

Banking Supervision



3. Banking Supervision

3.1. Development of the banking sector

The positive trend of the banking sector's development continued in 2004. In the year under review, in particular in its last quarter, the already launched trend of the risk-based supervision was fully manifested. The Banking Supervision Division, besides issuing methodological instructions, focused on the implementation of rules relating to additional supervision of financial conglomerates, as well as on the legal framework of integrated supervision of the financial market.

In connection with the performance of on-site inspections it may generally be said that compared to past years there has been a reduction in the number and severity of findings resulting from inspections at banks. This fact results from the new strategy of the Banking Supervision Division, which undertakes on-site inspections with greater intensity and frequency and which, in turn, has a positive impact on the banks' efforts towards improvement and qualitative growth.

As at 31 December 2004, there were eighteen banks, three branches of foreign banks, forty-eight providers of free cross-border banking services, and seven representative offices of foreign banks, operating in the Slovak banking sector. Of the eighteen banks, there are three building societies: ČSOB stavebná sporiteľňa, a.s., Prvá stavebná sporiteľňa, a.s., and Wüstenrot stavebná sporiteľňa, a.s. As at 31 December 2004 the licence to provide mortgage services was held by nine banks and one branch of a foreign bank (HVB Bank Slovakia, a.s., Dexia banka Slovensko, a.s., ISTROBANKA, a.s., ĽUDOVÁ BANKA, a.s., OTP Banka Slovensko, a.s., Slovenská sporiteľňa, a.s., Tatra banka, a.s., UniBanka, a.s., Všeobecná úverová banka, a.s. and Československá obchodní banka, a.s., branch of foreign bank in the SR).

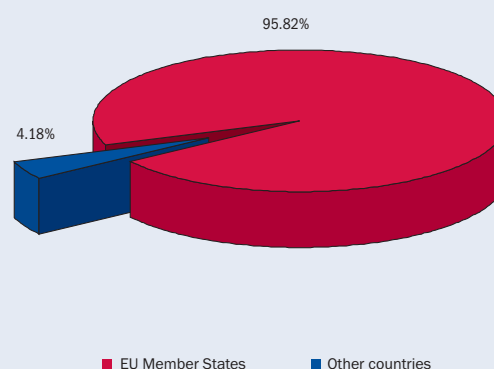
The volume of subscribed share capital of banks (excluding the NBS) increased by SKK 1.0 billion compared with the figure for 31 December 2003, i.e. from SKK 40.4 billion to SKK 41.4 billion. The development of share capital was affected by the subscription of new shares in Poštová banka, a.s. and in ISTROBANKA, a.s.

The amount of funds provided by foreign banks to their branches remained unchanged, and as at 31 December 2004 equalled SKK 2.8 billion.

The share of foreign investors in the total subscribed share capital of banks and the funds provided by foreign banks to their branches increased on the previous year from 88.9% (as at 31 December 2003) to 89.6% (as at 31 December 2004). The increase was affected by the entry of a foreign investor into Banka Slovakia, a. s., accompanied by a rise of the share of foreign investors in the share capital of: ISTROBANKA, a.s.; ĽUDOVÁ BANKA, a.s.; Slovenská sporiteľňa, a.s.; Tatra banka, a.s.; Wüstenrot stavebná sporiteľňa, a.s.; and UniBanka, a.s. In addition, the above share was influenced by a reduction in the share capital of Tatra banka, a.s., as well as by raising the share capital of Poštová banka, a.s. by a local investor.

On 13 February 2004, the National Bank of Slovakia granted prior approval to Istrokapitál, a.s. to exceed its interest in share capital and voting rights of Poštová

Chart 32 Share of foreign investors by country of origin



Source: NBS.

