Global Megabanks in Poland in 1998–2005: Do Size and Ownership Matter?

Globalne megabanki w Polsce w latach 1998–2005: wpływ wielkości banku i jego struktury własnościowej na decyzje strategiczne i wyniki finansowe

Ewa Miklaszewska, Katarzyna Mikołajczyk***

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Abstract

This paper analyses the impact of global financial mega-institutions on the Polish banking market in 1998-2005: a period of a dynamic economic growth, connected with Polish accession to the EU and a new wave of foreign capital inflow, coming mainly into medium-sized banks. The research question posed is whether size and ownership structure matter when it comes to the strategies and profitability of banks? The paper, analysing various balance sheet ratios computed by the Authors, offers a positive answer to this question, particularly when analysing the group of medium-sized banks, belonging to global mega-institutions. For them, the support from owner's technology, operations, human capital and corporate culture seems to constitute an important competitive advantage, resulting in a dynamic growth and superior financial results.

Keywords: megabanks, bank strategies, bank profitability, foreign capital in banks.

JEL: G21

Streszczenie

Celem artykułu jest analiza wpływu globalnych megainstytucji finansowych na polski rynek bankowy w latach 1998–2005 – w okresie dynamicznego napływu kapitału zagranicznego, głównie do średnich banków. Na podstawie analizy danych bilansowych w artykule stwierdzono, że szczególnie ciekawa transformacja dokonała się w analizowanym okresie w bankach średnich, kontrolowanych przez globalne megainstytucje finansowe. W artykule przeanalizowane ich specyficzne strategie i źródła wysokiej rentowności, opartej głównie na ekspansji kredytowej na wybranych obszarach niszowych, co pozwoliło większości z nich osiągnąć bardzo dobre rezultaty finansowe i przyspieszony wzrost aktywów.

Słowa kluczowe: megabanki, strategie bankowe, rentowność banków, kapitał zagraniczny w bankach

* Cracow University of Economics, Chair of Finance; Jagiellonian University in Krakow, Faculty of Management and Social Communication, e-mail: umiklas@cyf-kr.edu.pl
** Cracow University of Economics, Chair of Finance, e-mail: efmikola@cyf-kr.edu.pl

1. Introduction

In recent years, the globalisation of financial markets and waves of mergers in the financial sector have resulted in the maturing of a group of large, global and in most cases complex financial institutions. For those globally active banks with assets above 100 billion US dollars, which derive most of their income from third countries, the term "megabanks" has been coined (Walter 2002). It is probably too early to judge on their overall long-term impact on the banking industry. On the one hand, megabanks provide, globally, high quality financial services and positively contribute to competition and efficiency of the local markets, by bringing low cost products and technological innovations. On the other hand, they are sometimes accused of bringing "less choice, higher price, scarcer credit" by concentration on the most profitable banking services and pushing out local banks out of those areas. Moreover, additional problem of mega institutions operating in a relatively small country may not be the traditional threat of asymmetric relations, but on the contrary – the possibility that megabanks may not be interested enough in influencing corporate practices and managerial culture in host countries and do not contribute adequately to local market's development. Thus in the first two paragraphs the paper discusses the rationale for creation of global megabanks: tendencies in the global markets, evolution of bank scale, scope, geographic diversification and organisational structures, and their advantages and threats for public policy.

The main focus of the paper is to analyse the impact of selected global megabanks on the Polish banking market, in terms of strategic decisions and choices affecting individual and overall bank efficiency in 1998–2005 – a period of dynamic economic growth, connected with Polish accession to the EU in 2004 (paragraph 4). For banks, this was a period of a new wave of foreign capital inflow. There is a substantial body of literature on transition banking, addressing the question of the impact of foreign entry on banks' efficiency, particularly during privatisation processes (for the review of empirical findings see Bonin et al. 2004). The paper focuses on the relatively recent foreign entries, particularly those of global financial mega-institutions. Foreign capital had first entered large banks as part of mass privatisation program *via* IPOs in the early 1990s. In the analysed period, the medium-sized banking group was actively penetrated by foreign capital, and increased competition in this segment has resulted in the reshaping and differentiating of their strategies. The main research question posed is whether size and ownership structure matter when it comes to the strategies and efficiency of the analysed banks. To answer this question, bank strategies and performance are analysed, based on their ba-

Table 1. *15 largest complex financial institutions: their dominant position in major banking fields*

Bank, country	Equities	Bonds	Syndicated loans	Interest rate derivatives	Foreign exchange	Custody assets	Number of categories with a dominant position
Citigroup, US	5	1	2	4	1	4	6
Deutsche Bank, Germany	9	4	4	2	3	5	6
Credit Suisse, Switzerland	6	6	8	-	4	-	4
JP Morgan Chase, US	-	5	1	1	-	3	4
Barclays, UK	-	10	5	8	6	-	3
Goldman Sachs., US	2	9	-	6	-	-	3
HSBC, UK	-	-	10	-	2	9	3
Societe General, France	8	-	-	9	-	10	3
Bank of America, US	-	-	3	3	8	-	3
Lehman Brothers, US	7	8	-	-	-	-	2
Merrill Lynch, US	1	3	-	-	-	-	2
Morgan Stanley, US	4	2	-	-	-	-	2
UBS, Switzerland	3	7	-	-	-	-	2
ABN Amro, Netherlands	-	-	-	-	7	6	2
BNP Paribas, France	-	-	-	5	-	7	2

Source: Marsh, Stevens (2003).

Table 2. *Banking market concentration: assets of five largest credit institutions as % of total assets*

Country	2005	2001	1995	1990
Belgium	85	78	54	48
The Netherlands	85	82	76	73
Finland	83	80	69	53
Portugal	69	60	74	58
Denmark	66	68	74	76
Greece	66	66	76	83
EU-15	54	52	51	50
Sweden	57	88	86	70
France	54	47	41	42
Ireland	46	43	44	42
Austria	45	45	39	35
Spain	42	53	46	19
The UK	36	30	27	n.a.
Luxembourg	31	28	21	n.a.
Italy	27	29	26	19
Germany	22	20	17	13

Source: For 1990-2001 based on CEPR (2005, p. 41), for 2005 based on ECB (2006b, p. 54).

lance sheet ratios, within two groups of banks: the large and medium ones (paragraphs 5 and 6).

2. The creation of global megabanks

Historically, M&A were principally undertaken as a cost-cutting devise, as a measure for increasing economies of scale or synergy based on economies of scope or, alternatively, mergers were seen as a strategic reorientation move. More controversial goals included assets and profits' diversification. The worst results were attained when expansion was politically motivated, as in the case of French Credit Lyonnais in the 90s. In all the above cases, reaction to competitive conditions was a decisive force. Hence, since the 90s, another goal has emerged as crucial – economies of geographic diversification for globally expanding banks.

In the EU, research has showed the following major motives for mergers (classification based on the ECB Reports: ECB 2000; Cabral et al. 2002):

– for small banks, economies of scale were typical (efficiency focus),

– for larger banks, strategic reorientation was important (brand-based economies of scale or expansion to capital markets),

– diversifications of risk and assets was also frequently mentioned,

– expanding into the insurance business was viewed as important for expanding and stabilising the depository base.

