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N. Moroz
PhD in Economics, Associate Professor of the Department of Finance,
Lviv Polytechnic National University, Lviv
ORCID ID: 0000-0002-8594-8014

U. Krip
Master's student of the Department of Finance,
Lviv Polytechnic National University, Lviv
ORCID ID: 0000-0003-2986-0875

BANKING SYSTEM OF UKRAINE: CURRENT DEVELOPMENT TRENDS

Н. В. Мороз,
к. е. н., доцент, доцент кафедри фінансів,
Національний університет «Львівська політехніка», м. Львів
У. В. Крип,
магістр 2-го курсу, кафедра фінансів,
Національний університет «Львівська політехніка», м. Львів

БАНКІВСЬКА СИСТЕМА УКРАЇНИ: СУЧАСНІ ТЕНДЕНЦІЇ РОЗВИТКУ

The banking system of Ukraine entered the crisis caused by the COVID-19 pandemic highly profitable, capitalized and with a high liquidity reserve. Macro-prudential policy of the National Bank of Ukraine has prepared the banking sector well for crisis phenomena. Macro-prudential policy of the National Bank of Ukraine has prepared the banking sector well for crisis phenomena. In 2020, only two banks (as in the previous year) were declared insolvent for failing to meet capital regulations. The regulator relaxed bank requirements during the pandemic to reduce its influence on the banking system.

In the article the dynamics of the main monetary policy instrument of the National Bank of Ukraine - the interest rate is investigated. The main trends in the development of the banking system over the last few years have been studied. In times of crisis, banks' assets, capital and liabilities, in particular fixed-term funds of both natural and legal persons, are growing. The fastest growth rate of funds of economic entities and funds of natural persons was exactly 2020, in which legal entities increased the amount of their fixed funds in banks by 43.3 per cent and natural persons significantly increased the volume of their funds in current accounts. However, lending (in 2019-2020) and bank profitability (during 2020) have been negative. The reasons for this are the financial difficulties of clients during the crisis and uncertainty about the future, the deterioration of the quality of credit and the additional formation of reserves by banks.

Credit risk is and will continue to be the defining factor for banks. During the study period, banks with public capital have poor quality credit portfolios, and private banks have the best. Ten banks have been identified as having the largest amount of non-performing loans as of 01.01.2021, seven of which are systemically important banks. They need to make greater use of the tools available to

deal with non-performing loans. A high share of NPL negatively affects the profitability and investment attractiveness of financial institutions. And the fact that 77% of non-performing bank-sector credit belongs to seven systemically important banks is a threat to the growth of systemic risk.

Although the COVID-19 pandemic has had an impact on Ukraine's banking sector, as on all other areas of society, there are as yet no significant threats to the banking system, it remains financially sustainable and profitable.

Банківська система України увійшла у кризу, що спричинена пандемією COVID-19, високо прибутковою, капіталізованою та із високим запасом ліквідності. Макропруденційна політика Національного банку України добре підготувала банківський сектор до кризових явищ. У 2020 році лише два банки (як і в попередньому році) визнано неплатоспроможними через невиконання нормативів капіталу. Регулятор послабив вимоги до банків під час пандемії для зменшення її впливу на банківську систему.

У статті досліджено динаміку основного інструменту монетарної політики Національного банку України – облікової ставки. Досліджено основні тенденції розвитку банківської системи за останні декілька років. У період кризи спостерігається зростання активів, капіталу та зобов'язань банків, зокрема строкових коштів як фізичних, так і юридичних осіб. Найвищі темпи зростання коштів суб'єктів господарювання та коштів фізичних осіб були саме за 2020 рік, у якому юридичні особи збільшили обсяг своїх строкових коштів у банках на 43,3 %, а фізичні особи значно збільшили обсяги своїх коштів на поточних рахунках. Проте негативні тенденції мають показники кредитування (у 2019-2020) та прибутковості (упродовж 2020) банків. Причинами цього є виникнення фінансових труднощів у клієнтів під час кризи та невпевненість у завтрашньому дні, погіршення якості кредитів і додаткове формування резервів банками.

Кредитний ризик є та буде і надалі визначальним для банків. Упродовж дослідженого періоду найгірша якість кредитного портфелю у банків із державним капіталом, найкраща у банків із приватним капіталом. Визначено десять банків із найбільшою величиною непрацюючих кредитів станом на 01.01.2021 р., семеро з яких є системно важливими банками. Їм потрібно активніше застосовувати наявні інструменти роботи із непрацюючими кредитами. Висока частка NPL негативно впливає на прибутковість та інвестиційну привабливість фінансових установ. А те, що 77 % непрацюючих кредитів банківського сектору належать сімом системно важливим банкам, є загрозою до зростання системних ризиків банківської системи.

