

BANKS IN THE SYSTEM OF FINANCING ECONOMY AND FINANCIAL MANAGEMENT IN BOSNIA AND HERZEGOVINA

Željana Vručinić⁶⁶

DOI: <https://doi.org/10.31410/eraz.2018.147>

ABSTRACT: *The goal and contribution of this paper is to look at the importance of banks as the most important entities in the financial market and in the overall system of financing the economy. In the system of overall financing of the economy (and the state) banks get a basic role, whether it is direct crediting of enterprises, or indirectly through the financial market (securities).*

BiH is ranked third in the region by the number of banks, but it is the first if this parameter is viewed on the basis of size and market development, which is why bankers and economists believe that there are too many banks and that the banking sector needs to be consolidated.

By reading this paper, we can see that with the rapid development of credit money, especially after the disappearance of the metal standard, and its active use from the modern capitalist state, through a highly developed mechanism of monetary regulation, there have been two opposite effects: first, there is an increase in the elasticity of the money supply, and secondly, there is a wider use of this mechanism in state-monopolistic capitalism, followed by a sharpening of crisis situations and disproportions in almost all modern economies. The dominance of banking capital in modern economies, constant concentration and centralization processes, the growing interest in financial and industrial capital, and the creation of a financial oligarchy, was followed by the simultaneous process of creating large international banks, the process of creating multinational societies, along with the simultaneous process of diversification of jobs by which modern banks increasingly deal in regular business.

Financial instability is a greater danger to the economic system and central banks, which is why financial stability is expected to become a priority goal for these institutions. The global financial crisis and the wave of bankruptcy of banks and a large number of other institutions opened a new discussion aimed at redefining the objectives of the monetary policy. The research was carried out using the standard methodological procedure, using local and foreign professional literature (books, articles, journals, reports from relevant institutions) and publications related to this issue in the region. Methods of induction and deduction, systematization and methods of analysis and synthesis were applied to these data. Poor economic and credit activity in the country in the past two years, as well as a relatively high proportion of non-performing loans in total system-level loans, imposed a need to find a systematic solution to the issue of non-performing loans. Domestic institutions have begun to create a comprehensive framework for resolving the issue of non-performing loans and to ensure a better position for commissioners, better protection of the guarantors, faster collection of claims, as well as disruption of the borrower's business activities up to the moment of settlement of the commitments, thus creating better conditions for providing significant support of the banking sector to the economic growth of BiH.

Key words: *issuance, central bank, multiplication, interest rates, liberalization.*

⁶⁶ Edukos d.o.o., 78 000 Banja Luka, Bosnia and Hercegovina

1. INTRODUCTION

"The credit activity of the bank leads to the emission of money based on the credit - deposit multiplication. In the western literature for the credit multiplication process, the term credit expansion or contraction is used."⁶⁷

The central bank in all monetary systems in the world continued to retain the previously acquired monopoly right to create primary money (printing of banknotes and coins), although today, along with the central bank, the entire banking system, i.e. all commercial banks, appear as banks which on the basis of bank loans, do real emission of money. True, there is still a difference between the issuance of the central bank and the issuance of commercial bank money, given that the central bank creates the so-called primary money, and commercial banks create deposit or banking (secondary) money. "The state assumes directly (true, through the Central Bank, which is in its hands) responsibility for the credit and monetary policy in general, for regulating the money supply, but also for regulating the basic goods - cash flows within the economy"⁶⁸.

Primary central bank emission can be done in theory and practice over 5 basic flows or channels:

- a) By monetization of securities (bills of exchange, bonds and similar securities issued by business enterprises that are in circulation within that sector), i.e. directly to economic entities, transactors. Monetization of securities is done through the system of commercial banks,
- b) By Central bank loans to commercial banks,
- c) By state (federation) crediting, i.e. "government borrowing from the central bank" (government borrowings with the central bank, i.e. monetization of public debt bonds of the state through the "open market"),
- d) By loans to other direct customers of the central bank;
- e) By purchasing and selling foreign currency assets (foreign exchange transactions, foreign exchange reserves operations).

Each of the mentioned channels or streams of issuance has its own specificity and a deeper reflection on all the basic flows in the reproduction as a whole, especially in our economy. Therefore, it is not about a formal one, but about a fundamental difference in the flow of emission of primary money, because they have a different effect on: the stability of the economy, mastering the economy by direct money emission, adjusting the emission of money to real goods-money transactions in the economy, forming an optimal money supply, and the efficiency and elasticity of monetary policy and so on.