In some European countries, overcapacity in retail banking has also been an important driver for merging (Smith, Walter 2003, p. 363). Many of these reasons are controversial, particularly for large banks, as economies of scale are largely exhausted for banks with relatively small assets (Boot 2003). Diversification, on the other hand, may lead to problems with corporate culture in huge conglomerates, particularly between the commercial and investment part of the business. Thus, analysing concentration processes, the important factor may be globalisation of the financial market, which has been a response to economic forces, and at the same time a major challenge, forcing firms and customers to adjust or to reshape their strategies. For many firms, competing on global market and generating profits in external areas, rather than in the home market, has become the dominant strategic priority. Consequently, globalisation has increased not only the scale, but also the risk and complexity of financial institutions (Table 1) and ultimately has resulted in the increased concentration in many national banking markets (Table 2).

In 2005, in the EU-25 the CR-5 average was 60%, with the most concentrated market being Estonia (98%), Lithuania (81%) and Malta (76%), and the least concentrated Poland (49%) and Hungary (53%) (ECB 2006b, p. 54). The concentration in Europe is still in progress, and 2005 acquisitions of HVB by Unicredit (18 billion US dollars in value, subsequent to former acquisition of Bank of Austria), or 2004 mergers between Santander and Abbey National (16 billion US dollars) or between Royal Bank of Scotland and Charter One (10 billion US dollars) and the 2007 fight for the acquisition of Dutch ABN-AMRO are cases in point.

The long term effects of the concentration processes on national markets and global expansion of national banking leaders have been the creation of a new type of financial institution: megabanks, described by Walter (2002) as global financial services companies, with assets above 100 billion US dollars and global strategies and coverage. Moreover, globalisation of financial markets has been an equally strong factor as regional financial integration – in the EU, banks have complained that a lack of a fully integrated home market has resulted in a lack of strong economies of scale, which has intensified competition with huge American financial firms, allowing American banks to dominate the wholesale market (The Economist 2005). However, it is interesting to

Table 3. *The World's largest financial services firms (market value, in billions of US dollars, III 2007)*

	Bank	Country	Profit	Assets	Market value
1	Citigroup	US	21	1,884	247
2	Bank of America	US	21	1,459	226
3	HSBC Holdings	UK	16	1,860	202
4	ICBC	China	4	800	176
5	American Int. Group	US	14	979	174
6	JPMorgan Chase	US	14	1,351	170
7	Berkshire Hathaway*	US	11	248	163
8	Bank of China	China	3	585	143
9	CCB-China Const. Bank	China	5	568	126
10	Mitsubishi UFJ Financial	Japan	6	1,585	124
11	Royal Bank of Scotland	UK	12	1,705	124
12	Wells Fargo	US	8	482	117
13	UBS*	Switzerland	9	1,776	116
14	Banco Santander	Spain	7	945	115
15	Wachovia	US	7	707	105
16	BNP Paribas	France	9	1,898	97
17	UniCredito Italiano	Italy	2	922	96
18	Barclays	UK	8	1,949	94
19	Intesa Sanpaolo	Italy	3	321	92
20	BBVA	Spain	5	536	82

* classified as Diversified Financials

Source: Based on Forbes (2007)

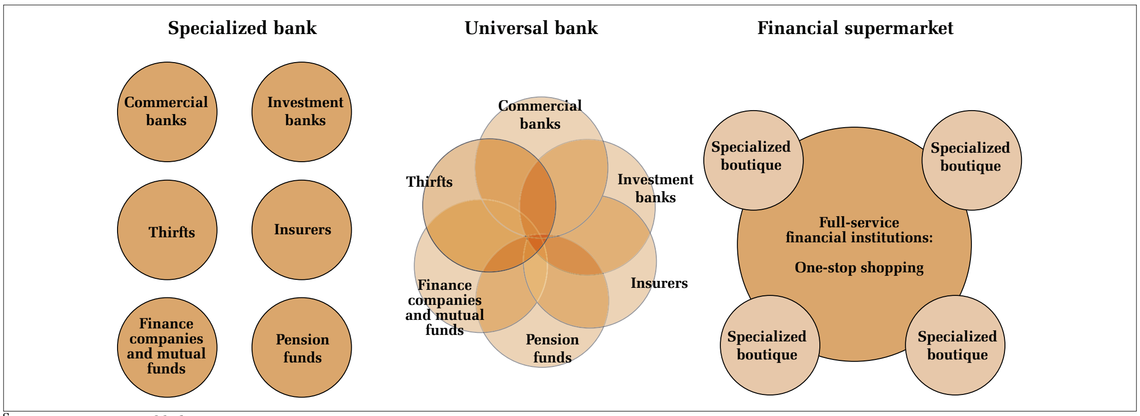
observe that also in retail banking, where success should largely be based on relationships and access to local knowledge and experiences, American banks have also been very effective in both European and global markets (Table 3).

A megabank can be structured as a simple and focused firm, or as a complex conglomerate, defined by Joint Forum as a firm that undertakes at least two out of three basic financial activities: banking, insurance, securities.[1] The rationale behind the creation of megabanks is not necessarily the complexity and multiplication of products. Some financial mega-institutions have based their global expansion on just a handful of loan-related products and the dominant defining feature is their strategic approach, based on consumers and market. As can be seen in Figure1, they are buyer-integrated financial companies, and not vendor-integrated specialised banks (Smith, Walter 2003, p. 364).

Citibank was a pioneer in the strategic orientation towards the creation of a financial supermarket. J. Reed, the bank's president in 1984-2000 period, established its position as a leading US and global commercial bank. Initially Citibank stressed its commercial nature and aimed strategically at the creation of a "McDonalds of finance": a simple and efficient mass market firm. Its strategic focus was to become "the smallest large bank" – a global institution based on a strong relationship with selected markets and customers (Lee 1996). However, increased competition resulted in the necessity to undergo fundamental change in 1998 - the sudden merger with Travellers Group, a diversified financial services company engaged in investment services, asset management, insurance and consumer lending. John Reed commented the strategic shift by saying: "*commercial banks that have succeeded in converting themselves into*

[1] Joint Forum, established in 1996 by Basel Committee on Banking Supervision, The International Organisation of Securities Commissions and the International Association of Insurance Supervisors defined conglomerate as *"any group of companies under common control whose exclusive or predominant activity consists of providing significant services in at least two different financial sectors"*, www.bis.org/bcbs/jfhistory.

Figure 1. *Evolution of bank scope and scale*



Source: Santomero, Babbel (1997, p. 613).

Table 4. *Tendencies in distributing retail banking products in the EU*

Provision channels	2000	2005	2010*
Branch	70	42	30
Internet	4	18	28
Phone	5	9	12
ATM machines	19	29	28
Other	2	2	2

* Estimates based on bank survey.
Source: Based on Capgemini (2006, p.18).

investment banks generate average returns on equity of between 12%-14 %, well below the 20% that successful commercial banks achieve. The problem is that this market is not growing." (quoted in Boot, Thakor 1997). For Citicorp, the reorientation turned out to be successful – today the corporation services 200 million customers in a global market of over 100 countries, generating large profits in both commercial and investment activities. Former Citibank's strategy of a simple and friendly bank was adopted by other American giant institutions, such as AIG or General Electric (GE), which have successfully entered the banking field.

