

18. Cultural Values and Their Importance for Ethical Codes in Banking Sector

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Abstract

This article is one of the results of an interdisciplinary research project between the Department of Civic Education, University of Ostrava and Department of Economics, VŠB – Technical University of Ostrava. The main goal of this research project is the description of relations between society and ethical codes in companies. The initial phase of the project is focused on the banking sector, because we assume that in this sector is the code of ethics mostly used. The aim of this article is analyzing the banking sector in the Czech Republic, its history and present, ownership structure and identifying bank leaders in the Czech Republic, its ethical codes and consistency with cultural values. The final analysis focusses on economic efficiency and the ethical content analysis of selected entities.

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Introduction

The banking sector is one of the most important sectors in the economy of a country. Banks are the engine of the economy because banks decide on the amount of credits, loans, interest rates for savings or investment. Bank clerks are faced with households or companies which are the most important for the economy. That's why most banks in the Czech Republic are focused just on corporate clients. Therefore, there is a presumption that the code of ethics, which should be used by bank clerks, is a very important part of the banks culture. For a better understanding of relationships in the banking sector and the creation of codes of ethics it is necessary to know the background of this sector. The history of the banking sector and its development can give some answers. Also, disentanglement of current links in ownership can help to understand the cultural and ethical values in the ethical codes, which banks use.

18.1. History of Czech banking system

The first banks founded in Czech lands (which were part of the Austro-Hungarian Empire) in the early 19th century. On the initiative of the Czech aristocracy was founded in 1824 in Prague, the Czech Savings Bank (Českásporitelna). In 1847 began to operate in Prague a branch of the Austrian National Bank. In the future, were founded a lot of banks and banking houses. One of the important banks, especially for small savers, was the State Postal Savings Bank. But, some banks soon suffered from imprudent behavior. The banking sector was particularly affected by the stock market crash in Vienna Stock Exchange in 1873. For example during period 1873–1883 were founded 6 new banks, but 99 banks went bankrupt.

Another important milestone of the Czech banking sector was formed in Czechoslovakia in 1918, respectively the emergence of Czechoslovak National Bank in 1926. Czechoslovak National Bank was a limited company with the nature of a public institution, received a 15-year exclusive right to issue banknotes (which were fully covered by gold) in Czechoslovakia (Polouček, 2006, p. 39).

The Czech banks (including the central bank) had to submit to German requirements in the Protectorate of Bohemia and Moravia. In 1939 Slovak banking became independent and the Slovak National Bank and the National Bank of Bohemia and Moravia were founded. After World War II, these banks were again integrated. Based on the Benes Decrees 102/1945 were nationalized all stock banks in Czechoslovakia.

Another milestone of the Czech banking system took place in 1948. There were major political changes during February of that year, which significantly influenced all areas of human life. The Communist Party of Bohemia and Moravia came to power and wanted to adapt the Czech banking system to the Soviet model. It began a period of centralizing the state of the economy, when the banking sector was subject to the fulfillment of financial plans. The Czechoslovak National Bank was merged with the Tatrabanka, Postal Savings Bank and Živnostenská Bank and renamed to the Czechoslovak State Bank. It was the monopoly of the central and commercial banking for a long period. All private banks were nationalized and almost all non-bank financial institutions in the country were closed. The whole banking market became subordinate to the Ministry of Finance.

The year 1989 was an important for the whole of Central and Eastern Europe. There were, besides political and social changes, also a few very important changes in the banking sector. Firstly, till 1989 there was strict specialization of individual banks. The new banking act was adopted in 1992. This act had the typical character of the world banking system, which led to the universalization of banks and other financial institutions. This year also started a conversion of state financial institutions into joint stock companies and their entry into the coupon privatization. Secondly, two years earlier, was adopted another law on the State Bank of Czechoslovakia, which laid the foundations for a two-stage banking system – on the one hand there was a central bank with the right of printing money, supervision and regulation of commercial banks and on the other hand there were several commercial banks. Very soon after the Velvet Revolution in 1989 also showed the first problems with old bad loans, which were provided by the State Bank of Czechoslovakia to state-owned enterprises. Therefore, was founded the Consolidation Bank (state-owned), which took all these bad loans – it was almost 80 billion Czech crowns (CZK), which was about 7% of GDP in 1992.

