

## **THE COMPREHENSIVE PUBLICATION**

### **“Commercial Banking: Analysis and Evaluations”**

**(the monograph by Dr. Filomena Jasevičienė in Lithuanian)**

Banks account for the major part of the financial market in Lithuania, offering a wide range of financial services. The banking sector has long been considered to be merely a reflection of economic development, its function being to act as a broker to satisfy the saving and investment needs of economic entities, distributing money across economic activities. However, it is said more and more often that a strong financial sector could be not only a product of economic development, but its cause as well, with a valid impact on the growth of the economy itself.

Having carried out a series of studies and summarised their outcomes, as well as upon analysing Lithuanian and foreign literary resources, the author has stated that the safe and reliable banking and adherence to ethical norms helps creating and developing healthy business.

The book accentuates that commercial banks as financial brokers accumulate financial resources and distribute them across companies, households, governmental bodies to satisfy their economic and social needs. The success of banks' business and confidence in banks depend on the extent of a bank's risks and how well it is able to manage them. Banking risks may provide grounds to making extra profit, but also they may serve as an indicator of potential losses that a bank may incur as a result of insecure transactions. One of the essential banking risks is credit risk. It is critical for banks to manage their credit risk so that they do not suffer major losses or minimise them as much as possible. If the credit risk is not managed properly and if there is no credit risk analysis in place, not only can a bank run great losses, but it can even turn bankrupt as well. It is therefore very important that the credit risk is duly assessed and properly managed.

In the monograph, the author broadly analyses the Lithuanian and foreign literature dealing with the development of banking, the functions of managing bodies, the importance of in-house management, the potential banking risks and their management, the importance of capital to guarantee the security of banks, as well as ethical issues. Her sources included works by Ghosch A., Gregory J., Heffernan S., Koslowski P., Choudhry M., Dudzevičiūtė G., Valvonis V., Bonfim D., Bessis J., Laeven L., Koch T.W., and other authors.

So far, there have been no attempts to examine the underlying aspects of commercial banking in an integrated fashion, particularly in Lithuania. The author analyses the tendencies of bank development, the characteristics of managing a bank, capital structure and its impact on the stability of a bank's business, appraises banking risks and identifies the main risk categories, such as credit, liquidity, etc., systemises the main ways and principles of risk management, analyses and evaluates banking ethics and the factors that affect the choice of a bank. This study, furthermore, introduces the indicators used to assess the operations of a bank, gives an evaluation of the factors that create the value of a bank, and presents a bank analysis model, all the while analysing banking services, revealing their characteristics and importance to the bank, its clients and to public, showing different types of banks, their specific attributes and importance for the purposes of rendering financial services. Finally, the author analyses the capital structure of a bank and assesses the new requirements for compliance to the Basel III criteria, or how the new capital adequacy system will be applied.

The monograph also contains a theoretical and historical analysis of data, a summary, a comparable analysis, a multidimensional linear regression model, as well as a study and analysis of the factors that affect the choice of a bank, which was done using the MS Excel Pivot Table functionality and a factor analysis.

The monograph consists of nine chapters and is structured so that it is easy to read both for those who are fresh to banking and for people who have enough savvy of the field, offering the right chapter to everyone.

Chapter One deals with the theoretical fundamentals of banking and identifies the underlying elements of commercial banking. The book highlights the fact that banks play a crucial part in minimising risks by controlling a package of diverse assets – something that a private individual who has access to free money cannot do. The individual investor in a commercial bank has the risks pertaining to that commercial bank mitigated by the ability of the bank's equity to absorb potential losses. Commercial banks are also able to offer their deposit holders better liquidity, set fixed interest rates on different deposits, and provide a variety of services. Another useful thing about commercial banks is that they create liquidity by providing lenders with an opportunity to extend a short-term credit and borrowers with a possibility to take long-term loans. This helps resolve a certain degree of conflict between borrowers' wishes to borrow moneys for periods longer than lenders can issue loans for.

Chapter Two reviews phases of bank development, dealing with four of them: phase one, which happened in 1918–1941, phase two of 1990–1995, phase three of 1996–2011, and phase four of 2011–early 2013.

The monograph goes on to say that the year 2011 for the financial sector was a year of an exceptionally gruesome trial caused by the termination of the operations of the bank

AB SNORAS at the year-end. No such shocks had happened in the banking sector for more than a decade, and that is why this development caused such a big ripple; however, the banking system proved to be prepared and able to withstand stressful situations. An equally significant event took place in February 2013 when the board of the Bank of Lithuania imposed a restriction on the operations of the private limited company Ūkio Bankas.

Chapter Three analyses different types of banks. It accentuates that banks are typically classed as commercial and special-purpose banks. Commercial banks are then sub-classed into retail, wholesale, and universal banks, while special-purpose banks are sub-categorised into investment banks, mortgage banks, savings banks, branch banks, consumer credit banks, etc. The chapter introduces a concise material on both the types of banks and the characteristics of their activities, as well as on services they provide.

