



THE ECONOMY AND THE BANKING SECTOR IN BULGARIA

THIRD QUARTER OF 2020



SOFIA



HIGHLIGHTS

- In Q2 2020 the Bulgarian economy contracted by 8,6% on an annual basis, as there was a positive contribution only by the government consumption
- The inflation slowed its growth to 0,6% year-on-year in Q3 2020
- As of the end of September 2020 the unemployment in Bulgaria increased to 6,2%
- The budget surplus was 0,7% of the GDP as of the end of Q3 2020
- As of the end of Q3 2020 the total assets of the banking system were at the amount of BGN 119,22 billion, representing 100,1% of the forecasted GDP
- In Q3 2020 the net profit of the banking sector was BGN 186 million (recording a decline of 15,1% on a quarterly basis)
- The subdued lending activity, the lower income from fees and commissions, the low interest rates, the impairment expenses, the management of the operating expenses and the quality of the credit portfolio as well as some one-off effects influenced the financial result of the sector
- In Q3 2020 the deadline for submitting requests by the bank's customers under the proposed by the Association of Banks in Bulgaria (ABB) and approved by the BNB in April 2020 *Procedure for Deferral and Settlement of Liabilities Payable to Banks and their Subsidiaries – Financial Institutions* in relation to the state of emergency enforced by the National Assembly on 13 March 2020 was extended and households and non-financial corporations took advantage of it
- The average interest rates on new loans and on new deposits with agreed maturity retained their low levels



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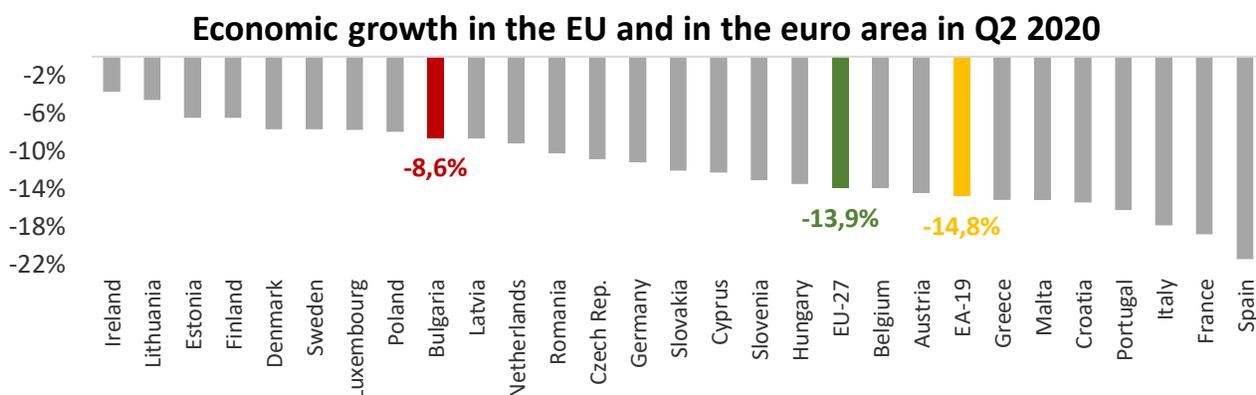
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I. The Bulgarian economy

Economic growth

In Q2 2020 the Bulgarian gross domestic product (GDP) contracted by 8,6% on an annual basis, according to the preliminary seasonal and calendar adjusted data of Eurostat. The average drop for the EU in the period April-June 2020 was by 13,9% year-on-year, and that of the euro area – by 14,8% on an annual basis.



Source: Eurostat (Seasonally and calendar adjusted data; unadjusted data for Slovakia)

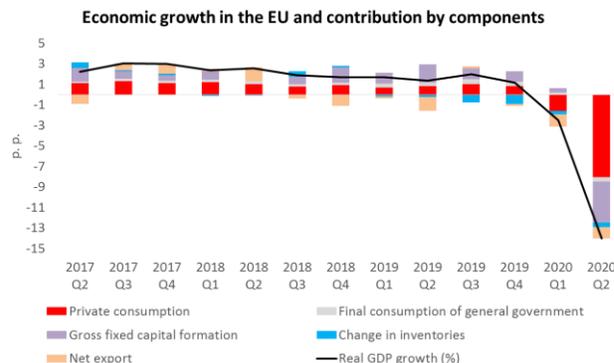
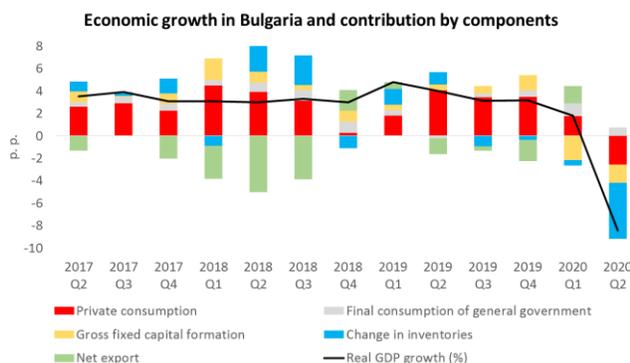
According to the preliminary data of Eurostat, the economic dip in Q2 2020 was driven by declines of the private consumption, investments and net export, as the government consumption had the only positive contribution.

During the observed period the growth of private consumption, which includes the consumption of the households and non-profit institutions, serving households (NPISH), declined by 4% on an annual basis (compared to the growth of 2,9% Y-o-Y in Q1 2020) and contributed to the yearly GDP drop by 2,5 percentage points (p.p.) compared to the registered contribution of 1,8 p.p. to the economic growth in Q1 2020.

The consumption of the general government, which growth rate slowed to 3,9% on an annual basis (from 6,3% Y-o-Y in the previous quarter), contributed by 0,8 p.p. compared to 1,2 p.p. a quarter earlier.

In Q2 2020 the growth of the gross fixed capital formation decreased by 11,8% on an annual basis after a decline by 10,2% on an annual basis in the previous quarter. In Q2 2020 the contribution of the business investments to the GDP was negative (-1,6 p.p.) compared to the negative -2,2 p.p. three months earlier. The contribution of inventories was negative (-5 p.p.) in comparison with the negative contribution of -0,5 p.p. in the first quarter of 2020.

In Q2 2020 the export of goods and services decreased by 19% on an annual basis compared with the growth of 3,2% Y-o-Y three months earlier. The import dipped by 19,5% on an annual basis after an increase of 0,4% Y-o-Y in Q1 2020. The contribution of the net export was negative in the second quarter of 2020. The trade deficit was 0,9% of GDP compared with the deficit of 0,7% as of the end of the previous quarter.



Source: Eurostat, own calculations

In comparison, all components contributed to the drop of the GDP in the EU by 13,9% on an annual basis in Q2 2020.

In its [Autumn economic forecast](#) the European Commission (EC) expects the Bulgarian economy to continue recovering, with the main contribution of the domestic demand and export. In its quarterly publication [Macroeconomic Forecast](#) the Bulgarian National Bank (BNB) expects that the fiscal policy would have a strong countercyclical effect and would contribute positively to the economic activity, both through a higher amount of government consumption expenditures and investments, as well as through increased net transfers to households. In line with the assumed developments in the external environment and the containment of the pandemic, in 2021-2022 the BNB forecasts a gradual recovery in the economic activity.

Different national and international organizations and institutions forecast that the economic slump in Bulgaria is going to vary between -5,5% and -3% in 2020. The forecasts are for an increase of the GDP between 2,5% and 4,1% in 2021.

Key indicators for the Bulgarian economy																	
	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020 Q1	2020 Q2	2020 Q3	2020F	2021F	2022F	2023F	
Gross domestic product																	
GDP (mln. BGN)	80 714	82 239	81 955	83 885	89 362	95 131	102 345	109 743	119 772	25 993	27 774	-	-	-	-	-	
GDP (real Y-o-Y growth, %)	2,4	0,4	0,3	1,9	4,0	3,8	3,5	3,1	3,7	1,8	-8,5	-	-	-	-	-	
GDP (real Y-o-Y growth, %) - forecasts													MF (October 2020)	-3	2,5	3	3,2
													BNB (October 2020)	-5,5	4	3,8	-
													IMF (October 2020)	-4	4,1	2,8	2,8
													WB (October 2020)	-5,1	3,9	3,2	-
													EC (November 2020)	-5,1	2,6	3,7	-
													EBRD (October 2020)	-5,5	3	-	-
Total final consumption	2,6	2,3	-2,0	2,3	3,4	3,2	3,9	4,6	4,7	3,7	-2,2	-	-	-	-	-	
Private consumption (of Households and NPISH)	2,6	3,3	-2,6	2,9	3,8	3,5	3,8	4,4	5,5	2,9	-4,0	-	-	-	-	-	
Final consumption of general government	2,3	-1,8	0,7	-0,1	1,8	2,2	4,3	5,3	2,0	6,3	3,9	-	-	-	-	-	
Gross fixed capital formation	-4,4	1,8	0,5	3,5	2,7	-6,6	3,2	5,4	4,5	-10,2	-11,8	-	-	-	-	-	
Export of goods and services	12,6	2,0	9,6	3,1	6,4	8,6	5,8	1,7	3,9	3,2	-19,0	-	-	-	-	-	
Import of goods and services	9,9	5,6	4,3	5,2	4,8	5,2	7,4	5,7	5,2	0,4	-19,5	-	-	-	-	-	
Trade balance/GDP (%)	-6,5	-9,5	-7,0	-6,5	-5,7	-2	-1,5	-4,8	-4,7	-0,7	-0,9	-	-	-	-	-	
Foreign direct investments in Bulgaria (mln. EUR)	1 476,3	1 320,9	1 383,7	347,4	2 000,9	927,2	1 618,9	983,0	1 138,5	291,0	448,6	-	-	-	-	-	
Foreign direct investments/GDP (%)	3,6	3,1	3,3	0,8	4,4	1,9	3,1	1,8	1,9	0,5	0,8	-	-	-	-	-	
Harmonised index of consumer prices (HICP) (Y-o-Y change, average for the period)	3,4	2,4	0,4	-1,6	-1,1	-1,3	1,2	2,6	2,5	3	1,1	0,6	-	-	-	-	

