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A STUDY ON THE FEES AND COMMISSIONS BURDEN ON THE SMALL SAVERS OF THE BULGARIAN BANKING SECTOR IN 2019

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Abstract: *Amidst the legislative push towards unifying and lowering banking service fees and commissions in order to make them more available to a larger public, the following paper explores the profitability of savings, deposit and payment accounts within the Bulgarian banking sector in 2019 from the lense of the small, retail customer, offering a new approach towards the calculation of the burden of operational taxes. The main thesis of the paper stipulates that with interest rates and operational fees on banking services as they are, savings accounts can be a significant drain on the finances of the average household in terms of income and savings potential. Since, traditionally, the Bulgarian banking sector dominates over the capital markets, from the standpoint of the average Bulgarian household the lossess incurred from using a payment or savings account can be compensated by owning deposit assets, but, as it turns out - only if said assets are above a significant threshold. An attempt was made to calculate the aforementioned threshold by using empirical data.*

Keywords: *Bulgarian banking sector 2019, banking service operational fees, banking fee burden*

INTRODUCTION

In accordance with EU legislature, in 2016 the Bulgarian National Bank started to extend its regulatory oversight over the size of fees and commissions that the banking system charged its retail customers. The regulation was aimed at gradually reducing and equilizing the charges for using a basic payment account for everyday needs across all banks. The new regulatory practices, instated within the BNB statutes (BNB Ordinance №3*)* have been active for close to 2 years now, but their effects are yet hard to measure, since the data concerning the average size of fees and commissions for banking services is published yearly and its official publishing has just started in 2019.

We noted in a previous study that "for the current year of 2016 the Bulgarian monetary sector registers unconventional changes in the structure of its income and expenditures. The current dynamic is becoming a cause of disquietude in small depositors and concerns for the primary functions of the banking sector are raised among the general public" (Stanev, 2016). The current state of the Bulgarian banking sector has not changed much in the past few years: super-liquidity has accompanied it for the period of 2016-2019, forcing both credit and deposit interest rates lower and lower. Following that development, deposit and savings account profitability has plummeted, reaching close to zero percent returns. Stimulated by low interest rates, credit activity among households has almost recovered to its pre-crisis levels, with mortgages in particular systemically surpassing their 2007 volume during 2018-19. As forecasted by our previous study, the deposits generated by households within the banking system have been steadily increasing for the past year by 8.2% in terms of volume, but the number of deposits have been on the decline (by -1.5%)[5] – which is a reflection of the continuing trend of having less, but larger deposits overall.

In terms of income structure, the banking sector has retained the tendency for a faster growth rate of income generated through fees and commissions that equals 6.93% (August, 2018-August, 2019) as opposed to a slower rate of increase of the income generated by credit interest (close to 1.67% for the same period). At the end of August, 2019 approximately 26% of the net total operational

[5] BNB, Monetary Statistics

income of the banking sector has its origins in service fees and commissions and that number has been on a steady increase – for comparison, the average number for 2016 was around 21-22%.

All of these observations constitute signals that the fundamental function of the banking sector as a relay of surplus capital between savers and borrowers is lacking at the moment due to excess liquidity, leaving the small savers with limited choices concerning their excess capital. This problem is exasperated due to the underdeveloped capital markets in Bulgaria, which are rarely used as a valid alternative by the general population. In these conditions – especially keeping the close-to-zero returns on savings and deposit accounts in mind - it becomes apparent that banking service fees have become a sort of a "tax for money-keeping".

In this paper we will attempt to formulate a methodology for calculating the burden of said fees for a set period of time and provide empirical examples by using current tariff and interest rate data from the three largest Bulgarian banks and the sector on average.

EXPOSITION

The thesis of this paper is that interest rates and fees on savings and deposit accounts as they are in 2019 are pushing the small saver away from the banking system, with savings accounts becoming obsolete as a long-term savings alternative because of a high fee burden.

The goals of this paper are as follows:

- formulate a methodology for calculating the burden of banking fees on different account holders;
- provide example calculations using said methodology with example data from selected banks for 2019;
- approximate the capability for compensating the burden of owning a payment or savings account through the interest generated by a separate deposit account with example data from 2019;

Banks offer a wide variety of savings instruments, but the classification of basic accounts has remained relatively constant across the sector. The three main types of accounts currently offered to the retail customer are: payment account, savings account, deposit accounts. Every other savings instrument that is more complex in nature is a derivative or some combination of the three types, offering promotional rates or fees, or is targeted at a particular population segment. For the needs of this study, we have chosen to focus on the three most basic types and not on any promotional equivalents or more complex products. Deposit accounts are pre-fixed in their time period and withdrawal results in loss of the accumulated interest, while payment and savings accounts allow the withdrawing and depositing of money and are unlimited in time.

A standard holding period of 12 months for deposit accounts has been chosen for the needs of this paper. Savings accounts are treated as having to be created, used once per month for a savings injection in the account (assumed based on the Bulgarian wage payment periodicity practices, which are mostly on a monthly basis) and, ultimately, closed at a certain point in the future. The same assumption is applied to payment accounts with the addition of one withdrawal at a cash desk per month.

Calculating the simple fee burden (FB)

We are going to demonstrate the methodology using data for the average fees for banking services for 30.09.2019 (BNB, 2019). Provided that opening and closing account fees are one-off charges, and upkeep costs are accrued on a month-by-month basis, keeping in mind the assumption of monthly injections and withdrawals, then we can constitute a simple model for yearly calculation (formula 1, table 1).