In 1993 there was a split of the Czechoslovak Federal Republic into two separate states: Czech Republic and Slovak Republic. In this year was also adopted the law on building savings and state support for building savings, leading to the formation of new actors – building societies. This law was motivated by the experience of Germany and Austria. The act on banks was amended in 1995 and has been supplemented by the law on deposit insurance. From this year on all deposits were insured up to 80% of the value of the deposit, maximum was 100 000 CZK for one person in one bank. Over the years there have been several amendments to this Act – the latest legal version is from 2010, when deposits were

insured up to 100% of the value, maximum is 100 000 EUR for one person in one bank.

In 1995 was founded another state-owned bank – the Czech Export Bank, which was established to support the foreign business activities of domestic firms. The last important milestone of the Czech banking sector, was the privatization of large banks, which had been gradually prepared since 1990. Finally, the largest banking houses of the Czech Republic (Komerčníbanka, Českáspůřitelna and Československáobchodníbanka) were privatized between the years 1999 and 2001. In the following years there were only minor changes in the individual laws, harmonizing them with some European laws and in 2006 unification of supervision of all financial institutions under one authority, namely the Czech National Bank.

During the whole described period came and went many financial institutions – from small credit unions to mid-sized banks. As mentioned earlier, till 1990 banks were strictly divided according to their purpose and de facto existed only 5 banks. After 1990 the number of banks sharply increased, because the conditions for obtaining a banking license was not too complicated, and therefore came various foreign entities to the Czech banking market. The numbers of banks in selected years summarized table 18.1. These banks are divided to group: large banks, medium-sized banks, small banks, foreign bank branches and building societies. The definition of the size of banks has changed over the years, that's why there is described last "valid" version from 2012. Large banks are those with total assets of more than CZK 250 billion, medium-sized banks have total assets of between CZK 50 billion and 250 billion and small banks have total assets of less than CZK 50 billion (CNB, 2015).

Year	1990	1993	1995	2000	2005	2010	2014
Banks total	5	52	55	40	36	41	45
Large banks	5	5	5	4	4	4	4
Medium-sized banks	0	2	10	11	10	8	8
Small banks	0	32	24	8	5	6	6
Foreign bank branches	0	7	10	10	11	21	22
Building societies	0	5	6	6	6	5	5
Banks under conservatorship	0	1	0	1	0	0	0

Table 18.1. Number of banks and their classification by size in selected years

Source: Bank statistics ARAD, Czech National Bank, 2015.

The table 18.1 shows that the early years of the modern history of the Czechoslovak Federative Republic were specific by big increase in the number of small banks. Banking standards are still not fully adjusted, therefore a lot of different companies got a banking license easily. When began the first problems with the liquidity of these banks, the Czech National Bank tightened the conditions for issuing banking licenses, and the banking sector in the Czech Republic has stabilized. The last 10 years of the Czech banking sector is characterized by an increase in foreign bank branches.

Figure 18.1 shows an overview of entities that are currently operating in the banking market in the Czech Republic. Banks are divided in to groups which use the Czech National Bank, it means there are four large banks, eight medium-sized banks, six small banks, twenty two foreign bank branches and five building societies.

Large bank	Foreign bank branches
Česká spořitelna, Československá obchodní banka Komerční banka UniCredit Bank Czech Republic and Slovakia	Bank Gutmann Bank of Tokyo-Mitsubishi UFJ (Holland) BNP Paribas Fortis BRE Bank Citibank Europe COMMERZBANK Deutsche Bank HSBC Bank ING Bank Meinl Bank Oberbank Poštová banka PRIVAT BANK Raiffeisenbank im Stifland Saxo Bank Sumitomo Mitsui Banking Corp. Europe The Royal Bank of Scotland Volksbank Löbau-Zittau Všeobecná úverová banka Waldviertler Sparkasse Bank Western Union International Bank
Medium-sized banks	
Česká exportní banka Českomoravská záruční a rozvojová banka GE Money Bank Hypoteční banka J&T BANKA PPF banka Raiffeisenbank Sberbank CZ	
Small banks	
Air Bank Equa bank Evropsko-ruská banka Expobank Fio Banka Wüstenrot hypoteční banka	Českomoravská stavební spořitelna Modrá pyramida stavební spořitelna Raiffeisen stavební spořitelna Stavební spořitelna České spořitelny Wüstenrot – stavební spořitelna
Building Societies	

Figure 18.1. Entities operating in the banking market in the Czech Republic

Source: Financial market supervision report 2013, CNB.

