

**UDC 339.92**  
**JEL: F21, O19**

**Andrii Ramskyi**

D.Sc. (Economics), Professor,  
Head of the Finance and Economics Department,  
Borys Grinchenko Kyiv University  
Kyiv, Ukraine  
ORCID ID: 0000-0001-7368-697X  
*e-mail: rama@ukr*

**Inna Budnichenko**

Master of Science Degree  
Boris Grinchenko Kyiv University  
Kyiv, Ukraine  
*e-mail: i.bud@ukr.net*

**FINANCIAL STABILITY OF A BANK - FACTOR OF STABILITY OF  
BANKING SYSTEM**

**Abstract.** The article is devoted to the analysis of the financial stability of Ukrainian banks at the present stage of development and the identification of the main factors of influence that are associated with it. The main tendencies of development of the banking system of Ukraine are considered. The present state of the banking system of Ukraine is determined. Financial stability plays a significant role in planning the activities of commercial banks. In general, its indicators reflect the level of riskiness of the functioning of the entity of the banking system. Managing financial sustainability has a significant impact on the functioning of banks. That is why it is necessary to create special control departments in banking institutions. The research of financial stability of banks is based on financial sustainability indicators developed and used by the IMF and the World Bank as the basis for the "Integrated Financial Sector Development Program until 2020".

The necessity of applying different methods for evaluating the financial stability of commercial banks has been established in order to identify a wider range of problems related to the efficiency of the functioning of the banking system. The description of two main groups of factors, under the influence of which the financial stability of banks undergoes changes, is presented. It was revealed that external factors have a more significant impact on the financial stability of a bank. In particular, the factors of mega environment have become more important when banks enter the international financial space.

Internal factors lie mostly in the management plane, and it is just the inefficient management of the bank that leads to the disruption of its stable financial condition. Specific features of management of financial stability and methods of its evaluation are considered. The analysis of economic standards of the banking system of Ukraine is carried out. The measures are proposed to minimize the risks and maintain the stability of banking institutions at the required level for normal functioning in modern conditions. It has been proved that providing, supporting, analyzing and evaluating the financial stability of commercial banks is a driving force in the development of the banking system, and hence the entire Ukrainian economy.

**Key words:** banking system, financial status, financial stability.

**DOI:**<http://doi.org/10.32750/2018-0201>

**INTRODUCTION**

**Formulation of the problem.** The key to the effective functioning and sustainable development of the economy of any country or even a regional alliance is its stable and reliable banking system. The banking system is one of the main parts of Ukraine's economic system, and, consequently, its dynamic development contributes to the growth of the Ukrainian economy and its emergence on the international arena. An important category that is responsible for the stability of the banking sector is the financial soundness of commercial banks. It is an indicator of the financial condition of banking institutions that determines their

development. In this way the relevance of the impact of the financial stability of banks on the sustainability of the banking system of Ukraine is manifested.

**The analysis of recent research and publications.** Issues related to ensuring the financial stability of the banking system and individual banks, financial analysis, problems of regulation of financial stability are highlighted in the works of such scholars as O.V. Dzyublyuk, V.V. Kovalenko, Yu.A. Garkusha, Yu. S. Dovgal, R.O.Chamara.

**The purpose of the article** is to review the financial state of Ukrainian banks, analyze the financial stability of the bank as a factor of stability of the banking system as a whole and develop ways to improve it.

#### **RESEARCH RESULTS.**

There are many interpretations of the notion “financial stability of the bank”. It is generally explained that financial stability is a qualitative characteristic of the financial condition of a bank that is determined by the adequacy, equilibrium and optimal correlation of assets and financial resources, under the conditions that the necessary level of liquidity and solvency, profit growth and risk reduction are provided and the ability to withstand unpredictable costs and maintain the state of effective functioning is ensured [1, c. 38].

The research of financial stability of banks is based on indicators of financial sustainability that have been developed and used by the IMF and the World Bank as the basis for the "Integrated program of financial sector development till 2020".

