EUROASIAN PERSPECTIVES OF THE BANKING SYSTEMS DEVELOPMENT

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INTRODUCTION

World financial crisis is a great challenge to the community, its ability to consolidate efforts of the representatives of different nations and resist destructive influence of crisis phenomena. International cooperation and knowledge as the result of cooperation are remedies for the crisis. Therefore the world scientific community should be in front of struggle with the crisis as science is the bearer of the community aspiration to new knowledge.

Starting from 2008 the world financial crisis struck the system of relations which developed between representatives of science and business, especially in developed countries of the world. Financing of many perspective scientific projects has got negative reflection as the result of worsening of the financial state of the majority of transnational corporations and banks. Leaders of international business, transnational banks “BNP Paribas”, “Bank of New York Mellon”, “Deutsche Bank”, “Lloyds Bank”, “Sumitomo Mitsui Banking Corp.” reduced financing of research and development projects in economics in 2009 by 2.3 billiard US dollars compared to 2007. This amount is equal to annual research and development budgets in economic sciences of 170 leading world universities. It should be predicted that in middle term perspective it will negatively influence the level of scientific research in leading countries of the world.

Evidently, in terms of reducing research financing by business structures, especially in developed countries, higher educational institutions of the developing countries are to unite their efforts and research potential, take the initiative and, the most important, responsibility for the further stable development of the science in global scale.

This aim was followed by the specialists from three higher educational institutions from Taiwan, Jordan, and Ukraine, namely Takming University of Science and Technology, The Arab Academy of Banking and Financial Studies and the Ukrainian Academy of Banking. It was the initiative proposal of the professionals from the Department of International Economics of the state higher educational institution “Ukrainian Academy of Banking of the National Bank of Ukraine” to their foreign colleagues that started international scientific cooperation, the result of which is the monograph “Euroasian Perspectives of the Banking Systems Development”. This monograph will improve the level of understanding of the reasons of causes of banking crisis by scientific as well as business communities of the world countries. Deductions and recommendations made in the book will be accepted with great interest by regulators of bank services market.

At least we, scientists from Ukraine, Taiwan and Jordan, hope for this.

Yours sincerely, the team of authors:

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Chapter 1

THE WORLD HISTORY OF ORIGIN AND DEVELOPMENT OF BANKING SYSTEMS

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CHAPTER 1. THE WORLD HISTORY OF ORIGIN AND DEVELOPMENT OF BANKING SYSTEMS

1.1. ORIGIN OF BANKING IN THE WORLD

Priority task of any state is ensuring stable economic development, effective functioning of elements of the state mechanism, combination of strategies of the national policy in different spheres of economic, political and social life. To guarantee macro-economic stability and development of economic relations it is essential to study and estimate the elements of banking system, monetary and credit policy in terms of interrelation and coordination between them as well as between them and the national policy.

Aspects of the world banking system's historical formation and development were researched by scientists from different countries, which allowed forming an essential theoretical and methodological basis of banking activity; but the questions about the time of origin of banks, awareness of their specific role in economies of different historical formations are still under discussion.

Study of peculiarities and analysis of factors of origin and formation of the first banks are directed mainly to research their practical function in building a national economy. During the states formation origin of banks was caused by economic needs, which started to appear together with the development of the economy, commodities – monetary and credit relations in different countries. These needs were the following: the need to securely retain personal savings (jewellery, money); desire to maximum simplify performance of different payment operations; necessity to have permanent standard of value for determining the prices of goods. Thus, the process of origin and evolution of banks was objectively stipulated by evolution of credit relations and became important stage of the society's economic progress.

Banks as institutions of the corresponding name firstly appeared in XII century and fulfilled different functions, serving not only consumer needs. Origin of a loan as a phenomenon of economic life of a community, on the basis of which banks appear, occurred long before Common Era.

Banking activities appeared at the period of slave-owning system. The centre of the birth of banking is considered to be the Babylon kingdom (VII-VI cent. BC), at the period of existence of which such Babylon bankers houses as Murashu, Igibi, Idin-Maduka operated. They gave loans under written obligations and on the security of different values, made payments for their clients, were guarantors in different deals, participated in trading on share basis, took deposits with charged interest.

