

DEVELOPMENT AND THE CURRENT SITUATION IN THE FINANCIAL MARKET IN SLOVAKIA



received: 17 December 2014

accepted: 30 June 2015

MONIKA ZATROCHOVÁ, MARTINA KUPEROVÁ

ABSTRACT

The aim of the submitted paper is to summarize and analyze the current situation, conditions and factors influencing the further development in the financial market area. Afterwards, the development in the last years (2011, 2012 and 2013) are described and the factors contributing to changes that have occurred in the financial-market area during the investment development in Slovakia are pointed out. Consequently, it is obvious that investments are closely associated with changes ongoing in the financial market. In this paper the stress is laid on collective investments, interest rates and income investments which affect the company investments realized in the financial market. For the fulfillment of the main goal of this work, the inductive and deductive methods are used in order to achieve the results enabling the comparison to investments realized in the above-indicated individual years and to point out the changes associated with a development in the European Union.

KEY WORDS

financial market, investment, development in Slovakia

DOI: 10.12846/J.EM.2015.02.07

Corresponding author:

Monika Zatrochová
Slovak University of Technology
in Bratislava,
Institute of Management,
Slovak Republic

e-mail:

monika.zatrochova@stuba.sk

Martina Kuperová
Slovak University of Technology
in Bratislava,
Institute of Management,
Slovak Republic

e-mail:

martina.kuperova@stuba.sk

INTRODUCTION

Financial markets are typically defined by having transparent pricing, basic regulations on trading, costs and fees and market forces determining the prices of securities of that trade. Some financial markets allow only participants that meet certain criteria, which can be based on factors like the amount of money held, the investor's geographical location, knowledge of the markets or the profession of the participant.

The financial market can be defined as the market, in which financial participants and mediators ensure, by means of the financial instruments, the movement of the short-, medium- and long-term capital among individual economic subjects at the national and international scale (Chovancová et al., 2006). The segmentation of the financial market is presented in the Tab. 1.

Tab. 1. The segmentation of the financial market

Financial market			
Exchange market	Monetary market	Capital market	Market of precious metals
	Market of short-term credits	Long-term securities market	
	Short-term securities market	Market of long-term credits	

Source: (Zatrochová, 2011).

The financial market can be also defined as a market in which the short-, medium- and long-term capital movement, existing among individual economic subjects at the national and international level, is ensured by financial mediators using financial instruments. This definition underscores three basic aspects, namely:

- the system of financial instruments,
- the system of financial institutions,
- the mechanism which ensures the transformation of monetary surpluses of one economic sector to a deficit economic sector in order to finance its needs (Mishkin, 2011).

The financial market functions according to the mechanism based, on the one hand, on market principles ensuring the meeting of an offer with a demand, which results in the balanced prices of financial instruments and services, and, on the other hand, on regulative state elements determining the general rules of the financial market in operation. The aim of these rules is to achieve the market functionality and also the protection of investors. For companies the crucial external financial source is the financial market. The financial market is a “heart” of the financial system performing its life functions. It estimates the volume of useable sources, stimulates savings, imposes interest rates and the prices of securities (Chovanová, 2014).

In advanced market economics, active participants are financial organizations and institutions involving, for example, banks and insurance companies. The bank sector belongs to the most important branches of the national economy which ensure the functioning of the economic system in every country. This is valid also for the Slovak Republic where, in recent years, the bank sector has played an important role in developing the transforming economics. The inspection of the bank sector activity is effected by the National Bank of Slovakia (NBS) within the integrated inspection of the financial markets which are one of its un-separable parts. The NBS is oriented to the monitoring of risks and its fundamental objective is to take steps to the minimization of various kinds of risks occurring in the bank sector (NBS, 2012, p. 54).

1. ECONOMY DEVELOPMENT IN 2011

The analysis of the financial sector evaluating the year of 2010 in Slovakia pointed out the relatively favorable trends in the macroeconomic development and indications of the stabilized financial markets. On the other hand, the NBS warned that behind this

development were hidden risks which could have a negative impact on the macroeconomic development and the situation in financial markets.

