18. Fiscal cost of state-owned banks in selected economies of Central and Eastern Europe

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The aim of this chapter is to determine the fiscal cost of state banks to selected economies in Central and Eastern Europe, as well as to examine some of the most fiscally draining banks in the process. For this purpose we examined state banks in 14 countries, ranging from countries on the verge of acceding to the European Union in 2004 (namely the Czech Republic, Hungary, Latvia, Lithuania, Poland, Slovak Republic, Slovenia) to countries that will not accede for many years (namely Albania, Bulgaria, Croatia, Macedonia, Romania, Turkey) or possibly at all (Ukraine). In addition, some data have been included on two CIS countries that have broadly resisted structural reforms to move banking to a more private sector-driven market (Turkmenistan, Uzbekistan), although specific information on their banks is not included.[2]

In the process, nearly 50 state banks were examined, of which 29 were reviewed in fairly thorough detail. These banks required significant amounts of Government assistance to restore them to financial, managerial and operational viability. Among the 29 banks, 10 received at least USD 1 billion in fiscal recapitalization, including five banks that received anywhere from USD 2.4 billion (Bancorex in Romania) to USD 15 billion (Ziraat in Turkey). Among the 29 banks reviewed, only eight received less than USD 250 million in direct fiscal recapitalization, with the lowest amount to date recorded being USD 100 million for Oschadny Bank in Ukraine.

This assistance has generally been provided in two forms: either in additional capital to restore solvency, or the removal of bad loans from troubled banks' balance sheets. In the first case, bad loans have remained on banks' balance sheets to be worked out over time, but also showing the earnings and capital effects of provisions and reserves. In the second case, bad assets have been transferred to a loan recovery institution or asset management company, and given incentives to recover bad debts that have been provisioned but not forgiven.[3] In most cases, the most significant and

successful restructurings took place in preparation for or at the time of privatization. Of the banks reviewed, most have been successfully privatized. However, there are still some large state banks to be privatized in countries like Poland, Romania,[4] Slovenia, Turkey and Ukraine.

Thirteen of the countries examined were former communist countries, with the only exception being Turkey. However, Turkey's direct fiscal costs related to state banks amounted to the greatest fiscal cost in dollar terms among the 14 countries. This indicates that systemic and structural problems associated with state ownership, connected lending, political patronage, subsidization, counter-productive forbearance, insufficient accountability and transparency, poor governance, and market volatility resulting from macroeconomic imbalances exist as risks and points of vulnerability for non-communist countries as well. It also points to the impediments in many 'capitalist' societies that fall short of fully functioning market economies that include sound macroeconomic fundamentals, prudential regulatory oversight, and risk-based management systems that are predicated on sound governance, systems and internal controls.

Based on various documents and reports – mainly from central banks and supervisory agencies, banks' own financial statements, multilateral institutions' documentation on costs and sales proceeds, and several articles and press releases detailing individual bank privatizations – the assessment has determined that the direct fiscal costs associated with state bank recapitalization have exceeded USD 50 billion. For the banks examined, the approximate gross fiscal cost is USD 53 billion. This does not include other state banks that may have been earlier recapitalized fiscally, and for which data have not been made available. Likewise, as this excludes several countries, mainly CIS countries apart from Ukraine, the figure may be higher for transition countries in general. For instance, Russia recapitalized state banks after the 1998 crisis, and such figures are not included.

Moreover, this figure does not include additional indirect or hidden costs, such as the cost of forbearance when exercised, losses run through non-bank creditors (such as utilities, power companies), higher interest rates on Government securities to generate income for troubled banks, or generally higher interest rates charged on loans to assist troubled banks with recapitalization from earnings. For instance, the direct fiscal cost of bank restructuring and recapitalization among the largest banks in the Czech Republic was about USD 10 billion, while the total cost of banking system restructuring efforts is reported to have approximated USD 18 billion.