Source: NSI, Eurostat, Bulgarian National Bank

Forecasts: Bulgarian National Bank, Ministry of Finance, International Monetary Fund, World Bank, European Commission, European Bank for Reconstruction and Development

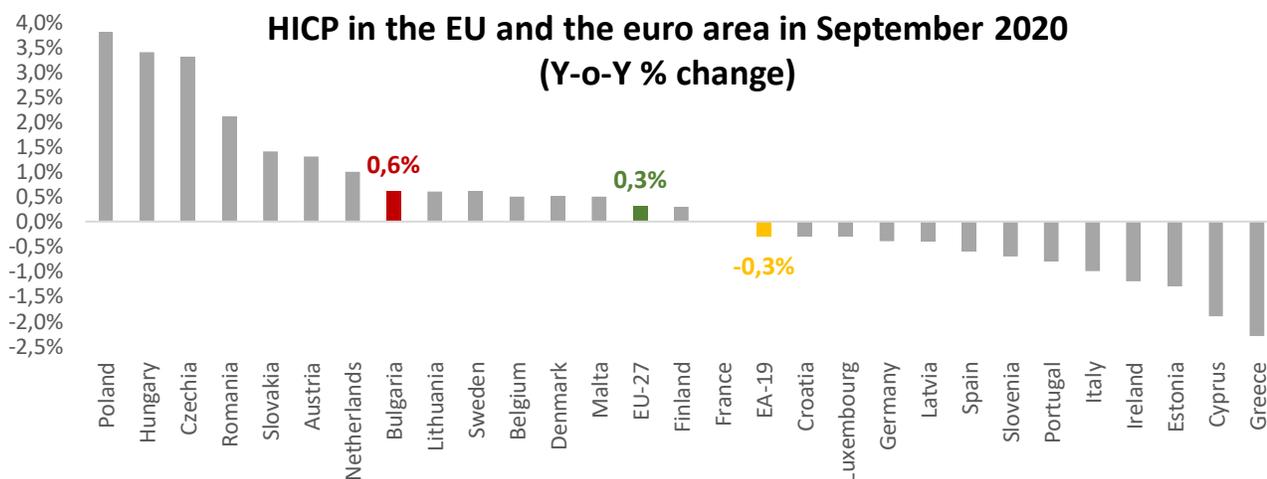


Inflation

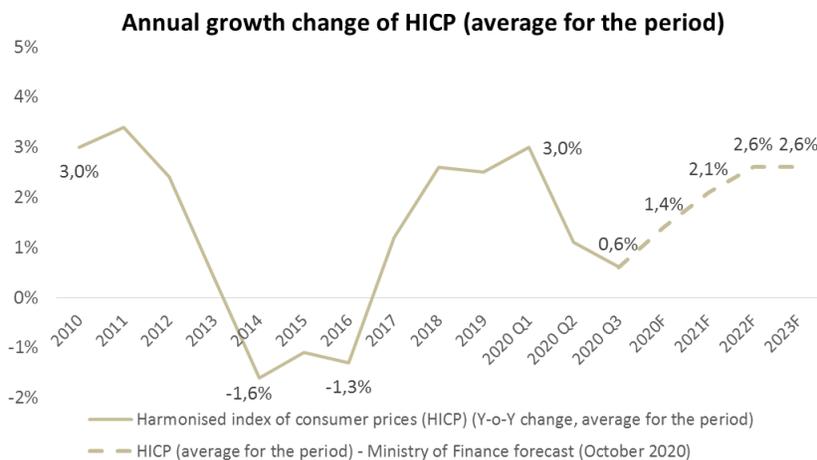
In Q3 2020 the growth of the harmonized index of consumer prices (HICP) slowed down to 0,6% on an annual basis from 1,1% Y-o-Y in Q2 2020. In September 2020 the inflation in Bulgaria stood at 0,6% Y-o-Y, which was higher than the average for the EU (0,3%) and the euro area (-0,3%). In September 2020 Bulgaria ranked eight regarding the level of the HICP.

In its quarterly publication [Macroeconomic Forecast](#) the BNB expects the annual inflation to slow down significantly to 0,3% at the end of 2020, reflecting the strong decline of international oil prices in euro and moderation in core inflation under the influence of the decreased private consumption on an annual basis. According to the BNB, the headline inflation is expected to accelerate to 1,9% by end-2021 mainly due to the increased oil prices and a gradual rise in the core inflation, thereafter slowing down to 1,6% in 2022.

In its [Autumn economic forecast](#) the EC foresees a decline of the inflation in Bulgaria to 1,2% at the end of 2020 and increase to 1,4% in 2021 and further to 1,8% in 2022.



Source: Eurostat



Source: NSI, Eurostat

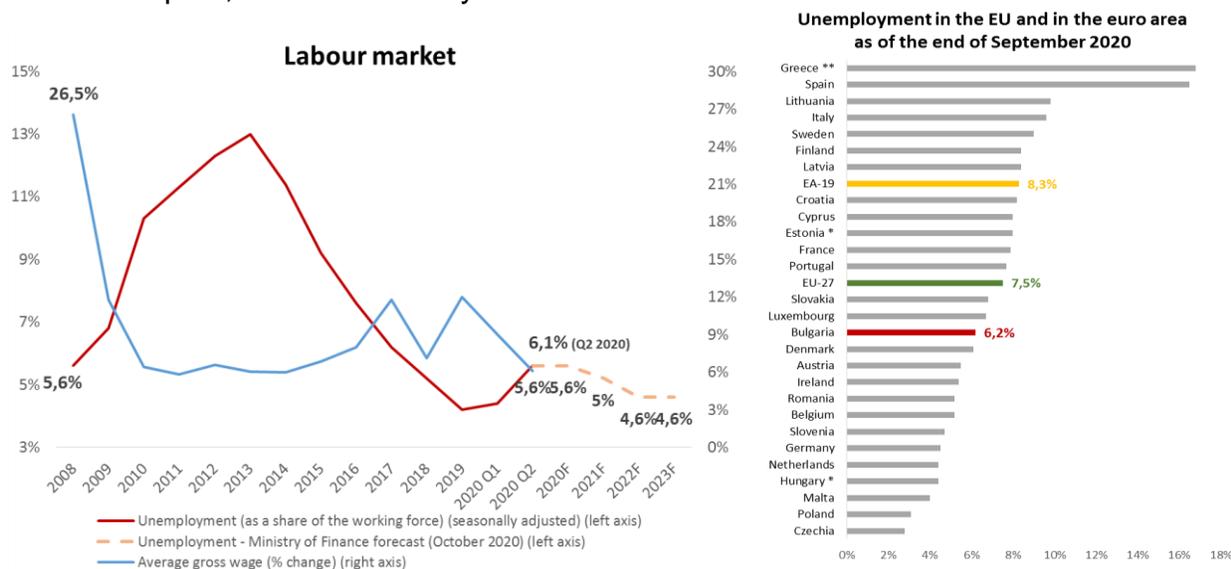
Forecast: Ministry of Finance, October 2020



Labour market

In September 2020 the level of unemployment, measured as a share of the working force, increased to 6,2% from 5,6% at the end of Q2 2020. The unemployment in the country was lower than the EU average. In the period, Bulgaria ranked 13th amongst the EU Member States with the lowest unemployment rate and sixth amongst the countries in the Central and Eastern European (CEE) region. As of the end of September 2020 the number of unemployed in Bulgaria rose to 198 thousand from 182 thousand as of the end of Q2 2020 and from 133 thousand as of the end of Q3 2019.

The level of the unemployed young people (under 25 years) increased to 18,3% as of the end of September 2020 compared to 16,4% three months earlier. At the end of September 2020 the average level of the youth unemployment in the EU was 17,1%, as the largest share is observed in Spain, Greece and Italy.



Source: Eurostat, Ministry of Finance, NSI

Note: * August 2020 ** July 2020

Key indicators for the Bulgarian economy												
	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020 Q1	2020 Q2	September 2020
Labour market												
Unemployment (as a share of the working force) (seasonally adjusted)	11,3	12,3	13	11,4	9,2	7,6	6,2	5,2	4,2	4,4	5,6	6,2
Employed (15+ years) (thousands)	2 965,2	2 934	2 934,9	2 981,4	3 031,9	3 016,8	3 150,3	3 152,7	3 233,1	3 107,2	3 079,6	-
Employed in "Finance and Insurance" sector (thousands), of which:	55	52,7	51,6	60,5	62,3	58,6	63,7	65,4	67,3	58,5	62,4	-
Employed in the banking sector (thousands)	33,9	33,5	32,8	31,7	30,7	30,4	30,1	29,9	28,2	-	-	-
Average monthly gross wage in "Finance and Insurance" sector	1 438	1 459	1 508	1 578	1 608	1 709	1 788	1 904	2 074	2 120	2 287	-

Source: Eurostat, Ministry of Finance, NSI, ECB



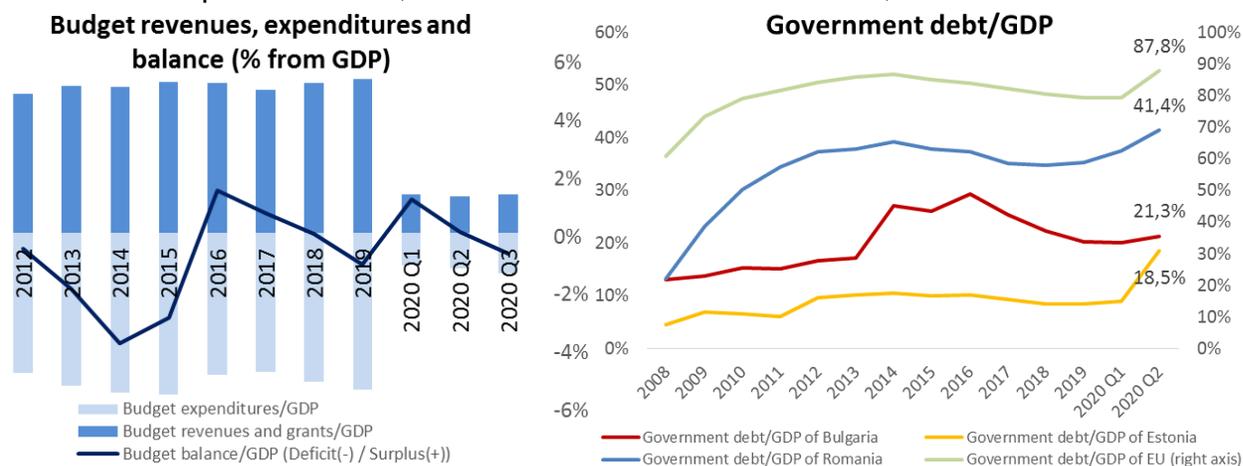
Public sector

According to the Ministry of Finance (MF) preliminary data, as of the end of September 2020 the state budget had a positive balance of BGN 871,4 million (0,7% from the projected GDP). For October 2020 the MF forecasts a surplus of BGN 618 billion (0,5% from the projected GDP).