Other states: the United States, Switzerland and Canada. The share of EU member states in 2004 increased on the year earlier by 14.43%. This increase was due in particular to the re-ordering of two states, the Czech Republic and Hungary into this group following their accession to the European Union. At present the EU member states are ranked as follows: Austria (36.07%), the United Kingdom (4.40%), the Czech Republic (8.79%), France (1.39%), Germany (2.17%), the Netherlands (1.55%), Hungary (5.05%), Italy (4.82%), and Luxembourg (31.58%).



banka, a.s. by 50% in relation to the raising of share capital of the bank by the mentioned company.

On 15 March 2004 the National Bank of Slovakia granted prior approval to the NPF of the SR to acquire the share in the share capital and voting rights of Slovenská sporiteľňa, a.s. owned by the Ministry of Finance of the SR, which represented a share of 10%. This share was (according to the record from the Central Depository of Securities as at 30 April 2004) transferred to ERSTE BANK DER OESTERREICHISCHEN SPARKASSEN AG, Vienna, a total share of which in the share capital of Slovenská sporiteľňa, a.s. was 80.01%.

On 23 April 2004 the decision of the National Bank of Slovakia to withdraw the banking licence from DEVÍN BANKA, a. s. entered into force.

In 2004 the trade name of Stavebná sporiteľňa VÚB-Wüstenrot, a. s. was changed to Wüstenrot stavebná sporiteľňa, a. s. and CREDIT LYONNAIS BANK SLOVAKIA, a. s. was changed to CALYON BANK SLOVAKIA a. s.

The National Bank of Slovakia in its decision of 3 December 2004 gave prior approval to Poštová banka, a. s. to change its registered office from Gorkého ulica to Prievozská ulica in Bratislava. As at 31 January 2005 the bank sent an excerpt from the Commercial Register documenting the entry of this change.

On 5 February 2004 the National Bank of Slovakia registered the representative office of ABN AMRO Bank N. V., Amsterdam, AG in Bratislava. Based on the application submitted by COMMERZBANK Aktiengesellschaft, Frankfurt am Main on 27 February 2004, the National Bank of Slovakia cancelled the registration of the representative office of the mentioned bank. Based on the application submitted by Dresdner Bank AG, Frankfurt am Main on 14 May 2004, the National Bank of Slovakia cancelled the registration of the representative office of the mentioned bank. Total number of representative offices of foreign banks was seven as at 31 December 2004.

Following the Slovak Republic's accession to the European Union the provisions of Articles 11 to 20 of the Act on Banks entered into force, on the basis of which credit institutions registered in the European Economic Area (all EU member states plus Norway, Lichtenstein and Iceland) may conduct banking activities in the Slovak Republic without a banking licence granted by the National Bank of Slovakia, provided the bank has been granted a banking licence in its home state (the principle of a single banking licence). The principle of a single banking licence applies to all banking activities listed in the Act on Banks, except:

- the provision of mortgage loans pursuant to Article 67 paragraph 1 of the Act on Banks, and
- acting as depository pursuant to the Act on collective investment.

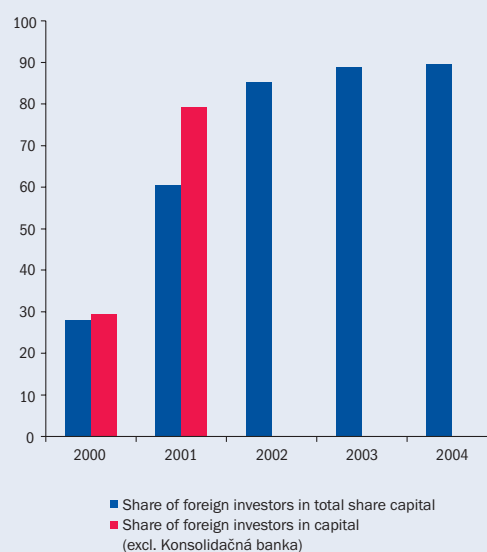
For these activities a licence must still be obtained from the National Bank of Slovakia.