Пандемія COVID-19 хоча і спричинила свій вплив на банківський сектор України, як і на всі інші сфери життя нашого суспільства, проте суттєвих загроз у функціонуванні банківської системи наразі немає, вона залишається фінансово стійкою та прибутковою.

Keywords: bank; banking system; non-performing loans; credit risk.

Ключові слова: банк; банківська система; непрацюючі кредити; кредитний ризик.

Formulation of the problem. Trends in the banking system are of interest to a wide range of society, as a financially sound banking sector is a prerequisite for an efficient economy. In times of crisis, it is important to know about the economic processes of transformation. The banking sector is now stable enough to maintain public confidence in banks.

Analysis of research and publications. Scientists such as Gura A. [1], Lyvdar M. [2], Rysin V. [3], Ruda A. [4], Fedevych L. and many others have investigated the current trends of development of the banking system of Ukraine.

Formulation of the objectives of the article. The purpose of the article is to study current trends in the development of the banking system, to identify its main problems and prospects.

Presentation of the main results and their substantiation. The last few years of operation of the banking system of Ukraine are characterized by the increasing requirements of the regulator to banks aimed at improving the quality of the system. However, during the pandemic, the NBU relaxed certain requirements, such as delaying the

introduction of capital buffers, as well as allowing banks to restructure client loans on mutually beneficial terms. The rate of reduction in the number of banks slowed down considerably and during 2019 two banks with foreign capital left the market, and two more during 2020.

Since March 2020, the regulator has introduced long-term refinancing of banks using a floating interest rate for up to five years to support their liquidity and lending. The new instrument makes it possible to provide uninterrupted customer service aimed at supporting financial market stability and economic growth.

The National Bank of Ukraine relaxes monetary policy, gradually reducing the interest rate, which was 6% during 12.06.2020 - 04.03.2021, which is the lowest rate in all time (fig. 1). However, the NBU Board decided to raise the discount rate to 6.5% from 05.03.2021. This is due to the acceleration of inflation due to rising consumer prices, as well as the risks of increased quarantine in the fight against the spread of the COVID-19 pandemic.