However, the economic situation in the first half of the 2011 year became worse in many areas. The uncertainty in financial markets was rising as well as worries about the health of European banks, about the crisis in the euro-zone countries and also about the decrease in the global economic growth. These negative trends influenced each other aggravating the situation in most areas even more. While economic reports in some countries remained positive in the first quarter of the year, in the second quarter of the 2011 the majority of economic blocks experienced the economic slowdown or even recession. The most important factor of the deteriorated economic situation was a growing inflation and the anticipation of the economic slowdown in developed economics. In the U.S.A, the slowdown appeared already in the first quarter of the year of 2011 and in the euro-zone it occurred later, i.e. in the next quarter of the year. The negative trends of a slowdown of the economic growth manifested themselves also in Germany, which might have a harmful effect on the Slovak Republic, the export of which is oriented to this country. Such negative expectations of the economic growth escalated the crisis in the euro-zone increasingly. Both the fear of the sustainable debt service and the deteriorated situation in a bank sector expanded also to other countries. As for the Slovak banks, their profits in the third quarter of the 2011 were still doubled in comparison with the same period of the previous year. The debt crisis and other negative phenomena caused that in global financial markets the uncertainty was increasing and worsening the financial system stability. The International Monetary Fund (IMF) along with the European Central Bank (ECB) are of the opinion that the stability of the global and European financial system is threatened and therefore it is necessary to find a joint solution. Despite this statement, the economic situation in the Slovak Republic and its financial sector have not experienced markedly the negative global trends so far. When considering the first six months of the 2011 the situation was relatively good and neither the uncertainty in global financial markets nor a decreasing economic growth had a damaging effect on the Slovak economics. The next development will depend on the impact of the crisis on Slovak households and companies. Most sectors recorded the growing volume of assets. In some sectors the profitability increased and in some of them even approached a level before the crisis. This can be accounted for mainly the orientation of the national financial system to the country's economics and also the fact that in the first six months there still

predominated positive data about the economic growth in Slovakia. In the next period the stability of the home financial sector will depend, to a large extent, on the development of macroeconomic foundations in the national and foreign economics. For the Slovak financial sector a great importance will have mainly the situation in export-based industrial branches and also the development in the sector of households, the significance of which is given an increased attention. The households participate, to a large extent, in the growth of credits contributing to the profitability of banks. They constitute the important part of insurance businesses and dominate in the growth of assets within the second- and third pension-saving pillars. The financial position and ability to reimburse commitments to banks, and also the consumption mood in households, will influence considerably the growth of assets and the profitability of the national financial sector. Since the year of 2009 the importance of the company sector in the Slovak financial system has been slightly decreasing. However, its financial position has a direct impact mainly on the bank sector. Now a period of stagnation proceeds between them because the demand for credits from the side of companies is low and meanwhile the banks do not expect any improvement. Consequently, the deterioration of the companies' performance and negative expectations for future can directly or indirectly influence the stability of the financial sector. The situation in the company sector is important also for the sector of households.

A key event of the year of 2011 was a rise of the debt crisis in euro-zone countries. For its elimination it was vitally important to find a way how to overcome this problem in a short- or medium-range perspective and thus support the next macroeconomic development and financial stability practically in the whole world. Since the beginning of the year of 2011 the debt crisis in euro-zone countries has passed through many phases. When Ireland accepted rescue fund from the European Union and the International Monetary Fund in December of 2010, attention shifted to Portugal. Despite the fact that the leading politicians of the euro-zone concluded in March 2011 an agreement to strengthen the temporary rescue fund EFSF (European Financial Stability Facility) and the future permanent rescue mechanism ESM (European Stability Mechanism), the pressure of financial markets finally necessitated the provision of a financial aid to Portugal. Thus Portugal became the third euro-zone country which received a rescue fund within the rescue programme of the European Union and the International Monetary Fund. At the first half of the 2011 Greece returned again to the centre of the crisis when it was obvious that it was impossible to realize

its comeback to bond markets in the initially intended time horizon. As a consequence, it was necessary to provide the second rescue fund to Greece. The revenues into the maturity of governmental bonds and CDS (Credit Default Swap) spreads, i.e. the fees of Greece and also of other inflicted countries, increased to new historical maxima on the background of the complicated and time-consuming discussion about the structure of the rescue fund. The tension in markets arose due to a long-time unsolved question whether the financial burden should be transmitted, at least partially, also to a private sector and if so, in which form it should be done. Finally, the following variant was accepted: private investors will be involved in the process in the form of a relatively comprehensive scheme implying for them the realization of a loss from the holding of these securities. The participation in this scheme was based on the voluntary decision.

