

## **Banking capitalization strategy and its impact on enhancing its digital transformations**

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**Abstract.** The study addressed the issue of the banking capitalization strategy with its indicators (retained profits, issuance of new shares, and reserves) and its impact on enhancing its digital transformations with its indicators (the electronic clearing system and the gross real-time settlement system). The study sought to identify the nature of the banking capitalization strategy and provide a theoretical and philosophical framework based on intellectual qualification. And make a modest contribution regarding the variables and dimensions of the study. The study sample was chosen at the Central Bank of Iraq due to the major role it plays in the country's economy, and through the financial reports published on the official website of the Central Bank for the period from (2011-2022). The researcher also used a set of statistical methods (SPSSV25, Excel V). 10, Eviews v.12) in order to process data and information. The study also tested a set of main and sub-hypotheses regarding the influence relationships between the variables of the study.

**Keywords.** Banking capitalization strategy, digital transformations, Central Bank

### **1. Introduction:**

Recent work and new developments on the scene necessitate new strategies to recognize what exists in other countries. Rasma has developed one of the most important of these strategies, whereby it resorts to increasing the capabilities of its funds through the process, part of its permissions and reserves, by strengthening its financial position, and keeping pace with the new number of available businesses and the diversification of its capabilities in developing and assets. In addition to strengthening their competitive positions vis-à-vis international banks, on the one hand, and on the other hand, increasing the banks' capital will give them a greater ability to grant credit to their customers, especially in light of the critical circumstances that the global economy is going through, especially the financial sector after the global crisis that occurred in the United States of America. It extended to countries around the world at different times.

The late twentieth century and the beginning of the twenty-first century witnessed great progress in information technology in various aspects of life, including the noticeable digital transformations in banking and the use of new technology, until users became in dire need of it due to the qualitative and scientific leaps the world has achieved at various levels, and the customer is now looking for what It is more modern in providing services, and as a result of the

rapid development in the field of digital technology, which has cast its shadow on all fields and banks in particular, life today, especially in developed countries, has become closely linked to the banking world and therefore it has become called citizenship banking.

Under the current circumstances, the Central Bank of Iraq faces great challenges, the most important of which is a severe weakness in the size of its capital, compared to international standards for determining capital adequacy, such as the Basel standard, as well as the type and quality of services it provides compared to international banks.

The problem with the Central Bank of Iraq is that it directs the majority of its efforts towards maintaining a narrow profit margin. Because it lacks the necessary resources to face the challenges of globalization, the main problem is usually attributed to the small size of capital and its failure to keep pace with new developments, and thus its failure to address the main obstacles.

Analyzing data on the Iraqi banks, sample of the study, using statistical methods to determine the strategic option among the available alternatives (capitalization, digital transformation). Thus Contributing to providing a theoretical framework for modern approaches to increasing capital and improving digital banking services. Moreover, providing an analytical description of the Iraqi banks sampled in the study to help identify the current problems facing banking activity and develop appropriate solutions to them.

## **2. Literature review**

### **2.1. The concept of capitalization strategy:**

First, we explain the concept of strategy in its general form :

A series of actions and decisions that lead to improving effective strategies in order to achieve the organization's goals (Casey& Goldman, 2010) . Accordingly, a set of concepts addressed by a number of writers and researchers regarding the concept of banking capitalization strategy can be clarified : A set of equations that study the relationship between capital and the returns achieved from it, as it measures the efficiency of the financing structure in the bank and is morally linked to an increase in the return on assets, and this is a positive thing (Van Horne & Wachowicz,2008).

The direct path, which is characterized by ease and simplification when viewed as a financing policy, as this method guarantees expected returns to the investor, and these returns are usually achieved after a period of time has passed to demonstrate the impact on achieving profitability and reducing the costs of financing and increasing the capital of joint-stock companies.( Todora,2011)

The strategy that aims to reduce external borrowing costs, and is strongly linked to the policies of changing capital in banks, which is one of the methods relied upon to expand their activities and finance their assets (Schuneman.2015)

### **2.2. Bank capitalization strategy indicators:**

The three indicators of bank capitalization that were chosen as variables for the study can be summarized through the following explanation (the report of the central bank of Iraq 2010):

#### **Retained earnings:**

Some departments use the method of detaining a percentage of the achieved profits, which represents part of the achieved distributable surplus, and adding it to a separate account called reserves.