18.2. The ownership structure of banks

When the Czech banking sector was opened for foreign subjects (after 1989), market competition increased and banks owned by the state and municipalities were unable compete with these “modern” banks. For that reason, the government decided to privatize Czech banks. Till 1997, state and municipalities owned almost 75% capital of banks, foreign investors only 25%. As mentioned above, the biggest privatization wave was between the years 1999 and 2001, which were sold to foreign subjects the biggest Czech banks on the market. After this wave, the share of foreign capital increased in the banking sector to almost 83%. The last five years is characterized by increase of Czech (private) capital in the banking sector. That's why the share of foreign capital slightly decreased to 74%, it means, that the share of Czech capital is about 26% (the percentage for year 2013). Despite this slightly decreased we can say that the Czech banking sector has a stable ownership structure. Foreign capital with a direct share (i.e. direct foreign shareholders holding shares directly) has long dominated the domestic banking sector's capital. Ten banks are wholly owned by foreign capital, and foreign capital predominates in five banks. Two banks are majority owned by Czech shareholders. Seven banks are wholly Czech-owned (Financial market supervision report, ČNB, 2014). Figure 18.2 shows how Bank ownership structure changed in the 2011–2013 period.

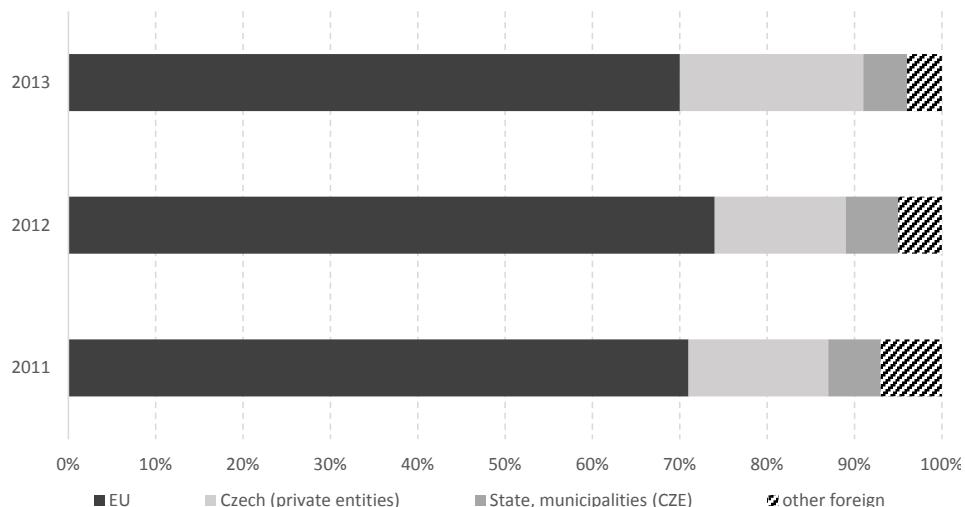


Figure 18.2. Bank ownership structure (in %) between 2011–2013

Source: Financial market supervision report 2013, ČNB, 2015.

Figure 18.2 shows what has been managed above the share of foreign capital in the bank slightly decreases while domestic capital slightly increases. The graph also shows the dominant ownership of European capital, currently non-European ownership is approx. 4% (this capital comes mainly from Russian Federation).

Because of the differences in cultural values of individual nations, authors make an analysis of the ownership structure. Therefore, figure 18.3 shows the nationality of parent banks, including foreign bank branches.

The map shows that the majority of banks operating in the Czech Republic have established their parent bank in Austria or Germany. We can almost say that every second foreign banking institutions operating in the Czech Republic has established his parent in Germany or Austria.



Figure 18.3. Map of nationality of parent bank

Source: Own processing of Lists of regulated and registered financial market entities, CNB, 2015.

Other countries in the imaginary “nationality” ranking are Great Britain with four entities and Russia with three entities. As mentioned in figure 18.2, non-European entities operating in the Czech’s banking sector are only four (three from Russia and one is from the United States of America).

“Tracking down” the real majority shareholders is problematic, because most entities are joint stock companies, therefore ownership of these entities is variable. An example might be a GE Money Bank, which is owned by the largest multinational company in the world, General Electrics, which was founded in the United States of America, but the real owners may be entities outside the US market. Other “ownership problematic” bank is PPF bank, which is owned by the PPF Group (the richest Czech man Petr Kellner) but the bank headquarters is in the Netherlands, because of lower taxes. And thirdly “troubled bank” may be mBank, respectively BRE Bank, which is based in Poland, but the bank is part of the largest financial groups in Europe – German Commerzbank.

