

# Strategic tools for the formation of leadership positions of Ukrainian banking business in a global competitive environment

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## Abstract

With the economic growth of Ukraine, taking into account the experience of world leading banks, it is necessary to modernize the financial policy in the country in order to strengthen the competitive position of the banking business in global markets. In this regard, the article shows the key activities of the National Bank of Ukraine in the context of compliance with the principle of independence of the requirements of the Basel agreements and EU directives, as well as developing favorable conditions for the functioning of commercial banks, businesses and improving macroeconomic indicators.

*Keywords:* National Bank, inflation, lending, global competition, foreign investment, financial regulation, foreign exchange transactions, leadership

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## 1 Introduction

The National Bank of Ukraine (NBU) is the main regulator of the country's financial sector and the subject of increasing its international competitiveness. At the end of 2018, it managed to achieve the planned relatively low inflation and lower interest rates. Price stability is the most important goal of the NBU, fixed at the level of the law. Last year, inflation surpassed the 10% mark and in the end of the year, it was at 9.8% level. This means that the regulator approached its target of  $6 \pm 2\%$  (inflationary target), although it did not reach it. The hryvnia exchange rate remained flexible. The interest rate of 14.5% in 2017 and 18% in 2018 is still one of the highest in the world [1].

One digit inflation is a win. To do this, the NBU had to keep high interest rates and maintain currency restrictions, which adversely affected the development of lending and economic growth. But from the point of view of a longer-term perspective, this price was not paid for nothing: the "roller coaster" in prices has not yet brought any economy to the good result.

So then, in the coming year, inflation at 5% is hardly achievable, the rate of 7.4% is in the budget, and the NBU forecasts inflation at no more than 7%. Moreover, even if the National Bank repulses politicians, there are other factors uncontrolled by the regulator: global growth is slowing, raw materials markets are unstable, Europe seasaws because of Brexit, the "yellow vests" and the Italian budget, the US trade war with China continues. And Ukraine still has foreign currency debt, - payments on it in 2019 will amount \$13.5 billion [2].

There is also a risk posed by Ukrainian politicians: a departure from inflation targeting in favor of low interest rates and concessional loans. These slogans attract by imaginary simplicity, but the popular solution does not lead

to prosperity, but to the failure. Ukraine has a very high risk of default on debts, and it is not covered by European or world rates of 2–5% per annum. Sustained growth requires a solid foundation, but not card houses.

The goal in the Strategy-2019 includes the banking system that is resistant to macro-shocks and systemic risks, the standards that meet the standards of Basel III and EU directives, improved quality of loan portfolios, corporate governance that meets best practices, and international financial institutions do not refuse to maintain relations with Ukrainian banks.

The latest crisis cost Ukraine 38% of GDP, so it is extremely important to prevent its recurrence in the future. In 2018, two banks entered the liquidation stage (compared to 70 in 2015–2017), and the banking system ended the year with a profit. Although the peak of the crisis has passed, the banking system is far from ideal stability. The last stress testing showed that 8 out of 24 banks that had passed the test needed additional capitalization. But now, there is only one such bank. At least one of the 11 standards of the NBU (data as of December 1, 2018) was violated by 25 banks. The accumulated volume of problem loans is the largest in state banks - 68% of the portfolio, in private and foreign (except for those related to the Russian Federation), the situation is better – 24% and 39%, respectively [3].

During 2018, the National Bank has actively reformed and tightened the requirements for the stability of banks, seriously revised the processes in banking supervision, introduced international standards for assessing bank resilience and stress testing, ordered banks to introduce independent directors to supervisory boards. Banks themselves do not share many of the ideas of the regulator and prudential requirements, so they may still be adjusted.

Taking into account the global trend, an important strategic objective of banking policy is the constant reduction of bank troubled debts, the growth of the bank

loan portfolio at a level not lower than the growth rate of nominal GDP, the reduction of banks' credit risks. The cost of loans in the past year did not decrease, but rather increased along with the increase in the NBU rate. Accordingly, lending, with the exception of the consumer segment, was restrained. While in the countries with an average level of economic development, domestic loans for private sector have almost reached GDP volume, and in Poland and Turkey, they have made up about half of it, in Ukraine, they decreased from 90% in 2008 to 35% in 2017.

