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## **Poland**

### ***Central bank***

The reform of the Polish banking system started in 1989 when the domination of the mono-bank in the financial system was overcome with the Act on the National Bank of Poland of January 31, 1989.<sup>64</sup> At that time the National Bank of Poland became the central bank, a state institution which, according to the provision of the Constitution of the Republic of Poland<sup>65</sup> of 1997, is responsible for the value of the Polish currency. Under the NBP Act<sup>66</sup>, the primary objective for the central bank is to maintain stability of prices and, simultaneously, support government's economic policy as long as it does not hinder the fulfillment of the primary objective. The National Bank of Poland has the exclusive right to issue currency and regulate money circulation. Furthermore, the NBP is obliged to:

- manage reserves of the foreign exchange;
- organize money settlements;
- conduct foreign currency operations;
- conduct bank services towards the national budget;
- regulate banks' liquidity and their refinancing;
- provide conditions conducive to banking system's development.

The National Bank of Poland is highly independent. Among others, it results from the fact that its independence concerning issue of currency and running monetary policy is written into the Constitution. The NBP can be a member of international financial institutions but it may not be a shareholder of legal entities other than those rendering services towards financial institutions or the Treasury.

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<sup>64</sup> See, among others, Janc (1997, p. 89 and further); also: Janc and Sury-Walterowicz (1998b, p. 113 and further).

<sup>65</sup> The Constitution of the Republic of Poland of April 2, 1997 (Journal of Laws no. 78, item 483, correction: Journal of Laws of 2001, no. 28, pos. 319), art. 227, par. 1.

<sup>66</sup> The Act on the National Bank of Poland of August 29, 1997 (Journal of Laws no. 140, item 938 of 1998, no. 160, item 1063, amendment following the verdict of the Constitutional Tribunal of June 28 2000: Journal of Laws of 2000, no. 53, item 648, no. 62, item 718, no. 119, item 1252 and of 2001, no. 8, item 64, no. 110, item 1189 and no. 154, item 1784 and 1800, of 2002, no. 126, item 1070, no. 141, item 1178).

The governing bodies of the NBP are as follows: the President of the NBP, the Monetary Policy Council (MPC, *Rada Polityki Pieniężnej*) and the NBP Management Board. The President is appointed by the Sejm (the lower house of the Polish parliament) for six years on the recommendation of the President of Poland. The President may serve the maximum of two terms. Recall of the President is possible only in rare cases provided by the law. The President presides over the Monetary Policy Council, the NBP Management Board and the Commission for Banking Supervision. Apart from the President, there are nine other MPC members appointed for six years by the Sejm, the Senate (the higher house of the Polish parliament) and the President of Poland (3 members each). A representative of the Council of Ministers may participate in MPC sessions without, however, the right to vote. He/she may put forward proposals to be considered by the MPC.

Annually, the Monetary Policy Council determines principles of monetary policy. Following the primary objective of the NBP and the adopted monetary policy, the Council determines NBP interest rates, principles for open market operations and rules and rates of compulsory reserves for commercial banks. The primary goal of the NBP Management Board is to realize resolutions of the MPC; first of all, putting in motion operational activities concerning implementation of the principles of monetary policy.

The current activity of the National Bank of Poland is governed by the NBP Management Board. It implements Council resolutions and takes decisions concerning matters not within the exclusive power of other NBP governing bodies. The NBP may be a financial agent for the Government with respect to concluding and realization of loan agreements and servicing state's foreign debt. Under the law, the National Bank of Poland is financially independent which is reflected in the principles for establishment and distribution of bank's funds. On the basis of a financial plan approved by the Monetary Policy Council, the NBP runs independent financial management. Bank's own funds include base funds (statute and reserve) and special funds.