Irrespective of the precise figure, the approximate USD 53 billion in direct fiscal costs is enormous by any standard, particularly when one takes account of the fiscal pressures on these economies, and the scarcity of public

resources available for investment in health, education, social services and infrastructure. As a percentage of GDP over the long span of 1991–2002, these costs routinely ranged from 1 to 2 per cent of annualized GDP for about half the countries, and 0.5–1.0 per cent for most of the other countries. Taking a tighter time span (that is, 1995–2002) raises these ratios, reflecting higher costs. With the fiscal and expenditure challenges faced by most transition economies, combined with the task of taming what were high inflation rates at the time, the economic cost of state bank recapitalization proved to be high in most cases.

Given that sales proceeds have generated less than 20 per cent of fiscal recapitalization costs, the overall proposition has been a net loser for virtually all countries. This is reinforced by the very small number of recapitalized banks that sold for more than recapitalization costs. Overall proceeds to governments have approximated USD 10 billion, about 19 per cent of gross fiscal costs of recapitalization. Thus, on a net basis, the 14 countries reviewed have experienced a net fiscal outflow of about USD 43 billion or about 1 per cent per year of GDP. Other costs (monetary, forbearance, and so on) suggest the overall burden has exceeded this figure.

The results need to account for concentration. Turkey's recapitalization of two large state banks accounts for about 44 per cent of the total. As the two banks – Ziraat and Halk – have not yet been sold, the ratios will change when transactions are eventually concluded. Smaller examples, such as Savings Bank in Albania, have also been offered for sale, although proceeds will not be generated until at least 2004. Slovenia's second largest bank – NK Maribor – has also been offered for sale, but like Savings Bank in Albania, the sale has yet to occur. In due time, these proceeds would change the ratios. For instance, it remains to be seen what will happen in Ukraine if it proceeds to offer Oschadny and/or Ukreximbank for sale. Smaller privatizations that will occur in Hungary are not expected to change the balance much.

At the same time, countries like Poland (as with Ukraine) still have comparatively large banks for sale. In the case of PKO BP, there are predictions that future recapitalization costs may approximate USD 1 billion. Likewise, BGZ, which has already been recapitalized with about USD 1 billion, has not been offered for sale. As Poland moves closer to EU accession, it is unclear how long these banks will be retained by the state, and what the net outcome will be. However, given the substantial anticipated recapitalization of PKO BP, Poland's experience with bank recapitalization is expected to be about breakeven when finally concluded. By comparison with the other countries, this is relatively sound performance. On the other hand, there are questions about the opportunity cost of having held on to such banks for so long, including whether retention by the state has also added

economic costs in the form of forbearance, delays in what is now a more robust housing finance market (PKO BP), and whether rural finance is as efficient as it could be if BGZ had been resolved more forthrightly.

The assessment evaluated other costs and trends. Key findings are outlined in the following sections.

1. GENERAL MACROECONOMIC TRENDS

The 14 selected economies (plus two CIS countries whose banks were not reviewed in any great detail) have shown improved financial discipline in recent years, particularly in the effort to reduce inflation rates. On the fiscal side, most countries are also showing reasonable levels of financial discipline. Fiscal deficits (as a share of GDP) have either declined or only modestly increased in 10 of 16 countries. Government expenditure (as a share of GDP) has generally decreased or slightly increased, with only three countries showing major increases exceeding 5 per cent. Government debt has increased, partly offsetting the generally tighter fiscal policy. However, even here, only four of 16 countries have shown Government debt to exceed 50 per cent of GDP in 2000–02. As inflation rates decline and stabilize, real GDP growth continues, fiscal bases expand and debt profiles remain stable, the transition economies will have scope for rising fiscal expenditure and borrowings.

2. THE ROLE OF STATE BANKS IN THE SELECTED ECONOMIES

State banks accounted for at least a sizeable share of assets (greater than 40 per cent), and in some cases the majority of banking system assets, in most countries until the late 1990s. Thus, dealing with state banks' costs and losses was more than a policy issue. In several countries, they remained prominent, with high levels of asset and/or deposit concentration.