The amount of the budget revenues and grants on the Consolidated Fiscal Programme for the period January-September 2020 was BGN 32,42 billion (27,2% from the projected GDP). Compared to the same period last year, the tax and the non-tax revenues declined by 2,4% on an annual basis.

Budget expenditures (including the EU budget contribution of Bulgaria) for the nine months of 2020 amounted to BGN 31,54 billion (26,5% from the projected GDP). The amount of the expenditures was close to that for the same period of the previous year, with a decrease being registered mainly in the part referring to capital expenditures. When comparing the total amount of expenditures and capital expenditures with the same period of the previous year, according to the MF, it should be taken into consideration the effect in 2019 from the expenditures made for the implementation of the project for acquisition of a new type of military aircraft for the Bulgarian air force, which has one-off effect.

As of the end of September 2020, the fiscal reserve totaled BGN 13,53 billion.



Source: Ministry of Finance, Eurostat

The share of the government debt to GDP increased to 21,3% as of the end of Q2 2020 compared to 20,1% at the end of Q1 2020. Bulgaria is the second among the countries with the lowest government debt after Estonia (18,5%). The government debt to GDP ratio for Bulgaria is below the EU average, which rose to 87,8% at the end of Q2 2020.

The Long-term Interest Rate for Convergence Assessment Purposes (LTIR) dropped to 0,2% as of the end of September 2020 from 0,68%, as it was at the 30th of June 2020. For comparison, as of the end of September 2020 the LTIR in Romania was 3,49%, in Poland – 1,35%, in Hungary – 2,39%, in Croatia – 0,79%, and in the Czech Republic – 0,98%. The level of the LTIR in Bulgaria continues to be the lowest in comparison with the countries in the CEE region, members of the EU but not members of the euro area.



Capital market

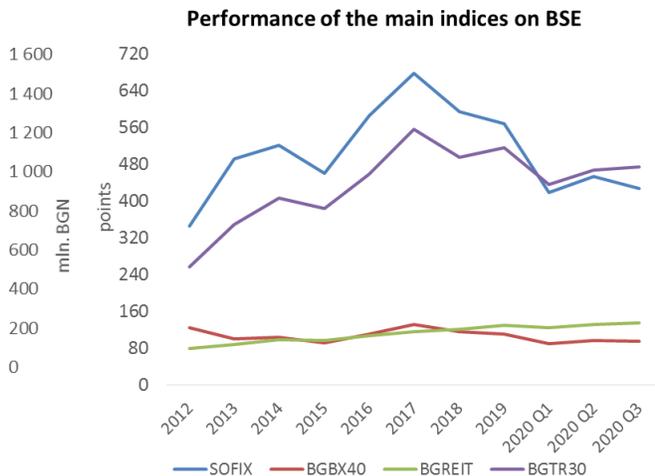
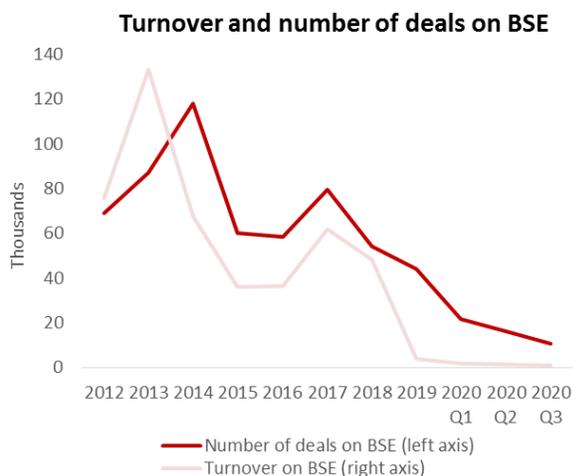
At the end of September 2020 the main indices on the Bulgarian Stock Exchange (BSE) changed compared to the end of Q1 2020 as follows: SOFIX dropped by 5,7%, BGBX40 declined by 0,4%, BGREIT grew by 2,1% and BGTR30 increased by 1,8%.

In Q3 2020 the Bulgarian index SOFIX was with the second biggest drop among the major stock market indices in the CEE region, as well with the third largest decline year-to-date.

As of September 30, 2020, the market capitalization on the BSE (main market and alternative market) increased by 0,5% on a quarterly basis to BGN 27,85 billion (23,4% of GDP) from BGN 27,71 billion (23,3% of GDP).

During the period July-September 2020 the turnover on the stock exchange rose by 21% on a quarterly basis and on an annual basis it reaches to BGN 103,27 million. In Q3 2020 the number of transactions dropped by 34,2% on a quarterly basis to 10 441, while they rose by 7,1% on an annual basis.

In Q3 2020 the banks, members of the BSE, performed 12,5% of the turnover and 5,1% of the total transactions on the regulated market (the principle of double reporting). In the previous quarter the banks, members of BSE, concluded 4% of all transactions and 12,3% of the total turnover on the regulated market.



Source: BSE, own calculations



No	Country	Index	31 December 2019	30 June 2020	30 September 2020	Change in Q3 2020	Year to date change
1	North Macedonia	MBI 10	4 645,17	4 116,66	4 485,18	8,95%	-3,44%
2	Russia	MOEX	3 045,87	2 743,20	2 910,12	6,08%	-4,46%
3	Slovakia	SAX	351,14	337,38	355,39	5,34%	1,21%
4	Romania	BET	9 977,30	8 586,12	9 007,20	4,90%	-9,72%
5	Serbia	BELEX	1 726,82	1 497,57	1 503,29	0,38%	-12,94%
6	Slovenia	SBITOP	926,10	849,82	846,20	-0,43%	-8,63%
7	Croatia	CROBEX	2 017,43	1 621,55	1 608,54	-0,80%	-20,27%
8	Poland	WIG	57 832,88	49 972,05	49 411,53	-1,12%	-14,56%
9	Turkey	XU 100	1 144,25	1 165,25	1 145,24	-1,72%	0,09%
10	Greece	ASE	916,67	638,90	624,75	-2,21%	-31,85%
11	Czech Republic	PSE	1 115,63	918,00	868,33	-5,41%	-22,17%
12	Bulgaria	SOFIX	568,14	453,26	427,55	-5,67%	-24,75%
13	Hungary	BUX	46 082,82	35 817,88	32 923,53	-8,08%	-28,56%

Source: BSE, Bloomberg, own calculations

Key indicators for the Bulgarian economy												
	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020 Q1	2020 Q2	2020 Q3
Capital market												
Market capitalization/GDP	15,4%	12,0%	12,2%	11,6%	9,6%	10,2%	24,3%	24,4%	23,3%	22,0%	23,3%	23,4%
SOFIX	322,11	345,46	491,52	522,1	460,9	586,43	677,45	594,46	568,14	419,35	453,26	427,55
BGBX40	113,69	125,11	100	104,61	92,82	111,3	132	115,91	111,83	90,38	96,7	96,36
BGREIT	51,25	79,62	88,66	98,75	97,03	108,11	116,1	121,07	130,03	125,07	132,53	135,3
BGTR30	264,5	257,87	349,03	407,5	383,82	459,19	555,98	496,14	516,28	436,89	466,98	475,16
Turnover on BSE (thousand BGN)	717 023	864 038	1 522 000	774 900	410 800	416 003	705 851	550 041	333 574	88 408	85 303	103 270
Number of deals on BSE	109 260	68 855	87 069	118 074	60 047	58 442	79 629	54 341	44 167	21 480	15 870	10 441

Source: BSE, Bloomberg, own calculations



II. The banking sector in Bulgaria

The state of the economic environment continued to affect the activities of the banking system. In its quarterly publication [Macroeconomic Forecast](#) the BNB expects by the end-2020 non-government sector deposits in the banking system to continue growing at comparatively high rates. According to the BNB, this dynamics will be driven by the continuous build-up of precautionary savings by the economic agents in the context of an increased uncertainty about the future development of the macroeconomic environment and the absence of a safe and low-risk alternative to bank deposits.

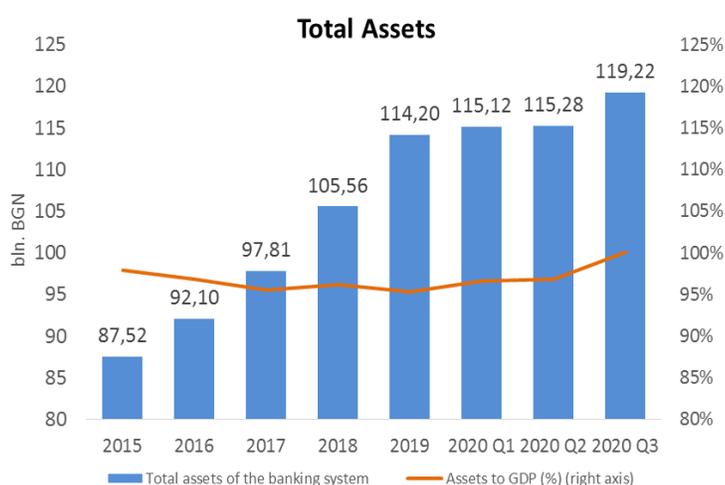
In 2020 the BNB forecasts a significant slowdown in the non-government sector's credit growth in 2020 due to the deteriorating macroeconomic environment and tightened credit standards. In 2021-2022 the BNB assumes acceleration of the credit growth, which would stay below the registered pace in 2019.