ING Bank N. V. Amsterdam decided that following 1 May 2004 it would conduct banking activities in the SR on the basis of a banking licence granted to it in the Kingdom of the Netherlands. In this regard, on 9 August 2004 it returned the banking licence issued by the National Bank of Slovakia and on the same day the National Bank of Slovakia's decision granting a banking licence to the Bank for performing the function of a depository by means of its organisational unit – a branch of foreign bank – entered into force. As of 9 August 2004 ING Bank, a. s., Bratislava, has operated on the basis of a single banking licence, i.e. it is supervised and regulated by the home state supervisory authority, in this case De Nederlandsche Bank.

Likewise, COMMERZBANK Aktiengesellschaft, Frankfurt am Main returned its banking licence on 23 August 2004 and on this day the branch of this foreign bank also began to operate on the basis of the single banking licence, i.e. being supervised and regulated by the home state supervisory authority, in this case Bundesanstalt für Finanzdienstleistungsaufsicht.

Both branches remain obliged to provide regular information about their activities to the National Bank of

Chart 33 Share of foreign investors in the share capital and funds provided by foreign banks to their branches (%)



Source: NBS.

Table 37 Foreign banks in the SR

EU Member State	No. of foreign banks
Denmark	1
France	2
the Netherlands	2
Ireland	3
Luxembourg	1
Hungary	2
Germany	9
Austria	9
United Kingdom	18
Italy	1

Source: NBS.

Slovakia; at the same time the National Bank of Slovakia performs supervision of the branches' liquidity, though the mentioned foreign supervisory authorities are authorised to impose fines and perform corrective measures and perform on-site inspections associated with prudential banking activities of the respective branch, in some instances also in cooperation and coordination with the NBS.

On the basis of notifications sent by foreign supervisory authorities pursuant to Article 11(2) of the Act on Banks and Article 21 (2) of Directive 2000/12/EC relating to the taking up and pursuit of the business of credit institutions on the intention of a foreign bank to perform, or provide, banking activities stated in Annex 1 to the Directive, the Banking Supervision Division as

at 31 December 2004 registered forty-eight entities, or foreign banks freely providing cross border banking services (Table 37 shows the breakdown of foreign banks by country).

3.2. Economic results of the banking sector

The total assets (total net assets) for the twenty-one banks of the SR banking sector had grown as at the end of 2004 in comparison with the end of 2003 by SKK 177.5 billion (by 18.0%) to SKK 1,162.9 billion.

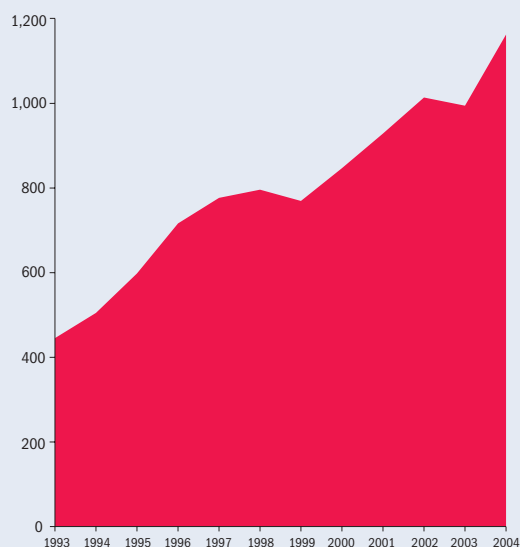
The development of the banking sector's total assets was influenced both by the growth of secondary funds (SKK 86.8 billion), as well as primary funds (SKK 83.1 billion). The volume of non-anonymous deposits grew by SKK 17.5 billion (by 4.3%) to SKK 423.3 billion.

The volume of earning assets reported by the banking sector grew in comparison with the end of 2003 by SKK 182.4 billion to SKK 1,091.0 billion. The share of earning assets in total assets had over the course of 2004 a similarly growing trend and as at 31 December 2004 reached 93.8%, representing a growth of 1.6% compared to the end of 2003.

Total claims from loans reported by banks as at the end of 2004 were SKK 442.4 billion. Classified loans fell by SKK 4.2 billion to SKK 31.7 billion, i.e. by 11.6%. Banks created SKK 25.5 billion in provisions. Coverage of classified loans by created provisions as at the end of 2004 stood at 80.4%. The share of classified loans in total loans fell to 7.2%.