3. GENERAL COST ESTIMATES OF TROUBLED BANKS

State banks have not been the only problem banks in transition country banking systems. In some cases, state banks have been relatively well managed, while many private banks have been thoroughly mismanaged. However, on the whole, state banks inherited past assets, organizational

structures and operating systems from the earlier socialist phase. Even after restructuring efforts (which have been applied to virtually all state banks at some point in one form or another), many have remained uncompetitive, sluggish, weak in terms of risk management, and costly in terms of head count and operations.

Non-performing loan (NPL) figures provide clear support for the benefits of rapid privatization in the banking sector, rather than spending significant time and resources to restructure troubled banks. Where there are low levels of state bank NPLs (as a share of total system capital), this is the result of relatively low levels of state bank ownership. There have been a few exceptions when corrective actions have been taken or reasonably sound governance, management, controls and systems have been in place. However, in most cases, state banks have had a tendency to run up non-performing loans, and be costly to restructure. Thus, in most cases, it appears that long restructuring periods have a tendency to run up fiscal and other costs on a net basis.

4. STATE BANKS' FISCAL COSTS RELATIVE TO TROUBLED ASSETS

Figures indicate that a complete clean-up of state banks' NPLs would have cost USD 61 billion from 1995 to 2001. Rough estimates of fiscal costs over the years have accounted for about 87 per cent of these banks' financial restructuring, often linked to a privatization objective, and sometimes to cover potential losses following a privatization transaction. However, as these apply only to NPLs, the figures do not account for other potential costs, such as (i) reversed income due to *ex post* provisioning for loan losses and reversals of income previously posted but not collected, as well as (ii) revalued assets such as securities and properties that may have been previously overvalued. Thus, estimates of fiscal costs likely account for less than 87 per cent of the total costs associated with state banks.

5. GROSS FISCAL COSTS OF STATE BANKS

Fiscal costs related to the recapitalization and financial restructuring of state banks in selected economies has approximated USD 53 billion in recent years. This has involved a combination of securities issued to recapitalize banks, the transfer of bad assets to asset recovery agencies, guarantees that have been called, and the issuance of guarantees for potential future loan losses following privatization transactions.

6. CONCENTRATION OF FISCAL COSTS

Based on these figures, Turkey has incurred the highest level of direct fiscal expenditure to recapitalize state banks. Turkey's fiscal costs approximate 44 per cent of the total fiscal cost of the 14 countries related to bank recapitalization and restructuring. The fact that it was not a socialist economy like the other countries evaluated also shows that non-socialist economies with high levels of state ownership in the banking system are vulnerable. The Czech Republic has also incurred high aggregate fiscal costs of about USD 10 billion, or about 19 per cent of total for the selected countries. Thus, when reviewing the selected countries, there is a high level of concentration of fiscal costs centred on Turkey and the Czech Republic.

7. DISTRIBUTION AND IMPACT OF COSTS

Relative to average GDP, gross fiscal costs of bank restructuring (prior to any sales proceeds) show a broad distribution of costs, rather than a high level of concentration by country. Of the 14 countries for which data are available, six countries had costs exceeding 10 per cent of average GDP. Most other countries are in the range of 4–9 per cent. Ukraine's figures are the lowest, at less than 0.2 per cent, followed by Poland at 2 per cent. However, these figures may not be entirely accurate. In the case of Ukraine, the Government has incurred more than 0.2 per cent in costs associated with Oschadny Bank, while in Poland the 2 per cent figure does not account for potential fiscal costs associated with the recapitalization of PKO BP (and possible future costs related to BGZ).

Extending the logic on an annualized basis (as these costs are usually not incurred in just one year), the same six countries with the highest gross fiscal costs relative to GDP also had the highest annualized fiscal costs. Each of the six countries incurred fiscal costs of 1–2 per cent of GDP per year on average from 1991 to 2002 as a result of their troubled state banks. In effect, these costs have served as a tax on national output and income.

Considering that most countries faced the above fiscal costs in more concentrated periods, adjusted fiscal impact figures when spread across an eight-year time horizon from 1995 to 2002 show that most countries' gross fiscal costs were higher when measured on a more concentrated time line (of eight years). In general, annualized gross fiscal costs relative to GDP showed a wide range, from as low as 0.03 per cent in Ukraine to as high as 2.26 per cent in the Czech Republic.