In order to see the flows of creating primary money in our economy, we will indicate real channels and their significance in the past few years.

- Emission of the National Bank (primary issue) – loans to banks (for recycling of securities, for liquidity of banks, other loans);
- Placements to securities through banks (bills of exchange, commercial bills, other securities);
- Loans to the state;
- Other placements;

⁶⁷ Alijagić, M. (2006) Bankarski Menadžment, Univerzitet za poslovne studije, Banja Luka, pp. 356

⁶⁸ Jovičić, J. Klincov, R. Ristić, Ž.(2010) Međunarodno bankarstvo, Etno stil, Beograd, pp. 11

- Securities on the open market (commercial papers).

Here, the basic questions raised are if the central bank can control the mass of primary money, that is if it can successfully adapt it to the needs of economic development; and secondly, to which flows the central bank can influence (controlled flows), and what are the flows to which it cannot influence (autonomous flows)? Therefore, the question arises regarding the nature of these flows, their autonomy in relation to the decisions and measures of the central bank, and the ability of this bank to keep them under control. "The internal value of money is based on the purchasing power of money that money has on the domestic market, i.e. the quantity of goods and services that can be obtained for a certain number of monetary units."⁶⁹

For all of the above, we will consider all the basic flows of creating primary money, we will emphasize their basic characteristics, basic activities in the economy, and the positive and weak sides of our monetary and credit system. However, we will first give, for the purpose of comparison only, a brief overview of the emission system and the channels of the creation of primary money in some developed capitalist countries.

2. BANKING SYSTEM OF BOSNIA AND HERZEGOVINA (Central Bank of BiH and Currency Board)

The Central Bank of BiH was formed in accordance with the Law on the Central Bank of Bosnia and Herzegovina adopted in 1997. According to the legal provisions, the Central bank cannot give loans on the basis of money creation, and therefore it functions as a "Currency Board" with two main units, one in the Federation of BiH and one in the Republic of Srpska. "The main task of the Central bank is to maintain the stability of the domestic currency (Convertible Mark) by broadcasting the domestic currency under an arrangement known as the "Currency Board"⁷⁰. The tasks of the Central bank under the authority of the Governing Board relate to: providing and maintaining the stability of the domestic currency that is issued with full coverage in freely convertible funds (the convertible mark is issued in accordance with an arrangement known as the Currency Board at the fixed exchange rate of 1 KM = 0,511 E), defining and controlling the implementation of monetary policy in BiH, managing in a safe and profitable way with the foreign exchange reserves of the central bank, establishing and maintaining an appropriate payment and settlement system of the country, issuing appropriate regulations, coordinating the activities of the BH Entity Banking Agencies which are in charge of bank licensing and supervision, the implementation of monetary policy (issuance and withdrawal of the domestic currency from circulation), including banknotes and coins, with strict adherence to the rules of the "Currency Board" and receipt of deposits from the Federation of BiH and the Republic of Srpska, i.e. deposits of the entities.

The Central Bank is completely independent of the Federation of Bosnia and Herzegovina, the Republic of Srpska or any other public agency or body, and does not have any organizational connections with any commercial bank in order to carry out its tasks objectively. The Central Bank exercises international cooperation in the conduct of monetary policy, is responsible for carrying out transactions with international organizations. The Central Bank provides banking services for the benefit of foreign governments, works on determining financial and economic stability through international monetary cooperation, etc.⁷¹

⁶⁹ Ristić, K. Komazec, S. Ristić, Ž.(2016) Monetarni i bankarski menadžment, Etno stil, Beograd, pp. 41

⁷⁰ www.cbbh.ba

⁷¹ www.cbbh.ba

A well-organized financial and banking system and its efficient functioning contribute to: increasing the national savings rate; rapid concentration and centralization of capital; more effective use of national savings; increasing the general rate of return on social capital; greater stability of economic and financial flows; increasing the overall growth rate; greater social control of monetary and financial flows; optimal allocation of financial resources in the process of financing economic development; greater "flowability" and liquidity of reproduction, the total flows of reproduction, etc.

3. INTEREST RATES IN BOSNIA AND HERZEGOVINA

The transition process also implied a significant transformation of the role of commercial banks in the financial and economic system.

