



ALLIED IRISH BANKS IN POLAND

INTERNATIONAL EXPANSION AT AIB

Since its establishment, the AIB Group has been ambitious to grow in international banking, both for its customers and its shareholders. This ambition has not only seen the group appreciably expand its operations and services in Ireland, but also move to establish significant operations in international markets. This expansion strategy is driven by key objectives and motivations that are common to many firms that seek to expand in international markets, including:

- ▶ **Profit and growth goals:** AIB was already the leading player in the domestic Irish market but competition in the market was increasing and opportunities for significantly growing revenue were reducing. Therefore it was necessary for AIB to consider achieving external growth in international markets.
- ▶ **Managerial ambitions:** The management of the Group considered that it had developed key strengths and capabilities that could be exploited in new markets. It had also gathered important information on international markets that indicated opportunities for growth potential for the group.
- ▶ **Opportunities to exploit existing skills in new markets:** Operating in the Irish market, AIB developed important strengths in key areas including management, information technology, customer service and risk management. These capabilities could be transferred and exploited in other markets.
- ▶ **Industry trends and risk management:** The European banking sector had become very competitive with significant cross-border activity in the form of mergers and acquisitions. It was considered a requirement for banks to spread their risks across several markets.

A STRATEGY OF GEOGRAPHIC DIVERSIFICATION

The emergence of AIB Group as an international bank has been carefully planned and developed over each decade of the organisation's existence. In the 1970's AIB created its branch network in the UK. In the 1980s, AIB first established its interests in the USA. In the 1990s AIB turned its attention towards eastern and central Europe when it invested in two major Polish banking operations. Over the decades, AIB has become an increasingly international organisation with significant investments abroad, mainly in the United Kingdom and the United States. Its strategy over the last 20 years or so has been one of steady diversification in key geographic and financial services markets. This process commenced in Britain through organic growth and continued in the United States with the acquisitions of First Maryland Bancorp in 1983, York Bank and Trust Company in 1991, and Dauphin Deposit Corporation in 1997. With the acquisition of First Washington Bancorp the operations have also expanded into Washington D.C. In 1999 the various American acquisitions came together under the new, single corporate identity Allfirst. In April 2003 AIB Group merged Allfirst and M&T Bank Corporation to create a strong mid-Atlantic banking franchise with over 700 branches. The merged entity would result in AIB Group becoming part of one of the top twenty largest US Banking companies.

RATIONALE FOR ENTERING THE POLISH MARKET

Buoyed by the success of the group's entry into the UK and US markets, management at AIB considered it important to continue the international expansion strategy and turned its attention towards **emerging markets** in developing countries. The former Soviet block countries of Central and Eastern Europe held particular appeal.

In the late 1980s, a number of AIB managers were charged with undertaking consultancy projects for the World Bank in the newly opened economies of Central and Eastern Europe, and in particular Poland, Hungary and the Czech Republic. These managers reported market opportunities in these countries to AIB Head Office. While positive and negative findings were presented, the Polish market was singled out to be the most attractive opportunity. Benefits of entering the Polish market included:

- ▶ A domestic market of 39 million people – Poland is the most populous former Communist, non-Soviet country.
- ▶ A developing middle class/affluent segment of the population.
- ▶ Estimated small and medium sized enterprise segment of 650,000 companies.
- ▶ Political stability and projected EU accession in May 2004.
- ▶ The Polish economy performance for better than most of its former communist peers in the post-Cold war era.
- ▶ A strong educational support system including strong academic centres in key cities.
- ▶ Significant investment by other international companies into Poland.
- ▶ A fast developing communication network supporting the latest technology advances.
- ▶ Low banking penetration among the general public.

AIB also found parallels between Poland in the late 1990s and Ireland 25 years earlier; with government trying to attract foreign direct investment, alleviate the impact of closing traditional heavy industries and encourage the growth and internationalisation of small and medium sized enterprises.

ABOUT AIB

Allied Irish Banks was formed in 1966 bringing together three distinctive Irish banking traditions. The Provincial Bank, founded in 1825, pioneered branch banking in Ireland, the Royal Bank, established eleven years later, was famous for its mercantile links. The Munster and Leinster, formed in 1885, with the most extensive branch network was the largest of the three banks.

Three decades since its formation, AIB is dynamic and successful and is Ireland's leading banking and financial services organisation, with total assets of over €76 billion, up from €323 million in 1966. It has also established significant investments in Britain, Poland and the USA, and it employs more than 25,000 people worldwide in over 800 offices.