**Increasing capital through issuing new shares:**

This method consists of issuing new shares to be subscribed by old shareholders or offering them to new shareholders to subscribe for them. This method enables banks to obtain new financial resources, and this strategy or method is one of the financial policies called external financing.

Reserves are amounts deducted from current accounts, for example, by the bank over the years from its profits achieved during this period to enhance the strength of the bank's financial position so that it has the ability to confront emergency events related to the bank or the economic situation in general to implement a specific policy, that is, The bank wants to reserve a certain amount for this purpose for expansion. Reserves are considered a strong guarantee for creditors of all types.

**2.3. Digital transformation:**

At the beginning, we must explain what digital transformation is, how to use Internet technology for banking operations, and how this technology had a very important impact on the rapid transformation in providing banking services from their old traditional state to what science has reached in providing them in their current form. Digital transformation is a related phenomenon. With technological development, and with the increasing interest in the necessity of applying it in banking systems to keep pace with technological developments occurring at the world level, and from here a group of questions have emerged stating that digital transformation is a truly new phenomenon worthy of application or is it merely an attractive concept that is used to demonstrate the change processes used by banks? Organizations rely on technologies (Wessel et al, 2021)

Based on the above, a group of concepts addressed by a number of researchers and writers regarding the concept of digital transformation can be clarified:

A complex part that an organization addresses in order to maintain its competitive position in the digital world. ( Svahn et al, 2017)

The process of organization and radical change that takes place by reinventing the organization itself, its methods of operation and other sources, and then the change is made by the organization and its relationship with other parties such as customers, employees, and suppliers. (Bauernhajas, Goerzing, 2018)

A process supported by digital technologies that brings about changes in organizations and has a tremendous impact on organizational assessment through the Internet of Things and data analysis (Feroz et al, 2021).

**2.4. The importance of digital transformation:**

High productivity is achieved when what is required is achieved in a short period of time by accessing all work effectively and quickly. The importance of digital transformation is working at one level of speed, and for a long period of time. Therefore, digital transformation has contributed positively and directly to organizing time through the programs prepared for it. For which it exists, many countries, especially the developed ones, have worked to activate this service in all sectors, Digital transformation is also important in modern developments in production and distribution, with knowledge of digital channels for customers, good customer experience, and flexibility in customer offers, as it enables the customer to obtain a place in the industry. ( Nicoletti ,2017)

### **2.5. Objectives of digital transformation of banking operations:**

Digital transformation has the benefit of providing information and services, providing advanced transactions for commercial and industrial businesses, and allowing individuals to do their work themselves by providing all information. Digital transformation has included many goals that are fundamentally transformed through companies and organizations enhancing the value in digital thought, creative innovations, and offering services. And products in an easier, faster and more modern way using innovative technologies, taking into account the requirements of society and the behaviors of the organization ( Berghaus, 2018).

**2.6. Indicators of digital transformation of electronic banking operations:** (Mohammad et al., 2014) , (Premchand & Choudhry, 2015) , (Asmah And Others ,2018).

#### **Electronic clearing:**

Electronic or automated clearing, which is a financial settlement network based in the United States of America and which was established through the “National Electronic Clearing Union” in 1974. The widespread use of bank checks in daily life leads to the development of electronic clearing systems in banks.

#### **Real-time gross settlement system:**

The gross settlement system is a mechanism through which payment orders of high value can receive final processing and settlement.

#### **Electronic Payment:**

At present, the Internet has turned into an essential factor in the financial and paper economy According to this development, the global trading system for trading coins and paper currencies has changed to electronic finance, which is considered the fastest and most reliable.