In Q3 2020 the deadline for submitting requests by banks' customers under the proposed by the Association of Banks in Bulgaria (ABB) and approved by the BNB in April 2020 [Procedure for Deferral and Settlement of Liabilities Payable to Banks and their Subsidiaries – Financial Institutions](#) in relation to the state of emergency enforced by the National Assembly on 13 March 2020 was extended and the households and non-financial corporations took advantage of it.

Balance sheet statement (Statement of financial position)

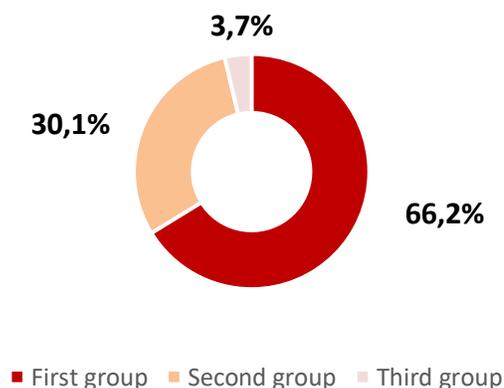
Assets

The growth of assets in the banking sector at the end of Q3 2020 was 6,9% on an annual basis reaching BGN 119,22 billion. The share of the assets to the projected GDP was 100,1% as of the end of September 2020.



Source: BNB, Ministry of Finance, own calculations

Market share in terms of assets as of the end of Q3 2020





As of the end of Q3 2020 the market share of the five biggest banks in terms of assets decreased to 66,2% from 66,3% as it was at the end of Q2 2020. The market share of the banks from the second group declined to 30,1% from 30,2%. The share of the assets of foreign bank branches increased to 3,7% from 3,5% of the total assets of the banking system as of the end of Q2 2020.

As of September 30, 2020, 60,4% of the assets in the banking system were in the form of loans and receivables, totaling BGN 71,98 billion. Cash balances amounted to BGN 23,85 billion and they comprised 20% of the assets. The share of investments in financial instruments was 14,9% (BGN 17,73 billion). For comparison, as of the end of Q2 2020 the share of loans and receivables was 61,2%, the share of the cash balances – 19,5%, and the investments in financial instruments – 14,5%.

Liabilities

The liabilities in the banking system (excluding equity) were at the amount of BGN 104,11 billion and rose by 7,1% on an annual basis. The banks in the first group comprised 68,3% of the liabilities (BGN 68,63 billion), the second group – 31% (BGN 31,15 billion), and branches of foreign banks – 4,3% (BGN 4,33 billion).

The growth of liabilities was driven by the increase in deposits, which comprised 97,1% of their total amount (excluding equity). From the statement of financial position of the system it was evident that the amount of deposits grew by 7% on an annual basis to BGN 101,14 billion.

The share of the provisions for loan losses which include unsettled legal issues and lawsuits, credit commitments, guarantees, pensions, etc., accounted for 0,3%, or BGN 297,54 million in absolute terms. The share of financial liabilities, held for trading and other liabilities were respectively 0,2% and 0,8%. The share of all other remaining liabilities is negligible, complementing the sum up to 100%.

Equity

In Q3 2020 the total equity in the banking system increased by BGN 366 million (2,5% Q-o-Q) and at the end of September 2020 it stood at the amount of BGN 15,11 billion. At the end of June 2020, its amount was BGN 14,75 billion. The dynamic was influenced mainly by the paid-in capital, premium reserves, accumulated other income and the profit in the banking sector. As of the end of September 2020 the equity increased by 5,5% compared to the same period of the previous year. The equity of the banks in the first group amounted to BGN 10,35 billion, and that of the second group – BGN 4,7 billion.



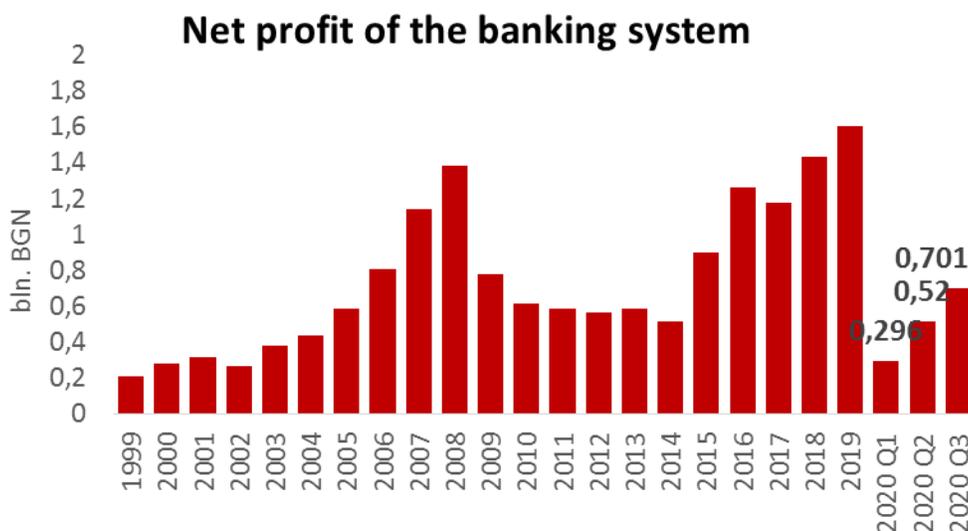
Statement of profit or loss

Net profit

In Q3 2020 the banking sector registered a decrease in the net profit by 47,2% on an annual basis and by 15,1% on a quarterly basis to BGN 186 million. For comparison, in Q3 2019 the net profit of the banking sector was at the amount of BGN 352,5 million, while in Q2 2020 the net profit was BGN 219,1 million.

The financial performance of the system was influenced by the dynamics in the lending activity, the lower income from fees and commissions, low interest rates, the impairment costs, the optimization of the core expenses and the better quality of the credit portfolio. Some one-off effects observed in the financial statements of some banks, as received dividends, positive result from derecognition of financial assets and liabilities, currency exchange differences and higher impairments also influence the financial result of the system.

The net profit of the banking sector for the third quarter of 2020 was at the amount of BGN 701,3 million, which was a decline by 44,8% on an annual basis. By taking into account the one-off effects, the drop of the net profit would be higher.



Source: BNB

The first group of banks generated 77,3% of the net profit at the end of Q3 2020, the second group – 18,5%, and the third group – 4,2%. For comparison, as of the end of Q2 2020 the five biggest banks in terms of assets contributed by 78,1% to the net profit, the banks in the second group – by 19,9%, and the share of the third group was 2%.



Net interest income

As of the end of Q3 2020 the total net operating income of the banking system was at the amount of BGN 3,107 billion compared to BGN 3,165 billion as of the end of Q3 2019. It dropped by 1,8% on an annual basis.

The net interest income of the banks decreased by 5,2% on an annual basis (BGN -108,4 million) to BGN 1,973 billion as of the end of September 2020.

The net interest income is the difference between the interest income and the interest expenses. As of September 30, 2020, the interest income declined by 3% Y-o-Y (BGN -68,4 million) to BGN 2,23 billion. The interest expenses were at the amount of BGN 256,9 million, which was by 18,4% higher on an annual basis.

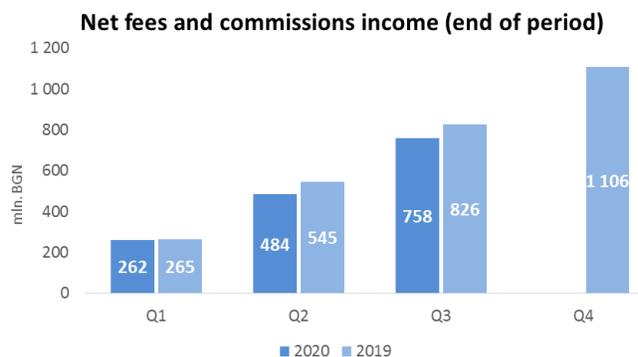
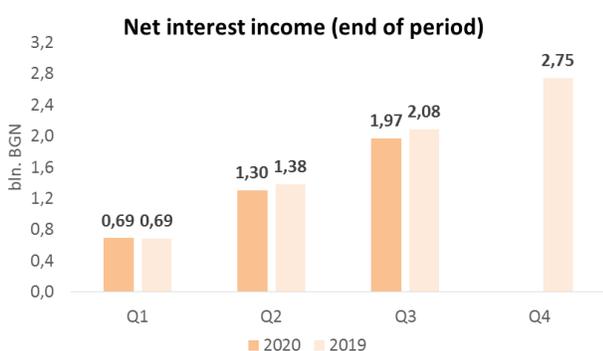
The net interest income comprised 63,5% of the net total operating income of the banking system at the end of Q3 2020. For comparison, in the EU the share of the net interest income was 60,3% of the total operating income, according to the EBA data as of the end of Q2 2020.

Net income from fees and commissions

As of the end of Q3 2020 the net income from fees and commissions decreased by 8,2% on an annual basis (BGN -67,5 million) to BGN 758,3 million from BGN 825,7 million a year ago.

The income from fees and commissions dropped by 7,8% on an annual basis (after a drop of 10,1% on an annual basis as of the end of June 2020) to BGN 908,5 million, and the expenses related with fees and commissions decreased by 5,9% on an annual basis to BGN 150,3 million.

The income from fees and commissions made up 24,4% of the total net operating income of the system as the share of fees was lower than the EU average, which was 30,4%, according to the EBA data for the second quarter of 2020.