The fact is that price containment and an increase in lending are two goals from which it is always necessary to choose one. They have one instrument of achievement - a change in the discount rate, but it acts in opposite directions. The rate increase holds back inflation, but makes loans more expensive. Reducing the rate contributes to the availability of credit, but raises prices. The objectives of the NBU, formulated in the legislation, put price stability in the first place. Therefore, lowering rates is a matter of future steady and low inflation.

Another opportunity to form the leading positions of the Ukrainian banking business in global markets is to protect the rights of creditors. Nowadays, the worst trouble of the system are problem loans. Borrowers refuse to pay on them and withdraw assets from bail, taking advantage of gaps in the law, corrupting judges or officials. Protected rights are better prospects for repaying loans, which means lower risks, which means lower risk payments in the interest rate structure, and therefore, finally, cheaper loans. The relevant law, to the development of which the NBU joined, should help, but not immediately. As in the case of the stability of the banking system, the rule of law, high quality courts, and the political will to provide that are required.

An important role in getting the leading positions by Ukrainian banks in global financial markets is occupied by the expansion of currency operations, the deepening of Ukraine's integration into international capital markets, the increase in foreign investment in the economy, and the increase of financial and tax transparency of businesses and individuals.

Legislative changes were mostly managed to implement. In 2018, the Law of Ukraine "On Currency and Currency Transactions" was adopted. The law allows the regulator, at its discretion, to simplify the conditions for foreign exchange transactions and capital movements, which was previously impossible. While the regulator is not in a hurry: free capital flow was laid on the altar of inflationary stability, along with the revival of lending. The restriction was lifted only partially, investments in Ukraine were almost never received, even if compared with not the super-successful 2004–2007, but with the conditional stagnation of 2011–2013. The next step in this direction - countering the erosion of the tax base (BEPS) and the withdrawal of profits abroad - faces serious resistance from the interests of the owners of large businesses represented in parliament. This is again a matter of rule of law.

One of the priorities for improving the global competitiveness of Ukrainian banks is strengthening the protection of the rights of consumers of financial services, expanding companies and the public's access to financial

infrastructure, developing remote and innovative banking products, using IBAN account numbers, speeding up payments, improving financial literacy of the population, expanding electronic document circulation, improving the efficiency and competitiveness of the banking system as a whole.

For example, financial inclusion is when citizens and businesses have access to useful and affordable financial products and services that meet their needs: transactions, payments, savings, loans or insurance, regardless of income, age, residence or activity. The National Bank does not formulate the goal of the percentage of coverage of citizens or small business with traditional or innovative banking products neither in the strategy for 2018, nor in the strategy for 2019, and does not provide statistics.

A positive moment there is the launch of Bank ID. This system allows to work with a bank account online. Progress in financial technologies will push IBAN - international account numbers, which make it possible to standardize interbank payments. The NBU also reports on the growth in the share of non-cash payments from 39% in 2017 to 44% in 2018 and an increase of 14% in the POS-terminals network. It is quite a good result, given the unsteady trust of people. However, many Ukrainians still do not have the physical ability to use financial products, especially in rural areas. Traditional, rather than innovative online or mobile banking, is declining in regions, - over the past two years, the number of operating bank branches decreased from 10,000 to 8,500. In its NBU report, this issue was missed.

The way the NBU's goals on financial inclusion are designed shows more the regulator's interest in another trend - reducing cash use, or "cashless". This is certainly related to inclusion, but not identical to it. Whether people in the regions are ready to change the receipts in the branches to mobile applications, or will the postmen continue to deliver monetized subsidies and pensions in the form of cash in the future, is an interesting question for sociologists only. For politicians, new or old, access of citizens to high-quality financial services is unlikely to be a priority.

## 2 Conclusions

Recently, the National Bank received an award for transparency from the international specialized magazine "Banker" on the activities of central banks and financial regulators of Central Banking. It really has become more open, publishes a lot of data and analytical reviews, minutes from committee meetings, etc. But the main political challenge for the NBU is to preserve its independence. And this is our main reserve for increasing the global competitiveness of the banking system as a whole.

Whether a new composition of the parliament will provide changes, is a question for billions - these are the amounts that are put offshore each year. There is reason for optimism here: tax transparency and the complication of working with tax havens is a global powerful trend. Such trends are lobbied at the highest world level and are quite capable to destroy the interests of individual corrupt officials. For Ukraine, in the following years, the support of western partners is very important. The system can resist for a long time, but in the end, it should come to civilized rules.

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