Personal independence of the central bank manifests itself in the way how members of its governing bodies are appointed and recalled as well as what the influence of state authorities on the structure of bank's governing bodies is. In Poland, the possibility of President of the NBP's recall is restricted to a few precisely defined cases (such as a long-lasting illness, or sentence of the court or the Tribunal of State). The government has no direct influence on the appointment of central bank's governing bodies, nor can it intervene in NBP's monetary policy. Nevertheless, the NBP cooperates with state authorities. Under the NBP Act, the central bank in Poland cooperates with state organs in matters concerning formulation and realization of the state economic policy. What, however, remains the main goal of the NBP is the realization of the primary objective and principles of monetary policy. The NBP runs currency policy as decided by the Council of Ministers in consultation with the Monetary Policy Council. The Council of Ministers, in consultation with the Monetary Policy

Council, defines principles for the determination of the exchange rate of the zloty to foreign currencies. Current exchange rates, though, are published by the NBP.

Until 1998, the NBP realized an indirect strategy concerning how supply of money was shaped and implemented a principle of stepwise devaluation of the zloty with respect to the currency basket. Fluctuations in the actual exchange rate of the zloty, however, were allowed only within the permissible brackets.<sup>67</sup> Since 1999, however, the Monetary Policy Council has determined the direct inflation target among principles of monetary policy. In order to run the monetary policy, the NBP makes use of instruments provided by the law. The central bank is allowed to provide refinancing loans, rediscount bills of exchange and grant lombard loans. Bank's administrative instruments include primarily the reserve requirement which, since October 2003, has amounted to 3.5% of deposits in zlotys and foreign currencies. Open market operations and interest rate policy, connected with loan/deposit operations are market instruments. Because in 2002 favorable conditions for the realization of the short- and medium-term inflation target occurred, decisions about interest rates reduction were taken several times. The interest rates of the NBP for the end of 2002 were as follows (*Założenia, 2002*)<sup>68</sup>:

- reference rate: 6.75%;
- rediscount rate: 7.5%;
- lombard rate: 8.75%;
- deposit rate: 4.75%.

Moreover, the MPC reduced the inflation target for 2002 from 4-6% to 2-4% and specified that the inflation target for the medium-term monetary policy strategy should be 3% with a tolerance of +/- one basis point (*Założenia, 2002*). As a result, a decrease in interest on money market instruments was observed. The average monthly rate of WIBOR 1M came down from 12.5% in December 2001 to 7.1% in December 2002. Following the decrease of money market interest rates, banks reduced interest rates on loans and deposits. Weighted average interest on deposits in zlotys came down to 1.2% for checking accounts and 4.3% for household and business entity deposits; in the case of loans for enterprises interest rates came down from 15.7% (2001) to 10.6% whereas for private persons from 20.8% (2001) to 17.5%. Thus interest rates in Poland were record low since the beginning of economic transformation.

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<sup>67</sup> Monetary policy conducted between 1989 and 1998 is discussed in detail in: Pietrzak (1999, pp. 104-131).

<sup>68</sup> Following the low inflation rate in 2003 (approximately 1% annually), the MPC gradually reduced official interest rates. For the end of June, 2003 interest rates were as follows: reference rate – 5.25%, rediscount rate – 5.75%, lombard rate – 6.75%, deposit rate – 3.75%. It must be pointed out; however, that ever less was the response of market interest rates to successive reductions.

### ***Banking supervision and prudential regulations***

Banks' activity in Poland is supervised by a joint institution, that is, the Commission for Banking Supervision (CBS, *Komisja Nadzoru Bankowego*); its executive organ is the General Inspectorate of Banking Supervision (GIBS, *Generalny Inspektorat Nadzoru Bankowego*)<sup>69</sup>, separated from the structure of the NBP. The President of the NBP presides over the CBS as its Chairperson. Moreover, the following persons sit in the commission: the Minister of Finance, or a secretary delegated by the Minister, a representative of the President of Poland, the President of the Management Board of the Bank Guarantee Fund, the President of the Securities and Exchange Commission or his/her deputy, representatives of the Minister of Finance and the General Inspector of Banking Supervision.

The Commission is obliged to shape bank's operation, supervise banks as to whether they abide by the law, the statute and other regulations or financial norms they have to observe as well as estimate banks' financial condition and security of the banking sector. Furthermore, according to its prerogatives, the Commission takes decisions concerning reparatory proceedings in banks, takeovers, liquidations, bankruptcy claims, etc.