Key indicators of financial stability of banks usually include:

- the ratio of capital to assets as an indicator of capital adequacy or financial leverage of banks, which determines the degree of provision of assets by resources different from their own and which is calculated as the ratio of sum of capital and reserves to total assets;

- the ratios of regulatory capital to risk weighted assets as an indicator of capital adequacy of banks, which is calculated by dividing the aggregated data on the regulatory capital of all banks into an aggregate indicator of risk weighed assets;

- the ratio of overdue loans to total loans as an indicator of the quality of assets in the loan portfolio. This indicator is calculated as the ratio of the value of overdue loans to the total value of the entire loan portfolio;

- return on assets as a traditional indicator of the efficiency of using the assets of the bank, calculated as a fraction of the division of net profit into the average value of aggregate assets of banks;

- return on equity as an indicator of the efficiency of using the equity capital of the bank, calculated as a fraction of the division of net income into the average cost of capital.

To date, there is a huge variety of factors that affect the formation of financial stability of the commercial bank. Differences in the nature, directions and forms of their identification cause the need for their systematization. At the same time, such systematization is relevant, firstly, as a methodological tool for the study of financial stability; and, secondly, as a methodological basis for identifying quantitative dependencies on the factors that form it, and for creating a forecast of development; thirdly, accounting for factors is needed while developing specific proposals for improving financial stability [2].

Under the influence of external and internal factors, the financial condition of the bank is always subject to change, so it is worth saying that absolutely financially stable banks do not exist. Depending on the activities of the bank, the factors are divided into the following groups [5, p. 49]:

1. Dependent on the bank's activity (internal or endogenous):

- organizational: personnel policy, quality of corporate governance, quality of internal control systems, marketing, management system and level of innovation processes;

– information and technology: the level of application of the latest technologies, the level of scientific and technical progress, the use of information systems, the level of skills of personnel in this sphere;

– financial: capitalization, asset structure, level of risk, stability of financial results (profitability, efficiency, solvency, liquidity).

2. Independent of the activity of the bank (external or exogenous):

– world level (megawave): state of world economy and political stability, international investment position of the country, international standards, state of technology development;

– macro level (state level): stability of the domestic political situation, legal protection, demographic situation in the country, level of financial literacy, culture, public confidence in financial and credit institutions, stability of the national currency, deficit or budget surplus, monetary factor;

– micro level (banking sector level): monetary policy of the NBU, banking infrastructure development, financial market conditions.

External factors have a more significant impact on the financial stability of the bank. In particular, the factors of mega environment become more important when the banks enter the international financial space. Macro level plays its role when it comes to dynamic processes at the national level. The stability of a single bank needs to be analyzed in conjunction with the stability of the banking system as a holistic entity.

Internal factors are mostly managed by the bank itself, and it is exactly the inefficient management that leads to disruption of the stable financial condition of the bank. Such threatening factors include the provision of inaccurate information to clients, the imperfection of the structures responsible for the external and internal security of banking institutions, credit card manipulation, incomplete analysis of the risks of financial activities of the bank, business reputation breach and erroneous recruitment. Therefore, only banks that are capable of detecting and correcting errors in a timely manner can maintain effective functioning and provide financial stability at the highest level.

Ensuring financial stability is carried out through its sound management. The mechanism of financial stability management of commercial banks can be defined as a set of methods and tools used by the management and aimed at ensuring financial stability of banks.

Distinguished are such methods of managing financial stability of commercial banks as [1, p. 52]:

1. Planning - setting goals, defining tactics and strategy to achieve the main goal (ensuring financial stability of the bank). Here it is worthwhile to direct financial planning to transform the strategic goal into specific (absolute and relative) values of financial indicators through the use of appropriate tools.

2. Analysis of the main elements that determine a stable financial condition. It allows the identification of causal relationships between different aspects of the activities of the bank.

3. The evaluation and regulation of financial stability of commercial banks carried out with the help of a set of techniques and methodologies.

4. The control implies the verification of the conformity of the results with the planned indicators, the optimal values of which contribute to the level of financial stability of the commercial bank.

In accordance with the Law, the National Bank of Ukraine promotes financial stability, including the stability of the banking system, provided that this does not hinder the achievement of price stability. Therefore, the National Bank pays close attention to the state

of the financial system as a whole, and analyzes and counters the risks that may affect its stability.

The National Bank of Ukraine promotes financial stability by:

- implementation of macroprudential analysis, macro stress testing of the banking system to identify systemic risks;
- development and implementation of macroprudential policy tools to prevent crises;
- participation in the preparation of legislation governing the banking sector;
- supporting the banking system as a lender of last resort;
- the control of the financial stability of individual banks, especially systemically important, including through stress testing;
- supervision over payment systems and billing systems;
- cooperation with other government bodies contributing to financial stability.