8. ESTIMATED NET FISCAL COSTS OF STATE BANKS

Some of the state banks have been restructured under sound management. This has resulted in these banks generating substantial proceeds to Governments upon sale. However, most state banks have generated less in sales proceeds than the funds/securities injected to recapitalize them and to finance their restructuring. Among the 50 banks reviewed (excluding separate asset recovery agencies), only a few have generated proceeds in excess of fiscal costs. Overall proceeds for state bank transactions have approximated USD 9.8 billion, which is only about 19 per cent of gross fiscal costs incurred. This raises the question of whether the recapitalization of state banks has been worth the cost and effort. While other factors enter into the discussion, it is clear that governments should generally not expect to make a profit from the transaction. More often than not, the cost of recapitalization and restructuring far exceeds the proceeds generated.

9. CONCENTRATION OF SALES PROCEEDS AFTER RECAPITALIZATION

There has been a concentration of proceeds in a few countries. Of the approximately USD 9.8 billion generated in the countries reviewed, Poland, the Czech Republic, the Slovak Republic, Hungary and Bulgaria have accounted for most of the proceeds. These five countries have accounted for about 89 per cent of sales proceeds.

10. DISTRIBUTION AND IMPACT OF COSTS AFTER BANK SALES

Net fiscal costs have been in the billions in about half of the selected countries. Given the variation in size of national economies, even smaller amounts often led to higher costs relative to GDP. On the whole, among the 14 countries for which data have been made available, four countries' net fiscal costs approximated or exceeded 10 per cent of average GDP (that is the Czech Republic, Albania, Turkey and Croatia). In the cases of Albania and Turkey, these ratios may ultimately come down after the sale of Savings Bank in Albania and Ziraat and Halk in Turkey. However, as of 2003, these sales had not been achieved, thus the cost ratios stand above 10 per cent. Delays in privatization also raise the risk of additional fiscal costs. Thus, the final net fiscal cost ratio is currently unpredictable.

In the cases of the Czech Republic and Croatia where bank privatization is pretty well finalized, the figures reflect a fairly costly approach to bank restructuring.

At the low end, Ukraine has injected very little in the way of fiscal resources into its two state banks. However, as mentioned elsewhere, Oschadny has particularly benefited from other forms of state assistance. Thus, while not explicitly fiscal, the low ratio of 0.19 per cent probably understates the actual fiscal cost to the Government of Ukraine. In the case of Poland, its success in generating proceeds in excess of fiscal costs is unique, and partly reflects its successful bank privatization programme in the late 1990s (and into 2000). However, the figures do not include anticipated recapitalization costs associated with PKO BP which would bring the ratio closer to zero per cent. It also does not include borrowing costs associated with the restructuring of many of the state banks.

When annualizing the fiscal cost figures, three countries (that is the Czech Republic, Albania and Turkey) show they have incurred an annual average cost of more than 1 per cent of GDP from 1991 to 2002. As noted above, Albania and Turkey may see a change in these ratios when they conclude their bank privatization programmes. Nonetheless, these three countries have incurred the highest fiscal costs. The Slovak Republic is interesting in this regard, as it pursued a similar approach to that of the Czech Republic, yet shows costs just barely more than half the costs incurred by the Czech Republic on an average annualized basis relative to GDP.

As with gross fiscal costs, figures show that net fiscal costs were higher when measured on a more concentrated time line (of eight years). In general, net fiscal costs on an average annualized basis were about 0.5–1.5 per cent of GDP in the selected economies (for which data are available) from 1995 to 2002.

11. INEFFECTIVENESS OF RECOVERY AFTER TRANSFER

Countries that have transferred bad assets to workout agencies have also shown very low recoveries. In Albania, BART has only recovered USD 8 million, or about 3–4 per cent of assets transferred. The Czech and Slovak Republic have received about 5 per cent of the face value of securitized bad assets when taken to market. Turto in Lithuania has recovered about USD 80 million, equivalent to about 10 per cent of bad assets transferred. Thus, efforts to restructure and recover bad assets have generally proven ineffective, and worth little more than a small fraction of the face value of the bad assets.