**Table 5.1:** Prudential regulations for banks operating in Poland (for December 31, 2002)

<b>Regulation</b>	<b>Norm</b>
Own funds minimum	EUR 5 million 1 million for cooperative banks
Solvency ratio	8% (15 and 12% for newly established banks)
Reserve requirement	3.5% (from October 2003); reserves are interest-free – from May 2004 it is planned to introduce the market interest rate.
Concentration limits	
· with respect to one client	· 25% (20% for entities associated with the bank)
· with respect to the total commitment (over 10%)	· 800%
Currency risk	for the end of each working day: the individual currency position with respect to a single currency may not exceed 15% of bank's own funds in the case of convertible currencies and 2% in the case of inconvertible currencies; the total currency position

<sup>69</sup> Before January 1, 1998 it was the NBP that was responsible for banking supervision. The Commission for Banking Supervision was called into being under acts of August 29, 1997: the Banking Law Act and the Act on the National Bank of Poland. The issue of evolution of banking supervision is presented in detail in: Kwaśniak (2003a, pp. 31-40).

Regulation	Norm
	with respect to foreign inconvertible currencies may not exceed 5% of bank's own funds; the total currency position for all foreign currencies total may not exceed 30% of bank's own funds; daily data on currency position are reported with the GINB on a ten-day basis.
Reserves for irregular loans	2% – monitored loans 20% – substandard loans 50% – doubtful loans 100% – lost amounts due
Restrictions in investments in securities on own account <sup>a</sup>	15% of own funds with respect to one non-banking entity; the total may not exceed 60%.
Obligation to report with the CBS the intention to purchase shares in a bank and to obtain permission to exercise resulting rights.	5, 10, 25, 33, 50, 75%

<sup>a</sup> Restrictions are not applicable to, among others, banks, inter-bank telecommunications firms, entities which run brokerage firms, open-end and staff retirement funds, bank survey agencies, enterprises which render some types of services to the bank, such as bank cards, education of bank staff or consultations on financial matters.

Source: Banking Law Act of August 29, 1997 (Journal of Laws z 2002 , no. 72, item 665 – consolidated text, of 2001 , no. 130, item 1450, of 2002 , no. 126, item 1070, no. 144, item 1208, no. 141, item 1178, of 2001 , no. 111, item 1195 – amendment moved, of 2002 , no. 169, item 1385 and 1387, no. 241, item 2074); Resolution no. 13/98 CBS of December 22, 1998 (Official Journal of the NBP no. 29 of 2.12.98, item 65).

The reserve requirement system, which puts an obligation on commercial banks to keep financial reserves in the central bank, is one of the main instruments of NBP's influence on commercial banks. The NBP Act of 1997 introduced a broad definition of banks' reserve requirement which includes financial means deposited in bank accounts in zlotys and funds earned by banks from sale of securities and other returnable funds deposited in the bank. In the 1990s, the reserve requirement was very high; furthermore, reserves were without interest. They were for banks in fact a kind of a hurtful para-tax which lowered their profitability and influenced interest rates on loans. In 1999, part of requirement was converted into NBP bonds. Banks were obliged to keep those bonds in their portfolio until bought back by the NBP.

### ***Deposit guarantees***

In December 1994, the Bank Guarantee Fund Act (BGF, *Bankowy Fundusz Gwarancyjny*) was passed. The Fund has to: protect depositors, establish systemic conditions for granting financial aid to banks threatened with insolvency and monitor financial situation of entities covered by the deposit guarantee system<sup>70</sup>.

The Council of the Fund and the Management Board are the governing bodies of the Fund. Banks' employees may not be members of these bodies. The Council consists of the President and ten members. The President of the Council is appointed (for four years) and recalled by the Prime Minister upon joint request from the Minister of Finance and the President of the NBP with an opinion from the relevant committee of the Sejm. The BGF Management Board is appointed by the Council for three years and has five members.

All domestic and foreign banks which operate in Poland on the basis of the Banking Law Act and regional associations from the day of consolidation of their financial accounts partake in the guarantee system. Protection covers all guaranteed funds, that is, funds deposited in the bank by depositors in personal accounts and depositors' balances due resulting from other banking activities. A natural person, a legal entity or an organizational unit without legal personality can be a depositor, without, however:

- banks;
- the Treasury;
- entities operating under Public Securities Trade Act.
- banks' shareholders who, on the point when the bankruptcy application is filed, have over 5% of votes at the general meeting of shareholders;
- banks' top executives.