GE, established in the 19th century by Edison, nowadays the largest global conglomerate, attained in the '80s, under Jack Welch's leadership an AAA status and global low cost competitor image. Welch, like J. Reed of Citibank, based his strategic thinking on building the firm's strong identity. In the financial area, in the '80s and '90s the financial arm of the corporation (GE Capital) established itself as an independent bank, successfully competing on global financial markets. J. Immelt, President of the corporation since 2001, has declared further aggressive competition on the global financial market and direct competition with megabanks such as Citigroup and HSBC, largely by adoption of former Citibank strategy – creating a customer-friendly, simple and efficient global megabank. As Immelt put it: *„Banks are perceived as unfriendly. We want people to think about us the way they feel when they walk into a store"* (Engen 2004). In order to support strategic evolution towards an integrated industrial-financial conglomerate, in 2002, formerly independent GE Capital was directly incorporated into the whole corporate structure and divided into retail GE Consumer Finance (GE Money) and corporate CE Commercial Finance, GE Insurance and GE Leasing. Consequently, today almost half of GE profits came from its financial segment. GE Consumer Finance (GE Money) operates in 40 countries, in 16 of these having banking licences. In consumer finance, its strategy is implemented by product concentration on loan-related products (car loans, mortgages, personal loans, sales finance). Other areas are of minor importance (Engen 2004).

In the future, the drive for global banking coverage will be further supported by technological progress, as illustrated in Table 4. Branch-based barriers to entry to national banking markets are of diminishing importance, as customer are increasingly willing to use remote and cross-border channels for provision of banking products.

3. Megabanks and public policy

Historically, very few failures have occurred among the nation's largest banks, as they have tended to have a better access to funding sources, more diversified portfolios and more sophisticated risk management techniques. However, new global megabanks are not simple projections of the universal type of institutions in the German style. They are integrated financial services companies, active in many fields and in many geographical areas, generating profits largely outside the home country. Their emergence creates a number of questions. A regulatory dilemma is posed not only because of their scale, but also because of the complexity of their operation. A large global commercial bank, efficiently regulated and with insured deposit base, can pose a smaller threat to stability than a relatively smaller but much more complex financial institution, offering commercial, investment and insurance activities in many overlapping fields.

G10 report (quoted by Jones, Nguyen 2005) has stressed, as their main risks, geographic diversification, operational risk associated with complexity and difficulty of monitoring and potential credit risk, associated with the fact that today's megabanks rely on non-depository sources of funding which can be withdrawn at a short notice. The report has concluded that it is yet not clear whether the size of today's megabanks make them more or less likely to fail, in comparison with the largest banks of ten years ago. Moreover, as Dermine has pointed out, mega institutions can pose a moral hazard of being too big to fail, counting on the public support in a case of financial difficulty, as in the famous case of French Credit Lyonnais (Dermine 2000). The bankruptcy of a giant institution licensed in a relatively small country may constitute a serious blow to the domestic economy. Their scale may also negatively influence relationship banking, important in some banking areas. For example, empirical data showed the negative correlation between the scale of a bank and accessibility of credit line for smaller

Table 5. *The European customers banking survey (answers in % of total)*

I do not want to see the emergence of a handful of pan-European "super banks"	Agree	Disagree	Don't know
All	46	26	27
Czech Rep.	50	24	26
France	37	35	28
Germany	74	10	15
Italy	21	45	34
Netherlands	50	23	27
Poland	41	22	37
Spain	25	48	26
Sweden	36	32	32
Switzerland	57	22	21
UK	67	12	22

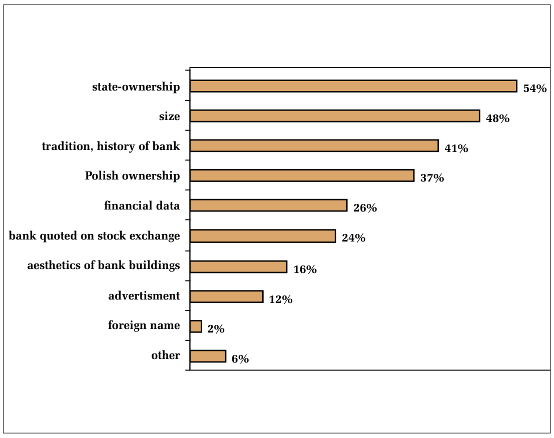
Source: KPMG International (2004, p.8).

customers.[2] On the other hand, global megabanks spread a uniform standard of products and services, increase domestic competitive pressures and offer domestic customers a bigger choice. Thus the negative side-effects may be outweighted by increased competition, which benefits customers and banks alike.

European customers do not have a unified attitude towards large global banking institutions, as illustrated by various surveys. For example, Table 5 contains the results of the European customer survey about public opinion on future of European banking conducted by KPMG in ten European countries in 2004. Based on this survey, one can draw the conclusion that although European consumers do not want a few megabanks dominating the whole banking market, in some countries (Spain, Italy) they approve of having a better choice – to be able to benefit from competition and cooperation of a number of banks, both domestic and foreign. Poles and Czechs were close to the average for the whole group. Also when asked whether they supported the creation of a unified European financial market, 90% of the responses were affirmative, which also suggests that the foreign institutions are not perceived as a major threat, once they operate in a well developed and deep market.

Polish banks, until 1989 owned almost exclusively by the State, today host almost every European country's capital. Strong presence of foreign capital is characteristic also for almost all East-European countries, with the exception of Slovenia, and has been largely transition-related: lacking domestic financial sources and experience, most East European governments opted for an active involvement of foreign banks in the privatisation processes. However, although the majority of Polish banks are foreign owned, Polish customers in various surveys have also stressed the attachment to Polish names

Figure 2. *Why customers trust their banks?*



Source: Pietrzak (2003, p. 183).

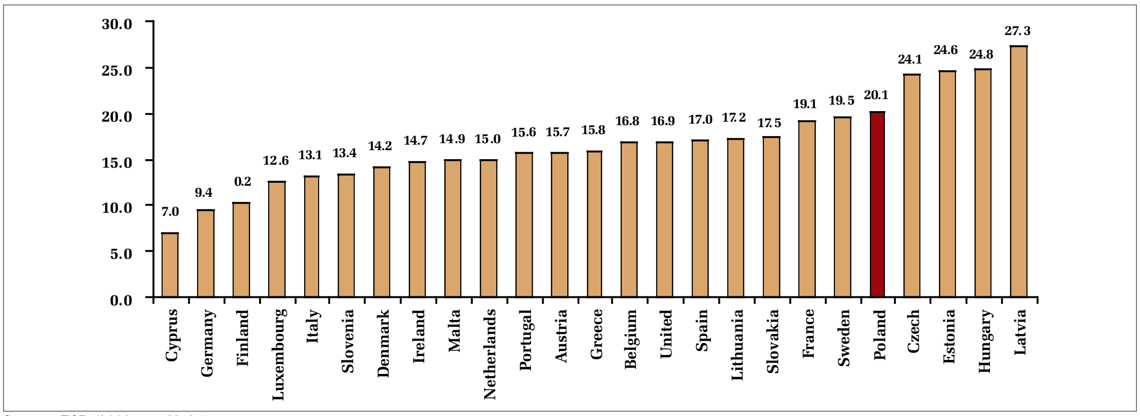
[2] The reasons for banks' inefficiencies in providing basic services are analysed in Carbo et al. (2005).

Table 6. *The structure of Polish banking sector's assets (in % of total)*

Banks	1993	1998	2000	IX 2006
Commercial, of which:	93.4	95.7	95.8	94.0
a. State-owned	80.4	45.9	22.9	20.4
b. Privately owned, (of which foreign owned)	13.0 (2,6)	49.8 (16,6)	72.9 (69,5)	71.6 (67,6)
c. Branches of credit institutions	-	-	-	2.0
Cooperative	6.6	4.3	4.2	6.0
Total Assets	100	100	100	100

Source: NBP (2006).