12. STATE BANK FISCAL COSTS RELATIVE TO FISCAL DEFICITS

The gross and net fiscal costs of state bank recapitalization relative to the general fiscal position of selected governments have varied country by country. From 1991 to 2002, the data show that gross and net fiscal costs were lower as a share of fiscal deficits in almost all of the countries than when they are consolidated from 1995 to 2002. The only exceptions in this regard were Albania and Slovenia. Notwithstanding gradually increasing fiscal rectitude in most transition countries in the latter part of the 1990s and early 2000s (relative to GDP), the higher average deficits suggest that bank recapitalization costs contributed to these deficits. Early denial or non-recognition of problems in the state banks, and the costs associated with resolving these problems eventually culminated in many countries during this more consolidated period, adding to the impact of the cost.

Given the varied time lines of when governments intervened to recapitalize their state banks, there is no set pattern to when direct fiscal costs of state bank recapitalization most severely affected fiscal deficits. However, there is recognition that perpetual non-performance added to these costs, thereby deepening fiscal deficits. At the same time, as countries first stabilized their monetary policies and then began gradually to shrink their fiscal deficits, as occurred by the mid- to late-1990s, the actual costs of bank recapitalization had greater impact due to the hardened budget constraints imposed as a function of macroeconomic and fiscal stabilization.

Meanwhile, the period in which the impact was more direct occurred from 1995 to 2002. On an average annualized basis, gross fiscal costs have been particularly high as a share of 1995–2002 fiscal deficits in Bulgaria, the Czech Republic, Macedonia and Slovenia, exceeding 50 per cent in all these countries. In fact, in Bulgaria, the ratio was nearly 100 per cent, reflecting both the high cost of state bank restructuring in that country along with the fiscal discipline introduced from 1997 following the crisis. Costly programmes also existed in Croatia, Lithuania, Romania and the Slovak Republic, all with costs ranging from 26 to 45 per cent of average annualized fiscal deficits during the same period.

On a net fiscal basis, the Czech Republic has incurred the highest costs, at 51 per cent, followed by Bulgaria at 47 per cent. The difference between gross and net costs for Bulgaria, albeit high in both cases, is that bank privatization generated higher proceeds relative to fiscal deficits than in the Czech Republic. Other countries whose net fiscal costs of state bank restructuring and recapitalization exceeded 25 per cent of average fiscal deficits included Slovenia (33 per cent), Croatia (29 per cent), and Romania and Slovakia (28 per cent).

Interestingly, Turkey's fiscal costs have been fairly moderate despite being the largest to date in recapitalization costs. This is partly due to the substantially larger fiscal deficit that Turkey averaged from 1995 to 2002, one of the many areas that are being brought under tighter control as Turkey stabilizes its economy. In the coming years, the net fiscal ratio may decline if Turkey generates proceeds from state bank sales.

On the other side of the spectrum, Poland actually shows a net surplus of funds. However, this does not take into account the costs associated with ultimately stabilizing or resolving PKO BP. Likewise, other costs to the economy and system (in the form of forbearance) are not captured by these direct fiscal costs. This is likely to be relevant as well for Ukraine, which shows low direct fiscal costs, but whose forbearance, blanket deposit guarantee and other kinds of support for Oschadny are not captured in the fiscal cost data. Hungary also shows a relatively low fiscal cost after the early efforts in 1991–94 to recapitalize state banks. Recognizing the costs associated with the effort, Hungary moved to privatization after 1995, and its fiscal costs ended up being relatively low as a result.

13. STATE BANK FISCAL COSTS RELATIVE TO GOVERNMENT DEBT

Relative to Government debt, gross fiscal costs annualized on an average basis from 1995 to 2002 were highest in the Czech Republic, at more than 14 per cent. This stands out as far higher than all other countries evaluated. As an example, the Slovak Republic's gross fiscal costs were about 5.5 per cent of Government debt on an annualized basis. Several other countries have been in the 3–4 per cent range, including Croatia, Latvia, Lithuania, Romania, Slovenia and Turkey. Countries whose gross fiscal costs have been less than 3 per cent of Government debt include Albania, Bulgaria, Hungary, Poland and Ukraine.