Source: BNB, own calculations

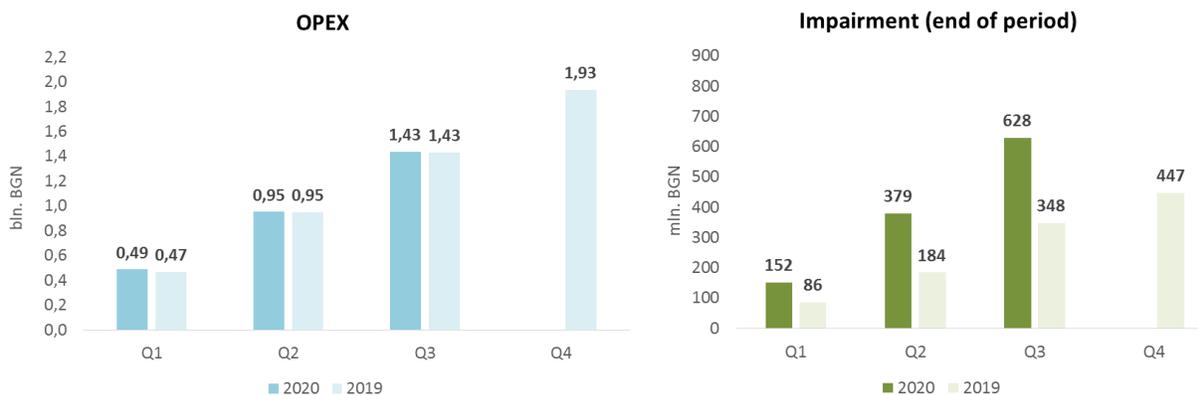


Operating expenses and impairments

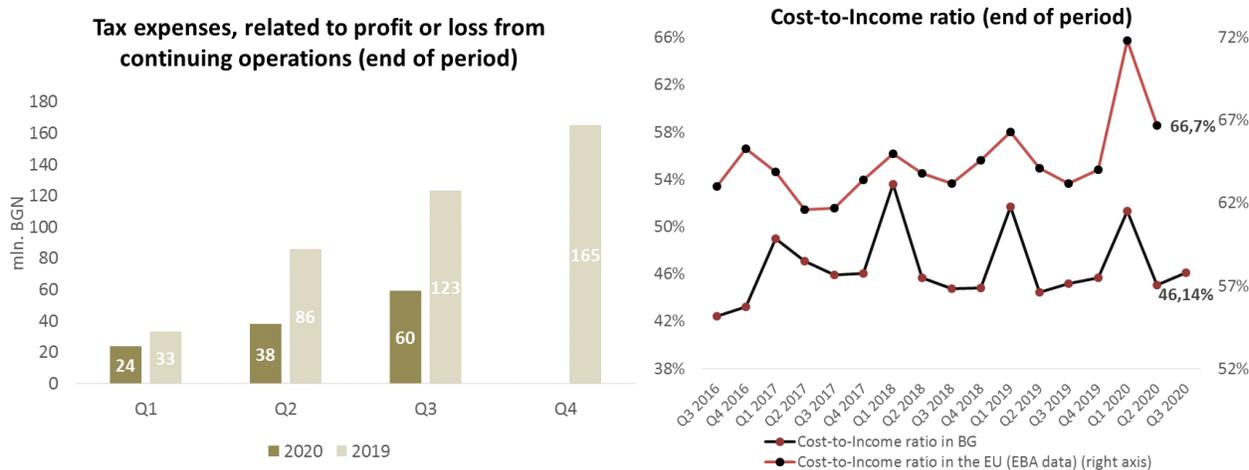
As of the end of Q3 2020 the administrative expenses, which include overhead expenses, were by 1,1% lower compared to the same period of 2019 as they reached BGN 1,22 billion. The total operating expenses, as a sum of the administrative expenses and depreciation, increased by 0,2% on an annual basis to BGN 1,433 billion.

The banking system made more impairments in comparison with the same period in the previous year. The impairments increased to BGN 627,6 million from BGN 347,6 million a year earlier. According to the application of the International Financial Reporting Standard 9 (IFRS 9), the banks by using their own models make forecasts for potential impairments for the expected credit losses due to COVID-19 and accumulate preliminary provisions before the potential negative effect on the loan impairments occurs. Those actions, in accordance with IFRS, affect the amount of the impairments, made by banks in the course of 2020.

As of the end of Q3 2020 Cost-to-Income ratio for the banking system increased to 46,14% from 45,08% as it was at the end of Q2 2020. According to the EBA data, the average Cost-to-Income ratio in the EU decreased to 66,7% as of the end of Q2 2020.



Source: BNB, own calculations



Source: BNB, EBA, own calculations

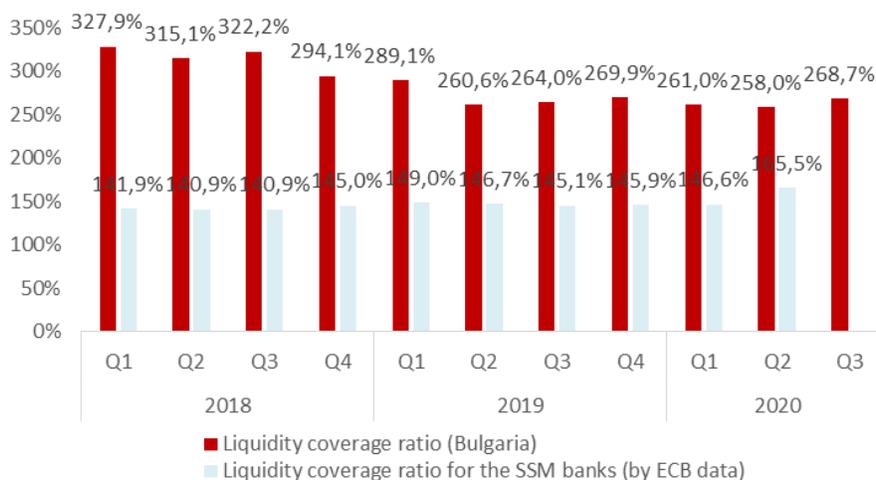


Financial indicators

Liquidity

As of the end of September 2020 the liquidity buffer and the net liquidity outflows were respectively BGN 32,4 billion and BGN 12 billion, according to the BNB data. The liquidity coverage ratio (LCR) was 268,7% compared to 258% as of the end of June 2020. According to the ECB data, as of the end of Q2 2020 the LCR for the banks in the Single Supervisory Mechanism was 165,5%.

Liquidity coverage ratio (LCR)



Source: BNB, ECB

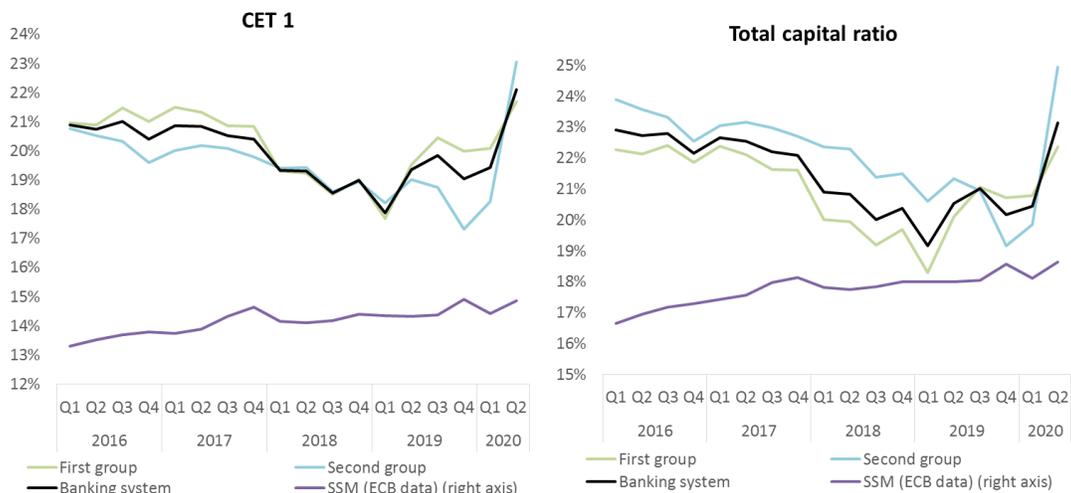
Capital adequacy

The capital position of the banking sector is being marked by a significant capital surplus above the regulatory requirements for the capital adequacy.

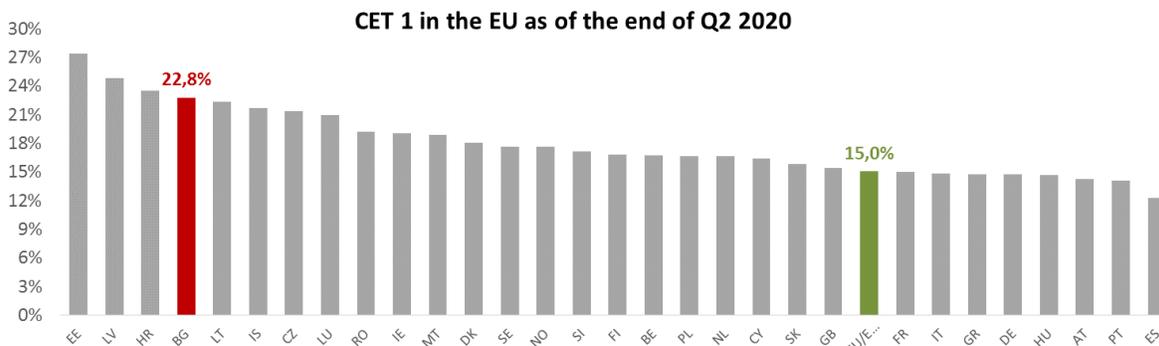
As of the end of Q2 2020 the common equity tier 1 (CET 1) of the whole banking system increased to 22,10% from 19,44%, as it was at the end of Q1 2020. For the first group of banks the level of the indicator increased to 21,69% from 20,09%, and for the second group – to 23,04% from 18,25%.

