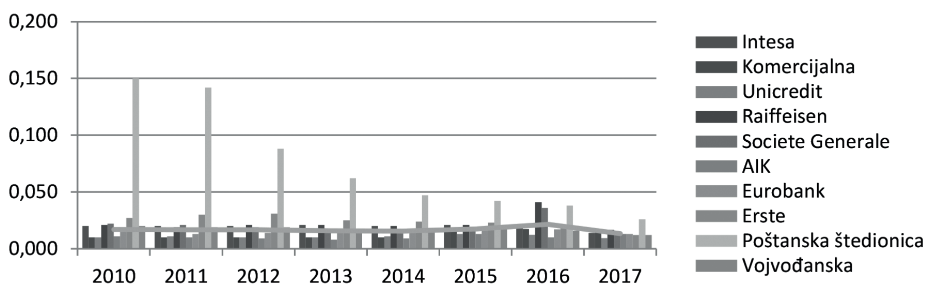
Illustration 3. Share of the noninterest income in total income



Source: Calculations and presentation by the author based on the data provided by the NBS

The second indicator of non-interest income shows the share of noninterest income of the average total assets, and in Graph 4 we see that this share is almost constant during the observed period, with a tendency of growth in 2016, after which it saw a slight decline. A large amount of noninterest bearing income is realized by Postanska stedionica a.d. Belgrade, because the values of this indicator for other banks are far below its values.

Illustration 4. Share of the noninterest income in the total assets



Source: Calculations and presentation by the author based on the data provided by the NBS

CONCLUSION

Roganovic et al. (2017) stated that today, in the conditions of globalization, the economic interdependence of states is greater than ever before. During the transition process, as Serbia opened up towards foreign capital, significant owner transformations and changes in the ownership structure of banks have occurred. Foreign banks became the owners of a portion of state-owned banks, and the number of domestic-owned banks decreased during the observed period. The Central Bank of Serbia has withdrawn its operating licenses, primarily due to the conduct of inefficient and irrational business policies. However, the efficiency of the banking sector has been improved as the foreign banks transferred their paradigm of efficient business along with their capital. Despite the downward trend in the number of the employees and the number of banks, we can see that the banking sector's assets have exhibited a trend of growth, which confirms that, among other things, banks are operating efficiently.

After calculating and graphically representing the indicator ratios, we get an insight into the financial performance of banks in our banking sector. According to Lukic and Trsic (2015), higher efficiency ratios indicate a lower risk, but also lower profitability of the bank, and vice versa. Vukosavljevic et al. (2016) believe that trends in unsecured loans show that banks could have a very big problem, and Kalas and Rakita (2017) consider that although the primary objective of banks is profit, it is necessary for banking organizations to function as economic flows by enabling the availability of cash to business entities and other participants present on the market. The problem in the operation of banks occurs in the collection of their loans because, due to the slowed economic activity, clients are increasingly less able to timely and fully settle their obligations. However, through everyday innovations in the banking sector, banks are attempting to improve their efficiency, the ultimate effect of which is profitability, as the main business motive of banks is the achievement of the greatest profits possible.

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