### **3. Results and Discussions**

Testing and analyzing correlations between the study variables:

The third main hypothesis: There is no statistically significant correlation between banking capitalization strategy and digital transformation. Sixteen sub-hypotheses branch out from this hypothesis:

□ The first sub-hypothesis: There is no statistically significant correlation between the retained earnings strategy and the gross instant settlement system in dinars.

From the Table below it is clear that there is no correlation between the retained earnings strategy and the gross instant settlement system in dinars. The correlation coefficient reached (0.405) at the level of significance (Sig. = 0.191). The level of significance was very small and cannot be relied upon to reject the null hypothesis. Therefore, the decision is not to reject the null hypothesis, meaning that there is no correlation between the retained earnings strategy and the gross instant settlement system in dinars.

Table.1 correlation coefficients between study variables

<b>Electronic instrument clearing system in dollars Y4</b>	<b>dinar electronic instrument clearing system Y3</b>	<b>Gross real-time settlement system in USD Y2</b>	<b>Total real-time settlement system in dinar Y1</b>	<b>Study variables</b>	
<b>0.111-</b>	<b>0.243</b>	<b>0.128-</b>	<b>0.405</b>	<b>Pearson</b>	<b>Retained Earnings Strategy X1</b>
<b>0.731</b>	<b>0.447</b>	<b>0.691</b>	<b>0.191</b>	<b>Sig.<sup>1</sup> (2-tailed)</b>	
<b>0.236</b>	<b>**0.817</b>	<b>0.456</b>	<b><sup>2**</sup>0.743</b>	<b>Pearson</b>	<b>common stock issuance strategy X2</b>
<b>0.459</b>	<b>0.001</b>	<b>0.136</b>	<b>0.006</b>	<b>Sig. (2-tailed)</b>	
<b>0.309</b>	<b>**0.805</b>	<b>0.500</b>	<b><sup>3*</sup>0.644</b>	<b>Pearson</b>	<b>Reserves strategy x3</b>
<b>0.329</b>	<b>0.002</b>	<b>0.098</b>	<b>0.024</b>	<b>Sig. (2-tailed)</b>	
<b>0.215</b>	<b>**0.751</b>	<b>0.216</b>	<b>**0.730</b>	<b>Pearson</b>	<b>Capitalization ratio x4</b>
<b>0.501</b>	<b>0.005</b>	<b>0.500</b>	<b>0.007</b>	<b>Sig. (2-tailed)</b>	

□ The second sub-hypothesis: - There is no statistically significant correlation between the strategy of issuing new shares and the gross instant settlement system in dinars.

We notice from the Table that there is a direct correlation between the common stock issuance strategy and the total real-time settlement system in dinars. The correlation coefficient reached (0.743\*\*) at the level of significance (Sig. = 0.006). Therefore, we reject the null hypothesis which states that there is no correlation. Between the strategy of issuing common shares and the total real-time settlement system in dinars. This indicates the existence of a correlation between the strategy of issuing common shares and the total real-time settlement system in dinars.

□ The third sub-hypothesis: - There is no statistically significant correlation between the reserves strategy and the gross instant settlement system in dinars.

It is clear from the Table that there is a direct correlation between the strategy of increasing capital through reserves and the gross instant settlement system in dinars. The correlation coefficient reached (0.644\*) at the level of significance (Sig. = 0.024). Accordingly, we reject the null hypothesis which states that there is no A correlation between the reserves strategy and the gross real-time settlement system in the dinar, which indicates the existence of a correlation between the reserves strategy and the gross real-time settlement system in the dinar.

<sup>1</sup> Sig .Moral level.

<sup>2</sup> \*\* The correlation is significant at one level) 0.01 2-tailed.(

<sup>3</sup> \* The correlation is significant at one level) 0.05 2-tailed.(

□ The fourth sub-hypothesis: - There is no statistically significant correlation between the capitalization ratio and the gross instant settlement system in dinars.