Table 1 Payment account average fees and fee burden for the first year (Source: BNB, author's calculations)

	Payment acc	
Variable	Service Fee	Average Banking Sector Fee Amount
z	Account Opening Fee	1.84
x	Monthly Upkeep Fee	2.14
k	Monthly Installment of Savings*	0
v	Account Closing fee**	0
w	Withdrawal***	1.37
FB	Fee Burden	43.96
t	#years	1
Avg Account Yield (%)	0%	

*** an assumed injection of savings into the account following monthly wage payment, made by the account owner with size <3889 BGN; larger injections will incur additional fees;**

**** at time of closing.**

*****assumed once per month withdrawal by the account owner with a size of 1000 BGN or less**

$$FB_{PAcc} = (z + v) + t(12x + 12k + 12w) \quad (1)$$

The data on the average fees that the banking sector applies towards its retail customers that open and use a payment account shows that two of the used variables' amounts are zero (with no tendency of increasing because of the new regulations), meaning banks offer said service free of charge, which simplifies the calculation even further. The services which require no fee are – account closing and depositing money into the account. Assuming the level of charges for banking services remains constant, the prognosis for the accumulated average fee burden (in BGN) of a payment account is provided below:

year	1	2	3	4	5
FB (PAcc, Avg)	43.96	86.08	128.2	170.32	212.44

Example calculations of the fee burden of a **savings account** in the 3 largest Bulgarian banks can be found in table 2. By the very purpose of a savings account (a long-term open deposit that allows the owner to withdraw or deposit money within certain constraints without losing the agreed upon interest) we will omit the withdrawal monthly component from the formula, modifying it to:

$$FB = (z + v) + t(12x + 12k) \quad (2)$$

Table 2 Savings account fee burden for the first year calculated with tariff data from the 3 largest Bulgarian banks (sources: Unicredit, DSK and UBB bank tariff data from their respective websites, provided in References)

	Savings Account			
Variable	Service Fee	UNC	DSK	UBB
z	Account Opening Fee	2.5	2	2
x	Monthly Upkeep Fee	2	2.5	2.5
k	Monthly Installment of Savings*	0	0	0
v	Account Closing fee	0	0	0
FB	Fee Burden	26.5	32	32
t	#years	1	1	1
y	Yearly Interest Rate (%)	0.01	0	0.04

As is evident from table 2, the simple fee burden largely outweights any profitability that the interest rate can offer at the current time. This problem comes to light clearly if one considers the average Bulgarian household income and Bulgarian household saving rate, which come at 13450 BGN yearly and approximately 5.071% for 2018 (NSI, 2019 and author's calculations). Provided the levels of fees remain constant the following scenario will unfold in the next 5 years (in BGN):

year	1	2	3	4	5
FB (SAcc, UNC)	26.5	50	74.5	98.5	122.5
FB (SAcc, DSK)	32	62	92	122	152
FB (SAcc, UBB)	32	62	92	122	152

When looking at the third account type - **deposits,** banks are keeping fees connected to opening, closing and upkeeping a deposit account at zero, therefore a calculation of the burden would not be appropriate. Since the yields of payment accounts have dropped to 0% interest rate across the sector, and savings account interest rates, although variable from bank to bank, still incline towards zero, it is certain that these instruments cannot sustain their own fees and commissions and are a net drain on their owners. On the other hand deposits still hold some merit in terms of profitability, albeit their returns have crumbled in the past few years too. Considering that most people who own a deposit account usually also possess a payment account, a valid question arises – can the returns on a separate deposit account compensate the basic fee burden of a payment account, and, if yes – then what is the necessary amount of money to keep in deposit in order to compensate the fees on a payment account. For the calculation we're going to use a 12-month period deposit and for the interest rate – an averaged deposit interest rate of 0.053% (based on the rates of the three example banks). The iterations are performed through Excel Solver with the following logic:

deposit balance*average interest rate < = fee burden on a payment account

The results for a full compensation of the fee burden through interest rate gains on a deposit show that for the first year a person owning both types of accounts must have at least 82943.40 BGN in a 12-month deposit which should just be sufficient to cover the expenses of the yearly existence of his payment account.

Constraints

The constraints of this study are as follows:

- only the 3 largest (in terms of assets) Bulgarian banks have been selected for the example calculations. The small sample might not be representative of the average fee burden of savings accounts across the whole banking sector. A wider study is needed;
- the income for savers has not been adjusted for inflation;
- households of more than 1 person usually have more than one payment/savings account – a wider study might correct this ommittance;
- the formula for calculating the banking fee burden is simplified and could be expanded to further include other standard services (for example – fees on payments of communal services, debit card, withdrawal from an ATM, etc.). Also, the formula must be adjusted if used to calculate FB with changes in fee levels over time.

CONCLUSION

In 2019 the small savers in Bulgaria are overburdened with fees and commissions coupled with zero interest rates, but are yet to react with a strong monetary retraction. Banks have continued to supplement their sluggish profit growth with the expansion of their product assortment and coverage, but mainly - through additional fees and charges for services performed as evidenced by their rate of growth of earnings from fees and commissions. If the trend continues as it is, newer alternatives for small-time, household investing are sure to gain more traction (e.g. peer-to-peer lending platforms) at the expense of the banking sector. As a recommendation, the Central bank should strive to encourage banks to segregate services and provide lower fees on those which can be self-performed after being digitalized (online banking transfers, communal service payments, etc.) in order to alleviate the overall burden of fees and charges on the retail customers and strengthen the processes of financial digitalization.

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