On a system level the total capital ratio for the Bulgarian banking system rose to 23,14% from 20,45%. As of the end of June 2020 its level for the banks in the first group was 22,37% and 24,94% for the banks in the second group compared to 20,78% and 19,85%, respectively, a quarter earlier.

The levels of the indicators for the capital adequacy for the banks in Bulgaria are above the average levels for the SSM banks, which according to the ECB data, as of the end of June 2020 were respectively for CET 1 – 14,87% and for the total capital ratio – 18,64%.



Source: BNB, ECB



Source: EBA, Risk Dashboard, Q2 2020

According to the BNB, the dynamics in the capital ratios was due to the regulatory changes, including the implementation of the International Financial Reporting Standard 9 (IFRS 9), accounting classifications, changes in the total amount of the risk exposures and in the total equity.

According to Regulation (EU) No 575/2013¹, in Q1 2020 a risk weight of 100% for the Bulgarian government bonds, denominated in euro, was applied, which led to an increase of the risk weighted assets. Meanwhile, in relation with the COVID-19 pandemic, in Q1 2020 the BNB announced [measures for the banking sector](#), one of which was full capitalization of the banking system's profit for 2019 amounting to BGN 1,6 billion. The decision of the BNB banks not to distribute dividends compensated the effect from the increased risk weight for the Bulgarian government bonds, denominated in euro, in the second quarter of 2020. The full capitalization of the profit is expected to be realized by the banks after receiving the related regulatory approvals.

¹ Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012



According to [the European Commission's decision from April 2020](#) for the so-called "Quick fix" of Regulation (EU) No 575/2013, part of the Commission's coronavirus response, in the field of banking sector, the Bulgarian government bonds, denominated in euro, were again treated as bonds in local currency, which means applying of 0% risk weight until 2023. This would lead to a decline in the risk weights of some risk weighted assets of the banks and respectively, to an increase of the capital adequacy.

Compared to the end of March 2020, according to the BNB data, the total banking system risk exposures declined significantly by BGN 6,1 billion (8,9%) to BGN 62,8 billion as of the end of June 2020. This decrease was mainly driven by credit risk exposures under the standardized approach (by BGN 5 billion, or 10%), reflecting to the highest extent the effect of Regulation amendments.

The share of the risk weighted exposures for credit risk in the total risk exposures fell to 90,9% at the end of June 2020 from 91,1% at the end of March 2020. The share of exposures to position, currency, and commodity risk decreased to 0,5% at the end of the period from 0,6% at the end of Q1 2020, while the share of risk exposures to operational risk increased to 8,6% from 8,3% three months earlier, the BNB data also showed.

Over the second quarter of 2020 the capital ratios developments were driven by the regulatory relief in response to the COVID-19 pandemic and the one-off transactions and events, including Expressbank merger into Bank DSK, reflecting on the amount of the total equity on group level.

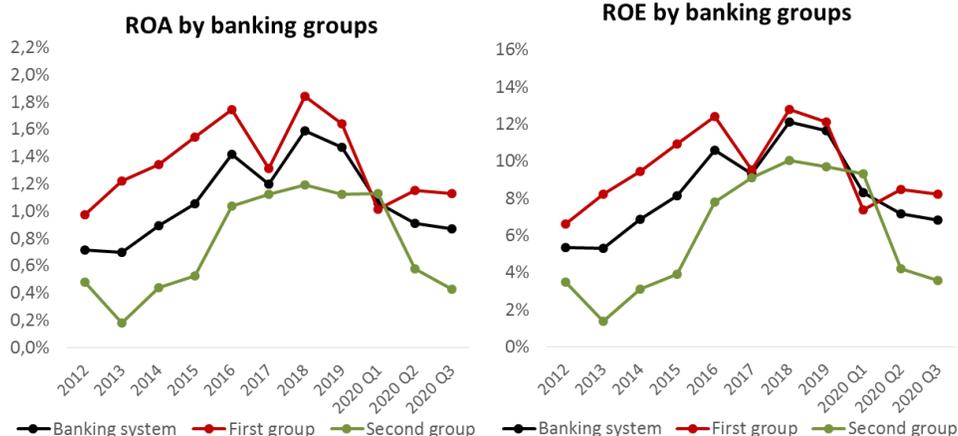
As regards the amount of the capital exceeding the capital requirements and the capital buffers, the BNB registered an increase over the quarter by BGN 1,4 billion to BGN 4,8 billion. This growth was supported by the decline in the total risk exposures and capital requirements and capital buffers calculated on that basis.



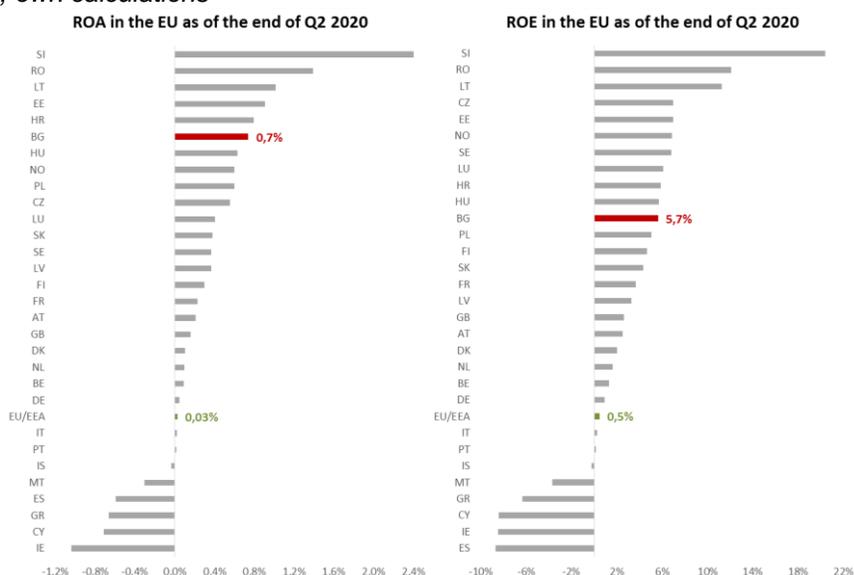
Profitability

As of September 30, 2020 the average Return on Assets (ROA) for the Bulgarian banking system was 0,87% compared to 0,91%, which was recorded as of the end of June 2020 (the average for the European banks was 0%, according to the ECB data for Q2 2020). The value of the indicator was 1,13% for the banks in the first group and 0,43% for the banks in the second group as of the end of September 2020.

The average Return on Equity (ROE) for the Bulgarian banking system was 6,81% as of the end of Q3 2020 compared to 7,15% as of the end of the second quarter of this year (according to the ECB data the average ROE for the European banks was 0,01% as of the end of Q2 2020). For the first group of banks in Bulgaria the ratio was 8,23% and for the second group – 3,55%, as of the end of Q3 2020.



Source: BNB, own calculations



Source: EBA Risk Dashboard, Q2 2020

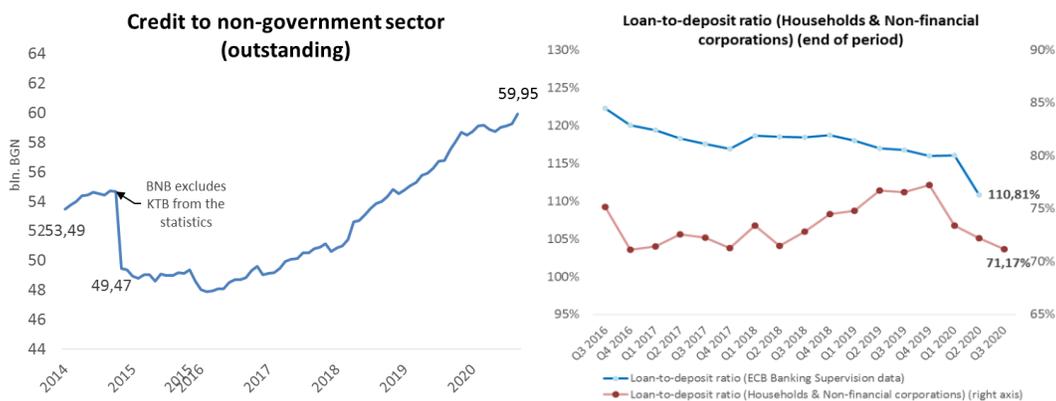
Note: On the graphs, the data for Bulgaria is based on the information submitted to EBA by four banks, and do not refer to the entire banking system



Loans and deposits

In its quarterly publication [Macroeconomic Forecast](#) the BNB projects, assuming that the pandemic will be gradually overcome, deposit growth to slow down slightly over 2021-2022 as a result of the exhausted base effect from the impossibility to consume during the state of emergency in the country and the increased savings rate for precautionary motives in 2020. According to the BNB, developments in loans over 2021-2022 will be driven by the expected gradual recovery of private consumption and investments.

As of the end of September 2020, according to the BNB monetary statistics data, the total outstanding amount of loans to the non-government sector (non-financial corporations and households) slowed down to 4,2% on an annual basis to BGN 59,95 billion, compared with the growth of 4,9% to BGN 5,02 billion as it was at the end of June 2020.



Source: BNB, Monetary Statistics, ECB, own calculations

In Q3 2020, by a decision of its Governing Council the BNB extended the deadline for submitting requests by bank customers under the submitted by the Association of Banks in Bulgaria (ABB) and approved by the BNB in April 2020 [Procedure for Deferral and Settlement of Liabilities Payable to Banks and their Subsidiaries – Financial Institutions](#) in relation to the state of emergency enforced by the National Assembly on 13 March 2020, and households and non-financial corporations took advantage of it.

As of 30 September 2020, 124 950 applications were filed consisting total amount of loans of BGN 9,998 billion as 106 481 applications for loans at the amount of BGN 9,023 billion were approved. Corporations submitted 14 343 applications amounting to BGN 7,711 billion, as 13 165 of them amounting to BGN 6,976 billion were approved. Households submitted 110 607 applications for BGN 2,267 billion, of which 93 316 amounting to BGN 2,047 billion were approved.