Chapter Four presents an analysis and evaluation of banks' structure, management, and business on an example of the management structure of one bank which is indicative of other banks, too. This chapter also describes, in great detail, the managing bodies of banks and their functions, the requirements for the internal management of banks and the way they are applied, talks about the system of indicators that are necessary for the analysis of a bank's performance. A statistical analysis done with the application of the method of main components is followed by a presentation of factors that affect the choice of a bank and by the methods to identify the value of a bank. This kind of analysis of banks' performance results, highlighting the dominants as the underlying factors that drive the performance results of a bank, not only helps to construct a better understanding of the factors that are of major influence on the operations of banks, but also gives information to the public, banks' shareholders, the academia, the boards of banks who, based on the results of this analysis, can make appropriate decisions or formulate the further guidelines for the activities of the bank.

Chapter Five deals with the kind of services and banking operations that commercial banks are entitled to offer and transact. It discusses in depth the services of accepting deposits and issuing loans, factoring and forfeiting. The book also touches upon leasing as one of the new and rapidly developing forms of credit. Its concept is very broad and embraces a combination of financial, commercial, legal, and technical aspects. In its widest sense, leasing covers a raft of property-related concepts pertaining to the transfer of property for temporary usage, the acquisition and further use of such property. Quite a lot of space is dedicated to electronic banking. The progress of electronic information technologies is an important factor that both causes banks to change their strategies and promotes the evolution of banking systems. Given the degree of competition on the market, financial institutions tend to prioritise on complete and accurate information given

in time when it comes to making decisions. This allows them to use analytical tools to look for promising fields, improve the quality of their services, cut costs, focusing on the most profitable financial instruments and transactions, as well as to draw general strategic plans for e-banking services. In addition to electronic banking, commercial banks also offer payment services through their branches.

Chapter Six is concerned with the importance of a bank's capital for securing the stability of the bank. The author stresses that capital is of immense significance to a bank for it to be able to protect itself against surprise losses. The 8 per cent requirement of regulatory capital adequacy can sometimes be too low for a bank to be able to sufficiently absorb losses as they occur. A bank's capital is an indicator of how efficiently and profitably its services are being provided. A capital deficit in a bank means that the bank's shareholders need to raise the capital or amend the operating policies to safeguard the operations. A great deal of attention in the book is given to the implementation of a new capital adequacy system (Basel III), specifying the potential issues that commercial losses may face while trying to comply with the new requirements.

The chapter on banking risks is one of the biggest in the book. It introduces the theoretical understanding of risks and lists different types of risks, the credit risk being one of the most important. In the financial markets' system, credit risk is defined as the probability that certain segments of the financial system might suffer significant losses due to a default on borrowers' part. In other words, credit risk is the risk that one of the parties in a transaction may become unable to fulfil its obligations duly and properly; as a result, the other party can incur losses. The author has conducted an analysis of the effects of macroeconomic factors on the quality of loans, using a multidimensional model of linear regression, and has established that the impact of such factors on credit risk in the banking sector is quite significant indeed.

One of the main sources of loan portfolio risks is loan concentration. The risk of loan concentration can be approached from different angles: by borrowers (large loans), related borrowers, borrowers related to the bank, and internal loans by types of economic activity, foreign countries, affiliation with the bank group, types of loans, security, and so on. The analysis presented in this book shows that the concentration of banks in Lithuania is relatively high.

Liquidity risk ranks second on the ladder of importance. According to the author, banks should always assess their liquidity risk, especially in times of recession. A proper liquidity planning and management can minimise the probability of running into serious problems. In fact, liquidity risk transcends the boundaries of just one bank. Liquidity deficit in one financial institution can have its repercussions across the system.

The book addresses also other risks, such as the market risk, interest rate risk, foreign exchange risk, operating risk, legal risk, and business risk.

Chapter Eight deals with the risk management analysis and the internal control system at commercial banks. For analysis purposes, an exceptionally heavy emphasis is placed on the liquidity risk management, because liquidity risk assessment and management methods have been somewhat neglected recently. Therefore, to carry on the study, the author and others had chosen to formulate a liquidity risk management model. The liquidity risk management model is made on the basis of theoretical liquidity risk management models that were addressed in the theoretical part of the study, and of the contemporary banking practice.

The last chapter – Chapter Nine – is concerned with the banking ethics. According to the monograph, ethical behaviour means reaching one's goals without infringing the interests of others, i.e. when the risks and the results are adequately shared. Ethics help reveal the underlying actions that are just or unjust, right or wrong, and to justify these actions with arguments or make the arguments more specific. The banking experience shows that success is driven by high ethical requirements for the quality of services, customer service culture, management, staff qualifications, and assessments of their performance. Failure to follow ethical norms, and in some cases pursuit of obscure business, had been among the reasons that caused the global financial crisis, which in turn led to banking problems in some countries. Confidence in banks is a key to successful banking. A lot of space is devoted to disclosing the business ethics of some of the foreign countries. The bank-and-client relations are analysed through a customer survey and an analysis of factors that affect the choice of bank, made by the factor analysis method.

The book ends with conclusions, as well as a comprehensive list of references.

The monograph “Commercial Banking: Analysis and Evaluations” by Dr. Filomena Jasevičiene presents well-structured information and assessments, employs mathematical–statistical methods, and addresses a variety of issues. It should be beneficial both to scholars and teachers, doctoral students, postgraduates, and banking practitioners as well as to anyone interested in the subject.

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