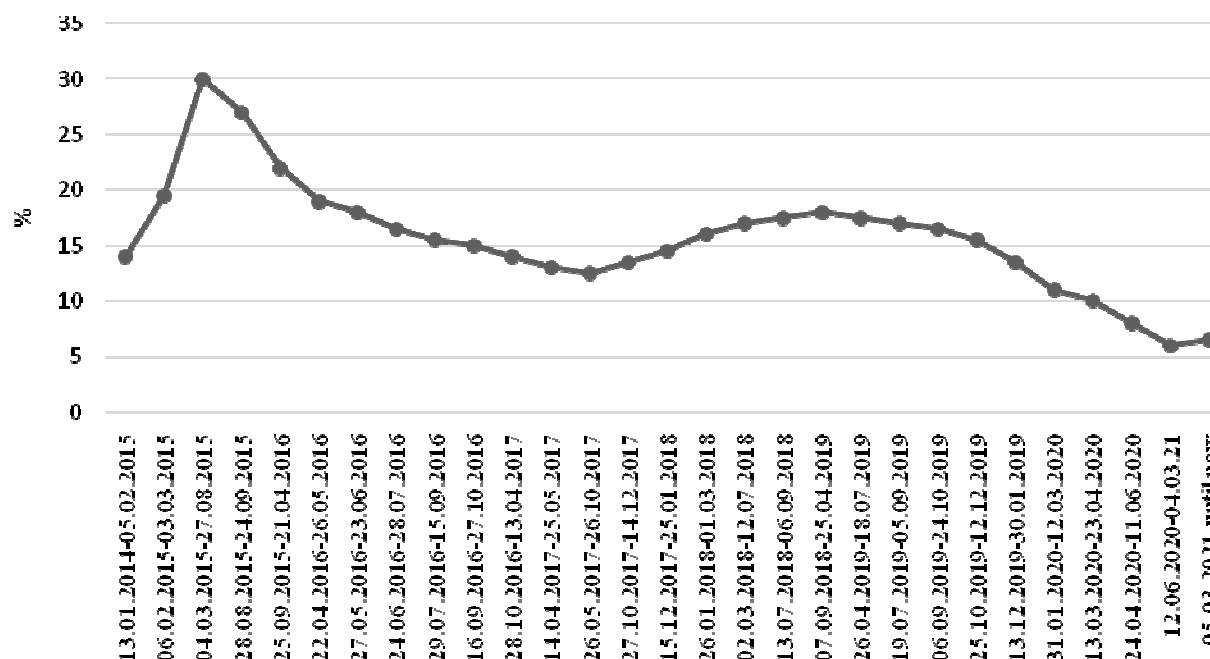


Fig. 1. Evolution of the NBU interest rate in 2014 - 2021

Source: compiled by authors on the basis of NBU data [5]

The volume of assets of the banking system grew during 2016-2020. The highest growth rate was 22.1% in 2020 compared to the previous year. This change is due to a 24.6 per cent increase in the authorized capital for the period (table 1).

Table 1. Dynamics of the banking system of Ukraine 2016-2020, million UAH

Indicators	01.01.2016	01.01.2017	01.01.2018	01.01.2019	01.01.2020	01.01.2021
assets	1 254 385	1 256 299	1 333 831	1 359 703	1 493 298	1 822 814
capital	103 713	123 784	161 108	154 960	199 921	210 640
of which: authorized capital	222 170	414 668	495 377	465 532	470 712	479 932
liabilities of banks	1 150 672	1 132 515	1 172 723	1 204 743	1 293 377	1 612 174

Source: compiled by authors on the basis of NBU data [5]

The share of capital in the liabilities of banks of Ukraine increased from 17.71% (as of 01.01.2016) to 37.14% (as of 01.01.2018) and further decreased to 26.33% (as of 01.01.2021). The share of authorized capital was small at the beginning of 2016 - 8.27% and the largest at the beginning of 2020 - 13.39%, as of 01.01.2021 was 11.56% (fig. 2).

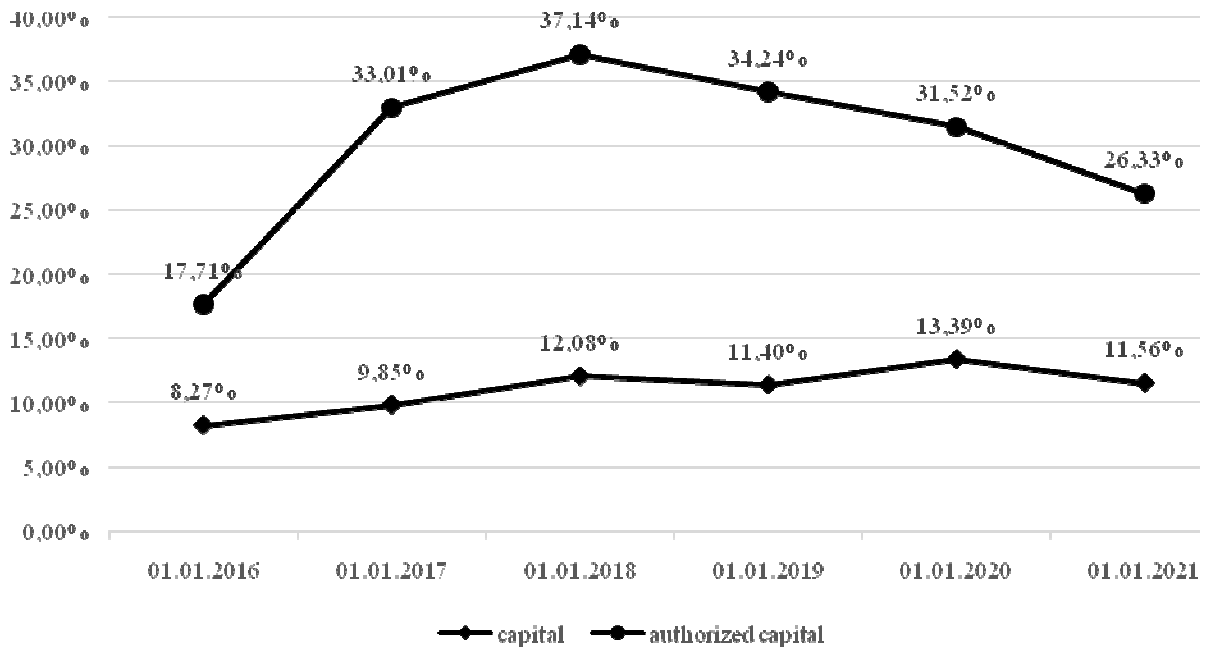


Figure 2. Trends in the share of capital in banks' liabilities in 2016 - 2020

Source: compiled by authors on the basis of NBU data [5]

The funds of economic entities grew during 2016-2020 (table 2), the high growth rate of 29.8% was 2020, in which legal entities increased their fixed funds in banks by 43.3%. During the period under review, 60-65 per cent of these funds were held in national currency.

