

# REGIONAL MARKETS

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## **DEVELOPMENT OF BANKING INSTITUTIONS IN THE TYUMEN REGION: CURRENT TRENDS AND PROBLEMS**

*SUMMARY. The banking institutions doing business in the Tyumen region work hard to be more customer-oriented, but they gradually lose control of the overall decision-making process and are viewed as an attractive acquisition target due to their lower risk profiles as compared to all the other banks in the Russian banking industry. The Russian regional banks are heavily involved in loan transactions to trading companies and service-dominated businesses. Loans to trading companies and service-dominated businesses represent a 56% part of their loan portfolios despite the fact that loans of this particular type are considered to be very risky and have the poorest collateral adequacy amongst the existing loan options. The overall investments made by regional banks in the industrial sector of the Russian economy are quite modest and the performance results of Tyumen-based banking institutions fully justify the trend in question. Due to a healthy spread between their loan and deposit rates commercial banks have a good income-generating power but at the same time they are not interested in making long-term investments in the real sector of the Russian economy. The growth rates for income-generating loans held by the Tyumen-based banking institutions are twice as high as their total asset growth rates.*

*KEY WORDS. Bank, development of banks, deposits, loan portfolio, gap, mergers and acquisitions, region, equity capital.*

As of September 1, 2013, the Tyumen regional banking services community, along with the Khanty-Mansi Autonomous Okrug and the Yamalo-Nenets Autonomous Okrug, includes 16 credit institutions and 46 branch offices operated by outside banks located in various regions of the Russian Federation. The Tyumen regional banking services community is reinforced by the presence of the West-Siberian Bank of the Savings Bank of Russia, which has a local network of 12

branch offices. Additionally, banking institutions headquartered in different parts of the Russian Federation have established 13 representative offices in the Tyumen Region [1]. The optimization of the regional branch network was initiated before the outbreak of the global financial crisis in 2008-2009. Some further steps towards the optimization of the regional banking sector were made in 2011-2013 as the local banks sought to transform their traditionally-run offices into remote sales channels (see Table 1 below).

*Table 1***Branch Network Operated by Banks in the Tyumen Region in 2011-2013 [1]**

Type of a banking institution	01.01.2011	01.01.2013	Increase (+)/decrease (-)
Additional offices	560	591	+131
Out-of-the-office cash counters	342	153	-189
Loan production offices and offices involved in cash and settlement services	53	85	+32
Operations offices	100	262	+162
Number of branches operated by local banks	61	38	-23
Number of branches operated by outside banks from other regions of the Russian Federation	72	60	-12
Total	1118	1289	+101

The local banks managed to cut their branches by one-third, while outside market participants had to close down every fifth branch office in the Tyumen Region. The Tyumen-based banks also made efforts to modify the number and composition of their internal structural units. The existing network of out-of-the-office cash counters showed a 2,3-fold decrease, while additional offices and operations offices, along with loan production offices and offices involved in cash and settlement services, experienced rapid growth. In 2012-2013, the number of banks and their branch offices doing business in the Tyumen region increased by 8,5%. As a result, the Tyumen-based banking institutions have become more customer-oriented, but they gradually lose control of the overall decision-making process. The decision-making in the regional banking market either exhibits clear signs of consolidation around a limited number of strong local players or is moved to some specific locations outside the Tyumen region.

To be successful in the market, any bank must have sufficient equity capital. The equity capital details for the local banking institutions are given in Table 2. It can be seen from Table 2 that only seven banks own an equity capital of over RUB 1 billion and, therefore, may be regarded as comparatively large banks in line with the requirements of the Russian banking system.

Table 2

**Size of Equity Capital and Major Shareholders of Regional Commercial Banks  
as of June 1, 2013 [1, 2, 6-9]**

Ranking No.	Name of the Bank	Equity Capital, in millions of RUB	Ranking No.	Name of the Bank	Equity Capital, in millions of RUB
1	OJSC "Bank of Khanty-Mansiysk"	35 535.9	9	OJSC "Akkobank"	451.6
2	OJSC "West-Siberian Commercial Bank"	9 425.7	10	CJSC Joint Stock Bank "Tyumenagroprombank"	439.1
3	CJSC "Surgutneftegasbank"	6 511.9	11	LLC Siberian Bank for Reconstruction and Development	336.1
4	OLSC Joint Stock Bank "Yugra"	2 492.4	12	CJSC Joint Stock Bank "Pripolyarny"	316.7
5	OJSC Commercial Bank "Stroilesbank"	1 163.8	13	OJSC Bank "Purpe"	246.9
6	OJSC "Sibbusinessbank"	1 132.0	14	OJSC Commercial Bank "Druzhba"	239.4
7	OJSC "Sibneftebank"	1 053.5	15	CJSC Joint Stock Bank "Priobye"	237.7
8	CJSC Nizhnevartovsk City Bank "Ermak"	767.7	16	OJSC "Surfut Central Commercial Bank"	216.4