From the perspective of our analysis, it is not important to find the real owners, but rather explore the environment, behavior, standards, values, which is used in the parent company, or is used in the country from which the parent comes from. And if (and how much) this foreign corporate culture affects domestic entities and if these standards and behavior are transferred to the domestic corporate culture (for example to the ethical codes).

The Czech National Bank also monitors the origin of capital for each group of banks (it means for large, medium-sized, small banks and for building societies). We have already mentioned above that in 2013 was the share of foreign capital in Czech banking sector about 74% and the share of domestic capital about 26%. Figure 18.4 shows that foreign and domestic capital are very unequally represented in different groups of banks.

In the large banks, which currently include Česká spořitelna (“the Czech Savings Bank”), Komerčníbanka (“the Commercial Bank”), CSOB (Československá obchodníbanka – “the Czechoslovakia Commercial Bank”) and the Unicredit bank, shared foreign capital in 2013 was more than 98%. This is a predictable result, because these banks were privatized at the turn of the millennium by foreign entities.

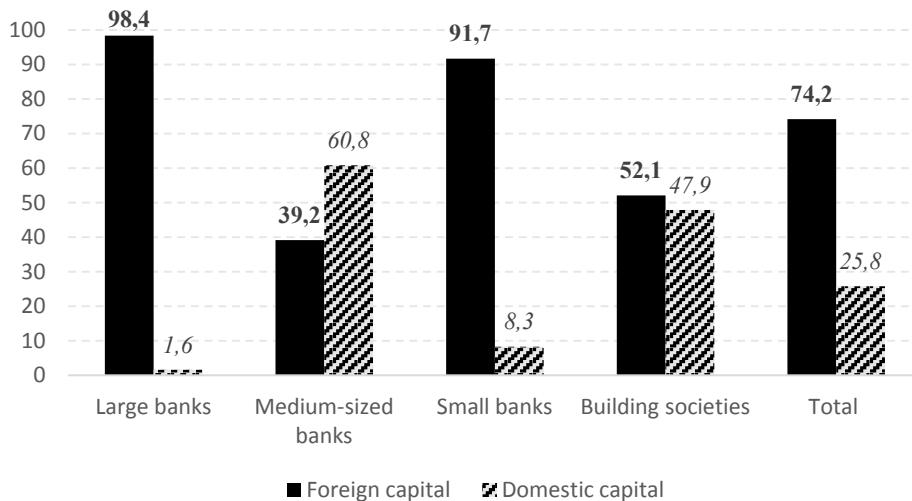


Figure 18.4. Capital origin (in % for banks with licenses as of 31st December 2013)

Source: Financial market supervision report 2013, CNB, 2015.

In the large banks, which currently include Česká spořitelna (“the Czech Savings Bank”), Komerční banka (“the Commercial Bank”), CSOB (Československá obchodní banka – “the Czechoslovakia Commercial Bank”) and the Unicredit bank, the shared foreign capital in 2013 was more than 98%. This is a predictable result, because these banks were privatized at the turn of the millennium by foreign entities. Czech capital (ownership) dominates in a medium-sized banks. This fact is mainly due to the fact that there are two large state banks, founded to support business and export. These banks are Česká exportní banka (“the Czech Export Bank”) and Česká moravská záruční a rozvojová banka (“the Czech-Moravian Guarantee and Development Bank”). This category includes also two relatively new banks in the hands of private Czech entities. These banks are the J&T BANKA and the Hypoteční banka (“Mortgage Bank”). In the category of small banks dominated again foreign capital, amounting to nearly 92%. In figure 18.4 does not show foreign bank branches, because there is a 100% proportion of foreign capital. A relatively balanced situation is in the category of building societies, where the ratio of foreign capital and domestic capital is almost equal. Foreign capital is higher than domestic capital by about 4%.

18.3. The Czech banking sector and Codes of Ethics

Before the analysis of ethical codes of selected domestic and foreign banks, it was necessary to analyse the occurrence of ethical codes of the Czech banking sector. During these analyses, it was found that 17 of 45 banks are focused on corporate clients. The remaining 28 banks have corporate and private clients. After a website analysis of individual banks, it was found that only 15 banks have their own ethical codes published on their websites. Eight banks declared affiliation to the Ethical Code of the Czech Bank Association. Some of the banks declared both. Banks, which have been found at least some mention about ethical codes on their website, are summarized in figure 18.5.

Figure 18.5 shows that the number of banks in the Czech Republic has not published a code of ethics on their website. The possibilities for subsequent analysis, therefore is “dramatically” reduced. Based on previous analyses (ownership in the banking sector and published codes of ethics on websites), it was necessary to select entities for the analysis of ethical values contained in their codes.