In most cases, banking systems have gone through three phases:

- 1) Consolidation – write-off of a significant portion of banks' claims on loans granted to large state-owned enterprises and the transfer of losses related to these loans to the state;
- 2) Privatization – sale of banks, primarily to foreign investors;
- 3) Beginning of standard banking operations, including increasing the granting of loans to truly private companies.

“The Central Bank of Bosnia and Herzegovina (CBBH) has set up new interest rate statistics, and started its publication, and thus made significant progress towards reaching EU standards in the field of statistics. New interest rate statistics are harmonized with the methodology prescribed by the European Central Bank (ECB) and applied by the EU Member States and the Eurozone. These statistics contain 82 indicators on weighted and weighted average interest rates of commercial banks, with data series starting in January 2012. Out of the above 82 indicators, 60 refer to interest rates for different types of commercial bank loans, and 20 to interest rates for deposits with commercial banks.”⁷²

During the preparatory phase, this project was supported by the technical assistance program from the IPA 2008 funds for the CBBH, and it was implemented through cooperation with the ECB and the Austrian National Bank (OeNB). "For the purpose of protecting banks, the central bank prescribed the upper limit of the largest possible loans which a bank can approve to one customer. The upper limit is 80% of the total capital of the bank."⁷³ At the same time, it is possible to make a direct comparison of the level of interest rates in BiH with those in countries that apply the same methodology.

The most characteristic interest rates on loans to citizens are those for general-purpose loans (in BAM with a currency clause) with a variable interest rate, which in February amounted to 9.06%, and also over the past several months was at a similar level. For housing loans (variable rate, currency clause) interest rates were significantly lower, and in February amounted to 6.75%, and did not exceed the level of 7% in the previous year. Interest rates on consumer loans (variable interest rate, currency clause) are slightly above 8% and in February amounted to 8.23%.

For corporate loans, interest rates are classified according to the loan amount (up to 500.000, from 500.000 to 2 million and over 2 million BAM). In the category of loans up to 500.000 BAM, the majority are loans in BAM with a variable rate, which was 8.1% in February (it is

⁷² www.cbbh.ba

⁷³ www.moj-bankar.hr

lower compared to trends in 2012). Loans in the category from 500.000 to 2 million BAM are significantly cheaper and the interest rate in February was 6.56%, and it is lower than the average in the previous year. Loans exceeding 2 million BAM (variable rate, in BAM) in February had an interest rate of 6.28%, while in 2012 they were generally above 6.5%.

"A loan is a temporary service that the creditor makes to the debtor by giving him a certain purchasing power (money) or some object at his disposal."⁷⁴

Loans in foreign currencies are very poorly represented in domestic banks, since most loans are realized in domestic currency BAM or in BAM with foreign currency clause.

According to the new methodology, interest rates on deposits now allow for comparison over different maturities. Interest rates on citizen deposits (in EUR) have a clear gradation in terms of the interest rate, because they have an interest rate of up to 2.2% with agreed maturity of one year, from 1 to 2 years of maturity have an interest rate of 3.45%, and over 2 years have 4.2%. Enterprises primarily deposit in local currency, with interest rates ranging from 3.34% (maturity up to 1 year) to 4.93% (maturity between 1 and 2 years).

3.1. Analysis of the Central Bank of BH: The lowest interest for companies, housing loans the most expensive ones

Interest rates on loans to nonfinancial companies with a currency clause related to the euro in the region are the lowest in BiH, while on the other hand, they are the highest for housing loans. It was showed by the analysis of the Central Bank of Bosnia and Herzegovina, which was carried out on the basis of the data from the central banks of the countries in the region on the average weighted interest rates on loans and deposits to non-financial enterprises and citizens. Apart from Bosnia and Herzegovina, Serbia, Croatia and Macedonia are included in the analysis, and in all categories exclusively interests on loans with a currency clause related to the euro were compared. In the case of loans to non-financial enterprises, the analysis showed that the level of interest rates is balanced in the region. The lowest average interest for short-term borrowings of 6.5% is in BiH, while with the long term loans it is in the second place with an interest rate of 7.5%. In both categories, Serbia has the highest interest rate.

On the other hand, housing loans in BiH are the most expensive in the region. This is particularly evident in long-term borrowings with interest rate of up to 8.1%, while in short-term loans, the interest rate is also the highest, amounting to 6.2%. In both categories, the lowest interest rate is in Croatia.