Should the court decide about bank's bankruptcy, the BGF pays out depositors funds deposited in accounts up to the amount provided by the law. Under the law, from 2003 on, funds to the amount of EUR 1,000 are to be paid out in full, while of the remaining sum (up to EUR 22,500) 90% is to be paid out. After a bank is declared bankrupt, guaranteed funds are paid out by the receiver in bankruptcy in places made publicly known. Then, for five years from the date of declaration of bank's bankruptcy, the Bank Guarantee Fund pays out amounts due.

The Fund is financed with obligatory annual fees paid by banks, funds from the guaranteed money protection fund, income from interest on loans granted by

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<sup>70</sup> Bank Guarantee Fund Act of December 14, 1994 (Journal of Laws of 2000, no. 9, item 131, consolidated text, no. 86, item 958, no. 119, item 1252 and of 2001, no. 154, item 1802).

the Fund, funds from non-returnable foreign aid, funds from loans granted by the NBP, and others.

Funds for the payout of guaranteed sums are acquired by the BFG from banks covered by the guarantee system. Each of these entities is obliged to establish a so-called guaranteed money protection fund to satisfy claims from bankrupt banks' depositors. The amount the guaranteed money protection fund is a product of a rate of 0.4% and the sum of funds accumulated in the bank in all accounts on the basis of which the amount of reserve requirement is calculated.

Moreover, all banks contribute annual fees. The BGF Council, before the end of November of each year determines rates for the following year. Entities covered by the guarantee system pay obligatory annual fees to the Fund, equal to the sum of products of<sup>71</sup>:

- a rate of 0.4% maximum and the sum of balance assets as well as risk-weighted guarantees and sureties;
- a rate of 0.2% maximum and the sum of other off-balance liabilities, risk-weighted.

As of January 1, 2001, obligatory annual fees have been reduced by 50% with the difference paid to the BGF by the NBP. Banks are obliged to contribute fees according to deadlines provided by the Fund, by not later than until March 31 of the following year. Funds to be contributed to the BFG do not have to be deposited in NBP's account. They may be invested in assets which constitute the coverage of the Fund (treasury bonds and NBP bonds).

Furthermore, the Bank Guarantee Fund grants returnable financial aid to banks on terms more favorable than on the market. Such aid, however, is granted only in certain cases and may be used only to eliminate threat of insolvency or to purchase bank's shares by its new shareholders. Financial aid granted by the Fund may not be higher than the total maximum amount of funds guaranteed by the system and deposited on depositors' accounts in the bank threatened with insolvency.

### ***Settlement system***

Settlements between banks are concluded through the clearing house. Banks which conclude settlements are obliged to have current accounts in the NBP.<sup>72</sup> Settlements can also be effected through banks which maintain accounts for other domestic banks or through direct exchange of orders between banks (Srokosz, 2003, p. 232).

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<sup>71</sup> Bank Guarantee Fund Act of December 14, 1994, op. cit, Art. 13.

<sup>72</sup> Disposition 2/98 of the President of the NBP of March 5, 1998, Official Journal of the NBP, no. 3.

The exchange of payment documents is concluded through a bank which is a direct member of the National Clearing House (NCH, *Krajowa Izba Rozliczeniowa SA*). The establishment of the National Clearing House was a major event in the reform of Polish banking as until 1993 the NBP had been a central settlement institution and functioned as a clearing house for settlements between banks. The National Clearing House was created November 22, 1991 with 16 largest banks, the NBP and the Polish Banks Association as founder-shareholders (Ołdakowski, 1999). The NCH is a joint-stock company and it consists of the Head Office in Warsaw and 17 Bank Regional Clearing Houses (BRCH, *Bankowa Regionalna Izba Rozliczeniowa*) seated in the Polish largest cities. The NCH is responsible for all kinds of activities concerning registration and compensation of liabilities as well as submission of orders to the NBP to execute inter-bank settlements (Szczygielska, 1998, p. 122).