In domestic practice a system of economic standards for the analysis of financial stability of commercial banks is used. In order to maintain the stability of banking activities, the NBU approved the "Instruction on the Procedure for Regulating the Activities of Banks in Ukraine" which sets out the economic standards mandatory for all banking institutions, which makes it possible to fairly evaluate the financial condition of a bank.

The study of financial soundness of banking institutions takes perhaps the first place among the key issues that affect the development of the banking sector and the economy as a whole.

For the analysis of the stable state of banking institutions it is necessary to consider the indicators of economic standards as of 01.10.2016 - 01.10.2018 (Table 1).

From table 1 one can see that almost all standards are met in accordance with the requirements. Analyzing it, it can be seen that standards S7, S8, S9 and S12 are steadily falling. With regard to the S12, in 2017 it dropped by 0.32% and in 2018 - by 0.16%. This indicates that the investment activity of banks in recent years is deteriorating.

The short-term liquidity ratio is steadily growing - in 2017 it grew by 9.06% compared to 2016, and by 2018 it slightly decreased to 95.54%. So commercial banks in Ukraine have sufficient assets to meet their obligations for the period under investigation.

The level of regulatory capital of commercial banks in 2017 and 2018 has significantly decreased. Compared to 2016, its decline was 20.9% and 13.9% respectively. However, paying attention to 2018, one can see the positive trend of growth of regulatory capital level by almost 7% as compared with 2017, which is a direct proof of increasing the possibility of securing deposits and financial sustainability of banking activities.

By examining the economic standards of liquidity, namely S4 and S5, we see that they are developing unevenly. In particular, the rate of instantaneous liquidity in 2017 decreased by 6.18%, and in 2018 it has increased sharply by 16.79% indicating a positive tendency in maintaining the required volume of highly liquid assets of banks that ensure fulfillment of current liabilities within a day. The indicators of current liquidity point to another picture: for the period from 2016 to 2018, the standard grew by 15.81%. This testifies to the fact that during the period from 01.10.2016 to 01.10.2018 commercial banks adhered to the minimum volume of bank assets to ensure fulfillment of the current amount of liabilities within one calendar month.

With regard to credit risk standards, from 2016 to 2017, standards S7 and S8 decreased by 0.89% and 27.44% respectively. As of 2018, compared with the same period in 2017, they have also decreased. Thus, the norm of the maximum amount of credit risk per one counterparty decreased by 0.43%, and the norm of large credit risks - by 61.13%.

Consequently, in 2018, the credit risk of non-fulfillment by individual counterparties or a group of related counteragents of their obligations has increased.

*Table 1*

**Indicators of economic norms as of 01.10.2016 - 01.10.2018 years**

№ by order	Standard		Normative value	As of		
				01.10.16	01.10.17	01.10.18
1	S1	Regulatory capital (mln. Uah.)	Not less than 500	142 335,6	112 653,8	122 538,1
2	S2	Standard of sufficiency (adequacy) of regulatory capital	Not less than 10 %	14,22	15,27	15,73
3	S4	Standard of instant liquidity	Not less than 20 %	59,42	53,24	70,03
4	S5	Standard of current liquidity	Not less than 40 %	86,31	105,55	102,12
5	S6	Standard of short-term liquidity	Not less than 60 %	88,41	97,47	95,54
6	S7	Maximum credit risk standard per counterparty	Not more than 25 %	21,38	20,49	20,06
7	S8	Standard of large credit risks	Not more than 8 times the size of regulatory capital	260,85	233,41	172,28
8	S9	Standard of the maximum amount of credit risk in transactions with bank related persons	Not more than 25 %	28,19	19,94	12,04
9	S11	Standard of investing in securities separately for each institution	Not more than 15 %	0,002	0,000005	0,0002
10	S12	Standard of total sum of investment	Not more than 60 %	0,66	0,32	0,16

Source: [8]

Due to instability of the national currency, growing inflation and political instability, banks are forced to seek new opportunities for profitability, expanding the volume of banking operations and services.

At the present stage of development of the banking system, one of the most common problems associated with the impact of the financial crisis on the activities of banks, is to ensure the financial stability of banking institutions and the banking system as a whole and return it to the pre-crisis level.