Table 2.
Trends in Funds Raised by the Banking System of Ukraine during 2016-2020, million UAH

Indicators	01.01.2016	01.01.2017	01.01.2018	01.01.2019	01.01.2020	01.01.2021
Term deposits of other banks and loans received from other banks	122 592	73 938	50 240	42 178	23 912	24 235
Amounts due to corporates	318 568	369 913	403 955	406 367	498 157	646 491
<i>of them: term deposits</i>	<i>96 679</i>	<i>102 469</i>	<i>108 214</i>	<i>110 359</i>	<i>103 191</i>	<i>147 871</i>
Amounts due to individuals (including saving (deposit) certificates)	402 137	437 152	478 100	508 457	552 115	682 029
<i>of them: term deposits</i>	<i>294 155</i>	<i>319 551</i>	<i>325 411</i>	<i>327 615</i>	<i>336 663</i>	<i>344 353</i>
Amounts due to non-bank financial institutions	30 474	42 813	22 907	23 794	26 885	34 704

Source: compiled by authors on the basis of NBU data [5]

The banks' corporate loan portfolio fell by 12% during 2019 and by another 6% through 2020. During the COVID-19 pandemic, many of the major borrowing companies experienced a decline in demand for their products, and uncertainty increased as legal entities concentrated their efforts on repaying existing loans rather than obtaining new ones. The dynamics of the indicators of credit of the Ukrainian banking system for 2017-2020 are shown in table 3.

Table 3.
Dynamics of lending indicators of the banking system of Ukraine for 2017-2020, million UAH

	01.02.2017	01.01.2018	01.01.2019	01.01.2020	01.01.2021
Loans granted to customers					
corporate loans	657 098	892 900	959 601	847 259	795 405
non-performing loans	345 661	500 263	535 770	456 074	371 157
retail loans	156 514	174 448	202 202	214 252	208 383
non-performing loans	98 538	93 353	93 086	73 077	58 230
Interbank loans, deposits	9 884	22 046	28 888	31 368	34 057
non-performing loans	454	1 372	1 073	946	984
Loans to state and local governments	118	1 519	2 867	4 717	11 734
non-performing loans	14	10	838	683	0
Total loans	823 614	1 090 914	1 193 558	1 097 595	1 049 579

Source: compiled by authors on the basis of NBU data [5]

During 2017-2018, the volume of lending to legal entities increased from UAH 657 billion as of 01.02.2017 to UAH 959 billion as of 01.01.2019. At the same time, the volume of non-performing loans increased. This trend has changed with the introduction of prudential measures aimed at improving the quality of corporate lending. During the period 2019 - 2020, there has been a decrease in both lending (by UAH 112.34 billion for 2019 and by UAH 51.85 billion for 2020) and non-performing loans (by UAH 79.69 billion for 2019 and by UAH 84.9 billion for 2020).

The share of non-performing loans of legal entities decreased from 2018 from 56.03% to 46.66% as of 01.01.2021, but this is still quite high (fig. 3).

The volume of lending to individuals increased, except for 2020, as of 01.02.2017 the sum was UAH 156.51 billion, and as of 01.01.2020 - UAH 214.25 billion. However, during 2020, retail lending fell by 2.7%, which is obviously a consequence of the coronary crisis. The quality of loans is improving every year, the share of non-performing loans to individuals as of 01.01.2021 is 27.94%.