2. METHODS

In the area of investigation carried out to find out the situation in the financial market many unsolved questions were detected. Their initial status was examined by using basic scientific methods incorporating a cycle of gathered empirical data, their classification and processing. The research methods enable one to formulate the new recognition, its elucidation and classification into outputs in the form of diagrams and tables. In the indicated output (of the paper) the fundamental experimental method based on the current state of the financial market in Slovakia was used. It analyzes the market financial situation, outlines basic problems and subsequently processes outputs by a logical deduction, and, of course, it also summarizes conclusions in the given field.

In 2012, the economic environment of the financial sector went through a continually proceeding uncertain development. Although it is true that in this year the development in financial markets gradually calmed down due to steps taken by the European Central Bank (ECB), the market expectations for a better macroeconomic development were not fulfilled. It was just the macroeconomic development which confirmed the continuation of the uncertain development at the end of the year of 2012. In comparison with the 2011, the situation partially improved, but, on the other hand, a problem of the insufficient economic growth associated with a low competitive ability became more pronounced.

In the course of the year of 2012, various factors influenced the creation of the profit of financial institutions, from among which the most important were

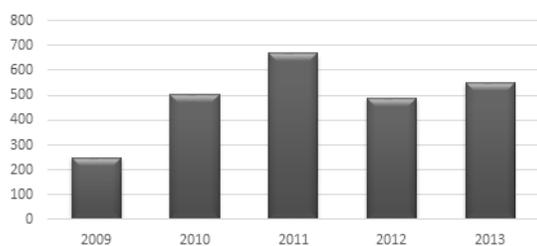


Fig. 1. Profit after the taxation of the bank-sector in Slovakia expressed in mln Euros

Source: own elaboration based on the information of the National Bank of Slovakia.

the following:

- the positive development in financial markets which contributed to higher sales in the collective investment funds and, at the same time, to better profitability in the sector of income savings,
- the mixed effect on the profit leading to the development of interest rates; on the one hand, the positive effect of falling interest rates on the growth of the obligation prices, which was experienced mainly by complementary income funds, and, on the other, low rates complicating the situation in insurance companies and exerting pressure on bank interest incomes.

In the bank sector, an independent negative role was attributed also to the obligatory payments of financial institutions (the so-called bank tax), which resulted in a decrease of the profitability of banks to the lowest values since the beginning of the financial crisis.

Consequences of the economic bank-sector recession have manifested themselves also in the risk reduction, which is illustrated in Fig. 1. According to the NBS data, the Slovak bank sector achieved in 2012 a profit amounting to 488.2 million Euros representing 27%, i.e. less than in 2011. In 2013, the above-mentioned bank sector achieved a profit amounting to 552.9 million Euros, which represents an increment of 10.7% in comparison with the year of 2012.

During the year of 2012, the total volume of the company deposits did not undergo any unambiguous trends. The positive phenomenon was a growth of residues in non-term deposits, which might be connected with the sufficient liquidity in the company

sector. However, a certain change occurred in the company deposit rates. In the last years an average company deposit rate was at a lower level than the monthly EURIBOR (Euro Interbank Offered Rate). Notwithstanding, in 2012 a decline of the interbank rates manifested itself in the company deposit rates only to a lesser extent. This resulted in higher rates for the company deposits than were monthly rates in the interbank market.

3. RESULTS, DISCUSSION AND LIMITATIONS

The development in 2013 was stimulated by a demand of the private sector in the euro-zone as well as by signals for termination of the negative development in the labour market. The improvement of the economic situation was transferred to the Slovak economics which was undergoing an increased rate of the economic growth. This could be observed in the recovery of the industry and civil engineering, which supported a growth of the investment demand. Financial markets were relatively stable, without any turbulences in comparison with previous periods (NBS, 2013).