On a net fiscal cost basis after sales proceeds, the Czech Republic still stands out. Notwithstanding some very large sales in recent years, net fiscal costs over the period were still more than 11 per cent of Government debt. Highest after that was Romania at 3.6 per cent, whose net fiscal costs were less than one-third of the Czech Republic's when compared as a share of Government debt. The ratios are fairly similar for Turkey, the Slovak Republic and Lithuania as well. No other countries have had net fiscal costs exceed 2.6 per cent shares of Government debt, and several have been at less than 1 per cent.

Turkey is currently carrying a high debt load, although its debt per capita ratio is far less than that of Hungary and Poland. Ultimately, its 3.5 per cent

fiscal cost to Government debt ratio appears to be consistent with practice in Latvia, Lithuania and Romania, and with the Slovak Republic on a net fiscal basis. These countries have all generally stabilized their financial systems and successfully privatized their banks (at least partly in Romania), suggesting that Turkey's ratios are not inconsistent with fiscal cost and debt parameters for effective financial sector turnaround. It remains to be seen what proceeds Turkey will be able to generate when it finally privatizes its remaining state banks.

14. STATE BANK FISCAL COSTS RELATIVE TO BANK CAPITAL

The varied fiscal costs of state bank recapitalization also reflected differently on banking system capital in the selected economies. Annual averages of state bank NPLs ranged from as low as USD 1–4 million in Macedonia and Latvia, respectively, to as high as USD 2408 million in Poland. Several countries have had severe problems with their state bank NPLs, and many of these countries also had undercapitalized banking systems resulting from non-performing loans, other bad/overvalued assets, and large proportions of non-earning assets. In most cases, this has culminated in fairly high fiscal costs to recapitalize banks.

Gross fiscal costs relative to average bank capital have been extraordinarily high in Turkey, a country in the process of correcting its problems of banking sector undercapitalization throughout the 1990s. Such costs have also been very high in seven other countries – Albania, Bulgaria, Croatia, Czech Republic, Lithuania, Romania and Slovakia – all approximating or in excess of average bank capital, and in several cases at least twice the value of bank capital. This has led to significant fiscal costs, sometimes requiring long amortization periods for bonds that add interest expense to annual budgets for years. Spreading average annualized gross fiscal costs over an eight-year time span from 1995 to 2002, the costs relative to bank capital have been highest in Turkey, Romania, Lithuania, Albania and Bulgaria. All of these countries have either faced severe banking sector crises at one point since the mid-1990s and/or have taken long periods to bring bank privatization to a close.

Net fiscal costs follow a similar pattern, with the exception of Bulgaria and, to a lesser extent, Slovakia, where proceeds from bank privatization have been substantial relative to capital. Ratios in Romania and Turkey are expected to diminish in the coming years as these countries sell their state banks. Albania may also experience a change in its ratios, depending on what proceeds it generates from the sale of Savings Bank.

At the other end of the spectrum have been Poland, Ukraine and Slovenia. Poland has generated proceeds in excess of cost, reflecting a positive return. In Ukraine, other methods of support have been provided to Oschadny, but direct fiscal costs have not been high. As neither Oschadny nor Ukreximbank have been privatized, there are no proceeds to record. Slovenia's fiscal costs have been fairly high, with a deficit to date of about USD 900 million. However, Slovenia has also long had a well capitalized banking system relative to regional norms. Thus, fiscal costs (gross or net) relative to capital have not been high.