Compared to the end of June 2020, the total number of approved applications by corporations and households increased by 7 982, and the gross amount of approved liabilities subject of the private moratorium, within the meaning of the Guidelines of the European Banking Authority on legislative and non-legislative moratoria on loan repayments applied in the light of the COVID-19 (EBA/GL/2020/02), rose by BGN 906 million. The BNB data includes the borrowers that



applied for, and subsequently voluntarily gave up using the benefits under the moratorium, and also those for whom the grace period had expired by the end of September 2020.

As of the end of Q3 2020 the amount of non-performing loans (past due more than 90 days; excluding Central Banks and Credit Institutions) declined to BGN 3,723 billion from BGN 3,825 billion a quarter earlier. The share of non-performing loans in the banking system dropped to 5,45% from 5,71% as of the end of June 2020, according to the calculations based on the data of the BNB Banking Supervision Department.

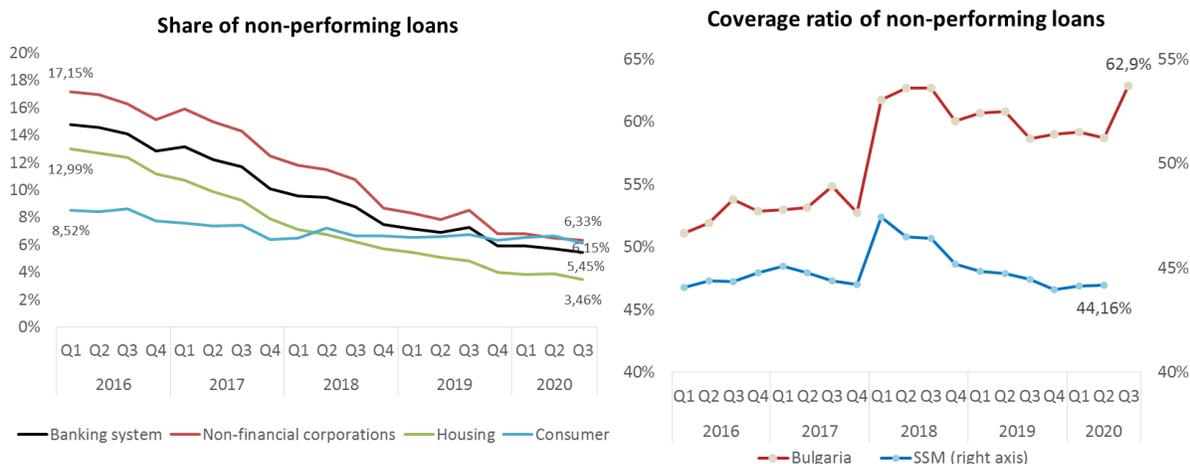
The share of non-performing loans to non-financial corporations declined to 6,33%, compared to 6,48% at the end of the second quarter of 2020. For the same period the ratio in the segment of housing loans decreased to 3,46% from 3,88%. The share of non-performing consumer loans fell to 6,15% from 6,63%.

At the end of September 2020 the amount of non-performing loans to non-financial corporations declined to BGN 2,342 billion from BGN 2,362 billion three months earlier. In the segment of housing loans the amount decreased to BGN 461,9 million from BGN 504,9 million. The non-performing consumer loans were at the amount of BGN 789,1 million, compared to BGN 833 million a quarter ago.

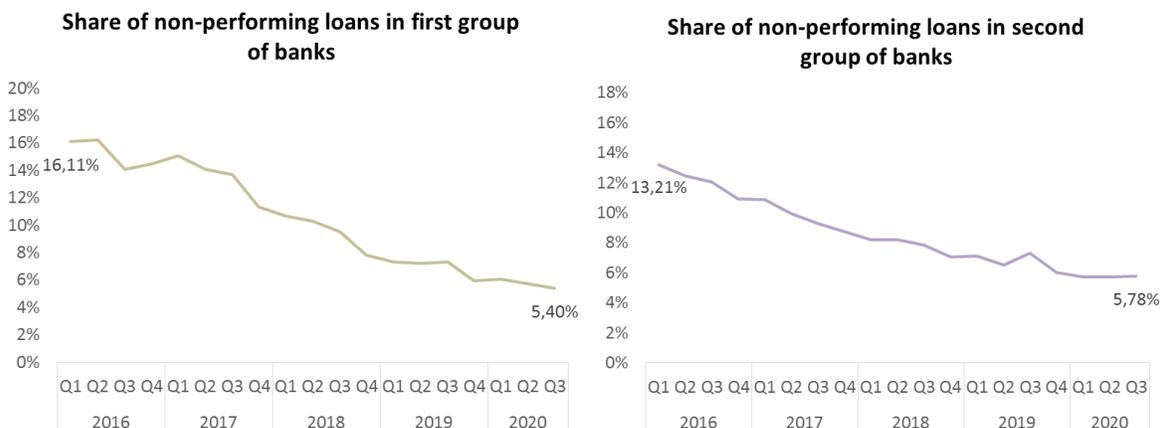
The level of non-performing gross loans reported by the banks in the first group declined to 5,4% as of the end of the third quarter of 2020 compared to 5,74% as of the end of Q2 2020. For the banks in the second group the level increased slightly to 5,78% from 5,73%.

Despite the higher level of non-performing loans compared with the average EU level, the coverage for gross non-performing loans by provisions in Bulgaria is higher compared with the average level of the EU countries.

The impairment coverage ratio of gross non-performing loans in the Bulgarian banking system was 62,9% as of the end of Q3 2020 compared to 58,7% a quarter earlier. For comparison, the coverage ratio for the European banks, according to the ECB data for the second quarter of 2020 was 44,16%.

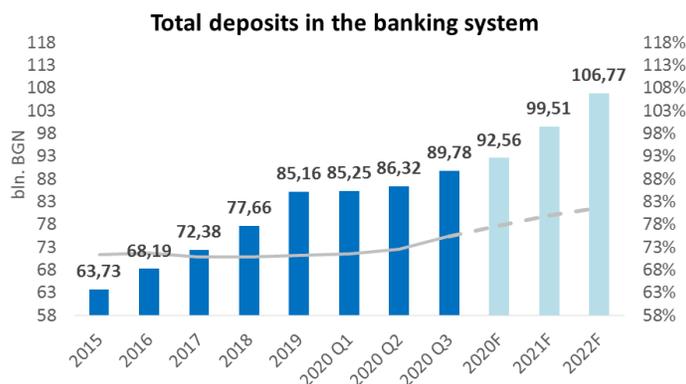


Source: BNB, ECB, own calculations



Source: BNB, own calculations

Deposits, attracted by the banks, continued to grow. As of the end of September 2020 the total amount of outstanding deposits in the banking system reached BGN 89,78 billion as an annual growth of 9% was recorded, despite the low interest rate levels. The deposits' growth was faster compared to the growth of 8,3% which was reported at the end of June 2020.

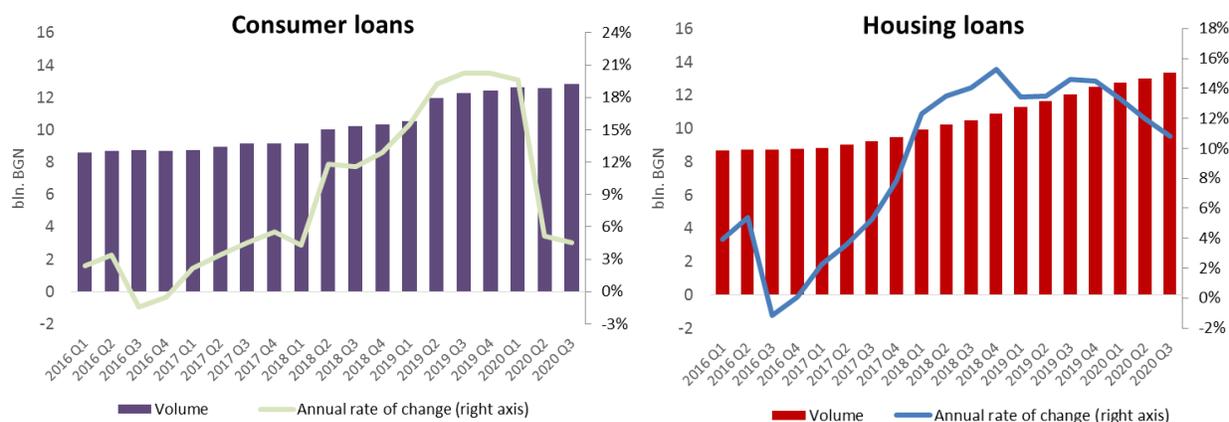


Source: BNB, own calculations, Forecast: BNB, Ministry of Finance

Loans and deposits to households

As of the end of Q3 2020, according to the data of the BNB Banking Supervision Department, the amount of consumer loans was BGN 12,82 billion compared to BGN 12,56 billion a quarter earlier and BGN 12,27 billion a year earlier. In Q3 2020 the amount of consumer loans grew by a slower pace of 4,5% on an annual basis and increased slightly by 2,1% on a quarterly basis (according to the data from the BNB Banking Supervision Department).

The amount of housing loans, according to the data of the BNB Banking Supervision Department, was BGN 13,33 billion compared to BGN 13 billion as of the end of Q2 2020 and BGN 12,03 billion as of the end of the third quarter in the previous year. The quarterly increase was by 2,5% and by 10,8% on an annual basis, which was slower, according to the BNB statistics.