Tab. 2. The number of bank subjects in Slovakia

A type of bank/year	2008	2009	2010	2011	2012	2013
Central bank (National bank of Slovakia)	1	1	1	1	1	1
Banks without a foreign property participation	1	2	2	2	2	2
Banks with a foreign property participation	15	15	13	13	12	12
Foreign bank branches	9	9	11	14	17	14
All branches in the Slovak Republic	26	27	27	30	32	29
Providers of the free cross-border bank services	190	252	274	296	294	310

Source: (NBS, 2011).

Despite the above-indicated signals of reviving the economic situation, the relatively great risks of the repeated and deteriorated economic conditions in the euro-zone persisted. The risks arose primarily from the excessively high indebtedness of the public and private sector as well as from the potentially overestimated prices of some more risky assets or currencies. The dynamics of the bank sector development in Slovakia is indicated along with the number of bank subjects in Tab. 2 where the number of commercial banks and of foreign commercial bank branches - which started to be active in the range of years of 2008 to 2013 - is incorporated.

After a decline in 2012 the bank sector experienced again a growing profitability. The main factor influencing the development in 2013 was a continual and relatively intense growth of retail credits, which showed itself in the increase of the net interest incomes of banks. Although the before-mentioned growth in 2013 was associated also with an accelerated rate of the growth of failed credits and with a growth of costs expended on credit risks in the sector, the negative trend was compensated by a fall of the aforesaid costs in the sector of companies. A positive trend in the Slovak bank sector was the continu-

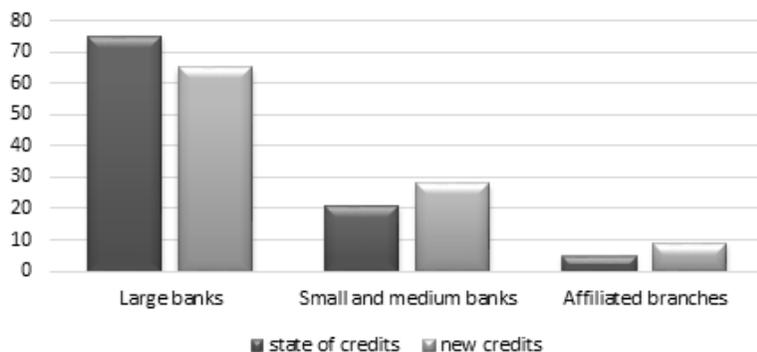


Fig. 2. Analysis of the Slovak financial sector in 2013

Source: (NBS, 2013, p. 21).

al increasing of the capital adequacy which raised in 2013 to as much as 17.2% exceeding an average value in the euro-zone (Jílek, 2013).

Throughout all year the total market share of large banks was decreasing for a benefit of small and medium banks, with the most remarkable effect being evident in the first half of the year. The portfolio size of foreign bank branches increased by as much as one third. The credits with a fixation from 1 to 5 years continued to dominate, while those with a fixation up to 1 year slightly decreased. The individual average shares of banks in the state of existing and new credits are documented by Fig. 2.

A rate of the growth of real estate credits rose in the first half of the year of 2013, then it slowed down and at the end of the year it achieved again the same speed as in the first half of the year. The overall dynamics of the real estate credits could be explained mainly by the historically low interest rates. The other partial cause of this phenomenon could be the stagnation or even the slight decline in real estate prices, which stimulated the real estate demand and subsequently also the credit demand for the financing of immovable assets.

Thanks to the level of adequate own sources and to the ability of banks to generate net interest incomes,

the bank sector could be resistant to scenarios of the unfavourable economic development and also to the undesirable development in financial markets.

