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Review Paper

Comparative Analysis of the Western Balkans Banking Sector in the Two Global Crises

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ABSTRACT

Western Balkan Countries have comparable economic determinants due to their geographical position, small size economy and issues experienced during economic crises. The world's precarious situation during the Covid-19 Pandemic was the initial motivation for this research. Due to the consequences that economic crises would have on the whole economies of these bank-structured countries, it is important to analyze their banking performance during times of economic instability. The primary objective of this study is to compare the banking performance of Western Balkan Countries during the Global Financial Crisis (GFC) and Covid-19 Pandemic Crisis. This study will provide as a reflection for policymakers to evaluate whether these countries learned from the GFC and were more prepared in their latest crises. The approach used in the research is a comparison of the performance of different countries, and the time period analyzed is divided into three distinct time pillars. The first one in Global financial Crisis (2008-2009), the second one is Post Crisis and Recovery (2010-2018) and the last one is Crisis Covid 19 Pandemic (2020-2021). Indicators selected for this research revealed a substantial negative tendency during periods of crises, with modest differences across countries that are positively correlated with their economic development, as shown by the results.

HIGHLIGHTS

- The article aims to compare the banking performance of Western Balkan Countries during the Global Financial Crisis and the Covid-19 Pandemic Crisis, in order to assess whether lessons were learned from the previous crisis and to provide insights for policymakers, highlighting negative tendencies and modest differences across countries.

Keywords: Banking Performance, Bank Structured Economies, Covid-19 Pandemic Crisis, GFC, Ranking Table

Due to the Western Balkan Region's small economy and its vulnerability to the consequences of financial shocks, the region has been subject to significant economic challenges during times of economic crisis. Six countries in the Western Balkan Region were originally closed and centralized economies, causing them significant economic problems as they transitioned to open, market-based economies after the fall of communism. From that point forward, the Western Balkan Countries (WBC) endeavored to adapt more to global circumstances and to establish financial stability as the primary component of their macroeconomic environment. Substantial positive developments that were evident in their macroeconomic environment included a significant decline in the inflation rate and a decline in the poverty rate.

The budget deficit as a percentage of GDP was an additional difficulty for WBC as an internal imbalance in 2008, with the greatest rate coming from Albania (-5.1%). In 2008, Albania had the

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highest share of GDP at 53%, while Bosnia and Herzegovina had the lowest share of GDP at 17%. High levels of public debt are another negative consequence of the WBC. Other challenges, such as higher inflation, factors that have an impact on weak competitiveness leading to low levels of investment, limited trade interactions, and limited foreign direct investments, were difficult for governments to strike a balance with (Diallo, 2018).

Considering the countries that are the focus of this study, the banking sector is regarded as one of the most regulated sectors of the economy. In addition to this, banks, as more conglomerate financial institutions, constitute the backbone of the entire financial system due to their function and impact on the evolution of the economy. Particularly in times of financial crisis, it is essential to remain vigilant regarding all elements related to the performance of the banking sector. In countries of the Western Balkans, the structure and size of the financial sector are dynamic and diverse in terms of the number of banks and their foreign or domestic capital ownership. The primary characteristic that links these nations' financial systems is that they are bank-based. Foreign-owned banks predominate the banking sector in the majority of these countries (World Bank Group, 2016; OECD, 2021).

This scientific paper will evaluate and compare, within countries, the detrimental consequences of each crisis on the performance of the banking sector. In this paper, will be examined whether or not these countries' banking sectors have managed to learn from the Global Financial Crisis (GFC) and are ready to weather economic shocks coming from external causes, more than a decade after the crisis.

MATERIALS AND METHODS

This comparative research analyzes Albania, Bosnia and Herzegovina, Kosovo, North Macedonia, Montenegro and Serbia as the six Western Balkans countries. In the analysis, Euro Zone countries serve as a baseline for a number of selected measures. The analysis is based on a cross-country comparison of financial ratios assessing the general efficiency of each country's banking sectors. The timeframe is from 2008 to 2020 upon which the analysis is based. This timeframe is separated figuratively to emphasize the most significant peaks of time. The interval 2008-2009 is termed Crisis 1 "Global Financial Crisis," whereas the period 2010-2018 is considered the post-crisis period, which includes the recovery phase, and the interval 2019-2020 is termed Crisis 2 "Covid-19 Pandemic." The results for each country are estimated as the mathematical mean for each of the aforementioned timeframes. A ranking table is provided in the analysis to compare the banking performance of the countries during each period. The ranking of countries has been determined by assigning each country a grade based on its average performance on each parameter.