BiH is in the middle in terms of interest rates on short-term non-cash and cash loans, while long-term borrowings in this category have the lowest interest rate of 8%.

When it comes to deposits, the highest interest rates are offered by banks in Croatia. Speaking of savings in BiH is the highest interest rate in the region on deposits with term of deposit longer than the year and amounts to 3.2%. With deposits with term of deposit of a year BiH and Serbia share the second position with an average interest rate of 1.8%, and in this category the best yield to the citizen is offered by banks in Croatia with interest rate of 2.2%.

⁷⁴ Vučković, M.(1967) Bankarstvo, Naučna knjiga, Beograd, pp. 38

BiH takes a second position regarding the height of the interest on deposits of non-financial companies, after Croatia. Interest on deposits with term of deposit of a year is 2.10% in BiH, and for a period longer than a year it amounts 3.08%. "The function of modern banks, all the more diverse tasks they perform, places them in a circle of organizations of special social interest."⁷⁵

The Central Bank of BiH says that the comparison of interest rates in different economies is very complicated, and that there are two main reasons for this. The amount of interest rates depends largely on monetary policy in each country, that is, from the reference interest rate dictated by the domestic central bank and from the level of inflation and the fluctuation of the exchange rate, which has a significant direct impact on the level of nominal interest rates. The second problem relates to different methodologies that are applied in calculating the average interest rates. Therefore, the interest rates observed in this case are the ones related to the euro and therefore should not be affected by different domestic monetary conditions - as explained by the Central Bank of BiH.

Željana Vrućinić

Date and place of birth:

October 21, 1984, Split

Education:

1999 - 2003 - Prijedor

Gymnasium

2003.- 2008.- University of Business Studies, UPS, Banja Luka

UPS, Banja Luka

- Faculty of Business and Financial Studies, Bachelor of Economics (180 ECTS) - Finance, Banking and Insurance - average grade 9.48

2013- 2014- University of Business Studies UPS, Banja Luka

- Faculty of Business and Financial Studies, Bachelor of Economics (240 ECTS) - Finance, Banking and Insurance - average grade 9.30

2015 - 2016 - University of Business Studies UPS, Banja Luka

- Faculty of Business and Financial Studies, Master Studies - Financial, Banking and Stock Exchange Management

2016-present- University of Business Studies, doctoral studies in the field of macroeconomics and development

Work experience: 13 months in the business of the head of the travel agency, 6 years worked in insurance business; since February 6, 2018, employed in the company "Edukos" d.o.o. on the affairs of the director of the firm



3.2. Methodology for determining interest rates in RS and BiH

Banking agencies in the Federation of Bosnia and Herzegovina and the Republic of Srpska have introduced regulations regarding the methodology that financial institutions (which were licensed by them) must use to calculate the EIR for their products. These requirements apply to:

- loans and deposits;
- banks and microcredit institutions.
- There are some differences between the methodologies imposed by the two Entity agencies. Although these differences are not essential, they still have the following effect on clients who use information on the EIR in BiH:
- It is possible to accurately compare EIR for similar products among banks in the Federation of Bosnia and Herzegovina or among banks in the Republic of Srpska, while comparing between the EIR of banks from the Federation of Bosnia and Herzegovina and from the Republic of Srpska banks is not possible for some types of loans.

⁷⁵ Golijanin, M.(1977), Bankarstvo Jugoslavije, Privatni pregled, Beograd, pp. 23

- Regulations in the Republic of Srpska have a wider definition of the costs that must be included in the calculation of the EIR, some of which are not directly related to bank loans. Therefore, EIR in the Republic of Srpska is higher for the same products than EIR in the Federation of BiH.

"Each unit of an approved and used short-term bank loan means the issuance of a certain amount of money in the economy. Therefore, by approving the credit every business bank issues money, which means that for the entire issue and withdrawal of money the central bank is not the only one responsible, but also the whole system of commercial banks has responsibility, that is, the banking system as a whole.⁷⁶"