THE POLISH BANKING SECTOR

As Poland's first non-communist government since the end of World War II assumed power in September 1989, the economy was in serious difficulty. At that time all banking in the country was controlled by the government through the National Bank of Poland which comprised a central bank and nine regional banks. In order to facilitate investment in Poland and its various industries the government moved to encourage the entry of foreign banks and privately owned banks to increase competition. Initially this change in policy saw Polish banks enter twinning arrangements with Western banks under the supervision of the European Bank for Reconstruction and Development. The purpose of this practice was to twin companies in East and Central European countries with a Western partner in order to teach them in free market business practices. The twinning arrangements were later expanded to allow foreign companies to invest in Polish companies. In the banking sector this led to an influx of foreign banks to the market, including AIB. The impact of these foreign banks has generally been regarded as positive. As well as bringing significant capital inflow into the Polish banking system, competition provided by the growing number of foreign banks helped to stimulate a wider range and better quality of banking services. These foreign banks have brought modern technology and management techniques which have enhanced the quality and sophistication of the financial services offered to the public.

ENTERING THE POLISH MARKET

In 1993 the World Bank in conjunction with the European Bank for Reconstruction and Development provided AIB with a further opportunity to examine the Polish market when they asked them to twin with a Polish bank. As mentioned above, twinning practices were commonly used to match western organisations with post-communist Central and East European organisations in order to facilitate the transfer of western and commercial business practices. AIB had already analysed the Polish market and chose to be twinned with Wielkopolski Bank Kredytowy (WBK), formerly based in Poznan. This twinning led to AIB buying a 16% share of WBK in 1995 for €18 million. It was the first capital investment of AIB in Central and Eastern Europe. By May 1997, AIB had increased its shareholding to 60%.



In June 1999, AIB further expanded its banking interests in Poland when it reached an agreement with the Polish State Treasury to buy an 80% shareholding in Wroclaw based Bank Zachodni S.A. At the time of the merger, Tom Mulcahy, then AIB Group Chief Executive Officer noted:

"This acquisition represents a major step forward for AIB in Poland, allowing us to address a 6% share of the Polish financial services market and bringing us important regional market concentration. Our strategic shareholdings provide us with a significant presence in two of the strongest economic regions in Poland, at a time when Poland is experiencing solid economic growth."

In 2001 Bank Zachodni S.A. was merged with WBK, with the new entity called Bank Zachodni WBK or BZ WBK. Commenting on the merger the President of Bank Zachodni WBK, Jacek Ksen, said:

"The merger of WBK and Bank Zachodni will create Poland's 5th largest bank with a very strong business base in the West of Poland. We believe that Bank Zachodni WBK has excellent prospects for growth and we plan to exploit this by the dynamic expansion and development of our branch and electronic networks in all attractive markets. This development will benefit customers, shareholders and staff by providing better coverage, enhancing earnings and synergy benefits and improved career prospects in a stronger more competitive environment."

Year	Key Event
1990/91	AIB International Consultants commence operations in Central Europe.
1992/97	AIB International Consultants "twinning" with Wielkopolski Bank Kredytowy (WBK).
1994	AIB explores investment potential in Central Europe – Poland selected.
1994	AIB takes an initial shareholding in WBK.
1996	AIB increases shareholding in WBK to 60.1%.
1999	AIB purchase 80% of Bank Zachodni.
2001	WBK and Bank Zachodni merge.
2001	Bank Zachodni WBK floated on Polish stock market.

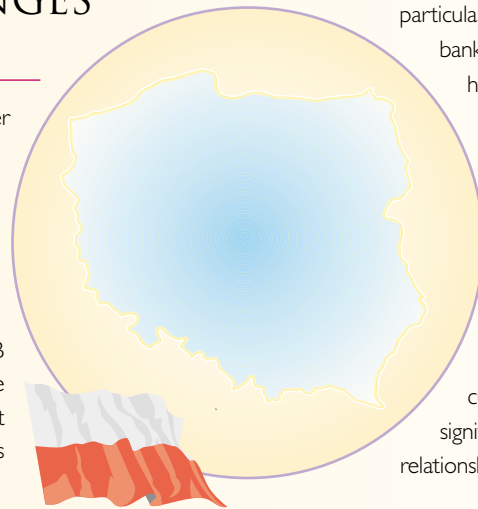
INTERNATIONAL MARKETS – FACING THE CHALLENGES OF MARKET ENTRY

Despite these supporting factors, the decision to enter the Polish market was not straightforward and a number of challenges and issues concerned AIB executives at the outset. A major issue to be addressed in the decision to expand into Poland, and Eastern Europe generally, was whether AIB would be able to successfully apply western management practices in a former communist country. Initially AIB management found the Polish banking system to be more bureaucratic than expected. This has required significant investment of money and managerial time with a focus on developing people.