The study relies on secondary data compiled from sources such as the World Bank, the International Monetary Fund, and each country's annual Financial Stability Report. This research is limited by the lack of recent data for some countries, such as Kosovo and Montenegro, due to the publishing date of the data.

Different scientific methods were used in the research. The main was quantitative data statistical methods, which allowed to form the main conclusions about the performance of banks in the Western Balkan countries. The historical method was also used, which allowed to evaluate the development of the sector in retrospect. It is also worth mentioning the graphical method, which allowed depicting the basic information that was used and found during the research. An important role was also played by the method of abstraction, which allowed to study the present state and possibilities of the development of the Balkan banking sector, ignoring some external factors of little importance.

RESULTS

Overview of Macroeconomic Efficiency Incentives

According to Table 1, WBC have demonstrated greater stability throughout the Global Financial Crisis than Euro Zone countries, which have lower GDP growth rates on an annual percentage basis. For all countries, the post-crisis period and subsequent recovery have been slow but positive. Comparing the Pandemic crisis to WBC, reveals that Montenegro has seen the biggest challenges.

Table 2 indicate, in accordance with the GDP Deflator, which aids in determining the extent

Table 1: GDP Growth Rate (annual, in %)

Country	Crisis GDC (average)	Post Crisis and Recovery (average)	Crisis Covid-19 (average)
Interval Periods	2008-2009	2010-2018	2019-2020
Albania	5.43	2.65	-0.57
Bosnia and Herzegovina	1.22	1.96	-0.75
Euro Zone	-2.04	1.38	-2.69
North Macedonia	2.56	2.50	-0.68
Montenegro	0.71	2.75	-5.55
Serbia	1.46	1.68	1.63
Kosovo	4.95	3.48	-0.97

Source: *compiled by author based on World Bank Group (2012; 2016; 2021).*

Table 2: GDP Deflator and annual inflation

Country	Crisis GDC (average)	Post Crisis and Recovery (average)	Crisis Covid-19 (average)
Interval Periods	2008-2009	2010-2018	2019-2020
Albania	3.27	1.38	-0.24
Bosnia and Herzegovina	3.76	1.40	1.62
Euro Zone	1.70	1.24	1.69
North Macedonia	2.89	2.77	1.00
Montenegro	5.02	2.27	0.93
Serbia	8.49	4.10	2.14
Kosovo	4.27	2.20	0.81

Table 3: Financial sector domestic credit as percent of GDP

Country	Crisis GDC (average)	Post Crisis and Recovery (average)	Crisis Covid-19 (average)
Interval Periods	2008-2009	2010-2018	2019-2020
Albania	68.29	62.77	66.34
Bosnia and Herzegovina	62.55	63.20	61.82
North Macedonia	42.43	54.86	67.24
Montenegro	81.67	60.96	N/A
Serbia	42.12	53.83	N/A
Kosovo	11.99	29.66	49.13

of price inflation during a certain time period, how much inflation has occurred that during GFC Western Balkans countries have had small variations in performance with the exception of country of Serbia which has seen a notable increase in comparison to other countries. Contrarily, the Eurozone has exhibited the lowest rate of this indicator, indicating that the impact was more gradual than in the Western Balkans. Post-crisis and throughout the time of economic recovery, the GDP deflator suggests that inflation has a smaller impact on the GDP. Even in the midst of the Covid-19 Pandemic, the steady decline continued.

Domestic credit given by the financial sector as a percentage of GDP is an additional essential indicator that reflects the banking sector's depth and the financial sector's growth in terms of size. The results of Table 3 indicate that during the GFC, Montenegro, Albania, and Bosnia and Herzegovina experienced the greatest increase in this ratio, whereas during the Covid-19 crisis period, the highest rate belongs to North Macedonia, which has shown a stable growth of the ratio with nearly 10% at each period analyzed in the table, along with Albania and Bosnia and Herzegovina.

According to Table 4, financial resources allocated to households and businesses by financial corporations in the form of loans and not simply as a percentage of GDP indicate that Crisis Covid-19 Pandemic has lower rates than Crisis GFC in the majority of countries. Kosovo experienced lower rate of domestic credit extended to the private sector during the Global Financial Crisis, while Montenegro recorded the highest. In contrast, Bosnia and Herzegovina reported the highest rate during the Crisis Covid-19 period, whereas Albania reported the lowest.

The banking sector of the economies of the Western Balkans has demonstrated economic stability and appears to be well capitalized. Referring to the Bank capital to Assets ratio as a percentage of GDP, the results are slightly higher during the GFC Crisis, indicating that there was sufficient capital to cover the assets during this period, with Serbia having the highest result and Albania the lowest. Compared to two other periods, there are little variations, indicating stability overall. Credits for this achievement are the immediate and prompt measures that governments of each country took to mitigate the significant damage that the crisis caused to all aspects of the economy, even though it was a harsh and stand-by lesson.