Figure 3. *The profitability of banking sector in EU: average level of ROE, 2005*



Source: ECB (2006a, p. 63-64)

and control, as illustrated by Figure 2, which makes the issue of foreign ownership politically very sensitive.

4. Global megabanks in Poland

The issue of foreign capital penetration is particularly important in Poland, where at the end of 2006 almost 70% of banking sector's assets were foreign owned (Table 6).

Almost since the beginning of the transformation processes, Polish banks could be divided into 3 groups: the largest banks, universal in nature; the group of about 20-30 medium-sized banks, mostly retail or specialised; and the largest group of the smallest banks, many of them of cooperative status.[3] Foreign capital inflow initially centred on the largest banks and this has turned out a profitable long-term investment. For 2004–2005, Poland found itself among the most profitable European banking systems, with the average ROE above 20%, way above the average Eurozone level, although less than for certain other East European countries, headed by Latvia and Hungary (Figure 3).

In the early and mid 1990s, the dominant issues for most banks were those of expansion and restructuring,

[3] The authors' classification of banking groups for the largest 50 banks is illustrated in the Appendix.

Table 7. *Dynamics of growth for large, medium and small banks' group, 2002-2005 (%)*

	Assets growth	Loans growth	Deposits growth	Securities growth*	Net profit growth	Branches growth	Employment growth
Large banks:							
2003/2002	2.0	5.6	1.2	4.1	-15.1	-9.7	-6.9
2004/2003	3.7	-3.8	2.3	-2.7	269.6	-12.2	-2.8
2005/2004	6.6	7.3	7.8	9.7	46.6	x	-3.3
average	4.1	*3.0*	*3.8*	*3.7*	*100.4*	*-11.0*	*-4.3*
Medium banks:							
2003/2002	17.9	28.9	19.5	14.9	25.4	8.8	7.1
2004/2003	31.1	28.8	19.5	0.5	90.2	17.8	25.4
2005/2004	23.1	24.4	22.6	13.9	19.5	x	16.8
average	*24.0*	*27.4*	*20.5*	*9.8*	*45.0*	*13.3*	*16.4*
Small banks:							
2003/2002	30.9	42.9	17.3	17.8	x	-13.8	-4.9
2004/2005	16.0	25.0	15.4	-39.3	60.1	13.1	-6.9
2005/2004	24.8	13.0	26.8	71.8	29.0	x	3.8
average	*23.9*	*27.0*	*19.8*	*16.8*	*44.6*	*-0.4*	*-2.7*

* for 2005/2004 Securities and Investment.
Source: Authors' estimates based on banks' balance sheet data in "Bank" magazine, 1998-2006.
Note: Authors' classification into banking groups is explained in the Appen0dix.

Table 8. *Balance sheet ratios by bank groups; 1998-2005*

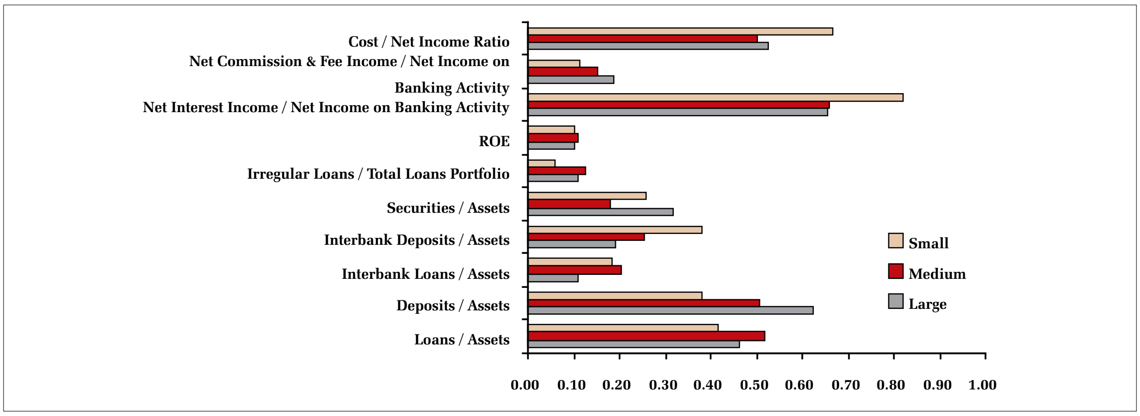
Groups	Year	Loans /Assets	Deposits/Assets	Interbank Loans/ Assets	Interbank Deposits/ Assets	Securities*/Assets	Irregular Loans / Total Loans Portfolio	ROE	Net Interest Income / Net Income on Banking Activity	Net Commission & Fee Income / Net Income on Banking Activity	Cost / Net Income Ratio	Net Profit / Employment (in thous. zl)
Large banks	1998	0.46	0.62	0.11	0.19	0.32	0.11	0.10	0.65	0.19	0.53	32
	2000	0.46	0.61	0.17	0.21	0.25	0.15	0.12	0.55	0.22	0.54	37
	2002	0.48	0.66	0.13	0.11	0.27	0.21	0.00	0.54	0.24	0.60	-1.5
	2004	0.44	0.69	0.18	0.08	0.29	0.16	0.11	0.54	0.32	0.64	45
	2005	0.43	0.71	0.17	0.07	0.31	0.13	0.19	0.52	0.28	0.60	83
Medium banks	1998	0.52	0.50	0.21	0.25	0.18	0.12	0.11	0.66	0.15	0.50	109
	2000	0.53	0.51	0.26	0.28	0.13	0.19	0.04	0.63	0.20	0.59	53
	2002	0.48	0.43	0.23	0.34	0.19	0.27	0.07	0.56	0.19	0.63	79
	2004	0.51	0.43	0.24	0.34	0.17	0.08	0.16	0.63	0.17	0.60	101
	2005	0.53	0.43	0.24	0.35	0.16	0.07	0.14	0.61	0.19	0.62	108
Small banks	1998	0.42	0.38	0.18	0.38	0.26	0.06	0.10	0.82	0.11	0.67	19
	2000	0.45	0.35	0.28	0.40	0.18	0.16	0.05	0.76	0.18	0.66	19
	2002	0.45	0.41	0.33	0.32	0.15	0.34	0.19	0.82	0.11	0.98	8
	2004	0.62	0.85	0.18	0.01	0.12	0.07	0.16	0.67	0.32	0.66	20
	2005	0.57	0.86	0.21	0.01	0.15	0.06	0.18	0.70	0.27	0.67	23

Source: Authors' estimates based on banks' reports.
** for 2004 and 2005 Securities and Investments.*

Figure 4. *Selected balance sheet ratios by bank groups; 1998-2005*

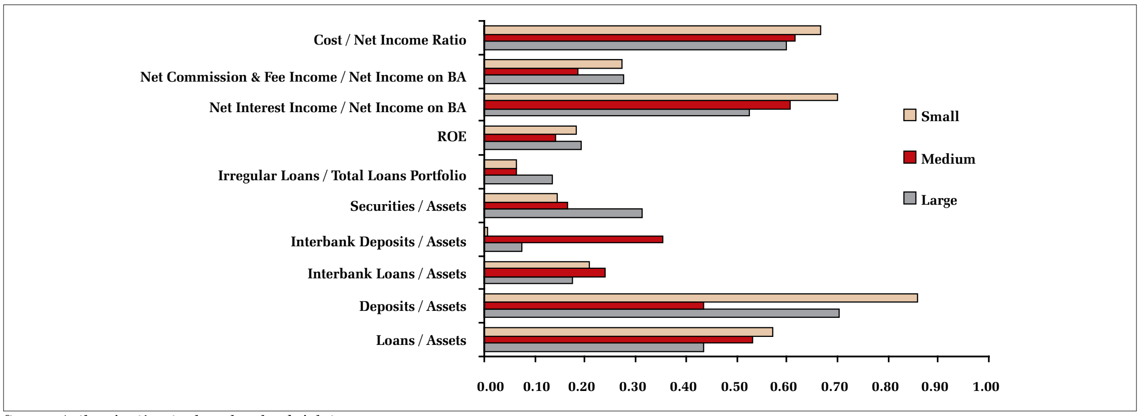
Source: Authors' estimates based on banks' data.

