Marko
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SLOVENIA

Marko Voljč started his career in the National Bank of Slovenia, which was then part of the system of the National Bank of Yugoslavia. In 1979 he joined the World Bank, serving as the first Head of Resident Mission in Mexico and the Head of Central America and Panama Division. In 1992, he became the CEO of Nova Ljubljanska Banka (NLB), the largest bank of Slovenia, where he successfully carried out the rehabilitation and partial privatisation of the bank. In 2004, he joined the KBC Group in Brussels, serving as the CEO of K&H, the second largest bank in Hungary, and as the Group ExCo member responsible for Russia, Central and Southeastern Europe, before retiring in 2015. He is currently a financial advisor to various international groups. He is also active in the NGO field in the SEE region.

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Fifteen years have passed since eight Central European (CE) and Baltic countries joined the EU, followed at later dates by three Southeastern European (SEE) countries. The anniversary is a good opportunity to take stock of the road travelled by the banking sector in these countries. and its achievements and challenges.

As a practicing banker, I was asked to share my personal experience in the countries I dealt with during the mid-nineties until now. Mine is more a testimonial and a subjective account of the evolution in the banking sectors of various CE (Poland, Czech Republic, Slovakia, Hungary, Slovenia) and SE countries (Romania, Bulgaria, Croatia) than a rigorous analysis of these countries' banking systems.

A quick look back at the period before the collapse of communism and market socialism reveals that, even in centrally planned countries, banking sectors evolved in somewhat different directions. On the one hand, there was a model that was emulating the Soviet framework of a mono bank (examples being Romania, Bulgaria and, to a certain extent, the former Czechoslovakia). On the other hand, a more decentralised system that was following the (timid) market reforms in other Eastern countries (Poland, Hungary, the former Yugoslavia) with central banks and "commercial banks"

borrowing abroad and from the IFIs. These nuances in the role and organisation of the banking systems to a certain degree stemmed from the socioeconomic systems in the region which had evolved over decades. The so-called reformers (Poland, Hungary, ex-Yugoslavia) allowed for a somewhat bigger role of the market than did the other countries. The international trade patterns also reflected these differences, with reformers trading more with the convertible currency areas of Europe and the rest of the world. All of this forced the banks in these countries to be more attuned to market forces.

The reforms following the fall of communism had a dramatic impact on the banks in the region where two groups of countries evolved: one group embarked on fast liberalization and privatization of their economies and financial systems (Czech Republic, Hungary, to a lesser degree Poland). The other group was still relying on the dominant role of the state in the banking system (Slovenia, Croatia, Bulgaria, Slovakia and to some extent Romania).

The above mentioned different starting positions and the initial attitude toward market reforms was also reflected in the role of foreign direct investments (FDI) in the region's banking systems. The faster reformers saw the penetration of foreign strategic owners into their banking institutions proceed much faster than the laggards. Many Western European financial groups (to a lesser extent US investors) sensed the historic opportunity to enter a promising market, one with significant potential for economic growth and largely underbanked. The most active investors came from mid-sized Western European countries (such as Austria, Belgium or Greece) although some strong players emerged from the larger EU member states as well (Italy, France, Spain, to a lesser degree Germany). The larger the market in CE and SEE (e.g., Poland) the bigger the interest and willingness to pay a higher price for an existing banking asset.

By the late 1990s there was a robust penetration by foreign strategic investors into Czech Republic, Poland, Hungary, followed a few years later by Romania, Croatia, Bulgaria and Slovakia. Slovenia was a special case to which I will turn later.

Thanks to this aggressive arrival of Western European banking and insurance groups into the region, financial intermediation in CE and SEE experienced its first "leapfrogging", narrowing the gap with Western Europe even prior to official EU membership which started in 2004. The opening up of trade and investment flows, the arrival of hundreds of experienced Western bank executives and financial experts had a profound impact on the banking landscape of CE and SE Europe by the early 2000s.

Most of the foreign groups came to the region with the idea of staying for a long time ("forever", as my Western European boss would mention quite often!). That had an impact on their attitudes, as many saw CE and SEE as their second home market (this could certainly be said for the Austrian, Italian, French, Greek, Portuguese and Belgian groups) and wanted to be fully integrated in the community while expanding their stakeholder base.

Complementing the political and market reforms, and the growing presence of foreign capital in the banks of the region, was also the regulatory framework that most of the countries started to shape along the lines of Western European models as part of the EU accession negotiations. This process was another manifestation of the "soft power" EU exerted on the aspiring member states!

When the "Big Bang" finally came on May 1, 2004, when ten new member states joined the EU, their banking systems were already humming along at full speed. By that date, roughly two-thirds of the banking assets in the Czech Republic, Slovakia, and Hungary were already foreign owned. Poland kept several large banks under state control, whereas in Slovenia political and public opinion did not favour foreign ownership in general and in banking in particular. Even in other countries in the region which had not yet joined the EU (Romania, Bulgaria, Croatia), foreign ownership of banks exceeded 50% by mid-2000s.

