

The Banking Sector and the Challenges in 2020



Dimitar Radev
Governor of BNB

The banking sector in Bulgaria ended 2019 with very good overall indicators and positive trends – high capital adequacy and liquidity, credit activity, improving asset quality and the historically highest annual profit of the sector. The asset quality review and the stress test conducted by the European Central Bank confirmed the resilience of the sector overall.

The banking sector in Bulgaria will be strategically impacted by the developments in the process of accession to ERM II and the Banking Union, part of which was the assessment of six Bulgarian banks undertaken by the ECB. The final stage of this process is to unfold in the coming months. The fulfillment of the commitments assumed by Bulgaria, including strengthening the capital of two Bulgarian banks, will be followed by relevant external assessment. Following the set path, Bulgaria is drawing near to achieving a fundamentally new level of EU integration – membership in the euro area institutions.

This will bring about significant change in terms of banking supervision and bank resolution activities.

The very onset of the process of establishing close cooperation of the Bulgarian National Bank with the ECB has already expanded the scope and enhanced the intensity of the two institutions' joint work. Actual membership in the Banking Union will further deepen our partnership with the ECB, the Single Supervisory Mechanism and the Single Resolution Mechanism.

Regarding supervision, according to the European Central Bank's rules the ECB will supervise the biggest banks in Bulgaria and the BNB's experts will participate in joint supervisory teams. This joint work will cover the off-site supervision aimed at on-going risk monitoring and assessment and also the on-site examinations in banks operating in Bulgaria. The other banks in Bulgaria will remain under the BNB's supervision, but supervisory information about them will be exchanged with the ECB continuously.

The joint work with the ECB will also cover many spheres of the practical organisation and operation of banking supervision. For example, the BNB's experts will have direct access to the overall analytical expertise in the Single Supervisory Mechanism. Historical experience shows that the accession to this mechanism generates new synergy between the national competent authorities and the ECB, and it is a two-way process.

Along with joining the Single Supervisory Mechanism, Bulgaria will also join the Single Resolution Mechanism. This would imply distribution of responsibilities and powers between the Single Resolution Board and the BNB as the national authority for resolution of credit institutions.

Bulgaria's legal framework for joining the Single Resolution Mechanism is already in place. The preparation for joining the Single Resolution Fund, including for calculating banks' contributions to the Fund, and the preparation of the bank resolution planning process after joining the Single Resolution Mechanism are very advanced.

The banks in Bulgaria have an important year ahead, which we expect to be overall successful for the sector. Banks' operations continue to take place in an environment of rather optimistic attitudes of enterprises and households amidst a relatively high growth of the Bulgarian economy. At the same time, the external environment holds risks and insecurity that, due to the openness and international integration of our economy, could potentially affect the economic situation in Bulgaria. Some adverse scenarios could exacerbate aspects of the risk profile of the banking sector. Therefore, it is essential that in their behaviour banks continue to take into account the main risks, including profitability risks and asset quality risks.



The banking sector continues to prosper, with innovation and high technology remaining the key to higher customer satisfaction



Peter Andronov

Chairman of the Executive Board of the ABB, Chief Executive Director of UBB AD

In 2020 to a large extent, banks will not operate in a fundamentally different economic environment and agenda compared to the previous year. This year will go by with expectations for slowing the pace of economic growth and keeping interest rates at unusually low levels, considering the signals from the external environment and the decisions of leading central banks. The environment of low and negative interest rates will continue to affect the cost of financing, the levels of net interest income and the interest margins of banks.

The consolidation processes that have been ongoing over the past year have also not been completed. They are a natural process that moves the market forward.

Accomplishing the possibility of Bulgaria's membership in the Exchange Rate Mechanism /ERM II/ and joining the Single Supervisory Mechanism /SSM/ by establishing a close cooperation with the European Central Bank /ECB/ are events of utmost importance not only for the banking sector, but also for the economy of the country in general. The progress on this topic in 2020 would have a positive impact both on the activities of the banks and on the overall assessment of national economic development and its perspectives.