Banks reported a net profit as at 31 December 2004 of SKK 12.3 billion. In a year-on-year comparison this represents a growth of SKK 1.0 billion (8.5%). One bank reported a loss for the current period as at 31 December 2004 (at 31 December 2003 two banks reported a loss).

Chart 34 Development of the Slovak banking sector's total assets (as at 31 December) (SKK billions)



Source: NBS.

3.3. Evaluation of the banking sector's risks

Banking entities take on a number of risks related to the conditions under which they conduct business. Specific risks arise in direct connection to banking activities and result from the internal conditions of the given sector, types of business, clientele, types of technology, etc. The main risks of banking business include credit risk, market risks (exchange rate/currency risk, interest rate risk, equity risk, commodity risk) liquidity risk and country risk.

Banking operations are also exposed to other risks which, however, are difficult to quantify and regulate,

Table 38 **Banking sector of the SR**

	31 Dec. 2003	31 Dec. 2004	Difference Dec. 04/Dec. 03	Change Dec. 04/Dec. 03
Number of employees	19,797	19,720	-77	-0.39%
Number of banks in the SR	18	18	0	0.00%
Number of branches of foreign banks in the SR	3	3	0	0.00%
Number of representative offices of foreign banks in the SR	8	7	-1	-12.50%
Number of branches in the SR	553	587	34	6.15%
Number of lower organisational units in the SR	504	526	22	4.37%
Number of branches in other countries	1	1	0	0.00%
Number of lower organisational units in other countries	2	0	-2	-100.00%
Number of representative offices in other countries	1	1	0	0.00%
Total assets (in SKK thousand)	985,445,707	1,162,935,361	177,489,654	18.01%
Earning assets (in SKK thousand)	908,597,027	1,090,962,975	182,365,948	20.07%
Total interbank assets (in SKK thousand)	271,575,986	378,117,213	106,541,227	39.23%
Total foreign exchange assets (in SKK thousand)	146,048,650	167,212,165	21,163,515	14.49%
Securities (in SKK thousand)	358,364,029	377,791,590	19,427,561	5.42%
Total loans (in SKK thousand)	395,154,645	442,361,143	47,206,498	11.95%
of which: classified loans (in SKK thousand)	35,868,781	31,703,394	-4,165,387	-11.61%
loans to households (in SKK thousand)	85,113,661	116,806,841	31,693,180	37.24%
loans to non-financial corporations (in SKK thousand)	247,933,822	225,925,388	-22,008,434	-8.88%
Share of classified loans in total loans (%)	9.08	7.17	-1.91	-
Uncovered expected loss (in SKK thousand)	510,688	10,355	-500,333	-97.97%
Provisions for loan losses (in SKK thousand)	29,093,617	25,489,675	-3,603,942	-12.39%
Statutory reserves (in SKK thousand)	2,733,706	6,961,072	4,227,366	154.64%
Share capital (in SKK thousand)	40,442,576	41,433,475	990,899	2.45%
Own funds (in SKK thousand)	105,875,293	100,626,465	-5,248,828	-4.96%
Secondary funds (in SKK thousand)	96,466,762	183,301,896	86,835,134	90.02%
Primary funds (in SKK thousand)	708,292,274	791,384,116	83,091,842	11.73%
of which: non-anonymous deposits (in SKK thousand)	405,802,712	423,290,430	17,487,718	4.31%
Current period profit (in SKK thousand) ¹⁾	11,548,335	12,287,442	739,107	6.40%
Current period loss (in SKK thousand) ¹⁾	231,918	6,614	-225,304	-97.15%
Net profit/loss (in SKK thousand) ¹⁾	11,316,417	12,280,828	964,411	8.52%
Cumulative profit/loss (in SKK thousand) ¹⁾	34,577,036	37,722,258	3,145,222	9.10%
Capital adequacy ratio (%)	21.59	18.68	-2.91	-

Source: NBS.