Every bank which is licensed to operate in Poland can be a member of the Clearing House. One of the conditions for the accession to the KIR is to sign an agreement with the NBP for a bank account and an agreement which makes it possible to get a lombard loan. Additionally, every bank must have an application which monitors settlements on the basis of the ELIXIR system. Banks must also achieve technological readiness for the execution of settlements.

The following inter-bank settlement systems, based on net settlements, are available within the KIR:

- SYBIR – system for the exchange of paper-based payment orders (so-called Paper House);
- ELIXIR – electronic clearing house;
- IMBIR – a system which scans and processes paper documents;
- SZAFIR – system for public key certification management.

From its start in 1993 until 2001, the SYBIR serviced approximately 378 million settlement and courier items. In the years 2001-2002 a significant decrease in settlement operations in this system was observed with the electronic system in the ascendancy.

In the aftermath of the start (April 18, 1994) of the electronic settlement system, ever fewer paper documents were sent between banks. From 1998, each member of the KIR has been obliged to participate in both the SYBIR and the ELIXIR systems. The latter is a net settlement system where result orders to be booked in banks' accounts result from compensation of mutual liabilities and amounts due. Settlement sessions are held in the Head Office of the NBP.

In 2000, in the efforts to improve the settlement system, the range of services was extended by the addition of the IMBIR system which optically reads and converts paper settlement documents into electronic documents. In 2002 the system handled approximately 38 million documents and 700 bank offices were serviced by the system in December 2002.

Although the paper clearing house will soon terminate its operation, three new types of services have been introduced which modify the SYBIR system. These consist in the conversion of paper documents into electronic ones. Due to dynamic changes in traditional forms of settlement and the domination of the ELIXIR system, it was decided in 2002 to terminate the SYBIR system by the end of 2004.<sup>73</sup>

Total turnover transferred by means of the SYBIR system in 1997-2001 amounted to over PLN 3214.5 million. However, due to the fast rate of decrease of the turnover in relation to the number of items sent in the SYBIR system, from 1997 a steady decrease in the average value of a settlement item was recorded. In 1997 it was PLN 21,000 whereas in 2002 – PLN 11,600.

The ELIXIR system has been developing quickly with respect to both the number of transactions and turnover. In the years 1997-2001 the system handled almost 644,734 thousand transactions for over PLN 11,000 billion. What was also observed was an increasing share of transactions handled by the ELIXIR system compared to the SYBIR. In 2001, 93.3% of the total turnover was handled by the ELIXIR. In 2001, the system handled over 519 million transactions for PLN 4,561 million total.

The final settlement, resulting from both electronic and paper house systems is conducted by the NBP within the SORBNET (System for Banks' Accounts Servicing). This system, based on real time gross settlements, also realizes banks' payment orders. Since 2003, all large-amount payments (over PLN 1 million<sup>74</sup>) must be sent through this system, apart from social security payments and payments executed on the basis of checks and other debit payment orders.

The SORBNET system started in April 1996. In 2002 the NBP operated accounts for 62 banks, direct members of the NCH. Banks which apply for the current account in the NBP must submit a positive opinion from the CBS and the approval from the President of the NBP.

The SORBNET system minimizes credit risk. In case of problems with liquidity, banks make use of lombard loans and resources from reserve requirement. No possibility is, though, provided for granting day and overnight loans if temporary difficulties with resources for settlements occur.

### ***Commercial banking***

It is universal and cooperative banks that provide the basis for the Polish banking system. Commercial banks were being established and developed following the 1989 reforms. The banking law of 1989 made it possible to form a two-tier banking system typical for market economies. The key process for banks was

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<sup>73</sup> Some banks decided it earlier to abolish the paper system completely and from 2002 they have used the electronic system only.

<sup>74</sup> Disposition no. 15/2001 of the President of the NBP of December 11, 2001.

privatization with the increase in foreign capital's share in the sector. Polish banking sector's development was effected through license policy and privatization followed by consolidation of banks.