Banking developed greatly in Ancient Greece. Temples and monasteries, the most famous of which were Delonian, Delphian, Ephenian fulfilled functions of saving money, providing loans, making transactions. Inviolability of values, which were secured in temple's treasuries by vendors and individuals, was guaranteed by honourable attitude to religion. Understanding that simple saving of great amounts of money in their treasuries is not profitable, *amphiktionites* who managed the temples, gave trusted values as loans at interest to citizens and even to the cities. Intensive development of the workmanship and trade in Ancient Greece promoted the growth of needs in exchange and credit operations and appearing individuals who made bank operations. As the result of using in trade different coins, which were minted by states as well as by cities and even by separate individuals, there were no common monetary system. There circulated coins of different shape, value and sometimes lower than their face value. Such diversity caused the need in new qualified specialists for money assessment and provision of business advice as to their exchange. During this period there appeared individuals – *trapezits* (from Turkish *trapeze* – a table) who exchanged cash at the tables in markets, gave loans on the security of land, slaves, buildings, movable property at 10 to 36 per cent per annum, entered data into the special register of the bank book. Roman bankers, who also had started their activity in money exchange, were called *mensaries* (from Latin *mensa* – a table).

Thus, as historians consider, the conception of a bank, which fixed on people's minds, corresponds to those individuals who made exchange operations with money at their special tables in Ancient Greece as well as in Ancient Rome.

In Ancient Rome banking reached higher level of record keeping than in Ancient Greece because of fixation of initial norms of bank and credit law, according to which during III century B.C. Roman bankers, who specialized in exchange business and were called *numularies,* had a permit for carrying out credit operation. *Arentaries,* who specialized in credit operation, according to the norms, had got an opportunity to give loans to their clients on the basis of mediation.

Together with credit operations of banks depositors' service had been gradually developing. These settlements were made with the help of "*transferit*", i.e. transferring money from one table (account0 onto another. Each depositor of the bank had their own document – a table with identification of their name. All payments for the client, who put money for depositing, were made by an experiences bank clerk, who had the deposit and the table with the client's name.

Gradually, together with formation of a common monetary system, money exchange operations were losing their significance. Banks started to fulfil the job in concluding deals between clients, getting inheritance, division of property, and also they were mediators in trade deals.

To facilitate calculations banknotes (*hudu)* were emitted. They circulated together with full value banknotes. At that period there were operations which could be characterised as a prototype of bill trading – using credit lists addressing to a bank for a payment.

Leading role of Rome as the centre of economic life of the great empire, which covered at that time big territories of Europe, Africa and Western Asia, promoted rapid development of banking, concentration of capitals of conquered countries in hands of bakers and provision of this money as loans to different regions. Significant amounts of money transactions promoted origin of affiliates of Roman bank houses in different countries.

1.2. EVOLUTION OF BANKING IN THE MIDDLE AGES

At the period of early Middle Ages, together with intensification of natural economy and corresponding elimination of the role of commodity and money relations, banking had temporarily declined. In feudal Europe diversity of banknotes in circulation retained development of trading which caused, as well as in antique times, realization of exchange operations. The highest level of expansion these operations in the X century had in Italy, which was the world trade centre where goods and money from different countries came to. In fact the word "bank" originates from Italian "*banco*" meaning "a table", at which doers of commodity and money operations were sitting. There was a register of settled deals and coins on the tables. So, exchange operations properly had become the basis for the development of banking activity in Medieval Europe.

Approximately in the XII century, evolution of fair trading resulted in the growth of monetary circulation in cities. Mostly metal money was used in international trade and was in hands of merchants who successfully traded with foreign countries.

During that period West-European citizens and feudal lords had a growing need in additional money and there was no enough existing means for covering the shortage of money. It is proper to say that evolution of crediting allowed covering the absence of cash. But as the result of increasing demand for cash, every owner of a sum of money aimed at the best usage of them to earn the highest surplus which led to the tendency of increasing interest rate. Thus, there appeared one more opportunity to get profit on very high interest rate – so called “usury”. Gradually there appeared the main circle of usurers’ clients among feudal lords. They hoped to repay the loan at the expense of a war or increasing taxes. One more reason which made merchants to become usurers was decrease of the trade profit and loss of interest in overseas trade because of development of local workmanship. It was foreseen that trading banknotes could guarantee to their possessors greater profit than trade operations (an award for provision of money loan reached 200% and more).