The key for selecting a relevant bank was:

- Has been selected bank, which is important for the Czech banking market – it means a bank which has a big market share.
- The bank has on its website a copy of a Code of Ethics or any mention of ethical behaviour.
- After selecting the Czech banks was also included to the analysis foreign banks which are the parent bank for the relevant Czech banks.

There were finally included in the analysis of codes of ethics the following banks (the list is given, including justification for this selection).

Česká spořitelna, Komerční banka, ČSOB – because these banks are the largest banks in the Czech banking market. Unicredit Bank Czech Republic and Slovakia was not included to the analysis, because there was not found any code of ethics on their website.

As representatives of foreign banks were selected parent banks of chosen Czech banks, ie. Sparkasse Erste Group Bank (from Austria), Société Générale (from France) and KBC Bank (from Belgium).

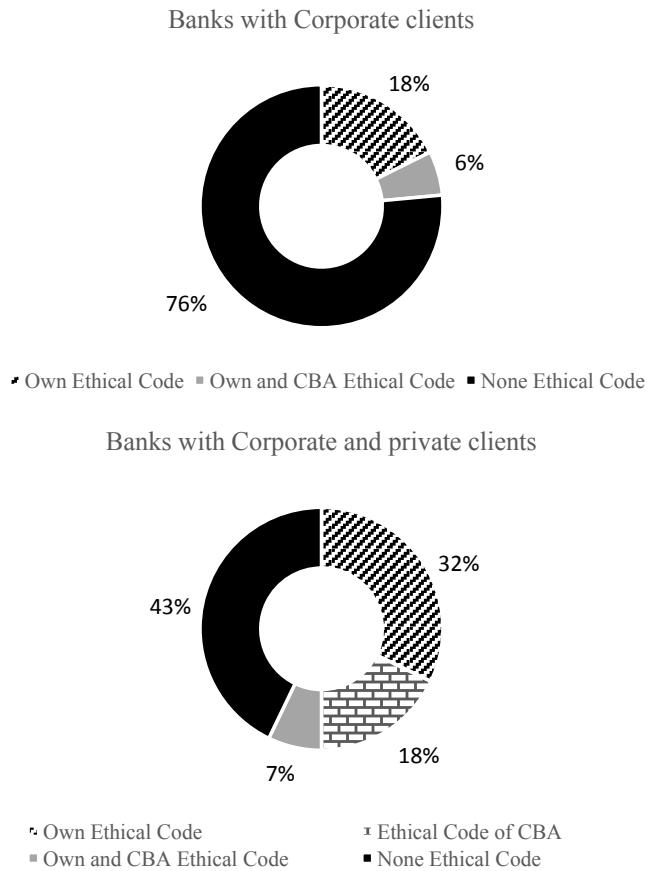


Figure 18.5. Banks with a published Code of Ethics on the website

Source: own data based on banks web pages, 2014.

To complete the selection, it was chosen one more bank on both sides (Czech and foreign). It has been selected one of the “youngest” banks in the Czech Republic – Air bank, which is fully owned by Czech capital. As a representative of a foreign bank a branch has been selected bank from Germany – Deutsche Bank, because Germany has (after Austria) the most branches in the Czech Republic.

18.4. Ethics content analysis and economic analysis of selected banks

In these selected banks were made a basic analysis (Ethics content analysis and economic analysis), which aimed to measure the efficiency of the selected banks based on the ethical values which these banks declare.

The main indicator for economic analysis was chosen ROAE (Return On Average Equity), because this indicator must be published by all banks and it is one of the best indicator of profitability of bank. This indicator refers to a company's performance over a fiscal year, so the average-equity denominator is usually computed as the sum of the equity value at the beginning and end of the year, divided by two. Higher value of this indicator means a better efficiency of the bank.

A certain distortion results may occur that ROAE at foreign (parent) banks, is usually the average value of all foreign branches; for example. Sparkasse (Erste Group) not includes only the results of Austrian bank branches, but also Slovak, Hungarian and last but not least Czech branches. There was a hypothesis, that parent banks will have smaller ROAE's than subsidiary banks, but the differences are too high (see Figure 18.6).

The methodology and process of the Ethics content analysis is part of the article *Cultural Values and Their Importance for Ethical Codes in Banking Sector from Ethical Perspective* from the same authors. That's why the following text, will mention only the results of this analysis.