Through the Table it is clear that there is a direct correlation between the capitalization ratio and the gross instant settlement system in dinars. The correlation coefficient reached (0.730\*\*) at the level of significance (Sig. = 0.007). Therefore, we reject the null hypothesis which states that there is no correlation between The capitalization ratio and the gross real-time settlement system in dinars. This indicates the existence of a correlation between the capitalization ratio and the gross real-time settlement system in dinars.

□ The fifth sub-hypothesis: - There is no statistically significant correlation between the retained earnings strategy and the gross instant settlement system in dollars.

When looking at the Table, we see that there is no correlation between the retained earnings strategy and the gross instant settlement system in dollars. The correlation coefficient reached (-0.128) at the level of significance (Sig. = 0.691). The level of significance was very small and cannot be relied upon to reject the hypothesis. The null hypothesis, therefore, the decision is not to reject the null hypothesis, that is, there is no correlation between the retained earnings strategy and the gross instant settlement system in dollars.

□ The sixth sub-hypothesis: - There is no statistically significant correlation between the strategy of issuing new shares and the gross instant settlement system in dollars.

By looking at the Table, we see that there is no correlation between the common stock issuance strategy and the gross instant settlement system in dollars. The correlation coefficient reached (0.456) at the level of significance (Sig. = 0.136). The level of significance was very small and cannot be relied upon to reject The null hypothesis, and therefore the decision is not to reject the null hypothesis, that is, the absence of a correlation between the common stock issuance strategy and the gross instant settlement system in dollars.

□ The seventh sub-hypothesis: - There is no statistically significant correlation between the reserves strategy and the gross instant settlement system in dollars.

Through the Table it is clear that there is a direct correlation between the strategy of increasing capital through reserves and the gross instant settlement system in dollars. The correlation coefficient reached (0.500) at the level of significance (Sig. = 0.098). Therefore, we reject the null hypothesis which states that there is no relationship. A correlation between the reserves strategy and the gross real-time settlement system in dollars, which indicates the existence of a correlation between the reserves strategy and the gross real-time settlement system in dollars.

□ The eighth sub-hypothesis: - There is no statistically significant correlation between the capitalization ratio and the gross instant settlement system in dollars.

We see by looking at the Table that there is no correlation between the capitalization ratio and the gross instant settlement system in dollars. The correlation coefficient reached (0.216) at the level of significance (Sig. = 0.500). The level of significance was very small and cannot be relied upon to reject the null hypothesis. Therefore, the decision is not to reject the null hypothesis, meaning that there is no correlation between the capitalization ratio and the gross instant settlement system in dollars.

□ The ninth sub-hypothesis: - There is no statistically significant correlation between the retained earnings strategy and the dinar electronic instrument clearing system.

When you look at the Table, we notice that there is no correlation between the retained earnings strategy and the system of clearing electronic instruments in dinars. The correlation coefficient reached (0.243) at the level of significance (Sig. = 0.447). The level of significance was very small and cannot be relied upon to reject the null hypothesis, and therefore The

decision is not to reject the null hypothesis, meaning that there is no correlation between the retained earnings strategy and the electronic instrument clearing system in dinars.

□ The tenth sub-hypothesis: - There is no statistically significant correlation between the strategy of issuing ordinary shares and the electronic instrument clearing system in dinars.

It is clear from the Table that there is a direct correlation between the strategy of issuing ordinary shares and the system of clearing electronic instruments in dinars. The correlation coefficient reached (0.817\*\*) at the level of significance (Sig. = 0.001). Accordingly, we reject the null hypothesis which states that there is no correlation. Between the strategy of issuing ordinary shares and the system of clearing electronic instruments in the dinar, which indicates the existence of a correlation between the strategy of issuing ordinary shares and the system of clearing electronic instruments in the dinar.

□ The eleventh sub-hypothesis: - There is no statistically significant correlation between the reserves strategy and the dinar electronic instrument clearing system.