Privatization was possible in the aftermath of processes, such as the establishment of new private banks, accompanied by liberal license policy. Subsequently, the priority was given to privatization of commercial banks, separated from the NBP in 1989 with Bank Rozwoju Eksportu first, Wielkopolski Bank Kredytowy second and Bank Śląski third. Privatization slowed down in the mid-1990s (*Bankowość krajów tworzących*, 1998, p. 132 and further). First consolidation processes began in 1993. In 1996 an act was passed on the merging and consolidation of some banks operating as joint-stock companies. On the basis of this act Grupa Pekao SA was established, consisting of Pekao SA and three banks which had emerged from the NBP in 1989. In 1997 Bank Inicjatyw Gospodarczych SA took over Bank Gdański SA. Also in 1997 a new group was established with Kredyt Bank as the main entity. Moreover, Bank Handlowy w Warszawie SA was privatized.

Profound changes in banking sector's ownership structure occurred in 1996 when foreign strategic investors took over shareholding in two stock exchange companies. In June 1996, Allied Irish Banks increased its share in WBK SA from 16.3% to 36.3% and in 1997 to over 60%, whereas in 1996 ING acquired shareholding in Bank Śląski SA of 54.1% of votes at the annual meeting of shareholders. In 1995, public offer for Bank Przemysłowo-Handlowy was announced so as to retain the possibility of using means from the Polish Banks' Privatization Fund. However, shares of this bank did not raise considerable interest. A block of shares remained which only in late 1998 was sold to a strategic investor, Bayerische Hypo- und Vereinsbank which for the end of 1999 had a share of 81.5%. For some period of time this bank was a minority shareholder but it made efforts to take up a share in BPH SA which guaranteed independence with respect to any decisions taken. Only in 1997 was the public offer for Powszechny Bank Kredytowy SA announced with Creditanstalt as the principal investor (soon taken over by the Bank Austria). For the end of 2000 Bank Austria Creditanstalt had a share of 53.7% in PBK SA.<sup>75</sup> In 2000 the global market witnessed the takeover of Bank Austria Creditanstalt by Bayerische Hypo- und Vereinsbank AG; thus, the BPH SA and the PBK SA were members of the same capital group. From January 1, 2002, through the merger of BPH SA and PBK SA, the BHV AG capital group began establishing a leading universal bank in Poland.<sup>76</sup>

Other private investors in privatized banks were: Commerzbank AG in BRE Bank SA (50% shares for the end of 2000); Citibank in Bank Handlowy w Warszawie SA (87.8% shares for the end of 2000) (*Sytuacja finansowa*

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<sup>75</sup> After Bank Austria Creditanstalt Polska joined PBK SA, the share increased to 57.1%.

<sup>76</sup> On July 4, 2001 Management Boards of PBK SA and BPH SA adopted a plan to consolidate both banks.

*banków w 2000 roku*, 2001, pp. 5-6). On March 1, 2001 these banks merged and they operate as Citibank Handlowy. In August 1999 a consortium of UniCredito Italiano SA and Allianz AG took up 52.09% of shares in Pekao SA.

Finally, the last bank separated from the NBP in 1989 owned by the Treasury, that is, Bank Zachodni, was privatized. The AIB European Investments Ltd. became the strategic investor and took up 80% shares. Contrary to those concluded before 1999, privatization agreements of Bank Zachodni, Pekao SA and Bank Własności Pracowniczej SA contained provisions that obliged investors to significantly raise stock capital of the privatized banks. In June 2001, the owner of WBK SA and Bank Zachodni SA merged both institutions under the name of Bank Zachodni WBK SA.

For the end of December 2002, 62 commercial banks operated in Poland, including 53 private banks (8 with a dominant share of Polish capital). The number of cooperative banks decreased from 642 (for the end of 2001) to 605 (for the end of 2002). Two cooperative banks conducted independent activity whereas others were associated in three structures: Mazowiecki Bank Regionalny SA (78 banks), Gospodarczy Bank Wielkopolski (157 banks) and Bank Polskiej Spółdzielczości (368 banks). The structure of the Polish banking sector (number of banks and share of foreign capital) is presented in Table 5.2.