CONCLUSIONS

After monitoring the development of the financial market in Slovakia it is possible to conclude that in recent years the positive and negative trends were alternating and influencing its stability with a different intensity. It was very much alike in the first half of the year of 2012, which brought several new trends in comparison with the year of 2011. While at the end of the 2011 the whole financial sector was experiencing a crisis in the euro-zone significantly, during the first six months of the 2012 its influence was somewhat moderate. In the first half of the year 2013 the development of the global economics and that in financial markets did not allow one to draw conclusions from the aspect of the future trend, not even from the aspect of the potential impact on the Slovak economics and national financial sector. Although the global economics should advance at least at a moderate rate and the recession in the euro-zone was expected to come to an end from the technical point of view, the risks still persisted and, in the case of materialization, they suppressed the activity. Besides other facts, there exist some unsolved questions concerned with potential impacts on the consolidation of public finances in most countries of the euro-zone, or the question of confidence in the future growth and in the positive development of the national demand. Financial markets were positively influenced by a number of realized or half-elaborated measures resulting in the more peaceful period. A growth of several market segments was supported, to a great extent, by historically lowest revenues of the minimum risk assets which created the conditions for a growth of demand for more risky assets in order to achieve higher revenues. Therefore, it is possible to maintain that the European revival emerging in 2013 was transferred also to the Slovak economics, which increased the national economic growth. The improvement was noticeable especially in the industrial and building production. These sectors are traditionally prepared to participate in further economic growth, which reflects also in the improved employment. It follows that in the last year economic condi-

tions for a growth of the financial sector were positive. In addition, the better situation in markets was favoured also by the supporting operations of central banks which helped to decrease the market turbulences to a minimum, to make the revenues of more risky assets stable, but, on the other hand, to assess the conservative investments near to zero.

In view of the financial analysts, the situation in the world economics will improve in the next year, i.e. it will grow more rapidly than in this year. It is expected that Europe would experience the first positive economic results in the last three years. In the euro-zone both the interest rates and the influence of austerity measures is decreased. As a reward, in 2014 a slight growth is anticipated to be approximately 1%. In this way the euro-zone will have a chance to achieve the first positive economic progress since the 2011. However, the main assumption for such a development is also the settlement of all controversial worldwide economic and political questions which would stabilize the system of the international financial market.

LITERATURE

- Chovancová, B., Žofčák, S. (2012), *Kolektívne investovanie*, IURA Edition, Bratislava
- Chovancová B. et al. (2014), *Finančné trhy - nástroje a transakcie*, Wolters Kluwer, Bratislava
- Jílek J., Svobodova J. (2009), *Účetnictví bank a finančních institucí*, Grada, Prague
- Jílek J. (2013), *Finance v globální ekonomice. I, Peníze a platební styk*, Grada, Prague
- Jílek J. (2013), *Finance v globální ekonomice II - Měnová a kurzová politika*, Grada, Prague
- Ministry of Justice of the Slovak Republic, *Statistic of bankruptcy proceedings 2007-2012*, http://www.nadsme.sk/files/Stav_MSP_2011.pdf [15.10.2014]
- Mishkin F.S. (2011), *Over the Cliff: From the Subprime to the Global Financial Crisis*, *Journal of Economic Perspectives*, American Economic Association 25 (1), pp. 49-70
- Mishkin F.S. (2007), *The Economics of Money, Banking, and Financial Markets*, Eight Edition, Pearson – Addison Wesley, Boston
- National agency for development of the small and medium business, <http://www.nadsme.sk> [15.10.2014]
- NBS - National Bank of Slovakia, *Analysis of the Slovak financial sector in 2010, 2011, 2012, 2013*, <http://www.nbs.sk> [15.10.2014]
- Pálenčáková E. (2013), *Risk capital as the internal financial source of small- and medium-sized companies*, <http://www.epi.sk> [15.10.2014]
- Report about the state of the small and medium business in the Slovak republic in 2011, http://www.nadsme.sk/files/Stav_MSP_2011.pdf [15.10.2014]
- Rose P.S. (1992), *Money and capital market*, Fourth edition, IRWIN, Boston
- Šimonová J. (2008), *Criminal attributes acting in the financial market in the Slovak Republic (in Slovak)*, *Proceedings of the international conference entitled "Policy, Law, Economics and Society – Present Time and Visions to the Year of 2025"*, European Polytechnic Institute, Kunovice, pp. 269-274
- Šubertová E. (2010), *Business activity of starting entrepreneurs in the period of crisis and after it In: How to go on after the crisis, part 1 (in Czech)*, *Proceedings of the International Conference in Prague*, Publishing house Oeconmica, University of Economy, Prague
- Zatrochová M. (2011), *Some selected problems of financial market*, Publishing of Slovak Technical University, Bratislava