4. INDICATORS OF CITIZEN SAVINGS AND INTEREST RATES ON TERM DEPOSITS IN BiH

In the observed period from 2003 to 2009 (Table 1), the total saving of the citizens of Bosnia and Herzegovina was increased by an impressive 254%, while in 2009 only citizens with resident banks saved more than 450 million BAM despite the financial crisis and the consequences which were manifested through citizens' nervousness and shattered confidence in banks, especially in September – October 2008, when about 700 million BAM were withdrawn, or 11.7% of the total savings of citizens. Savings deposits of all institutional sectors also grew in all observed years, except in 2009, when the savings and term deposits with the resident banks decreased, but by only 43 million BAM. Namely, the total amount of savings term deposits at the end of 2009 amounted 6.42 billion BAM and it represents more than tripled amount compared to the end of 2003 (1.8 billion BAM). Additionally, household deposits grew more than three times, from 1.03 billion BAM at the end of 2003 to 3.52 billion BAM at the end of 2009 and in contrast to total savings term deposits they rose even in 2009 (467 million BAM more than in 2008).

Table 1. Savings deposits and demand deposits in BiH
(Balance of deposits and average interest rates at the end of the year; in millions of BAM)

Year	Total savings term deposits	Savings term deposits Household sector (households)	Average interest rates on savings term deposits of citizens	Total demand deposits	Demand deposits by household sector	Average interest rates on demand deposits of citizens
2003	1 812	1 033	3.40 %	2 554	893	0.96 %
2004	2 457	1 354	4.02 %	3 122	1 135	0.77 %
2005	3 000	1 802	3.63 %	3 876	1 385	0.63 %
2006	3 856	2 329	3.48 %	4 942	1 772	0.49 %
2007	6 075	2 944	3.98 %	6 026	2 222	0.35 %
2008	6 460	3 052	3.61 %	5 479	2 155	0.32 %
2009	6 417	3 519	3.57 %	5 772	2 144	0.25 %

Source: CBBH - Monetary and Financial Sector Statistics

Average interest rates on savings deposits of citizens increased from 3.4% at the end of 2003 to 4% at the end of 2004. However, since the beginning of 2005, the average interest rates have oscillated, that is, they have fallen or increased over the years to reach 3.57% at the end of 2009.

⁷⁶ Sejmenović, J. Komazec, S. Ristić, Ž. (2008) Monetarne i javne finansije, Univerzitet za poslovne studije, Banja Luka, pp.180

Not only that savings deposits of citizens increased, but also transaction deposits and demand deposits, both of the citizens and of other institutional sectors of the Bosnia and Herzegovina economy have increased to a considerable extent.

From Table 2 it can be seen that in the period from 31.12.2002 to 31.12.2009 savings term deposits were continuously growing. Significant increase in savings term deposits is visible in the domestic currency, they have increased by more than 400% or they are five times higher at the end of 2009 compared to the end of 2002.

Table 2. Increase of term and savings deposits in BiH in millions of BAM

Increase of the deposits in the period (ending with 31.12.)	Savings term deposits					
	Total		In domestic currency		In foreign currency	
	In Million BAM	In %	In Million BAM	In %	In Million BAM	In %
2002.-2003.	318	25,5	190	69,7	128	13,2
2003.-2004.	744	47,5	242	52,3	502	45,5
2004.-2005.	509	22,1	115	16,3	395	24,6
2005.-2006.	785	27,9	240	29,4	545	27,3
2006.-2007.	990	27,5	421	39,8	569	22,4
2007.-2008.	604	13,9	247	16,7	357	11,5
2008-2009.	476	9,2	58	3,3	418	12,1

Source: CBBH - Monetary and Financial Sector Statistics and own calculations

Observed by years, the biggest annual growth was realized in 2007, when savings term deposits increased by 57.8%, i.e. from 3 856 to 6 075 billion BAM.

The same applies to saving term deposits in domestic currency and savings term deposits in foreign currency, with the highest annual growth rate of deposits in domestic currency realized in 2003, and deposits in foreign currency in 2007 of the observed period.

4.1. The effects of financial liberalization on savings in BiH

Financial liberalization in BiH was realized through the liberalization of the financial market, i.e. by eliminating interest rate controls, abolishing credit control and controlling capital movements, reconstructing and privatizing the banking sector. The key problem of the household sector relation with the banking sector, which is the holder of private savings with regard to the very weak private sector of the enterprises, is the lack of confidence of the citizens in relation to the state and the banking sector.

The first problem that was present before the war, in the 1990s, was rather expressed financial repression, because the citizens that save received a really negative interest rate on their savings (domestic currency deposits are mostly not indexed in relation to long-term and often very high inflation rates). Debtors were big winners, and the savers were at a great loss. This risk was being overcome by currency substitution and foreign currency savings. The financial and every other collapse of the country delayed the issue of old savings for a long term.