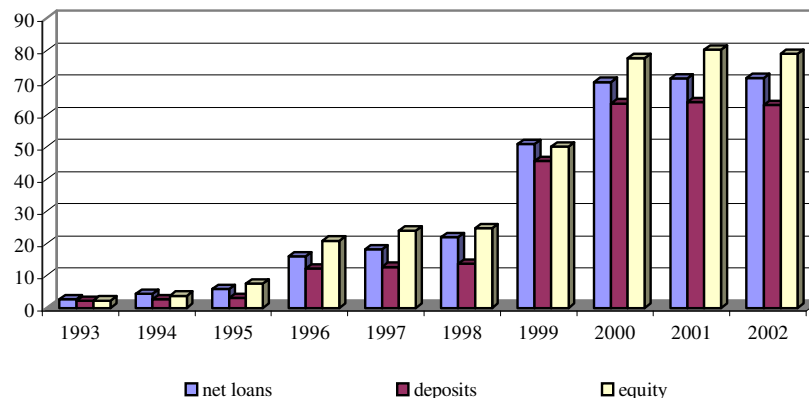
**Table 5.2:** Structure of the Polish banking sector in the years 1993-2002

<b>Banks</b>	<b>1996</b>	<b>1997</b>	<b>1998</b>	<b>1999</b>	<b>2000</b>	<b>2001</b>	<b>2002</b>
Commercial (total)	81	83	83	77	74	71	63
With a majority of state capital	24	15	13	7	7	7	8
Controlled by foreign capital	25	29	31	39	47	48	47
Cooperative	1394	1295	1189	781	680	642	605

Source: NBP.

For September 31, 2002, foreign entities directly controlled 16 banks (joint-stock companies) with 100% share of foreign capital, 1 branch of a foreign bank and 20 companies with a majority of foreign capital as well as 8 banks indirectly (*Sytuacja finansowa banków w okresie styczeń–wrzesień 2002 rok*, 2003). For the end of December 2002, funds and net assets of 45 banks controlled by foreign capital amounted to 78.4% of funds and 67.2% of net assets of the banking sector. These banks accumulated 62.20% of non-finance sector deposits and granted 70.5% of loans, net (*Sytuacja finansowa banków w okresie styczeń–wrzesień 2002 rok*, 2003). In this period, investors from 15 countries operated in the Polish banking sector with the largest share of Germany, the United States, the Netherlands and Ireland followed by Belgium, France, Portugal, Sweden, Austria and Italy.

**Chart 5.1:** Total share of foreign capital in net loans, deposits and equity of the Polish banking sector in the years 1993-2003, %



Source: compiled on the basis of: *Sytuacja finansowa banków w 2002 roku* (2003).

The ten largest commercial banks controlled a total of 76.8% of banking sector assets. The 15 largest banks controlled 85% of banking sector deposits, almost 80% of loans and over 82% of assets (*Sytuacja finansowa banków w 2002 roku*, 2003).

From 2000 a systematic decrease in employment in the banking sector has been observed, especially in large banks which have undergone consolidation and reorganization. Development of modern distribution channels has also had an impact on employment reduction. Whereas in 1998 149,067 people were employed in the commercial banking sector, in 2002 employment came down to 131,874. Similarly, due to consolidation processes and development of modern distribution channels, the number of traditional banking offices decreased (see Table 5.3).

**Table 5.3:** Selected data about the Polish commercial banking sector

	1998	1999	2000	2001	2002
Employment	149,067	149,638	144,237	138,822	131,874
Number of banking offices	9,746	10,428	11,470	10,721	9,962

Source: *Sytuacja finansowa banków w 2002 roku* (2003).

From the beginning of reforms the ratio of bank assets in relation to GDP increased (48.8% in 1995 and over 65% of GDP in 2001) which means that a slow but systematic increase in this indicator was observed. In 2002, however, for the first time since 1993, the amount of bank assets diminished. Deterioration of banks' situation resulted from factors such as: new principles for valuation of assets, unfavorable economic conditions and, finally, large amount of targeted reserves, established by banks in case of irregular loans.

**Table 5.4:** Development of the Polish banking sector in the years 1998-2002 (PLN millions)

	1998	1999	2000	2001	2002
Assets	318,726	363,427	428,486	469,706	467,118
Equity	22,467	25,766	30,688	37,768	40,592
Gross profit	1,825	3,181	4,212	4,232	2,723

Source: *Sytuacja finansowa banków w 2002 roku* (2003).