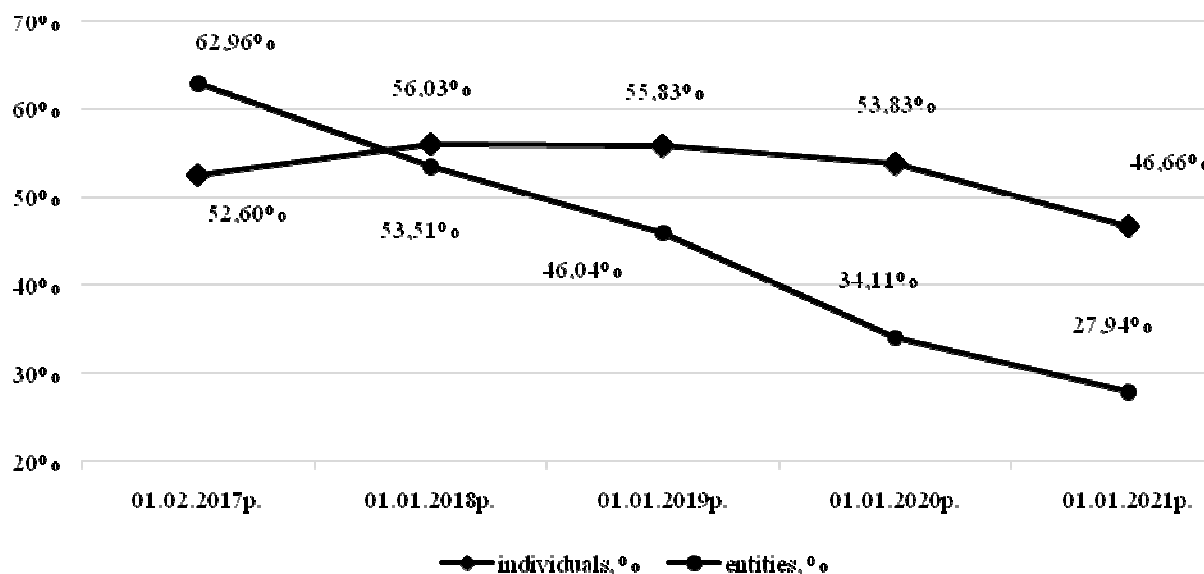


Figure 3. Dynamics of the share of non-performing loans of the banking system of Ukraine in 2017-2020

Source: compiled by authors on the basis of NBU data [5]

The quality of inter-bank loans and credits granted to State and local government bodies is quite high.

The value of the loans of the banking system increased from UAH 823 billion as of 01.02.2017 to UAH 1193 billion as of 01.01.2019, further decreased by 8% for 2019 and by 4.4% for 2020 as compared to each previous year.

The share of all non-performing loans of the Ukrainian banking system as of 01.01.2017 was 53.7 per cent and increased at the end of 2017 to a value of 54.5 per cent. Subsequently, there was a gradual drop in this index and as of 01.01.2021 the value of this indicator was 41 per cent (figure 4, table 4).

The worst quality of the loan portfolio of banks with state capital, the share of non-performing loans as of 01.02.2017 was 77.23%, gradually decreased to 57.41% as of 01.01.2021. In particular, as of 01.01.2021 non-

performing loans PJSC CB "Privatbank" accounted for 73.95% of its loan portfolio and 42.1% of all non-performing loans of the banking system.

Table 4.
Dynamics of non-performing loans of the banking system of Ukraine 2017-2020

Non-performing loans	01.01.2018p.		01.01.2019p.		01.01.2020p.		01.01.2021p.	
	billion UAH	%	billion UAH	%	billion UAH	%	billion UAH	%
1. Banks with state participation, of which:	397,5	71	437,1	68	396,9	64	310,2	57
1.1. CB "PrivatBank" PJSC	236,2	88	244,8	83	239,1	78	181,2	74
1.2. Other than CB "PrivatBank" PJSC	161,3	56	192,2	55	157,7	49	129,0	44
2. Banks belonging to foreign banking groups	156,8	41	151,1	39	107,4	33	95,9	28
3. Private	30,1	24	31,2	23	26,4	19	24,0	15
4. Insolvent	10,4	43	11,2	52	0,00	0	280	75
Total	594,9	55	630,7	53	530,7	48	430,4	41

Source: compiled by authors on the basis of NBU data [5]

Banks with private capital have the lowest share of non-performing loans of 14.56% as of 01.01.2021. Banks of foreign banking groups managed to improve the quality of their loan portfolio, reducing NPL's share of 49.66% as of 01.02.2017 in 27.86% as of 01.01.2021.

The largest amount of non-performing loans is JSC "PrivatBank" UAH 181 196 million, JSC "Ukreximbank" UAH 64 227 million, JSC "Oschadbank" UAH 56 900 million, JSC "SBERBANK" UAH 37 137 million, PSC "Prominvestbank" UAH 24 987 million, JSC "Alfa-Bank" UAH 19 240 million (fig. 4).