Frozen deposits in banks that were denominated in the domestic currency were practically written off at the expense of their owners (citizens) who were left without them, and on the basis of foreign currency deposits, newly born countries assumed the obligation to pay off these

deposits. For almost two decades, this issue in Bosnia and Herzegovina has not been fully resolved, unlike the neighboring countries that originated from the former Yugoslavia. All this had a strong negative impact on the level of confidence of the household sector in the domestic banking system, and for many years savings remained outside the official financial sector.

Financial liberalization meant that domestic banks were largely privatized by foreign capital originating from foreign bank owners, so domestic banks received the names of these foreign banks, that is, became their banks daughters. In this way, the presence of foreign banks has largely influenced the restoration of citizens' confidence and a more significant growth of savings deposits in banks. Important was the introduction of effective supervision and deposit protection, but for citizens it was certainly not of primary importance, nor one of the main elements of return of trust. On the other hand, a very important moment is the stable macroeconomic policy that has been led since the very beginning of the post-conflict recovery. The convertibility of the domestic currency to the reserve currency at the fixed exchange rate over a ten-year period and the low inflation rate, which has been maintained up to the recent years, had a strong influence that only five to six years later there was a strong increase in term and savings deposits in banks. The stable exchange rate (fixed) and officially guaranteed convertibility had influence that savings in a very significant portion was kept in domestic banks in the domestic currency.

The next positive effect of liberalization is reflected in the abolition of capital flow restrictions, which influenced the influx of foreign capital, among other things, to encourage secondary capital markets, which to some extent opened up space for both investment of domestic savings and in that market, and for the return of part of domestic capital from abroad. True, the primary emission of capital (shares and bonds) that would absorb the savings of the citizens are small in volume. There is no doubt that certain amounts of domestic savings have been attracted from informal to official flows during the period of the expansion of trading on domestic stock exchanges during the phase of the exceptional increase in the prices of financial instruments on those stock exchanges.

Liberalization in BiH has, in some way, unfavourably affected domestic savings too. These unfavourable effects can be recognized, starting from the fact that the free capital inflow has opened very wide credit opportunities for domestic entities. Thus, the increased loan offer has reduced the need of citizens to save so as to be able to invest. "The increase in bank loans and the increase in foreign exchange reserves affect the increase in money supply, while the increase in the limited deposits acts in the opposite direction."⁷⁷ Otherwise, the poor orientation of the private sector to productive investments is additionally disturbed by the possibilities of obtaining loans and investing in real estate. "Investing in real estate, especially in residential property, is the result of easier access to credit on the one hand, and on the other hand, of the risk associated with production or investment in a business that is not present to that extent when it comes to the real estate investments. Furthermore, the effects of investment in real estate were faster, especially in conditions of rising real estate prices, as a result of the growth in demand for real estate, while investments in business were linked (in addition to the necessary entrepreneurial abilities owned by fewer people) additionally with longer waiting for effects, and greater risk. In this way, savings through such investments are increasingly directed to non-productive purposes motivated by renting."⁷⁸

⁷⁷ Ćirović, M. (1963) *Mehanizam emisije kredita i novca* (script), Skoplje, pp.44

⁷⁸ Out of all financial intermediaries, the increase in assets was only recorded in insurance and reinsurance companies (6.1%), (Financial Stability Report for BIH for 2009).

"The liberalization of the financial sector has influenced the more dynamic development of the financial structure, primarily the structure of financial institutions and financial instruments. In addition to the dominant banks, in the structure of institutions, funds, leasing companies, microcredit organizations and insurance companies are gaining increasing importance. Reforms of the pension system lead to the formation of private pension funds. These institutions will become increasingly important in mobilizing domestic private savings. With the financial market, investment funds (open and closed) are formed, and it can be expected that they will also mobilize new savings.⁷⁹"

However, the structure of the financial sector in BiH did not change much in comparison to previous periods. Financial intermediation, measured by the assets of financial intermediaries, after a significant slowdown in growth in the previous year, recorded a decrease of 2.5% in 2009.

Thus, the processes of liberalization and development of financial infrastructure have not yet been completed, so, according to the current development trends, it can be expected that the overall effects on savings will be net positive, counting on the strengths and factors that will pull and mobilize the savings and strengths that will minimize it.