The results of these analyses is summarized in figure 18.6, wherein the *x*-axis presents the Values indicator and the *y*-axis presents the ROAE of individual banks. The Values indicator was constructed as the social values minus the individual values. If the number of result is negative, the bank (code of ethics) preferred individual values. If the result is a positive number, the bank (code of ethics) preferred social values. Then the actual number of results will show how much is dominating individual or social values. For certain "anonymity" were encoded individual banks, where the parent bank and subsidiary banks have the same code (i.e. A and AA). When two letters are marked for parent banks and one letter for subsidiary banks. The pair of banks were created from the Czech bank (Air bank) and foreign bank branch (Deutsche Bank). Although these banks have nothing in common, they were also called with the same letters, not to be easily identifiable.

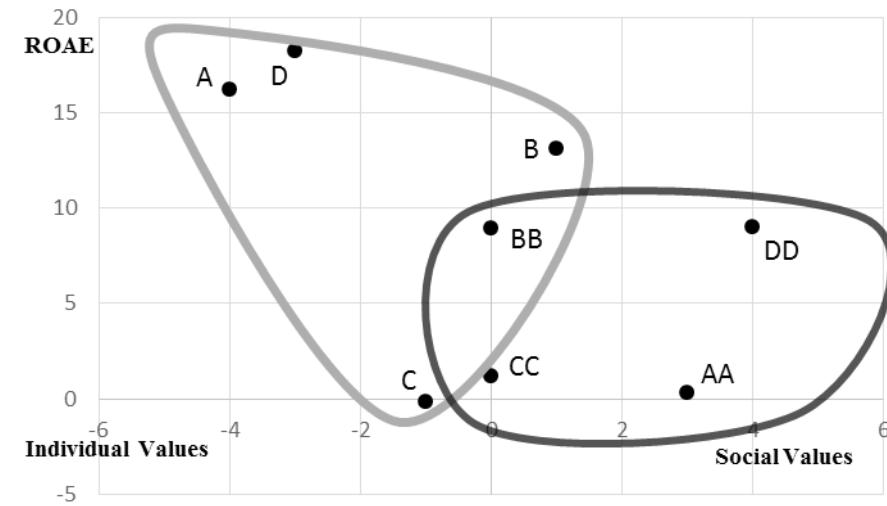


Figure 18.6. Values indicator and economic efficiency of selected banks

Source: own calculation, 2015.

Figure 18.6 shows that Czech subsidiary banks are more efficient, respectively have bigger profits than their parent banks. From the perspective of values indicator, the subsidiary banks preferred individual values, on the contrary parent banks are rather balanced values or social values predominate. From this analysis should be a simple conclusion: that ethical behaviour (code of ethics) of Czech subsidiary banks is focused more individual and got bigger profit than their parent. One of the reasons why the Czech banks are profitable than their parent is the fact that a large part of the profit is fees for banking services. This was one of the reasons why large Czech banks were profitable even in the financial crisis (in 2008–2010) when most parent banks were unprofitable.

Two pairs of banks (B-BB and C-CC) are relative consistent. It means, that codes of ethics are equally balanced and the profitability of these banks is not too different. In contrast, an absolutely different outcome for the remaining couples – where the balance between individual and social values totally different, what also reflects on the profitability of banks. For example the difference in profitability between pair A-AA is 15 percentage points and between pair D-DD is nearly 9 percentage points. It can be deducted from this analysis that the focus of these banks is significantly different and this is also reflected on the “success” – profitability of the banks.

Conclusion

The aim of this article was to evaluate the influence of cultural values on codes of selected entities in the banking sector. Historically, when the Czech Republic was part of the Austro-Hungarian Empire, Austrian and German banks played an important role in the Czech banking sector. Other countries were in the minority. Another important fact is that the banking system of the Czech Republic was affected by government intervention after the 2nd World War. In this time free competition on the market was distorted. A few years after the Velvet Revolution, loose monetary policy has enabled the establishment of many entities. Within a few years many of these entities went bankrupt, which was a good thing for the entry of foreign bank branches, which brought to the domestic banking sector a different culture. The results of the analysis showed that domestic banks tend to focus on the person and client (codes of ethics contain more individual values). One of the reasons, why a code of ethics contains more individual values, is a bigger bank struggle of the customer. This "battle" might not be so strong abroad, that's why banks are trying to attract their clients through the preferring of social values. The results of the analysis also confirmed that domestic banks are more profitability than their parent in abroad. Therefore is a possible to say that, if a code of ethics contains more individual values than social values, it means that it is more focused on the customer, the company (bank) is more profitable.

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