Such high percent of private proprietors-usurers was of the stimulating factors for creation of community banks.

Usury existed in terms of capitalist industry as well, especially in those countries where capitalist commodity relations are weakly developed, e.g. India, Pakistan, Indonesia. Usury as the form of providing small amounts of money on high-interest loans existed also in industrially developed countries, thou these operations were prohibited by law and were carried out, as a rule, illegally.

The first community bank appeared in 1171 in Venice. This institution corresponded to this type of bank only in its name, but its functions mostly targeted at promotion of functioning of Venice city economy.

Form the end of XII century banking expanded to other European countries, mostly to France, where it was started by citizens of Lombard cities.

The first medieval community banks were institutions, which took from clients for saving deposits in form of money by weight; took responsibility to make different payment transactions for their clients (transfer settlements between clients); carried out crediting of different enterprises, where sea foreign trade was in the greatest demand. At that period origination of draft activity began.

Growth of trade operations promoted the further development and concentration of banking operations, which was reflected in appearance of bank institutions, which had the features of joint-stock companies. In such a way in 1407 there was established the Bank of Saint Georg *(casa di S.Giorgio)* in Genoa, which was initially the association of the state creditors, and the rulers of the republic, when they took their positions, swore to keep inviolability of rights and wills of this institution. In 1408 the bank was allowed taking private deposits and a special conventional coin, as well as in Venice bank, was accepted as the basis for all settlements. Later the Bank of St. Georg lent great amounts of money to Genoa government. To cover their amounts it had got the right to rule colonies of Genoa (the island of Corsica and the city of Kaffa in particular) and take great taxes.

Gradually bank appeared in other cities, taking more complex organizational forms. In 1593 the Bank of Saint Ambrosius in Milan was created. Its capital was formed by share investments and current deposits of citizens and used for provision of loans to the city. In 1584 to make trade and industry more lively there was created a bank in Venice *(Banko delta Piaza deRialto)*, which was managed by officials appointed by the government. Soon low experienced officials had to be substituted with private bankers who pledged a great security to guarantee their operations. During some period of time the Venice Bank had monopoly and private individuals were prohibited to open bank offices and conduct any operations with money. The bank didn't pay interest on the deposits.

In 1619 one more community bank in Venice was founded. It was one of the first giro banks in Europe formed by merchant gilds to provide clearing between their clients. All settlements of both Venice banks were made with special "bank coin" – *dukati d'argento* – one of the best coins in circulation in Venice. In accordance with its value all money to come into a bank cash box was calculated. The value of this coin was 20% higher than the value of an ordinary coin in circulation in Venice. As the historians say, giro bank didn't always follow the rules of inviolability of deposits; sometimes the board of directors secretly gave essential amounts to Venice government, in the result of which they had to stop payments in coins twice, in 1640 and 1717.

The similar banks also appeared in Barcelona, Milan, Naples and some other European cities. A bit later several community banks appeared in the Netherlands, England and Germany. In Amsterdam the first bank was founded in 1609, in Hamburg – in 1619, in Nurnberg – in 1621, in Rotterdam – in 1635, in Stockholm – in 1657. The main term of credit operation of giro banks was to hold 100% security of clients' deposits in form of precious metals, and because of constantly unstable political situation and unsatisfactory conditions of money circulation in Europe they were of a limited type.

Initially the activity of giro banks was only limited by accepting deposits for saving, for what they charged a small money award. Individuals who opened deposits were given certificates, and for each of them a personal account in the bank's books was opened. Later those certificates turned into issued by bank banknotes payable to bearer. These were the bank's obligations to pay the bearer the stated in the banknote amount of money. Gradually banks deviated from the practice of saving deposits only but began to use them for bank operations, mostly for providing short-term loans. Thus, there was a principle change in banking: banks, which were simple savers of values, became mediators between individuals who possess free money, and individuals who need loans. Giro banks become deposit banks.

As the result of transformation, the situations was beneficial for depositors, who were released from charges for saving their deposits, as well as for a bank, which got profit from providing loans. Aiming at expansion of operations and profits, bank institutions meanwhile had started to artificially get deposits, making depositor to pay certain charge at the deposits and earning profit from the difference between interests taken for loans and those paid for deposits.