¹⁾ Year-on-year data.

even if the potential risks of losses associated with them may sometimes be very high. This may mean, for example, the risk of goodwill loss, legal risks, unforeseeable circumstances risks, or operational risks, which grow with the continually new forms of alternative distribution channels. The basic rules and limits, the aim of which is to restrict the level of risks taken on and to ensure sufficient funds for covering possible losses, are codified in the respective regulations issued by NBS banking supervision. Internal prudential procedures for the banks overall management and for individual types of operations

remain the basic prerequisite for a bank's successful operation; the way in which banks are able to identify, monitor and manage individual risks will always be of critical importance for limiting banking risks.

3.4. Banking supervision performance

Banking supervision is also performed by means of secondary legislation, licensing decrees and prudential regulations.



In 2004 the Banking Supervision Division issued fifteen decrees; decrees amending existing decrees, as well as new decrees reflecting changes resulting, in particular, from the amendment to the Act on Banks.

Also approved was the Decree of the National Bank of Slovakia and Ministry of Finance of the SR amending the Decree of the NBS and MF of the SR on the mortgage register and details on the position and their activity of the mortgage administrator and his representative.

The Banking Supervision Division published as a part of the pro-active banking supervision seven methodological instructions concerning secondary legislation, which are published on the NBS website and in the Official Journal of the NBS.

Over the course of 2004 the Banking Supervision Division performed five full-scope, seven follow-up, and seven targeted on-site inspections.

In 2004 the Banking Supervision Division of the National Bank of Slovakia issued 143 decisions in the field of licensing activity including decisions on the suspension of proceedings, proceedings for breaches of law and decisions on the withdrawal of a banking licence.

3.5. Evaluation of banks' compliance with prudential banking rules

The adequacy of own funds ratio of the Slovak banking sector as at the end of December 2004 reached 18.96%. In a year-on-year comparison with the figure for 31 December 2003 this represents a decline of 2.64%. All banks complied with the limit for own funds adequacy of 8% during the fourth quarter of 2004, since own funds adequacy values moved in the range from 11.84% through 52.79%.

All banks complied with the limit on a bank's large exposure towards a parent or subsidiary or towards a group of economically connected persons one of whose members is a bank (20% of own funds) from March 2004, (as at 31 January 2004 and at 29 February 2004, one bank did not comply with this limit).

Five banks failed to comply with the limit on a bank's large exposure towards another person, a group of economically connected persons or towards countries and central banks (25% of own funds) in the period monitored to October 2004.

All banks complied with the limit on the sum of a bank's large exposures (800% of own funds) in 2004. All banks in 2004 also complied with the ratio of large exposure towards a natural person to the bank's own funds in the amount of 2%.

All banks in 2004 complied with the ratio of large exposure towards a legal person (other than a bank headquartered in a zone A state) to the bank's own funds in the amount of at most 10%. All banks likewise complied with the ratio of large exposure to all persons with a special relation to the bank, to its own funds in the amount of at most 40%.

The new NBS Decree No. 3/2004 on the liquidity of banks and branches of foreign banks and on the process of liquidity risk management of banks and liquidity of branches of foreign banks with effect from 31 January 2004 sets the following limit: the limit of the ratio of a bank's fixed assets to its non-liquid assets is at maximum 1. All banks in 2004 complied with this limit.

Cooperation of the banking supervision division with domestic and international institutions

The Banking Supervision Division in the fulfilment of tasks resulting from the long-term Supervisory Development Plan for banking supervision cooperates with domestic and foreign supervisory authorities. On 12 February 2004 a Memorandum of Understanding was concluded and signed with the Malta Financial Services Authority.

In view of the organisational changes made by the Ministry of the Interior of the SR, as well as of the increasing importance of terrorism financing detection, on 12 November 2004 an addendum to the Memorandum of Understanding with the Ministry of the Interior and the Presidium of the Police Corps was approved and signed.