Both qualitative and quantitative factors can affect the reduction of financial stability. The negative factors include:

- high credit risks due to the inefficient structure of the economy;
- dependence of banks on the financial condition of borrowers;

– the problem with the return of external borrowings, which had been actively made in previous years;

- problems of refinancing of banks;
- political interference in the banking system;
- lowering the quality of banking assets;
- loss of confidence on the part of depositors;
- decrease of liquidity;
- reduction of the resource base of banks;
- interest rate growth;
- high cost of financial intermediation;
- unresolved issues related to bank secrecy and customer protection.

The above mentioned factors define the tasks that need to be done to ensure a financially stable state of the bank:

- strengthening the stability of the banking system;
- strengthening the interaction of commercial banks with the real sector of the economy;
- raising the level of capitalization of the majority of banks;
- improvement of the quality of implementation of the functions of accumulation of savings of individuals and legal entities and their transformation into loans and investments by the banking sector;
- prevention of the use of the banking system in the shadow sectors of the economy to implement the objectives of unfair commercial policy.

#### **CONCLUSIONS AND PERSPECTIVES OF FURTHER RESEARCH.**

Thus, providing, supporting, analyzing and evaluating the financial stability of commercial banks are a driving force in the development of the banking system, and consequently the entire Ukrainian economy. Therefore, it requires comprehensive study and optimization of all possible methods for its evaluation and management and necessary support.

To accomplish these tasks, it is necessary to carry out such measures as:

- stabilization of the national currency by taking certain restrictive measures to increase the supply of foreign currency in the domestic currency market and to reduce demand for it;
- guaranteeing the preservation of deposits in banking institutions and provision of guarantees for inter-bank loans;
- control over the targeted use of refinancing loans;
- improvement of legal and regulatory framework for the activities of commercial banks through the introduction of amendments to the legislature in the part of systematization of mandatory economic standards, which will make it possible to increase the efficiency of banking regulation and supervision;
- introduction of tax incentives for banking activities.

#### **REFERENCES (TRANSLATED AND TRANSLITERATED)**

1. Dziubliuk O.V. (2009). *Finansova stiikist bankiv yak osnova efektyvnoho funktsionuvannia kredytnoi systemy*. Ternopil. [in Ukrainian].
2. Dovhal Yu. S. (2015). *Sutnist finansovoi stiikosti komertsiiinoho banku ta efektyvni shliakhy yii zabezpechennia*. Finansovyi prostir. (Vol.1). Retrieved October 10, 2018, from [http://nbuv.gov.ua/j-pdf/Fin\\_pr\\_2015\\_1\\_18.pdf](http://nbuv.gov.ua/j-pdf/Fin_pr_2015_1_18.pdf) [in Ukrainian].
3. Kovalenko V. V. & Garkusha Ju. A. (2017). *Zabezpechennja finansovoi' stijkosti bankiv: teoretychni ta praktychni aspekty*. LAP LAMBERT Academic Publishing. [in Ukrainian].
4. Kolodiziev O.M. (2010). *Zabezpechennia umov stabilnoho funktsionuvannia bankivskoho sektoru Ukrainy*. Kharkiv: KhNEU. [in Ukrainian].

5. Maiba V.V. (2011). *Otsiniuvannia faktoriv finansovoi stiikosti komertsiiynykh bankiv*. Kyiv: DVNZ Kyiv. nats. ekon. un-t im. V. Hetmana. Vol. 8, 49–65. [in Ukrainian].
6. Myhajljuk R. V. (2017) *Konceptual'ni zasady mehanizmu upravlinnja finansovoju stijkistju komercijnyh bankiv*. Svit finansiv. Vol. 3–4 (4–5), 21–32 [in Ukrainian].
7. Pogorelenko N. P. & Pylypchuk D. S. (2017) *Reguljarna dijaj'nist' Nacional'nogo banku Ukrai'ny dlja zabezpechennja finansovoi' stabil'nosti*. Uzhgorod. Gel'vetyka,. Vol.13(2), 87–91. [in Ukrainian].
8. Financial stability of the bank: official site of the National Bank of Ukraine. Retrieved October 3, 2018, from [http://www.bank.gov.ua/control/uk/publish/article?art\\_id=123698](http://www.bank.gov.ua/control/uk/publish/article?art_id=123698). [in Ukrainian].