These innovations had very important consequences for the development of banking. They allowed banks to increase their working assets which had caused, from the one hand, a great impulse to credit development, and from the other hand – created opportunity for banks management abuse, which constantly led to banking crises.

It is important to think of the greatest bankers of the Middle Ages. Florence is the biggest centre of the Renaissance culture. The most famous banker of Florence was Medici. Giovanni Medici, called *di Vici*, was a smart politician, who organized the network of banks which founded financial basis for his family. Having broadened the field of activity of his bank to the whole Europe, by means of the network of trading offices Medici had become the most prominent person among new capitalists.

During Renaissance the most powerful bankers were also representatives of the Fuggers and the Rothschilds.

The first prototype of modern banks, a more perfect and full-bodied bank, which started carrying out credit and emission operations, was founded in England (the Bank of England) on 5 July 1694 on the basis of William Peterson's project. In accordance with its status the bank provided own capital – 120.000 pounds – as a loan for the state, instead of which it got the right to issue own banknotes for the corresponding sum aimed at fulfilling credit operations. The origin of this bank started e new era in the history of banking development. In XVII – at the beginning of XVII century there were created bank institutions, the most famous of which were the Austro-Hungarian Bank (founded in1703-1706), the German bank (founded on 11 June 1765), the French Bank (1776) and others.

So, at the end of the XVII century the world banking system was an expanded network of developed, multifunctional banks, activity of which was based on commercial principles and targeted at support and development of capitalist economy in leading countries. Functional load fulfilled by all financial institutions, was originated by the needs of trade and industry spheres of economies of these countries, according to their social and economic organization.

The most attention should be paid to The Bank of New-York, which was founded in 1791 almost simultaneously with creation of the New-York Stock Exchange. The Bank of New-York is considered by specialists to be the first corporate structure, which actively started involving financial assets at stock exchange with the help of emission of stocks for carrying out their own activity (Supplement 1).

This organizational form of business started to develop more quickly beginning from 1815, when banks started to specialize in investment activity. Banks bought big amounts of state or private securities in the process of emission and later sold them on the market.

From the moment of its foundation in 1792 The New-York Stock Exchange became the main place of selling securities, especially corporate ones, in the world. Till 1817, when the Stock Exchange got appropriated legal status, several hundreds of corporations in the sphere of bank activity had been created and The Stock Exchange draw attention of the market participants, which possessed financial assets.

At the first stage of the development of stock market the banks formation was connected with essential authorizing procedures and limitations of different type. Gradually till the middle of the XIX century in the USA there was formed legislation which essentially simplified the procedure of banks registration and at the beginning of the XX century a lot of restricting barrier were completely eliminated (supplement B).

Rapid development of finance market at the beginning of the XX century had sharply changed American banks. Possession of banks had become more splintered; the percentage of primary stock holders of most banks didn't exceed 10%. Till that time the class of professional managers had practically been formed and the change to bank managing on professional basis had been made. Managers competed for the right to manage banks not on the basis of the amount of their investment into the bank's capital, but on the basis of their experience, knowledge and skills.

Thus, by the beginning of the XX century (the 30s of the XX cent.) one of the main principles of bank management had been finally formed. It was the principle of division of ownership and control. Stockholders are the owners of the bank's capital, but the right of control and management of this capital belong to the management. Manager is an employed agent reporting to stockholders.

This principle allows combining proprietary approach, typical of management, and the means of financing business from different sources. Management, having necessary professional skills, knowledge and qualities, is able to take and fulfil decisions aimed at optimization of usage of capital. It fulfils a proprietary function. Owners don't need to have necessary professional skills and can't recon on effective usage of the capital under their own direct management. They just carry out the function of the capital suppliers and can recon on the part of the bank's profit accordance with their contribution.

At the beginning of the XX century the number of stockholders considerably increased. The greatest majority of them were small owners. Also the mechanisms of transmission of great amounts of investment resources had got their development on a global scale and transfer of property management to the hands of employed managers was made. A wide approval was given to the idea that banks have certain obligations not only to their owners but also to a wider circle of groups concerned, i.e. the idea of corporate social responsibility was developed, and provision of banks clients with corresponding rights became key question of bank business organization in the world.

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