Figure 5. *Polish banks – major ratios, 1998*



Source: Authors' estimates, based on banks' reports

Figure 6. *Polish banks - major ratios, 2005*



Source: Authors' estimates based on banks' data.

and changes centred on the largest banks. However, the period 1998–2005 has been very important also for the medium-sized banks. They were subject of inflow of new foreign capital, which brought different priorities and strategies and far-reaching restructuring. Consequently, today the distance between the largest and medium-sized banks is diminishing, as the dynamics of growth is much stronger in the medium banks' than in the large banks' group (Table 7). The small banks' group is also dynamically growing and is led by increasingly profitable cooperative banks.

Analysing major balance sheet ratios for all groups of banks (Table 8, Figure 4) leads to a number of further observations:

- The large banks are cost efficient and universal in nature (highest proportion of securities in assets). They have large deposit base and are less dependent on loans and more on securities trading than other groups of banks. Except for 2002, they are also highly profitable.
- Medium banks have the smallest deposit base, but well developed loan-products, which results in their necessity to borrow on the interbank market, which, however, does not hinder their profitability (growing ROE, highest profit/employee ratio).
- Small banks are most traditional in nature (deposits and loans oriented), particularly in 2004-2005 period, but least cost-efficient. They are overstaffed, with smallest profit generated per employee.

At the beginning of the analysed period, the small bank group was significantly different, while large and medium-sized banks were following similar strategies, with exception of investment activities (Figure 5). 2002 was a bad year for all groups of banks, particularly for the large banks. However, financial difficulties have forced those banks' to restructure, allowing them to rebuild their profitability. 2005 to some extent reversed the situation of the 1998: the large and small banks developed many similar balance-sheet characteristics (with exception of the universalism) while the medium–sized group has become increasingly different (Figure 6). Some major changes in the groups' characteristics are thus of a recent nature.

5. Ownership and bank performance of large banks, 2002–2005

In the 1990s, the foreign capital inflow initially focused on the large banks. Consequently, this group has been first to complete the basic transformations in terms of product, technology or strategy definition. Now they are following quite a similar universal bank strategy, as illustrated by Table 9 and Figure 7, which compare selected balance-sheet data for the ten largest banks' average and for the major banks, Polish and foreign owned.

As can be seen from the above data, ownership by foreign or Polish capital have not dramatically influenced large bank strategies: all analysed large banks,

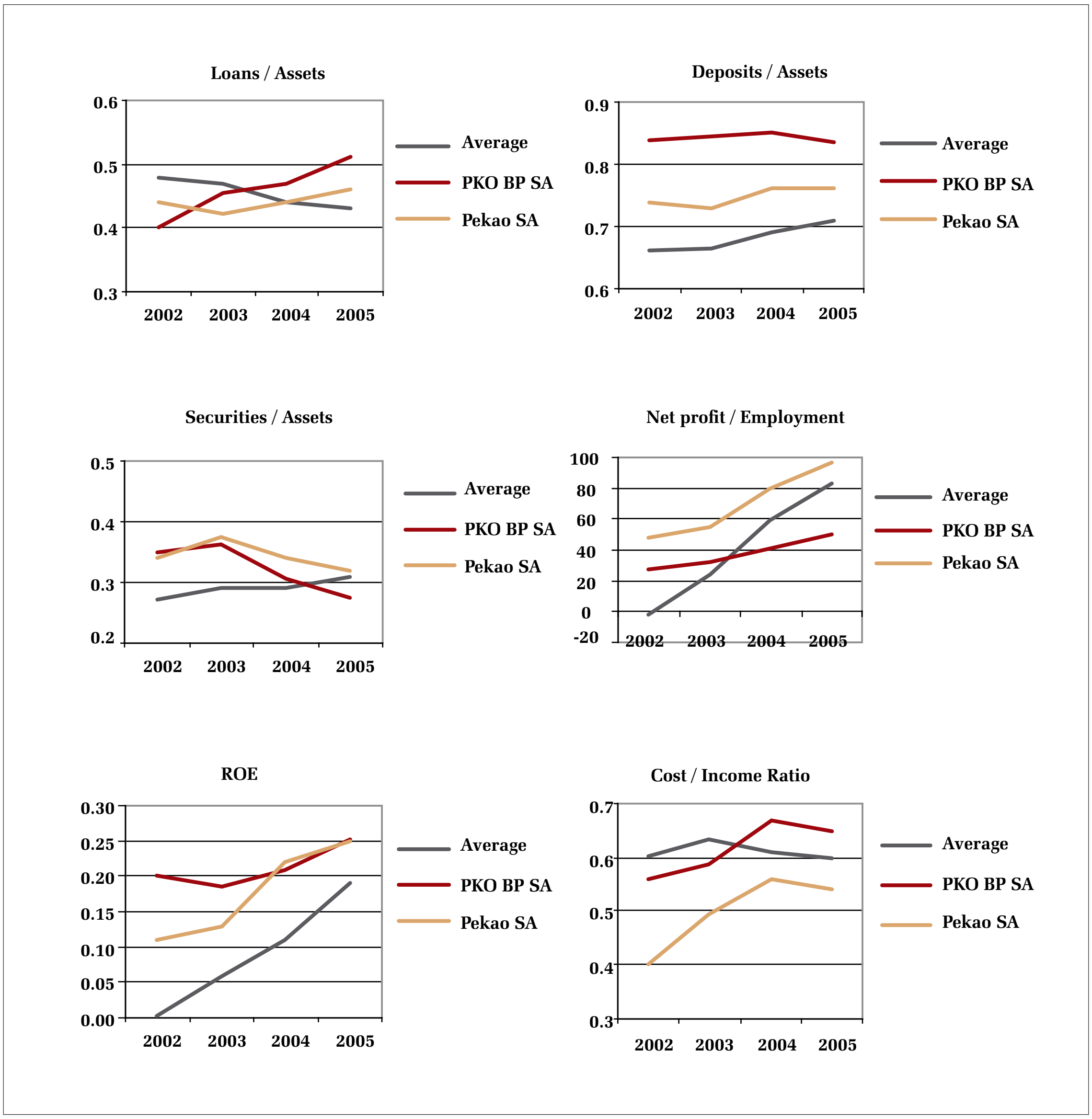
Table 9. *Foreign megabanks in the Polish large banks: 10 banks' average and selected banks' ratios, 2002-2005*