We notice from the Table that there is a direct correlation between the reserves strategy and the electronic instrument clearing system in dinars. The correlation coefficient reached (0.805\*\*) at the level of significance (Sig. = 0.002). Therefore, we reject the null hypothesis which states that there is no correlation between The reserves strategy and the electronic instrument clearing system in the dinar, which indicates that there is a correlation between the reserves strategy and the electronic instrument clearing system in the dinar.

□ The twelfth sub-hypothesis: - There is no statistically significant correlation between the capitalization ratio and the electronic instrument clearing system in dinars.

When looking at the Table, it is clear that there is a direct correlation between the capitalization ratio and the electronic instrument clearing system in dinars. The correlation coefficient reached (0.751\*\*) at the level of significance (Sig. = 0.005). Accordingly, we reject the null hypothesis which states that there is no correlation. Between the capitalization ratio and the electronic instrument clearing system in the dinar, which indicates that there is a correlation between the capitalization ratio and the electronic instrument clearing system in the dinar.

□ The thirteenth sub-hypothesis: - There is no statistically significant correlation between the retained earnings strategy and the electronic instrument clearing system in dollars.

When looking at the Table, we notice that there is no correlation between the retained earnings strategy and the system of clearing electronic instruments in dollars. The correlation coefficient reached (-0.111) at the level of significance (Sig. = 0.731). The level of significance was very small and cannot be relied upon to reject the null hypothesis. Therefore, the decision is not to reject the null hypothesis, meaning that there is no correlation between the retained earnings strategy and the electronic instrument clearing system in dollars.

□ The fourteenth sub-hypothesis: - There is no statistically significant correlation between the strategy of issuing new shares and the system of clearing electronic instruments in dollars.

When looking at the Table, we notice that there is no correlation between the common stock issuance strategy and the electronic instrument clearing system in dollars. The correlation coefficient reached (0.236) at the level of significance (Sig. = 0.459). The level of significance was very small and cannot be relied upon to reject the null hypothesis. Therefore, the decision is not to reject the null hypothesis, meaning that there is no correlation between the strategy of issuing ordinary shares and the system of clearing electronic instruments in dollars.

□ The fifteenth sub-hypothesis: - There is no statistically significant correlation between the reserves strategy and the electronic instrument clearing system in dollars.

When you look at the Table, we see that there is no correlation between the reserves strategy and the system of clearing electronic instruments in dollars. The correlation coefficient reached (0.309) at the level of significance (Sig. = 0.329). The level of significance was very small and cannot be relied upon to reject the null hypothesis. Therefore, the decision is not to reject the null hypothesis, meaning that there is no correlation between the reserves strategy and the electronic instrument clearing system in dollars.

□ Sixteenth sub-hypothesis: - There is no statistically significant correlation between the capitalization ratio and the electronic instrument clearing system in dollars.

When viewing the Table, we notice that there is no correlation between the capitalization ratio and the electronic instrument clearing system in dollars. The correlation coefficient reached (0.215) at the level of significance (Sig. = 0.501). The level of significance was very small and cannot be relied upon to reject the null hypothesis. Therefore, the The decision is not to reject the null hypothesis, meaning that there is no correlation between the capitalization rate and the electronic instrument clearing system in dollars.

#### **4. Conclusions**

The Iraqi banking sector has been adopting banking capitalization strategies in recent years, meaning increasing its capital by retaining profits and reserves and issuing common shares. Capitalization operations depend on several factors, including the size of costs, the speed of obtaining funds, the size of those funds, and the flexibility they enjoy. Profit retention is a process that represents retaining a portion of the income obtained in order to develop the business, and thus enhances digital transformation in general, whether in terms of value or in terms of financial ratio. The policy of increasing capital through issuing common shares enables banks to obtain new financial resources. This policy is considered one of the financial policies called external financing. The increase in capital by adding the reserve to it has many advantages for the bank, creditors, and shareholders alike, as it ensures that the bank achieves a balance between the distributed profit and the nominal value of the shares, as it facilitates the process of trading them.

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