4.2. The issue of the stability of the banking sector in BiH

The supervision of banks in the area of Entities is carried out on the basis of inter-entity harmonized regulatory bases. For a long time, a debate has been held on "including" the entity agencies under the "umbrella" of the CBBH, which by law has the function of coordinating the work of entity agencies or the creation of a single agency for the supervision of banks at the BiH level. Among observers, the dominant opinion is that there is no optimal supervisory structure, but that there are different arguments for and against, which must be considered in individual cases of countries.

One of the key institutional improvements in BiH would be to improve the information base on the financial condition and operations of legal entities, bank clients, which would strengthen the information base of banks and enable better customer knowledge and risk avoidance. Strengthening the principles of transparency and the publicity of banks' operations affect the strengthening of market discipline and the strengthening of confidence in the banking system.

"It should be borne in mind that banks' operations in BiH are much more risky than in Western countries, and the cause for this are economic and credit unreliable clients without a longer business tradition, weak and undeveloped risk protection mechanisms, inadequate institutional environment, etc. For these reasons it is necessary to have more rigorous regulation (rules) and supervision of banks. It is primarily reflected in stricter standards, and one of these is the required capital rate of 12% against the risk weighted assets. There are also lacking appropriate mechanisms and institutions that can efficiently conduct the process of restructuring of the troubled banks and provide additional resources for their rehabilitation.⁸⁰"

The last major financial crisis (2008) was strongly reflected in emerging markets, although the causes were in developed countries, primarily in the United States and England. Banks in

⁷⁹ banke.online.rs

⁸⁰ The acquired capital adequacy ratio in 2009 was 16.0%, which is higher than the required rate (12%), while the standard is 8.0%. This coefficient represents the ratio of net capital and weighted risk assets.

emerging markets have been hit by a slump in funding from their parent bank groups that have suffered losses, but also because of the general decline in available financing in the euro zone due to the crisis. Banks in emerging markets also suffered losses due to the worsening of the situation in domestic economies, as the quality of their loan portfolios was considerably worsened due to the difficulties in repaying loans to debtors faced with liquidity and solvency problems.

Under such circumstances, there was a risk that foreign banking groups would begin to leave the market in Central and Eastern Europe. International financial institutions, primarily the IMF and the EBRD, have been actively engaged in preventing such developments and have managed to coordinate the so-called Vienna Initiative for countries that received generous IMF assistance and the EU for their balance of payments problems. Within our region, four countries were covered by this initiative: BiH, Hungary, Romania and Serbia. Therefore, thanks to previously taken activities, we can conclude that banks in these countries are less confronted with problems related to their balances, that is, the limitation in terms of capital, liquidity and regulatory constraints is considerably lower, which indicates that stress from the financial crisis relaxed and that banks do not have business restrictions in this regards.

The more massive withdrawal of foreign currency deposits and effects, at the end of 2008, was stressful, and it could even be catastrophic. From that moment, the foreign currency reserves of the Central Bank of BH amounting to 6.7 billion BAM (around EUR 3.3 billion) decreased by 500-600 million BAM by the end of 2009. The reasons are that more than half of the formed foreign exchange reserves originate from the inflow of funds into the banking system of BiH through deposits, loans and investments in shares performed by "parental" banks. Not long ago, IMF experts estimated that foreign exchange reserves were threatened by a reduction, due to financing of the current account deficit for a longer period. In a way, this partly came true during 2008 and 2009, as a result of the developments caused by the financial crisis. In addition, the shattered confidence of the citizens in banks and domestic currency in that first year of the crisis has prompted citizens to convert the domestic currency into euro and BAM deposits into euro deposits, in addition to withdrawing deposits. This phenomenon took on significant proportions, which made additional pressure on the existing foreign currency reserves of the Central Bank. The size of the deficit in some way determines the extent of the decrease in foreign currency reserves in case of a reduced inflow of euro funds through the banking system.

This highlighted in the first place the importance of reducing the foreign trade deficit, in order to reduce the risk of financial instability. The risk of foreign exchange reserves lies primarily in the fact that there is a high level of Euroisation in BiH, that the exchange rate for more than thirteen years is fixed within the framework of the monetary board arrangement, that foreign banks are relying on external sources of funds and that there are large external imbalances.