Name	Loans/Assets	Deposits /Assets	Interbank Loans/Assets	Interbank Deposits/Assets	Securities*/Assets	Irregular Loans/Total Loans Portfolio	ROE	Net Interest Income / Net Income on Banking Activity	Net Commission & Fee Income / Net Income on Banking Activity	Cost/Net Income Ratio	Net profit/Employment
Year 2002											
Large banks: average	0.48	0.66	0.13	0.11	0.27	0.21	0.00	0.54	0.24	0.60	-1.5
PKO BP SA (Treasury)	0.40	0.84	0.14	0.02	0.35	0.08	0.20	0.62	0.19	0.56	28.1
Pekao SA (Unicredit)	0.44	0.74	0.13	0.04	0.34	0.21	0.11	0.60	0.24	0.40	47.7
Bank Handlowy SA (Citigroup)	0.42	0.52	0.14	0.10	0.32	x	0.04	0.33	0.24	0.52	51.4
Year 2003											
Large banks: average	0.47	0.66	0.13	0.10	0.29	0.23	0.06	0.52	0.29	0.64	23.8
PKO BP SA (Treasury)	0.45	0.85	0.10	0.01	0.36	x	0.19	0.64	0.25	0.59	32.6
Pekao SA (Unicredit)	0.42	0.73	0.10	0.04	0.37	x	0.13	0.58	0.34	0.49	54.3
Bank Handlowy SA (Citigroup)	0.39	0.54	0.24	0.11	0.24	x	0.05	0.38	0.28	0.58	59.3
Year 2004											
Large banks: average	0.44	0.69	0.18	0.08	0.29	0.16	0.11	0.52	0.31	0.61	59.1
PKO BP SA (Treasury)	0.47	0.85	0.15	0.01	0.31	x	0.21	0.64	0.29	0.67	40.9
Pekao SA (Unicredit)	0.44	0.76	0.11	0.02	0.34	x	0.22	0.54	0.38	0.56	80.1
Bank Handlowy SA (Citigroup)	0.31	0.50	0.24	0.10	0.34	0.29	0.12	0.49	0.28	0.66	94.5
Year 2005											
Large banks: average	0.43	0.71	0.17	0.07	0.31	0.13	0.19	0.52	0.28	0.60	83.0
PKO BP SA (Treasury)	0.51	0.83	0.14	0.02	0.28	x	0.25	0.63	0.21	0.65	50.0
Pekao SA (Unicredit)	0.46	0.76	0.12	0.03	0.32	0.19	0.25	0.54	0.37	0.54	96.3
Bank Handlowy SA (Citigroup)	0.29	0.52	0.20	0.16	0.40	0.21	0.19	0.46	0.27	0.63	115.2

* for 2004 and 2005 Securities and Investments.

Source: Authors' estimates based on banks' reports.

Figure 7. *Large banks' average and top two banks' individual characteristics, 2002-2005*



Source: Authors' estimates based on banks' data.

except for PKO BP SA, are controlled by foreign capital and all follow similar universal bank strategy, with the only major difference being the large depository base of Treasury-owned PKO BP SA.

6. Ownership and bank performance of medium banks, 2002–2005

In the analysed period, remarkable transformation has been recorded by many medium-sized banks, controlled by foreign capital, epitomised by GE Money or AIG Bank. Ownership structure affected much more banks' strategies, growth and profitability in this group. GE entered the Polish market in 1995, buying the Gdansk-based Solidarity Chase Bank and complemented its expansion in 1998, by buying the Polish-American Mortgage Bank (*GE Mieszkaniowy*). In 2004, it united these banks under one logo: GE Money. As in the global market, in Poland GE does not have a depositary base and has no branches and offers only a handful of loan-related products. This strategy is characterised by low operational and investment risks and is highly profitable. Another successful entry into the Polish market has been that of the American International Group (AIG), the largest US underwriter of insurance contracts, active also in asset management, capital markets and consumer finance. In Po-

Table 10. *Basic characteristics of foreign and Polish-owned medium banks, 2002-2005*

Name	Loans/Assets	Deposits/Assets	Interbank Loans/Assets	Interbank Deposits/Assets	Securities*/Assets	Irregular Loans/Total Loans Portfolio	ROE	Net Interest Income / Net Income on Banking Activity	Net Commission & Fee Income / Net Income on Banking Activity	Cost/Net Income Ratio	Net profit/Employment
Year 2002											
Polish capital - average	0.48	0.70	0.25	0.10	0.16	0.21	0.06	0.63	0.24	0.64	15.1
Foreign capital - average	0.61	0.49	0.15	0.29	0.14	0.26	0.09	0.56	0.23	0.62	48.4
GE Capital S.A.	0.94	0.02	0.00	0.77	0.01	0.16	0.20	0.63	0.41	0.37	65.7
AIG Bank Polska S.A.	0.87	0.36	0.00	0.18	0.02	0.17	0.16	0.76	0.23	0.23	91.2
Year 2003											
Polish capital - average	0.48	0.72	0.20	0.10	0.23	0.24	-0.01	0.62	0.32	0.79	-0.3
Foreign capital - average	0.66	0.44	0.14	0.29	0.11	0.23	0.10	0.63	0.17	0.71	54.3
GE Money Bank S.A.	0.94	0.01	0.00	0.74	0.01	0.18	0.24	0.63	0.38	0.34	79.9
AIG Bank Polska S.A.	0.86	0.34	0.00	0.19	0.04	0.16	0.27	1.36	-0.36	0.21	141.5
Year 2004											
Polish capital - average	0.47	0.75	0.19	0.10	0.23	0.09	0.02	0.67	0.28	0.76	6.9
Foreign capital - average	0.68	0.40	0.15	0.40	0.08	0.08	0.27	0.64	0.11	0.52	88.2
GE Money Bank SA	0.94	0.01	0.00	0.78	0.00	0.09	0.45	0.62	0.35	0.40	114.6
AIG Bank Polska S.A.	0.78	0.24	0.00	0.30	0.12	0.11	0.94	1.14	-0.14	0.23	195.1
Year 2005											
Polish capital - average	0.52	0.71	0.12	0.12	0.27	0.07	0.07	0.64	0.28	0.70	17.5
Foreign capital - average	0.72	0.38	0.14	0.42	0.06	0.05	0.22	0.62	0.12	0.57	90.2
GE Money Bank SA	0.96	0.01	0.00	0.77	0.00	0.09	0.32	0.60	0.36	0.42	108.3
AIG Bank Polska S.A.	0.83	0.15	0.00	0.37	0.07	0.12	0.73	1.22	-0.22	0.24	206.7

* for 2004 and 2005 Securities and Investments

Note: special-purpose banks (BGK), newly formed cooperative apex banks (BPS and GBW) and specialized one-branch banks are excluded from the averages.

Source: Authors' estimates based on banks' reports

land, it has first entered successfully the insurance sector, and in 1998 has expanded into banking, by acquiring small private Bank Podlaski and transforming it into AIG Bank, very active in consumer finance.