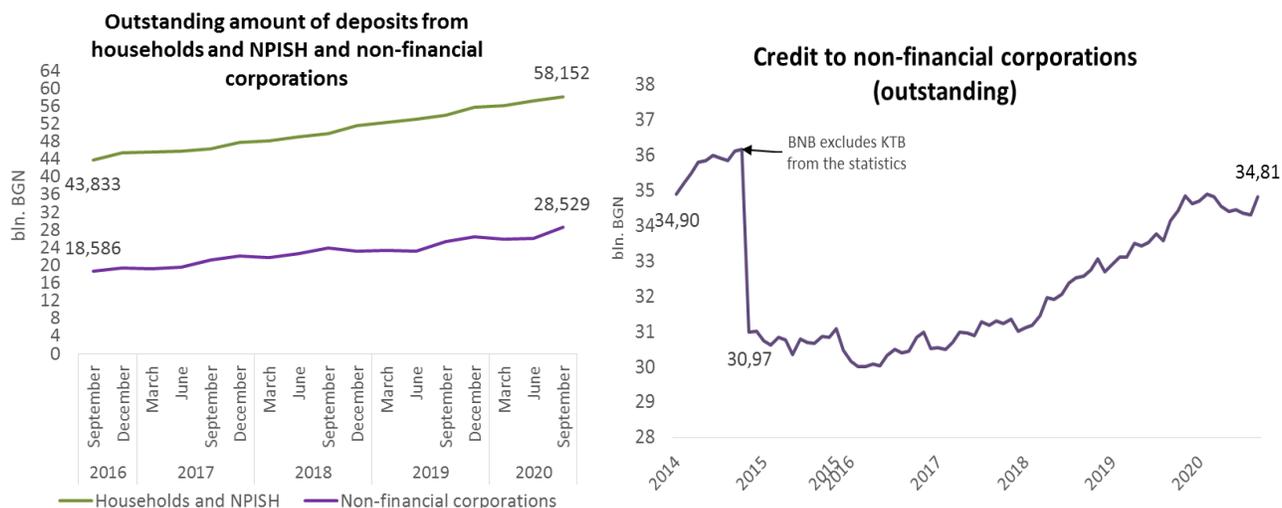


Source: BNB, Banking Supervision Department, own calculations

As of the end of Q3 2020 the total amount of deposits to households and NPISH grew by 7,9% on an annual basis after an annual increase by 7,8% at the end of June 2020. Deposits from households were BGN 58,15 billion. The share of the household sector in the total amount of deposits in the banking system was 64,8%.

Loans and deposits of non-financial corporations

As of September 30, 2020 the outstanding amount of deposits from non-financial corporations increased by 12,4% Y-o-Y, after an annual increase of 11,9% as of the end of June 2020 amounting to BGN 28,53 billion. The outstanding amount on loans to non-financial corporations grew by only 2% Y-o-Y to BGN 34,81 billion. Except overdrafts, loans to non-financial corporations slowed their pace of growth to 5,3% on an annual basis, reaching BGN 23,61 billion in absolute terms (after growth of 6,8% on an annual basis in March 2020).



Source: BNB, Monetary statistics



Interest rates

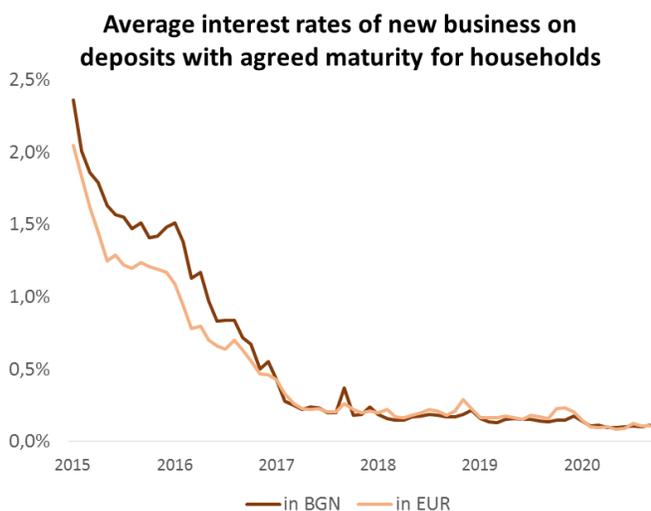
In its quarterly publication [Macroeconomic Forecast](#) the BNB assumes that after the phasing-out of the private moratorium on bank loan repayments in the light of the COVID-19 situation, a certain rise in interest rates on newly extended loans may be expected due to the increased share of non-performing loans in bank portfolios. The rise in risk premia due to the heightened uncertainty in the macroeconomic environment, the reduced creditworthiness of borrowers and banks' lower risk appetite, according to the BNB, could prompt an increase in lending interest rates and tightening of general standards and new loan terms.

At the same time, the BNB statistics showed that in the third quarter of 2020 the average interest rates on new housing loans and time deposits for non-financial corporations declined in comparison with the previous quarter, against the background of the reached low levels.

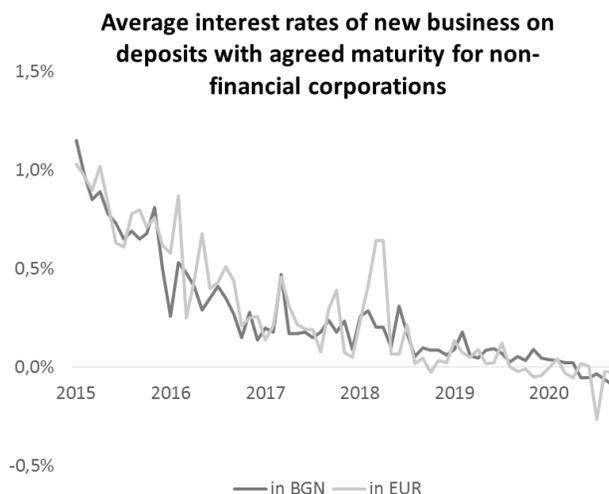
Interest rates on deposits

As of the end of Q3 2020 the average interest rates on deposits with agreed maturity to non-financial corporations on new business in BGN dropped to -0,09% from -0,05% as they were at the end of June 2020. Regarding the interest rates in EUR the BNB monetary statistics recorded an average level of -0,03% as of the end of September 2020 compared with 0,01% as of the end of June 2020.

As of the end of September 2020 the average interest rates on deposits with agreed maturity on new business in BGN to households increased slightly on a quarterly basis to 0,11% compared to 0,10% at the end of June 2020. The interest rate levels on deposits with agreed maturity on new business in EUR rose to 0,11% from 0,09% compared to the end of Q2 2020.



Source: BNB

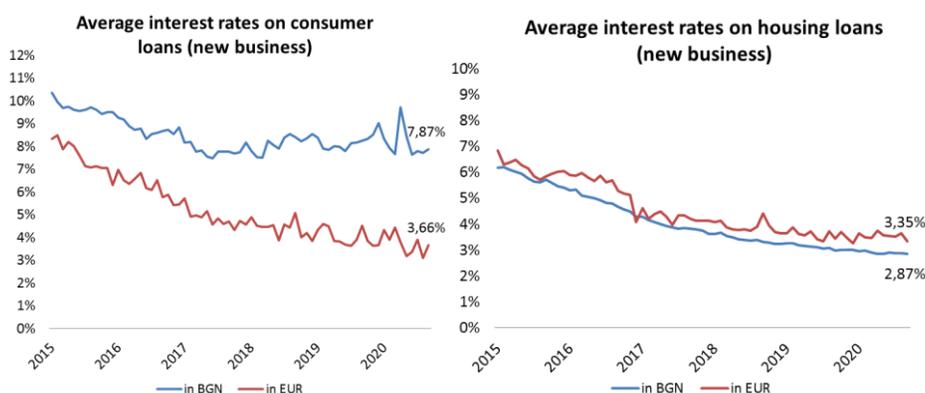




Interest rates on loans

As of the end of September 2020 the average interest rates on consumer loans agreed in BGN increased to 7,87%, compared to 7,65% at the end of the second quarter of 2020. The interest rates on consumer loans agreed in EUR rose to 3,66% as of the end of September 2020 in comparison with 3,36% three months earlier.

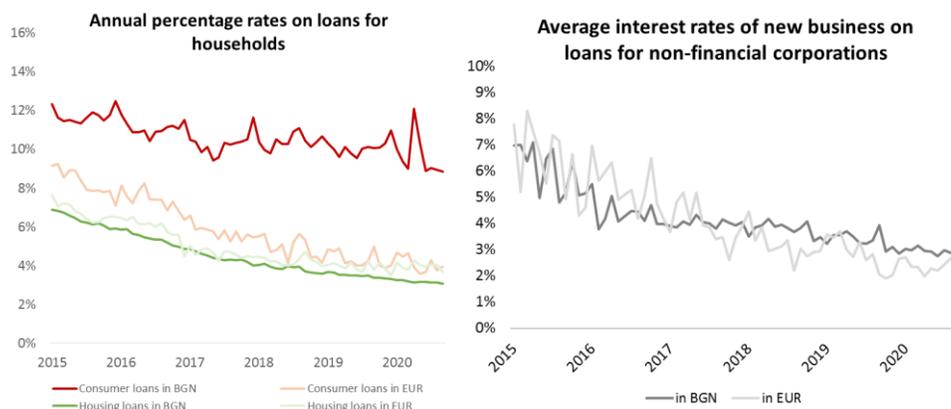
As of the end of Q3 2020 the average interest rates on housing loans fell to 2,87% for 2,91% for the loans agreed in BGN compared with a quarter earlier. For the same period the average interest rates on housing loans in EUR recorded a decline to 3,35% from 3,53%.



Source: BNB

As of the end of September 2020 the annual percentage rate (APR), which includes the interest rate component and the component of all other fees and commissions, dropped to 3,08% from 3,16% for housing loans in BGN and fell to 3,67% for housing loans in EUR from 3,94% a quarter earlier. The level of the APR on consumer loans was 8,85% and 3,94%, respectively, for loans in BGN and in EUR, compared with 8,87% and 3,69% three months earlier.

The average interest rates on new business on loans to non-financial corporations rose slightly to 2,80% for loans in BGN from 2,75% and to 2,26% from 2,20% for loans in EUR compared to the end of the previous quarter. The level of the interest rates for the loans to non-financial corporations agreed in US dollars increased to 3,01% from 2,04% a quarter ago.



Source: BNB



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All historical rates, statistical data and graphs are up to date, up to and including November 9, 2020, unless otherwise stated.

The views provided are those prevailing as of November 9, 2020.