The most influential banks are represented by the Bank of Khanty-Mansiysk, West-Siberian Commercial Bank and Surgutneftegasbank which control, in aggregate, a 8/10 share of the banking market belonging to local banking institutions. It must be emphasized that the Bank of Khanty-Mansiysk ranks comfortably among 30 top Russian banks.

It is obvious that the Tyumen regional banking services market is marked by numerous M&A transactions. Here are some examples to illustrate the above-mentioned developments. In 2012, Homos-Bank managed to purchase the Bank of Khanty-Mansiysk but this event did not make a strong impact on the local banking services market until now. The Bank of Khanty-Mansiysk holds a 10.45% stake in the Surgut-based Akkobank, but it does not have an opportunity to acquire the controlling interest because the Surgut municipal authorities, which possess a 61.49% stake in Akkobank, are not interested in the transaction. It can be added that Sibbusinessbank, which performs the bulk of its operations in Tyumen, has been purchased by a big Russian bank technically known as Expobank. So the local banks are gradually taken over by national banking giants through active M & A transactions in the Russian banking services market and it leads to what is technically termed as bank asset consolidation.

Traditionally, Russian regional banks work hard to strengthen their own resource bases. The budget funds are considered to be an important source of funds for the

banks to provide the needed operating wherewithal. In 2001, the total budget funds held by the Tyumen-based banking institutions amounted to RUB 6.1 billion. However, the year-end 2007 figure was quite disappointing for the local banks as balances in budget accounts maintained on their books fell dramatically to RUB 0.5 billion. As of April 1, 2013, balances in budget accounts maintained by budget organizations and institutions with the Tyumen-based banks declined to RUB 0.3 billion and came to account only for 0.4% of the total funds attracted by the Tyumen regional banking services community. It is interesting to note that the Tyumen regional budget for a three-year period 2013-2015 is expected to reach RUB 370 billion. In this context, the proposed liquidation of several settlement centers run by the Central Bank of Russia in the Tyumen region by 2015 is of a great benefit to the local commercial banks as they obtain an ample opportunity to dispose of the regional budget funds as an additional source to fund their active transactions.

In terms of importance personal deposit accounts outrank all other sources of funds because they constitute 56.8% to 59.1% of the total funds raised by the Tyumen regional banking services industry during the period of three previous years. In 2010-2013, personal customers from the Khanty-Mansi Autonomous Okrug – Yugra were treated as the most important customer group as they managed to provide the local banks with a steady inflow of funds at the level of 28.6% to 31.3% of the total attracted funds. The dynamics of fundraising operations performed by the Tyumen-based banks is given in Table 3 below.

Table 3

**Fundraising Transactions of the Tyumen Regional Banking Services Community in 2011-2013 (in millions of RUB) [3-5]**

Region	01.01.2011	01.01.2012	01.01.2013	01.04.2013
Tyumen region, total	516235	622713	719643	726104
Including:				
Khanty-Mansi Autonomous Okrug –Yugra	265080	302737	375713	392752
Yamalo-Nenets Autonomous Okrug	61459	70114	108608	109833
Southern Area of the Tyumen region	189696	249862	235322	223519

In 2012, RUB-denominated personal deposits and personal deposits denominated in foreign currencies dropped approximately by three percentage points in the south of the Tyumen region and the local banks failed to overcome this negative trend during the first half of the year 2013. The deposit base was down amid increased consumer lending and overall per capita income stagnation. It must be said that foreign currency deposits gradually lose their significance as a source of funds because their share in the total resource base of the Tyumen-based banks has shrunk from 14.9% at year-start 2011 to 12.5% in the first quarter of the year 2013.

With a share of nearly 28%, the local banks feel rather comfortably in the Tyumen regional banking market in terms of personal deposits, but the rival banks from Moscow and other regions of the Russian Federation take a lead in the market with a share of over 72%. It is not surprising that the West-Siberian Bank of the Savings Bank of Russia dominates the Tyumen regional market for personal deposits and controls a 27 % share in this segment of banking. On the other hand, many customers are not quite loyal to the West-Siberian Bank of the Savings Bank of Russia as they do not evaluate the bank's current product pricing strategy as fair and attractive. Under the existing circumstances, the local banks may expand customer bases of their own rather easily by getting customers away from the said banking giant.