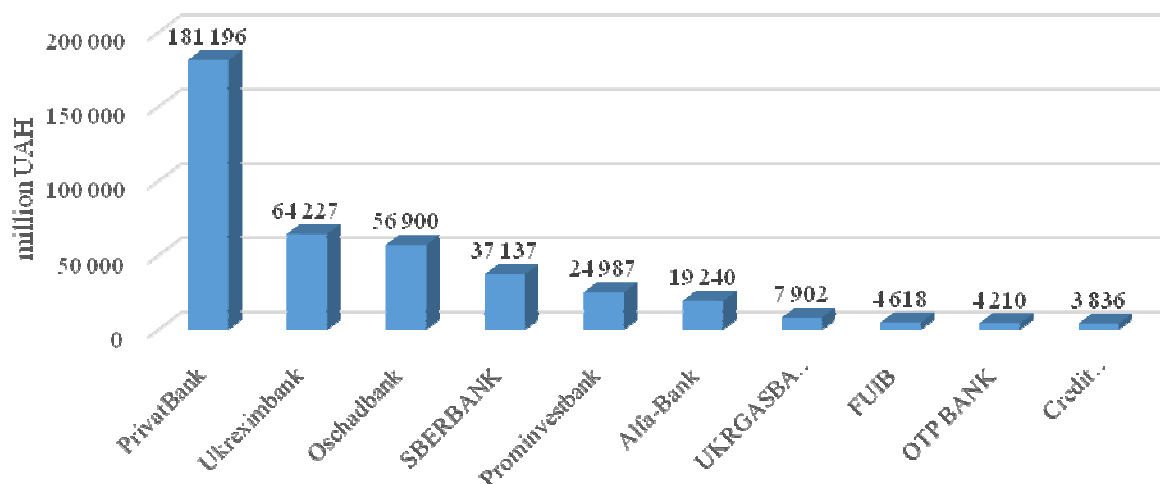


Figure 4. Ten banks with the largest amount of non-performing loans as of 01.01.2021

Source: compiled by authors on the basis of NBU data [5]

JSC «SBERBANK" and PSC "Prominvestbank" are banks that are under the control of the Russian Federation, JSC "Bank Credit Dnipro" is a bank with private capital. The remaining seven banks out of ten are systemically important and as of 01.01.2021 77% of all non-functional loans in the banking system belong to them.

Socially important insurance companies have better asset quality than other insurers, and systemically important banks, on the other hand, have had poorer asset quality than other banks for several years. The presence of such a large proportion of non-performing loans in systemically important banks can threaten a country's financial system. The national bank should take control of this situation and strengthen the quality requirements of the credit portfolio of systemically important banks.

More than 50 per cent of the total revenues of the banking system are interest income, which has a significant impact on the performance of the banking system (table 5).

Table 5.
Dynamics of income, profits and profitability of the banking system of Ukraine 2016-2020, million UAH

Indicators	2016 p.	2017 p.	2018 p.	2019 p.	2020 p.
Income	190 691	178 054	204 554	243 102	249 745
Interest income	135 807	124 009	140 803	152 954	147 312
Fee and commission income	31 362	37 138	50 969	62 057	70 640
Net profit (loss)	-159 388	-26 491	22 339	58 356	41 296
Return on assets, %	-12,60	-1,93	1,69	4,26	2,54
Return on equity, %	-116,74	-15,84	14,67	33,45	19,97

Source: compiled by authors on the basis of NBU data [5]

The rate of growth of total bank income slowed during the crisis, and interest income fell by 3.7% during 2020 compared to the previous year, during the same period net bank earnings fell by 29% and profitability by 40%. The decline in interest income is due to the credit crunch experienced by borrowers during the crisis and credit crunch.

Thus, the COVID-19 pandemic has caused a decline in lending to both legal and natural persons, and consequently in bank interest income and profitability. However, the banking system did not suffer major shocks due to the effective regulatory policies of the NBU. The regulator should tighten the asset quality requirements of systemically important banks. A large proportion of the non-performing loans in the entire banking system belong to these banks. In order to improve bank management of the quality of its loan portfolio, the regulator has taken a number of necessary measures to facilitate this process. Banks should more actively write-off, sell and restructure non-performing loans from their balance sheets. It is also important to maintain high standards of credit quality, but not to weaken conditionalities on borrowers.

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