There were also cultural challenges to deal with. Michael Buckley, current AIB Group CEO, explained that from the group's perspective, language and cultural issues were major challenges for AIB:

"Language in Poland is a major problem. A different language means different concepts, different ways of thinking and different ways of reaching consensus and communicating decisions."

There was a general lack of experience among staff in modern banking practices. On the positive side, AIB found that staff were generally well-educated individuals, ambitious and willing to learn. Importantly, AIB found an emerging generation eager to face challenges.



AIB AND BANK ZACHODNI WBK: A PARTNERSHIP FORMULA

AIB's investment in the Polish banking sector is based on a close partnership formula between Irish and Polish management. While retaining close control of their Polish operations, most of the management team are Polish. AIB has 3 members of the 10 on the supervisory board of Bank Zachodni WBK and 5 members of the 15 on the management board. The President of Bank Zachodni WBK, Jacek Ksen, is also Polish. Retaining local management is considered important as more likely to achieve a better understanding of the market. It is also reassuring for employees and the government. AIB also chose not to put its name on its Polish investments. This decision is based on its "local branding, local profile" approach.

AIB has invested in people working in the group's Polish operations. This includes skilled personnel being seconded to Poland and Polish management secondees to Ireland. On an on-going basis there is an average of 30 AIB staff working with executives of Bank Zachodni WBK. There has also been support for educational programmes both in Poland and abroad. Key objectives for AIB include transferring important competencies across a number of important areas including information technology, customer service improvement initiatives, product development, project management and risk management to its Polish operations.

Information technology is a key part of modern banking. This is particularly the case as a result of the success of internet banking in modern economies. Outside of Poland, AIB has excelled in this important area and is also investing heavily in information technology in its Polish operations. This investment will enhance significantly the services available to customers. AIB is also co-ordinating activities between Bank Zachodni WBK and its operations in Ireland, Great Britain and the USA for the purposes of managing key global accounts and international financial services required by Bank Zachodni WBK customers. In total, it is expected that there will be significant benefits for Bank Zachodni WBK in its relationship with AIB.

AIB'S FUTURE IN POLAND

AIB's commitment to Poland is unquestioned. Indeed by the end of 2000, AIB was the 12th largest foreign investor in Poland and the leading Irish investor. Independent economists believe that the banking system in Poland has room for further growth. For instance, by 2000 only 1.5% of Poles had a mortgage and 2% had credit cards.

To capture the projected growth in the market as it develops it is expected that AIB will seek to become more competitive by improving the financial services it offers potential customers and reducing its overall costs of doing business.

GLOSSARY OF TERMS

Capital inflow – This is the movement of money into a particular country.

Emerging Markets – The term 'emerging market' was originally coined to describe a fairly narrow list of middle-to-higher income economies among the developing countries, with stock markets in which foreigners could buy securities. The term's meaning has since been expanded to include more or less all developing countries.

EU accession – EU accession countries are countries that are due to become members of the European Union subject to meeting certain conditions.

Merger – This is the combining together of two or more firms into a single business on a basis that it is mutually agreed by the firms' managements and approved by their shareholders. It is an important form of external growth and market entry for firms.

Privatisation – The transfer of ownership of an industry or firm from the State or Government ownership to private ownership.

Synergy – Where the overall return on a firm's resources is greater than the sum of the parts. In the case of a merger this occurs where there is savings or improved performance by the two enterprises as a result of co-ordination of the merged firms activities and transfer of competences between the merged firms.

TASKS & ACTIVITIES

- 1) Outline the internal and external triggers for the expansion of AIB Group into the Polish banking market.
- 2) Prepare a PEST Assessment of the Polish banking industry. This analysis should consider the following items;
 1. Political and legal Issues faced by AIB when entering the Polish market.
 2. Economic issues considered by AIB when entering the Polish market.
 3. Social and Cultural issues.
 4. Technological issues.
- 3) List 4 reasons for expanding into an international market.
- 4) Why is it important for a company to diversify its operations across different geographical markets?



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