15. RECAPITALIZATION COSTS OF MAJOR STATE BANKS

In terms of absolute fiscal costs of recapitalization, the major banks in the selected countries were/have been Ziraat and Halk (Turkey), CSOB, Ceska Sporitelna and Komercni (Czech Republic), Bancorex (Romania), VUB (Slovak Republic), Privredna (Croatia), Magyar Hitel (Hungary), and BGZ (Poland). It is also estimated that PKO BP's recapitalization figures will equal or exceed USD 1 billion when that process is ultimately finished. Together, these 10 banks (excluding PKO BP) have accounted for more than USD 39 billion in recapitalization via fiscal means. Using a floor of USD 100 million, there have been at least 29 banks that have been fiscally recapitalized. However, the top 10 indicate that there has also been substantial concentration, with these banks accounting for 74 per cent of gross fiscal costs.

16. RETURN ON INVESTMENT

Troubled banks have generally sold for small fractions of their fiscal recapitalization costs. Only a total of USD 9.8 billion has been generated in sales proceeds against USD 52.7 billion in fiscal recapitalization costs. While a handful of banks have generated more than USD 500 million in proceeds, only five banks among those for which information has been made available – Komercni, Nova Ljubljanska, Slovenska Sporitelna, Bulbank and OTP – have been able to cover more than 50 per cent of their gross fiscal recapitalization costs. (Other banks have also generated comparable levels of proceeds and defrayed at least half and sometimes all recapitalization costs. For instance, this is also likely to be true of Wielkopolski, Handlowy and PKO SA in Poland. These banks generated USD 500 million, USD 1.0 billion and USD 1.1 billion, respectively, in

sales proceeds. However, recapitalization costs for these banks have not been made available on an individual basis.) On a net basis, only a few banks (for example, OTP of Hungary, Savings Bank of Lithuania, some of the Polish and Bulgarian banks) have generated more in proceeds than were invested by Government. Thus, apart from these examples, fiscal recapitalization has turned out to be a significant net loss for transition economies.

17. IMPACT OF RECAPITALIZATION COSTS ON GDP

Depending on the time line, the impact of gross and net fiscal costs has varied against average GDP figures. As a general rule, there have been about seven banks that have accounted for major fiscal costs when measured against average GDP. These banks include Ziraat (Turkey), CSOB (Czech Republic), Bancorex (Romania), VUB (Slovak Republic), Privredna (Croatia), Savings Bank (Albania), and Stopanska Bank (Macedonia). All of these banks' gross and net fiscal costs accounted for at least 5 per cent of GDP on average, and reached nearly 9 per cent in certain cases. Meanwhile, an additional eight banks accounted for 2.5 per cent to 5 per cent of average GDP on a gross (and often net) fiscal basis. Among this second group, only Komercni, Nova Ljubljanska, Slovenska Sporitelna and Bulbank were able to generate proceeds that markedly reduced the gross fiscal cost. Thus, only about half of the troubled banks accounted for less than 2.5 per cent of average GDP, and only four of the second group brought their net fiscal costs down to less than 2.5 per cent of average GDP. Thus, about half of these banks have served as major drains on GDP for sustained periods.

18. COMPARED WITH OTHER COUNTRIES . . .

Transition country banking systems are not the only ones to experience major crises and costs. Several advanced economies have experienced major crises, sometimes systemic, and other times not. The range of costs for recapitalization has varied from as low as an average 1.3 per cent in Norway from 1987 to 93 to 12 per cent of GDP in Japan in 1996 and 17 per cent of GNP in Spain from 1977 to 85.

Other countries around the globe have experienced systemic banking crises. Adding Turkey to the list (from its earlier crises in the 1980s), at least 70 other countries have also experienced systemic banking crises, with the costs often more severe than in the transition economies relative to GDP.

Moreover, many of the countries have had recurring crises (two or three times), suggesting that insufficient resolve during crises may serve as a harbinger of more severe crises to follow. In many cases, the recurring crises were more severe in cost than the earlier crises.

NOTES

1. Sector Manager for Finance and Private Sector Development for Europe and Central Asia, World Bank.
2. The full-length version of the paper can be downloaded from the World Bank's website.
3. There are costs and merits to both approaches. This chapter does not endorse specific methods or approaches, but simply seeks to demonstrate to the reader that both kinds of recapitalization and/or resolution are included in the cost estimates if these were based on fiscal means.
4. BCR was recently partly privatized, although a majority of the bank remains in state hands.