In terms of liquidity, the last indicator in Table 6 reveals the amount of liquidity that indicates the deposit-taking sector's ability to withstand balance sheet shocks. Due to the size of respective economies, the levels of this indicator are comparable across three time periods, with the GFC period showing the highest rate for Serbia and the lowest for Kosovo, and the Crisis Covid-19 period showing the highest rate for Bosnia and Herzegovina and the lowest for Kosovo. Overall, it is known that during periods of shocks there are effects on reduced growth rates and banking sector incapacity due to the sector's direct impact on this group of countries.

According to the return on equity measure, which represents how well a bank's management manages its assets to create profits, the rates for all Western Balkan countries are greater during the Pandemic crisis than the Global Financial Crisis. Specifically, Montenegro is the country with the lowest rate during both the crisis and post-crisis and recovery periods (Table 5).

There is a link between lending and deposit interest rates, with GFC rates being more than double those of Crisis Covid-19 for some countries. Kosovo has the highest interest rate, followed by Serbia in the GFC, according to the interest rate spread.

Table 4: Share of private sector domestic credit in GDP

Country	Crisis GDC (average)	Post Crisis and Recovery (average)	Crisis Covid-19 (average)
Interval Periods	2008-2009	2010-2018	2019-2020
Albania	38.21	37.96	36.63
Bosnia and Herzegovina	64.84	59.72	58.45
Euro Zone	104.98	94.20	90.56
North Macedonia	43.19	48.66	53.84
Montenegro	81.36	53.41	54.46
Serbia	38.48	42.63	43.94
Kosovo	33.61	37.63	46.36

Table 5: Return on Equity

Country	Crisis GDC (average)	Post Crisis and Recovery (average)	Crisis Covid-19 (average)
Interval Periods	2008-2009	2010-2018	2019-2020
Albania	8.00	8.61	11.95
Bosnia and Herzegovina	2.55	4.38	11.20
North Macedonia	9.05	9.01	11.50
Montenegro	-6.95	-6.16	6.80
Serbia	6.80	3.81	8.15
Kosovo	16.60	12.50	16.45

According to Covid-19, crisis spread is normalized at lower rates for the majority of Western Balkan countries.

The fact that the Western Balkan banking sector is dominated by foreign-owned banks is a significant topic of discussion. In this regard, they are highly dependent on the financial success of their parent bank. The majority of foreign banks are members of the European Union, including Austrian banks, Italian banks, Greek banks, etc. This includes the anticipated spikes in times of crisis, as well as any other condition that the parent banks seem to find or difficulties in addressing at their economies, which are mirrored as a consequence at their operating banks in Western Balkan.

This analysis is based on the hypothesis that the performance of the banking sectors in the countries that constitute the Western Balkans is significant for the decision-makers in charge of maintaining financial stability, particularly during times of crisis, because their economies are structured around banking. Keeping this common characteristic for all countries under study in mind, authors can conclude that this is a true statement based on all indicators analyzed above, as well as the significant changes these countries appear to experience during periods of crises and the slight differentials they appear to experience during post-crisis and recovery periods, indicating that these countries require time to make progress and are on the right track for future progress.

DISCUSSION

K. Tomczak (2022) studied in detail the problems of the financial crisis in 2008-2009 based on the European Union. As noted, its transmission was not through real links between the countries under study, but through contagion. In other words, countries in which a financial crisis had already occurred or had begun influenced others, causing them to become unstable. Although problems in the banking sector are considered the main causes for the emergence of this crisis, some other causes, such as rising inflation and unfavorable changes in exchange rates can also be identified. The negative effects of the 2008-2009 crisis in terms of institutional confidence were also studied by F. Roth (2022). Scholars have noted that it caused residents to lose confidence in European institutions, including the European Central Bank. In contrast, trust in the government increased, as did socialist and anti-capitalist sentiments. The impact of this crisis on the banking sector has been studied by S. Claessens and N.V. Horen (2014). As such, the most important change after the events of 2008-2009 was that the presence of foreign banks in different countries became less global. This allowed more effective development of national banks and led to an increase in the number of players in the world. Such trends can be used by the state of each country to achieve its benefit in terms of the development of its banking sector and take them into account in the formation of economic and social policy.