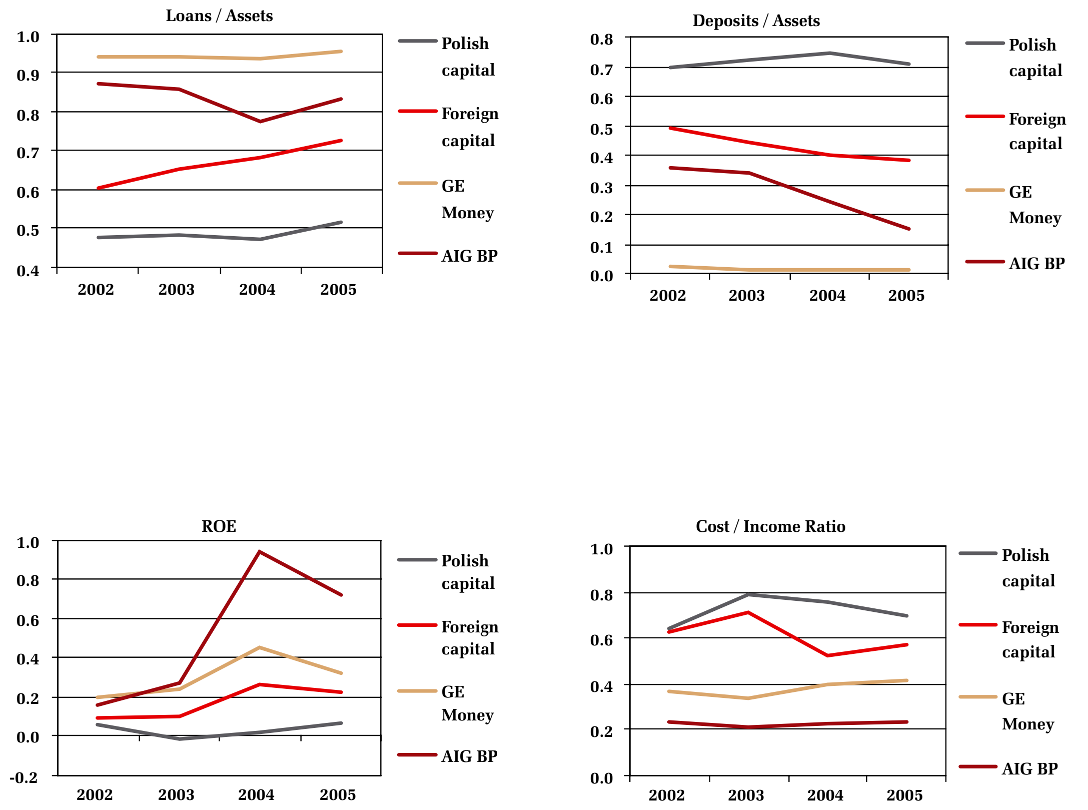
Looking at the balance sheet ratios for medium banks (Table 10, Figure 8) the following observations can be formulated:

- In the medium banks' group, the best results in terms of profitability (ROE), cost control and growth have been recorded by two banks owned by American mega-institutions: GE Money and AIG Bank, followed by other foreign-owned banks. Polish-owned banks have recorded on average much worse results in terms of profitability.
- GE Money and AIG Bank are strongly retail and consumer financing oriented and have bigger proportion of loans and smaller proportion of deposits and securities in their assets than the average. They also derive a smaller proportion of income from fees and commissions. However, their portfolio of irregular loans is growing and for 2005 is higher than the average.

Banks such as GE Money and AIG Bank, and to a lesser extent other medium-sized banks owned by foreign capital, such as Lukas (Credit Agricole) or Santander, base their strategy on entering profitable market niches, largely loan-oriented, and filling the gaps in the local market left by the large banks. Their other strong focus is on cost control and innovation. Looking at the outcome of their choices, it seems that these banks have correctly identified their competitive advantages.

Looking at Figure 8, some differences between the average data for Polish and foreign-owned banks in the medium banks' group are striking. Foreign-owned banks have a small depository base and are mostly loan-orien-

Figure 8. *Major ratios for Polish and foreign-owned medium banks, 2002- 05: averages and selected banks' data*



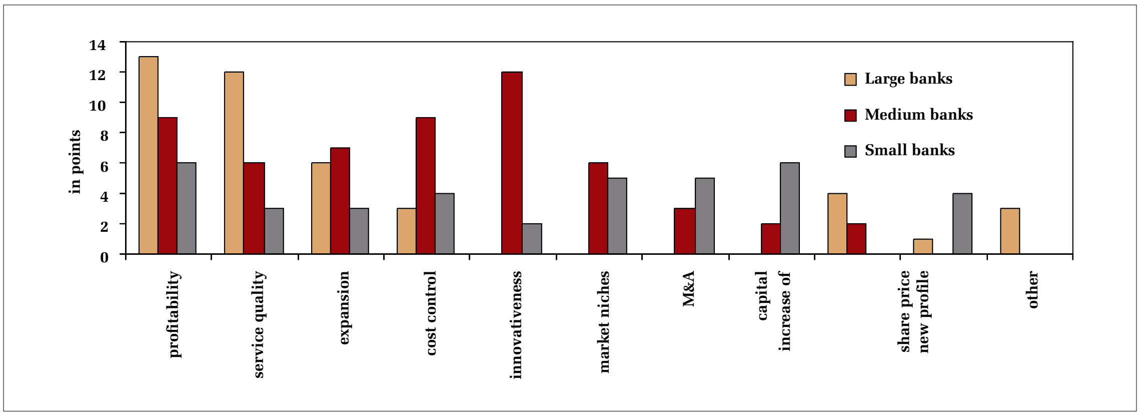
Source: Authors' estimates.

Table 11. *Strategic goals of Polish banks: result of bank surveys (major answers, % of total)*

	2003	1998
1. Strategic priorities:		
Profitability	26	17
Quality of service	14	20
Expansion of scale	11	-
Cost control	11	17
Innovations and new products	10	14
Market niches	8	-
Takeovers	5	6
Increase in capital	5	23
2. Sources of competitive advantages:		
Superior quality	33	38
Universalism	21	26
Specialisation	21	15
Innovation	12	7
Low price of products and services	12	1
No. of banks	27	29

Source: Autors' database.

Figure 9. *Strategic priorities of Polish banks: the results of 2003 bank survey*



Source: Authors' database.

ted, with minimal involvement in securities trading or other investment type activities. The result of this strategy in terms of profitability is also significant – in the foreign-owned banks' group the ROE and net profit per employee are a few times higher.

The above observations have also been supported by banks' responses to strategy-related questions in bank surveys, illustrated in Table 11 and Figure 6. The surveys support the assertion of growing diversification of the Polish banking sector (see also Miklaszewska 2004). In 2003, as in 1998, universalism and high quality of service was seen by the largest banks as a dominant competitive advantage, in contrast to medium sized banks, focusing on specialisation and innovativeness, which turned out to be a more promising strategy than following the large bank emphasis on universalism or low price. However, in 2003, the low price of products was important for all banks, contrary to 1998, which reflected growing competition on the banking market.

7. Conclusion

In the analysed period, the inflow of foreign capital to Poland has been largely the result of the broad strategic tendency towards building global financial mega-institutions, operating in a number of countries and exploiting economies of scale, scope and geographic diversification. As the executives of Deutsche Bank put it, *"many domestic banking markets are relatively mature and consolidated with only moderate top line growth prospects. The sector as a whole is generating excess capital and the larger banks have increasingly been looking to invest this through acquisition"* (The Banker 2005). The reasons for global expansion are controversial, particularly for large banks (Boot 2003). However, when analysing recent concentration processes, the major challenge seems to be the globalisation of the financial markets, forcing firms and customers to adjust. For many firms, competing on global market and generating profits in external areas, rather than in the home market, has become the dominant strategic decision.

In Poland, of particular note has been the transformation of many medium-sized banks, where foreign capital has entered relatively recently. For banks owned by Amercian institutions, such as GE Money and AIG Bank, closely followed by banks owned by European capital, such as Lukas (Credit Agricole) or Santander Consumer Bank, the "model of success" was clear:

- They are retail and consumer finance oriented, where they are prepared to take up a considerable lending risk;
- Their activities are based on few loan-related products, where these banks, borrowing freely from the inter-bank market, are not restricted by a small deposit base;
- Their other focus is on a leadership in quality, innovation and cost control. They try to avoid simple price competition by placing stress on innovative and high quality products and services.