As it is known, with a view to preparing for this membership, in 2019 the ECB carried out professionally and without compromise an asset quality review and stress tests in six banks. The evaluation results of the ECB are consistent with those of the 2016 asset quality review and stress test performed by the BNB and the performance of the banking system thereafter, taking into account the time that has passed. There was an affirmation of the assessment of the sustainability of the Bulgarian banking system, which, as a whole, continues to be characterized by a significant capital surplus over the regulatory requirements for the capital adequacy and liquidity coverage ratios.

Due to the regulatory challenges, competition and efficiency, the banks reported good financial results last year. For 2019 the result of the sector will be close to that of the previous year. The common equity tier 1 (CET 1) is 19% and regarding this indicator the Bulgarian banking system is among the top ten in Europe. The share of non-performing loans is still high, but is falling rapidly and is now just over 7%. At the same time, a characteristic feature of the banking system in Bulgaria is the higher level of the impairment coverage for gross non-performing loans by provisions compared with the average level for the EU countries. The return on equity /ROE/ is the eighth best on the Old Continent, and in terms of return on assets /ROA/, the Bulgarian banking system is ranked fourth in the EU,

according to the data of the European Banking Authority /EBA/ at the end of the third quarter of 2019.

In 2020 banks will continue with their active policies and presence in terms of lending and the various forms of financial intermediation as well as the diversification of the products and services they offer.

One of the key topics in banking is innovation and high technology, the development of digital channels and other modern ways to maintain a closer relationship with customers in order to understand better and meet their individual needs. Investments in digitalisation are part of the tools by which the banks can overcome the challenges arising due to the environment of the low interest rates. The innovations introduced by the banks allow customers to save time and efforts. Access to banking is uninterrupted, with a focus on expanding coverage and improving the quality of services through electronic channels, which is reflected in the lower cost of digital banking services.

In 2020 the Association will continue to follow a policy of openness and fair treatment, both to its members and to government bodies, other organizations, the media and the public in general.

We take the opportunity to express the gratitude of the Association of Banks in Bulgaria /ABB/ to the National Assembly, Ministry of Finance, Bulgarian National Bank, Financial Supervision Commission, National Revenue Agency, Prosecutor's Office of the Republic of Bulgaria and other state bodies and institutions for their constructive cooperation in legislative proposals, various regulatory changes or other socially significant events throughout the last year.

The banking sector in Bulgaria has taken as its mission to support actively and assist in raising financial literacy. Banks have also traditionally been involved in a number of projects demonstrating their socially responsible behaviour, as well as supporting the efforts of law enforcement agencies to prevent and detect financial crimes related to money laundering from illegal activities. In this context, we marked the [European Money Week 2019](#) for the fifth consecutive time last spring. Also for the fifth consecutive year, banks and law enforcement agencies launched a [campaign against the money mules](#). With the participation of its members, the ABB and the Foundation "Our Premature Children" have organized for the first time a [donation campaign](#) dedicated to the Children's Day.

As until now, the ABB will continue to rely heavily on the European Banking Federation of which it is a member, for the professionalism and efficiency of its operations. The participation in the work of this organization, which in 2020 celebrates its 60th anniversary, is extremely useful for the ABB's interaction with the European and local regulators, as well as in helping to find the most effective solutions to various issues relevant to the development of the system.

We express our appreciation and deep gratitude to the representatives of the banks – our members, who are actively involved in the work of the Association, taking part in 6 committees and 11 working groups at the ABB. We will continue to count on you in 2020, in view of the emerging challenges of the banking business and the high social responsibility we have, as one of the key sectors for the development of the national economy.



The Investor Compensation Fund – a Guarantor for the Confidence in the Capital Market



Teodora Drenska
Chairperson of the Management
Board Investor Compensation Fund

As of 31st of December 2019 the accumulated amounts at the Investor Compensation Fund (ICF) were 17,52 million BGN, invested in government securities. There are 37 non-bank investment intermediaries, 18 banks and 32 asset management companies participating in the Fund. Only 4 of the asset management companies hold clients' assets, protected by the Fund and thus, the active participants in the Fund as of 31st of December 2019 were 59. As of the end of 2019 the participants in the Fund manage clients' assets at the total value of 49,5 billion BGN as the increase on the annual basis is 24%. The increase is mainly due to the amounts of clients' assets to professional investors. The clients' assets protected by the Fund are at the amount of 2,25 billion BGN as the banks continue to manage the majority of the protected clients' assets held by all scheme participants (72%). The increasing amounts of clients' assets indicate a positive tendency for the development of the capital market.