The Tyumen-based banks have mobilized good corporate funds primarily from big businesses, including oil and gas companies. This achievement has enabled the participants of the Tyumen regional banking services market to obtain cheaper financial resources as many big businesses have a way to hold some of their funds on low-income accounts at local branch offices of the Russian national banks. In the period under review, the banks headquartered in the Tyumen region have successfully utilized the mobilized funds to finance a wide range of their active banking operations.

As of May 1, 2013, performing assets of the local banks stood at 83.8% versus the average result of 85.1% achieved by the Russian banking market. On the other hand, the Tyumen-based banks had a lower portion of interest-bearing liabilities of about 75% on their balance sheets compared to the average result of 80.5% across the Russian banking industry. The growth rates for income-generating loans held by the banking institutions in the Tyumen region were twice as high as their total asset growth rates. Due to a healthy spread of more than eight percentage points between their loan and deposit rates the local banks are in a very favorable position in the Russian banking market and have a significantly stronger income-generating capacity compared with any average bank in the Russian Federation.

One must keep it in mind that banking institutions doing business in the Tyumen region have a good consolidated loans-to-assets ratio of 72.2%, which is well in excess of the average loans-to-assets ratio of 70.7% across the Russian banking industry. However, both figures are not quite in line with an internationally accepted loans-to-assets ratio of 75%.

Table 4

**Loan Portfolio Held by Banking Institutions in the Tyumen Region Between 2011 and the First Quarter of 2013 in Dynamics (in millions of RUB) [2,10]**

Indicators	01.01.2012	01.01.2012	01.01.2013	Growth between 01.01.2012 and 01.04.2013
1	2	3	4	5
1. Total loan portfolio	592.3	757.2	796.9	+34.3%
1.1. including overdue and defaulted loans	10.9	14.9	17.4	+59.6%

1	2	3	4	5
2. Total loans granted to legal entities	291.3	345.5	369.9	+27%
2.1. including overdue and defaulted loans	6.9	10.5	12.5	81.2%
3. Total loans granted to private individuals	301.0	411.7	427.0	+41.9%
3.1. including overdue and defaulted loans	4.0	4.4	4.9	22.5%

In many situations the Russian regional banks cannot adequately meet the financial needs and wants of big corporate customers due to the lack of sufficient funds. Additionally, lots of small and medium-sized businesses which operate in the Tyumen region have limited access to the local loan market as they lack adequate collateral to fully repay the loan under the default scenario. Despite the existing challenges, the local banks have considerably expanded their loan portfolios. It can be seen from Table 4 that loans granted to private individuals dominate the loan portfolio held by the Tyumen regional banking community.

Although it is only natural to suppose that most loans must be made to companies heavily involved in oil and gas extraction projects in Russia's greatest oil and gas province, however, it can be clearly seen from Table 5 that the supposition is absolutely wrong. It appears that the local banks prefer to make loans to trading and service-dominated businesses despite the fact that loans of this particular type are considered to be very risky and have the poorest collateral adequacy amongst the existing loan options. It is common knowledge that companies involved in trade and service-dominated activities are usually characterized by the highest percentage of overdue and defaulted loans and the performance results of the Tyumen-based banking institutions fully justify the trend in question.

Table 5

**Composition of RUB-Denominated Loans Granted to Legal Entities and Private Entrepreneurs in 2011-2013 (in %) [1,3]**

Type of Economic Activity	01.01.2011	01.01.2012	01.01.2013
Trade and Services	58.4	56.2	59.2
Civil Engineering	17.3	18.4	15.4
Extraction of Natural Resources	6.9	7.4	7.9
Processing Sector	6.9	6.9	7.7
Transport and Telecommunications	7.1	6.7	5.5
Agriculture, Hunting and Forestry	1.4	1.1	1.4
Other Sectors	2.0	3.3	2.9
Total	100.0	100.0	100.0

The Tyumen region is one of the areas most attractive to investments, expert economists say. It must be noted that many investment and development projects are

currently in the process of implementation on the territory of the Tyumen region. The major investments are made in oil refining, machine-building, steel-making and agribusiness sectors of the Tyumen regional economy. The loan products intended to support some specific processing businesses are in the range of 6.9% - 7.7% of the total loan portfolio.