The bank operations that changed during the COVID-19 crisis were assessed by M. Mateev *et al.* (2022). Operations of these institutions and their potential change during the beginning of the pandemic, depending on their level of competition and efficiency of functioning, was evaluated. They proved that the better the bank's performance before the crisis — the better its performance after the crisis began. Thus, the top management of banks should spend more time on the specifics of the management of organizations to improve their financial stability, as this will allow to better resist such "black swans" as COVID-19. An assessment of bank performance in more than 100 countries from 2016 to 2021 was conducted by M. Shabir *et al.* (2023). Researchers showed that the crisis harmed the stability and efficiency of all banks in the world, but more than others felt the impact of the crisis on small, undercapitalized, less diversified. Factors that allowed to pass this period easier were a better regulatory environment, higher institutional quality, and a higher level of financial development.

Similar results were achieved by Y. Duan *et al.* (2021) and M. Ganic (2012). They showed that COVID-19 significantly increased instability in different countries of the world, which was caused by both the virus and overly restrictive government policies. Interestingly, the researchers conclude that large banks, with high loan-to-asset ratios, often insufficient capital, and low network centralization were more susceptible to systematic risks due to the shock of the pandemic. Deposit insurance (Alam *et al.* 2021; Ferrouhi, 2018; Borio, 2020), higher institutional development, and power distance also proved helpful in reducing risk. An analysis of how banks in China and the United States responded to the onset of the pandemic was conducted by A. Hasselgren (2021). He notes that although both countries were affected by the onset of the pandemic, Chinese banks took a relatively lower hit, as evidenced by changes in several ratios analyzed by the scholar, such as capital adequacy ratio (CAR), return on assets, non-performing loans, etc. In general, this may be caused by the fact that the Chinese system of the state system is better able to cope with various kinds of crises than the American one, which is due to the greater role of the state in the economy (Andries and Capraru, 2013; Cotula, 2021). It is worth noting that in most of the Western Balkan countries, too, the authorities play a fairly large role in regulating market processes, which may be one of the reasons for their successful passage through the COVID-19 crisis.

Another period, 1996-2017, and how the banks of Albania, Bulgaria, Greece, Turkey, Croatia, and Romania showed themselves was studied by D. Kirikkaleli and E.U. Kayar (2023). The researchers noted that there is a long-term statistically significant relationship between political, economic, and financial factors and the well-being of the banking sector, which can partially explain certain trends in the countries. Thus, they offer suggestions on how best to achieve greater macroeconomic stability as well as financial stability in the banking sector. Government policy (especially in the face of potential instability) should focus on improving foreign exchange reserve ratios and domestic credit, which pose volatility risks to stable economic growth and higher levels of prosperity. The authorities should consider as many forms of risk as possible that may be realized in the country, and be prepared to eliminate them all. It is worth noting that the good performance in terms of crisis resilience of the Balkan countries assessed above was also due to their sound policies in terms of domestic credit and yields.

Thus, banks in the Western Balkans have indeed proven to be resilient to all kinds of shocks and crises (Kubiszewska, 2018). Nevertheless, they still have some need to improve their financial sustainability, especially in countries such as Serbia, Kosovo, Montenegro, and Albania. The state, for its part, should aim to simultaneously create favorable conditions for the functioning of the banking sector and provide the highest possible level of protection for citizens in the event of certain difficulties (even to the detriment of investors). The implementation of such a policy will create the most favorable conditions for the functioning of the banking sector and significantly improve the financial stability of the country.

CONCLUSION

Based on the findings of this scientific article, the performance of the banking sector in the Western Balkan Countries is deemed to be satisfactory in light of the period of crises under consideration. There are also minor differences between the two periods of crisis: the Great Financial Crisis and the Pandemic of Covid-19. When it comes to their profitability, the countries in the Western Balkans have demonstrated better and higher rates during the Covid-19 Pandemic Crisis. Considering nonperforming loans, Crisis of Covid-19 Pandemic is highlighted as substantially lesser than the GFC, although they remain a risk.

The Banking system Compared to past periods, the overall performance tends to recover faster and be better overall. Being a country with a bank-based economy structure is crucial to the financial stability of the country. As mentioned previously in the analysis, the banking sector of the Western Balkans, in addition to being the primary source of liquidity for the country's economy, is characterized by foreign-owned banks, meaning that the performance of the parent banks is crucial for the banks conducting financial activity in the region. For the financial stability of the country as a whole, it is necessary to analyze the impact of parent bank vulnerabilities on the banking industry of Western Balkan countries.

From a comparative perspective of the banking sector performance of the Western Balkan countries, it can be stated that according to ranking tables, Montenegro has maintained the highest rating compared to other countries in the region during three distinct periods. With respect to the time with the lowest-ranked country, there are some minor differences.

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