At the end of the year by a decision of the Management Board of the Fund the size of the annual contribution for 2020 was kept at its level of 0,05% applied on the protected clients' instruments and 0,25% on monetary funds. Thus, for 11th subsequent year the participants in the Fund pay half of the maximum level that could be applied on the financial instruments as it set in the law and for a 4th subsequent year the participants in the scheme make a lower contribution on monetary funds.

Since 2017 the Fund has also been responsible for the management of the Investment Firms Resolution Fund /IFRF/, which is not a separate legal entity. The main activity of the IFRF is to fund the application of the instruments for the resolution and restructuring of troubled non-bank investment intermediaries. The participants in the IFRF are all investment intermediaries with a full license for providing investment services as the number of those investment intermediaries as of 31st of December 2019 was 18. The contributions to the IFRF are determined by the Financial Supervision Commission /FSC/ which is a resolution authority for investment intermediaries as the accumulated funds at the IFRF were at the amount of 110 thousand BGN as of 31st of December 2019.

In the last year the main focus in the Fund's activities was related with the activation of the procedures for the compensation payments by the Fund to the clients of Matador Prime Ltd. The activation of the procedures for compensation payments was due to revoking of the license of Matador Prime Ltd. by the FSC on the 11th of October 2018 and a conservator for a period of three months was appointed. On the basis of the results of the quaestorship the FSC took a decision N° 102-ИП on the 24th of January 2019 according to which there are circumstances for compensation payments to the clients of Matador Prime Ltd. as the investment intermediary has no possibility to perform its duties to the clients due to reasons

related with its financial state. As a result of the activation of the procedure 78 claims from clients of Matador Prime Ltd. for compensation payments were submitted at the Fund as the legally defined deadline for submitting claims by the clients expires on the 1st of February 2020. The Management Board of the Fund has taken a decision on a part of the submitted claims for compensation payments.

Along with the dynamic work related with the procedures for compensation payments to the clients of Matador Prime Ltd. the Fund's activities are also focused on collecting the contributions due by the participants in accordance with the legally set deadline; the management of the accumulated funds; collection and analyses of the information about the clients' assets held by the participants in the scheme; assessment of the Fund's exposition as well as other related activities.

In 2020 the Fund is going to celebrate its 15th anniversary. For that period the ICF proved to be an organization with high reputation contributing to the stability and confidence in the capital market.



IN BRIEF

■ Mr. Ivan Manev, Director Directorate “Security” at United Bulgarian Bank AD, was elected as the new Chairman of the Security Committee at the ABB Executive Board at a meeting of the Committee held in January. In place of Mr. Manev, who was a Deputy Chairman of the Committee, was elected Mr. Alexander Yordanov – Head of Security at Raiffeisenbank /Bulgaria/ EAD.

The two long-standing members of the Committee were unanimously elected, taking into account their significant contribution to the work of the Committee, as well as their indisputable professionalism and competence in the field of banking security.

■ In December, a meeting of the User Committee at the Central Depository AD was held, to which the ABB’s representative at that committee - Mr. Yavor Dozhdevski from Citibank, who is also a deputy Chairman of the Capital Markets Committee at the ABB, was elected as a rotating Chairman of the Committee for a period of one year. A representative of BSE AD was appointed as Secretary of the Committee.

■ In the first half of 2020 the ABB takes over the rotating presidency of the informal group of 8 national banking associations /Bulgaria, Romania, Poland, Hungary, Czech Republic, Slovakia, Slovenia, Croatia/, of which the ABB has been a member since 2017. The association is going to host a meeting of the secretaries-general and other representatives of the members of that informal group, which will take place in June in Sofia. The meetings of the group are held twice a year and are hosted by the respective association being the rotating chair.