The leading role of foreign strategic ownership in CE also resulted in a somewhat more pronounced market concentration than before. While the largest banks in Poland and Hungary, respectively, were not owned by strategic foreign investors, in all four Visegrad countries (Poland, Czech Republic, Slovakia, Hungary), the top four or five banks accounted for more than 60% of the market. A similar pattern of market concentration was soon followed by the banking sectors in Rumania, Bulgaria and Croatia.

The period following accession in 2004 saw a financial deepening of these economies where the banks played a key role - stock markets and non-bank financial intermediaries were at an incipient stage, as was the regulatory framework governing them. During the years 2004-2008, we witnessed an extremely fast growth in bank lending in the region, coupled with strong external borrowing. What was particularly noticeable was intense household borrowing in Euros and Swiss francs which later on, with the currency corrections, caused serious distress in many banking systems in the region.

Generally speaking, the years leading to the Great Recession saw a growing sophistication in the product and distribution channels of CE and SEE banks, thus making banks in the region increasingly similar to their counterparts in the Western part of the continent.

What was not yet up to date in the fast development of the banking systems was the regulatory and supervisory framework, both in the "old" as well as "new" member states. This made the crisis even deeper. In the CE and SE countries where banks were predominantly owned by foreign strategic investors the burden of capital increase and enhanced risk management techniques was borne by the Western parents, thus avoiding pressure on public finances in the host countries. Only in Slovenia, with more than 50% of the banking assets in state hands, was the post-crisis restructuring of the banks financed by public money and increased domestic debt.

Coping with the Great Recession in the region also depended, to a large extent, on the macro politics and institutional capabilities in individual countries. For example, Poland, with its sizeable domestic market and prudent macro policies, never experienced a real recession at the time when all other member states had negative economic growth for a couple of years. Other more advanced new member states (Czech Republic, Slovakia, Hungary) had an institutional framework in place which enabled a relatively smooth transition from the overheating of the pre-crisis period to more sustainable, prudent banking policies with improved supervision and risk management know-how. In the less advanced financial policy environments in SE Europe (Romania, Bulgaria, Croatia plus Slovenia with its slow and inappropriate reaction to the deepening economic crisis), the process of banking adjustment to the post-crisis conditions and standards was somewhat more time consuming and costlier.

After the crisis, the banking system in the region with the strong support of their parent groups from Western Europe (also based on ECB policies of quantitative easing), became better equipped to cope with the changing market conditions, to an extent becoming safer and better managed than in some of the Southern European countries. One could say that, following the years after 2009, CE and SE European banks have converged with their counterparts in the West, in many areas (digitalization, distribution channels, marketing) surpassing the more established banks in the "old" Europe.

The restructuring, increased capital requirements, ever more demanding prudential regulations and increased risk awareness over the past ten years have significantly lowered the appetite of the traditional strategic investors from the West. Many of

those banking groups which came to the CE and SEE region in the 1990s with the intention to "stay forever" have either exited or significantly reduced their presence in the region. This was due largely because of challenges and limitations imposed by the financial authorities supervising the parent banks. As a result of these developments, we are witnessing the dominance of a few foreign strategic investors in more mature and still lucrative markets (Poland – Banco Santander, Unicredit bank, Commerzbank, Czech Republic – Erste, Société General, KBC, Slovakia - Raiffeisen bank, Erste, Intesa) and the resultant further market concentration. Also, we are now seeing the entrance of large (mostly US based) Private Equity firms (Apollo Private Equity, Advent International) entering (at least temporarily) the CE and SEE banking institutions, buying banking assets either from the state or from the exiting Western banking groups (Slovenia, Croatia, Bulgaria). In Hungary we witnessed the emergence of the biggest bank in the country - OTP - as a SEE regional powerhouse, with significant market shares in Serbia, Croatia, Bulgaria, Montenegro, and Romania. Finally, we see some attempts by national governments to increase their ownership of banks with the intention of keeping some of the banking sector in government and/or domestic private sector hands (Hungary, Poland, Croatia).

In sum, the past two decades have seen some dramatic developments in the CE and SEE regions - if in the mid- to late 1990s, banking in the region was a world apart from the one in Western Europe, this difference has largely disappeared. The level of knowledge and sophistication in banking in these regions has by now reached a level on a par with mature Europe. The same could be said of the supervisory and regulatory frameworks and the level of knowledge and relative independence of financial authorities from political interference, closely linked to the accession process and the ECB's new role with the Single Supervisory Mechanism. The convergence with Western European banking and in some instances, the leapfrogging, continues to this day. The challenges facing banks and bankers on both sides of the EU are becoming increasingly similar.

I feel fortunate and privileged to have been an active participant in this exciting journey!