Analysing banks' balance sheet data, the impact of foreign megabanks operating in Poland can be seen as positive from the point of view of their contribution to competitive environment, bank innovation, product expansion and overall bank efficiency. Those banks are also highly profitable. For example, the strongest growth in revenues in 2005 was in Euro Bank, Polish-owned Getin Bank and Santander Consumer Bank (above 70%) and the highest ROE was that of AIG Bank Polska (86%) and Lukas Bank (47%) (BANK 2006). Typical of this group is AIG Bank Polska SA, the most profitable bank in Poland in 2005. Its strategy can be summarised as *"lending to the poor and collecting deposits from the rich"* (Więcław 2006). Banks such as AIG base their strategies on entering profitable market niches, particularly in offering loan-related products to a more high-risk group of clients. They are able to carry through this strategy due to adequate risk management models, low cost of delivery and stress on excellent marketing of selected, standardised products, mostly consumer loans. Their other strong focus has been on cost control: C/I ratio for AIG Bank Polska is 24% and 41% for GE Money (Bank 2006).

To conclude, foreign-owned medium banks, analysed in &5 and epitomised by AIG Bank Polska SA and GE Money Bank SA, have introduced distinctly different strategies which on average have turned out to be very profitable. For the large banks, where foreign capital entered a decade earlier, the strategic and profitability differences between Treasury-owned PKO BP SA and other foreign-owned banks are, however, small (&4.). This may suggest that foreign ownership does not seem to be decisive for large, universal and depository based banks, as opposed to smaller banks, which focus on selected, loan-oriented products. In the latter case, a support from the owner's technology, operations, human capital and corporate culture, seem to constitute an important competitive advantage.

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Appendix. 50 Largest Polish Banks, end of 2005

No.	Name	Group*	Assets (in 000 zl)	Net Profit (in 000 zl)	Main Shareholder	Percent of Equity
1	PKO BP SA	large	90 528 184	1 65 515	Polish Treasury	62
2	Bank Pekao SA	large	61 971 956	1 534 852	UniCredito Italiano	53
3	Bank BPH SA	large	57 922 199	1 027 436	UniCredito Italiano	71
4	ING Bank Śląski SA	large	42 268 311	549 319	ING Bank N.V.	75
5	Bank Handlowy w Warszawie SA	large	32 915 502	616 384	Citibank N.A.	75
6	BRE Bank SA	large	32 817 371	247 543	CommerzBank A.G.	71
7	Bank Zachodni WBK	large	28 182 947	446 223	AIB Ltd.	70
8	Bank Millennium SA	large	22 151 139	567 054	Banco Comercial Portugues S.A.	65
9	Kredyt Bank S.A.	large	20 841 344	415 878	KBC Bank N.V.	85
10	Bank Polskiej Spółdzielczości S.A.	excl.	18 949 499	293 222	Cooperative Banks	95
11	BGK	medium**	18 385 532	128 494	Polish Treasury	100
12	BGŻ S.A.	large	16 627 248	85 075	Polish Treasury	43
13	Raiffeisen BP SA	medium	11 140 274	219 296	Raiffeisen A.G.	100
14	GE Money Bank SA	medium	9 127 362	323 834	GE Capital Corp.	90
15	BOS S.A.	medium	7 767 412	45 624	NFOSiGW (P.Treasury)	77
16	GETIN BANK S.A.	medium	7 128 919	81 163	Getin Holding S.A.	98
17	Fortis Bank Polska S.A.	medium	6 363 892	101 102	Fortis Bank N.V.	75
18	Deutsche Bank Polska SA	medium	6 192 753	41 119	Deutsche Bank A.G.	100
19	NORDEA BP S.A.	medium	5 917 861	30 727	NORDEA Bank A.B.	98
20	LUKAS BANK S.A.	medium	5 021 511	247 109	Lucas SA (Credit Agricole-75%)	100
21	Deutsche Bank PBC S.A.	medium	4 702 186	-18 921	Deutsche Bank A.G.	95
22	Rabobank Polska S.A.	medium	4 249 032	7 819	Rabobank Int. B.V.	100
23	Santander Consumer Bank S.A.	medium	3 786 768	27 366	Santander Consumer Finance S.A.	100
24	Gospodarczy Bank Wielkopolski S.A.	medium	3 760 470	15 742	Cooperative Banks	97
25	ABN AMRO Bank Polska S.A.	medium	3 496 310	42 313	ABN AMRO N.V.	100
26	AIG Bank Polska S.A.	medium	2 850 591	174 888	AIG CF Group	100
27	WestlB Bank Polska S.A.	medium	2 420 328	16 284	WestLB A.G.	100
28	BISE S.A.	medium	2 343 450	6 568	Credit Cooperatif	47
29	Euro Bank S.A.	medium	2 019 250	-13 605	Société Générale	99
30	Danske Bank Polska S.A.	medium	1 939 271	21 050	Danske Bank A.G.	100
31	Invest-Bank S.A.	medium	1 930 602	2 665	Polaris Finance B.V.	30
32	NORD/LB BP SA,	medium	1 920 696	12 137	NORD/LB Girozentrale	100
33	Bank Pocztowy S.A.	medium	1 801 127	25 071	Polish Post Office (P.Treasury)	75
34	Volkswagen BP S.A.	excl.	1 707 375	39 602	Volkswagen Finan. Services A.G.	60
35	Krakowski Bank Spółdzielczy w Krakowie	small	772 940	7 925	Cooperative Bank	–
36	Podkarpacki BS	small	538 865	3 691	Cooperative Bank	–
37	Bank Współpracy Europejskiej S.A.	excl.	483 195	-6 714	PHZ Bartimpex SA	59
38	BS Rzemiosła w Krakowie	small	472 765	3 420	Cooperative Bank	–
39	BS w Brodnicy	small	456 786	6 716	Cooperative Bank	–

40	BS w Kielcach	small	297 319	3 145	Cooperative Bank	–
41	Daimler Chrysler BP S.A.	excl.	293 278	4 032	Daimler Chrysler AG	100
42	FCE BP S.A.	excl.	273 351	14 795	FCE Bank plc.	100
43	BS w Piasecznie	small	270 907	2 019	Cooperative Bank	–
44	BS w Jastrzębiu Zdroju	small	202 601	2 593	Cooperative Bank	–
45	Orzesko-Knurowski BS	small	198 350	2 118	Cooperative Bank	–
46	BS w Skierniewicach	small	181 718	2 089	Cooperative Bank	–
47	BS w Katowicach	small	168 906	7 220	Cooperative Bank	–
48	BS w Białymstoku	small	154 455	2 227	Cooperative Bank	–
49	BS w Stalowej Woli	small	113 908	2 459	Cooperative Bank	–
50	BS w Leśnicy	small	95 582	1 551	Cooperative Bank	–

Methodological notes:

* This column illustrates bank classification used in the paper (for 2005).

** BGK joined the large banks' group only in 2005, hence for the whole analyzed period was classified as a medium bank.

Source: „Bank", 50 największych banków w Polsce (50 Largest Polish Banks), various issues of "Bank" magazine, 1999-2006.

Thorough the whole analyzed period, the banking groups were defined as follows:

– large banks: assets above 6 billion zł in 1998–2000 and above 15 billion zł in 2001–2005. This group was stable in the analyses period, the only distorting factors were mergers among those banks;

– medium banks: assets above 1 billion zł in 1998–2000 and above 1.5 billion zł in 2001–2005. Despite the increased threshold in 2001, there were some migrations from small to medium bank group;

– excluded were banks offering either one product (car loans) or lacking audited data.