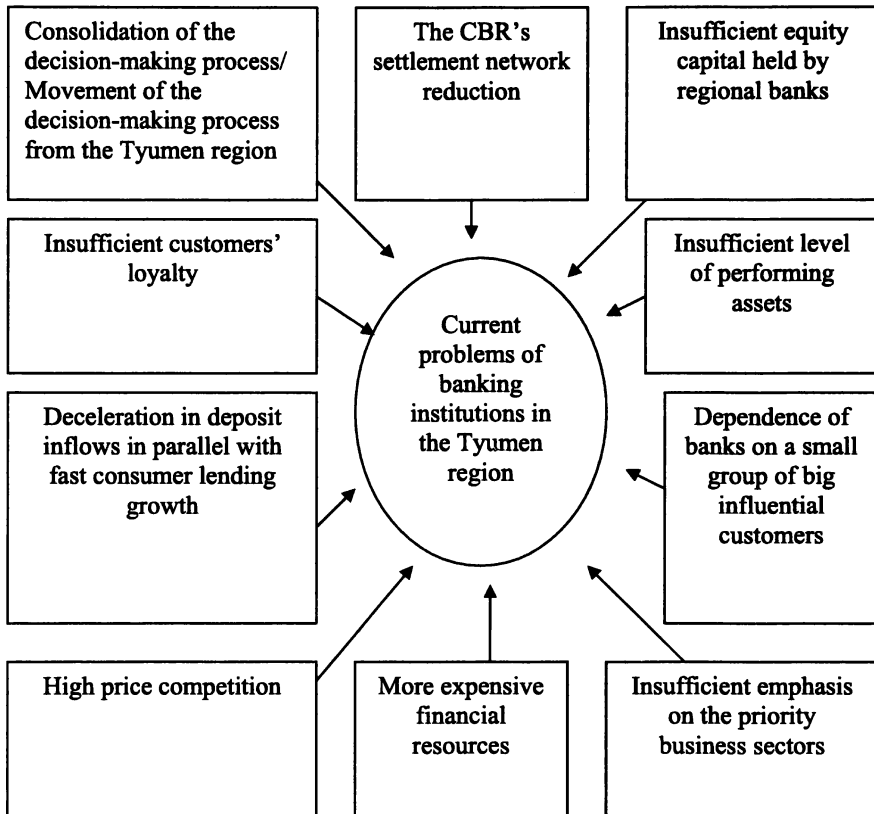


Figure 1. Development of Banking Institutions in the Tyumen Region: Current Problems

The strategic priority of the Tyumen regional authorities is the development of agricultural and forestry sectors of the local economy as well as the organization of new agribusinesses and wood-processing enterprises. These segments of the Tyumen regional economy are primarily financed by the Savings Bank of Russia and Rosselkhozbank followed by a regional banking giant known as OJSC West-Siberian Commercial Bank. The loans granted by the local banks to agribusinesses and hunting businesses as well as to firms involved in various wood-processing activities account for 1.4% of their total loan portfolio.

It must be stressed that the total investments made by banking institutions from the Tyumen region in the production sector of the regional economy are quite modest. Although the oil and gas production is a key sector of the Tyumen regional economy,

local banks have allocated only a 6.9% to a 7.9% part of their loan portfolios to finance the implementation of the existing oil and gas projects. On the other hand, the consumer loan products offered by banks show good growth which is apparently linked with the rapid development of the credit card segment of the banking services market. As of January 1, 2013, the Tyumen region, along with the Khanty-Mansi Autonomous Okrug and the Yamalo-Nenets Autonomous Okrug, ranks No.2 in the Russian Federation in terms of mortgage and home construction loans which total RUB 163,6 billion. Many local banking institutions have developed special loan programs which enable their customers to purchase homes in various parts of the Russian Federation, particularly in the North-Western and European regions of the country.

It can be said in conclusion that the funds allocation policy pursued by the banks located in the Tyumen region appears to be inefficient in several respects. The policy under consideration is not fully in line with the real needs of the Tyumen regional economy. Loans that are made by local banking institutions must be allocated more proportionately between the business sectors and industries. The existing funds allocation scheme is designed by local banks to satisfy the financial needs of financially sound customers. The total funds invested in a local agricultural sector are insufficient and, therefore, cannot contribute to the fast development of agricultural enterprises in the years to come. Due to a healthy spread between their loan and deposit rates commercial banks have a good income-generating power, but at the same time they are not interested in making long-term investments in the industrial sector of the regional economy. The drawbacks and limitations described in this paper do not seem to be critical and the overall size of these drawbacks and limitations is significantly lower compared to many territories in the Russian Federation (see Figure 1).

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