"The BiH financial stability analysis for 2009, made by the experts of the Central Bank of BH, indicate credit risk, market risk and liquidity risk, that potential risks are realistically present and that banks in the crisis periods become more cautious in assessing the quality of debtors and new placements. Demand for loans is decreasing, especially in the household sector, due to increased uncertainty and problems with finding quality insurance for loans. However, previously contracted obligations of the bank are activated to a large extent precisely in bad times; new loans to households are reduced, but credit cards debts are growing; a growing number of guarantees are being activated, and repayment of loans to legal entities to which the guarantee were issued are often late. The situation is further complicated by the fact that the share of industry in the approved guarantees is similar to that of the loan, and that guarantees,

especially payables can be activated in a very short period of time, which can further lead to liquidity problems with commercial banks.⁸¹ Foreign exchange risk represents a potential loss arising from changes in exchange rates. Due to the arrangement of the currency board and agency regulations on the net open position of banks, foreign exchange risk in BiH is low. Traditional indicators do not indicate a significant liquidity risk in BiH. Banks are still on the side of the liquidity offer, which is mostly seen through the balance of the mandatory reserve account with the CBBH.

External imbalances are just one of the indicators of potential monetary instability. Other indicators include weak export performance of the economy, instability of the financial sector, low or declining foreign exchange reserves, rapid growth of money supply and credits, low real GDP growth, domestic inflation and fiscal deficit. In BiH, even in times of crisis, some of these indicators are positive, such as inflation, a low current account deficit, liquidity and the health of banks. Other indicators deserve special monitoring.

5. CONCLUSION

For a faster recovery, it is necessary to raise the level of investment, which after the crisis in 2008 is significantly reduced. At the level of investment, there is a significant difference between the public and the private sector. There has been an increase in the number of public investments and their implementation in recent years. Governments have made efforts to start new investments, but also to speed up previously agreed investments, primarily in road infrastructure and energy. However, the mobilization of foreign as well as domestic private sector investments requires primarily political stability, significant improvement of the business environment and conducting reforms, primarily those related to harmonization with EU regulations. In this regard, BiH has not been making significant progress for many years, and this requires the urgent attention of the new authorities after the October elections. The rule of law and clear market regularity and accelerated administrative procedures are prerequisites for attracting investors and raising the level of private sector investment. There needs to be a lot of improvement in this regard.

Greater transparency of the monetary institution's operations can help in the more efficient implementation of monetary policy. Informing the public about the mandate of the central bank and to what extent it has been achieved can increase the credibility of the central bank. Strict compliance with the principle of transparency in business requires a kind of self-discipline from the creators of monetary policy and increases the likelihood of a consistent monetary policy. Likewise, regular communication gives directions to financial markets, which allows participants in the financial market to better understand monetary policy measures and their impact on economic trends and system shocks.

On the other hand, the monetary authority should influence: the expectations of market participants, as it will in this way be easier to achieve their monetary and economic policy objectives, the macroeconomic environment in which these goals are to be met, the monetary policy instruments for achieving the goals (as well as their application and limitations) and the Central Bank's forecasts.

⁸¹ Just for illustration, according to the data provided by the Banking Agency, off balance sheet items: irrevocable loan commitments and issued guarantees at the end of 2009 amounted to 22.9% of the short-term financial liabilities of the banking sector (CBBH, 2010).

LITERATURE:

- (1) Alijagić, M. (2006) Bankarski Menadžment, Univerzitet za poslovne studije, Banja Luka, pp. 356
- (2) Jovičić, J. Klincov, R. Ristić, Ž. (2010) Međunarodno bankarstvo, Etno stil, Beograd, pp. 11
- (3) Ristić, K. Komazec, S. Ristić, Ž. (2016) Monetarni i bankarski menadžment, Etno stil, Beograd, pp. 41
- (4) www.cbbh.ba
- (5) www.moj-bankar.hr
- (6) Vučković, M. (1967) Bankarstvo, Naučna knjiga, Beograd, pp. 38
- (7) Golijanin, M. (1977) Bankarstvo Jugoslavije, Privatni pregled, Beograd, pp. 23
- (8) Sejmenović, J. Komazec, S. Ristić, Ž. (2008) Monetarne i javne finansije, Univerzitet za poslovne studije, Banja Luka, pp. 180
- (9) Ćirović, M. (1963) Mehanizam emisije kredita i novca (skripta), Skoplje, pp. 44
- (10) banke.online.rs