In 2002, the quality of banks' loan portfolio decreased. The dynamics of irregular loans was higher than the increase in gross amounts due. The share of irregular loans for the end of 2002 was 21.4% total of commercial banks' loan portfolio. The share of irregular loans from the non-financial sector in the portfolio reached the level of 1995, the year when the restructuring period after the debt crisis of the early 1990s ended. Irregular amounts due, which called for the establishment of targeted reserves, made up over 10% of the portfolio, including 7.4% of lost dues (*Sytuacja finansowa banków w 2002 roku*, 2003).

**Table 5.5:** Structure of non-performing loans from the non-financial sector, gross in commercial banks in Poland in the years 1998-2002, %

Dues	1998	1999	2000	2001	2002
Lost	4.9	4.8	5.8	8.5	11.1
Doubtful	2.0	3.6	5.4	5.3	5.5
Substandard	4.0	5.3	4.5	4.8	4.8

Source: *Sytuacja finansowa banków w 2002 roku* (2003).

The result of a general recession in banking was that banks' development was stopped. Banking activity results in 2002 were only 0.2% higher than in 2001. Due to disproportion between the increase in results and the write-off for targeted reserves, the gross result decreased and the net result was almost 40% lower than in 2001. Accordingly, performance indicators came down (Table 5.5). The cost index (total costs/total income) increased by 2.1 basis points.

In 2002 banks' interest income increased by a small amount. Mark-ups came down to 3.2%, which was not made up for by banks' income from fees and commissions although they increased in 2002 by 7%. Interest income was to a large extent influenced by dues classified as threatened, as interest from these dues was not included in the income.

**Table 5.6:** Operational costs of commercial banks in Poland per one banking office or employee and performance

Indicator	2001	2002
Material costs per one banking office (PLN thousands)	1,643	1,681
Salary costs per one employee (PLN thousands)	55.5	57.2
Gross profit per one employee (PLN thousands)	37.3	28.5
Assets per one employee (PLN thousands)	3,158	3,276

Source: *Sytuacja finansowa banków w 2002 roku* (2003).

Banks still reduced labor costs through reduction of employment. Investments in modern technologies and high depreciation rate resulted in the increase in material costs. In 2002, operational costs increased to 63.1% (Table 5.6). Banks made every effort to reduce costs; many banks, however, had already completed reorganization and reduction of employment following implementation of modern technologies.

**Table 5.7:** Performance of banks in Poland in the years 1998-2002

Indicator	1998	1999	2000	2001	2002
ROE	9.2	12.9	14.5	12.8	6.2
ROA	0.7	0.9	1.1	1.0	0.5
Operational costs/banking activity results	62.2	64.5	62.8	61.9	63.1

Source: *Sytuacja finansowa banków w 2002 roku. Synteza* (2003).

Banks develop electronic banking services, including modern distribution channels, such as the Internet and cell phones (WAP). Majority of large commercial banks and more and more small banks offer access to accounts via the Internet. Three banks (BRE Bank SA, PKO BP SA and Volkswagen Bank Polska SA) run so-called virtual banks (mBank, Inteligo and Volkswagen Bank Direct).

**Table 5.8:** POS terminals, ATMs and credit cards in Poland in the years 1998-2002

	1996	1997	1998	1999	2000	2001
Number of POS terminals per 1 million people	67	119	229	543	1,158	1,698
Number of POS transactions per person	0.04	0.1	0.1	0.3	1	2
Average POS transaction value (EUR)	86	75	52	38	43	43
Change in the number of POS terminals (%)	110	78	93	137	113	47
Number of ATMs per 1 million people	14	37	54	102	136	168
Number of ATM transactions per person	0.2	1	1	2	6	7
Average ATM transaction value (EUR)	35	47	36	51	60	65
Number of credit cards per thousand people	-	-	-	-	13	23

Source: European Central Bank Blue Book, August 2002, Annex I, Comparative Tables.

Card activity of banks operating in Poland in the period in consideration quickly developed. For the end of September 2002, clients had over 16,162 thousand bank cards, with the majority (98.6%) of debit cards which could also be used in ATMs. Accordingly, the number and value of transactions concluded with bank cards increased to PLN 78.5 billion for the end of September 2002.