

Ardian Fullani: Important issues for the future of the Albanian banking system

Speech by Mr Ardian Fullani, Governor of the Bank of Albania, at the Inter Balkan Forum of Banking Associations, Durrës, 20 May 2005.

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Ladies and Gentlemen,

It's a great pleasure to participate in this prestigious event of the banking system of Balkan region. My pleasure is great due also to another reason, because I had for years and years governed the Albanian Association of Banks and in addition I had given my personal contribution in initiating and organising this meeting in Albania. I would like to thank you again for having accepted today my invitation already proposed last year for organising this meeting in Albania. Of course, my delight is great but also my responsibility today to present myself as Governor of the Bank of Albania; therefore please consider me as being yours.

In this spirit, I would like sincerely to begin my speech with the wishes: successful and fruitful proceedings of the meeting.

Allow me first to tackle an important issue, which within the context of this meeting, I believe, is of paramount importance. **I mean by that the regional co-operation, an initiative that has been completely supported by the European Central Bank.** We have already taken the first steps in this regard through establishing bilateral relationships in banking supervision with National Bank of Macedonia, Central Bank of Montenegro and Banking and Payment Authority of Kosovo. Meanwhile, we are in the process of negotiating with National Bank of Bosnia and Herzegovina, National Bank of Serbia, etc. **I estimate that regional co-operation is an important forerunner of the integration process of the region with the rest of Europe; therefore I will not stop working to encourage a regional co-operation of high standards among the financial systems of Balkan countries.**

I hope that you share the same opinion with me, because only in this way, our region will be more credible and efficient to have its European dream. On the other hand, a developed and financially integrated region will be more attractive for foreign strategic investors, opening up the path toward regional development projects, particularly infrastructure ones where region's banks might be the financing and co-financing ones.

Further on I would like to give you an overview on some different issues of importance for the future of the Albanian banking system. In diverse meetings organised by the Bank of Albania with the banking community and other actors on relevant opportunities, a range of problems were highlighted and evidenced of which I think there is still room for a joint commitment, of both the Bank of Albania and, of course, the banking system.

In my capacity of Governor of the Bank of Albania I would like to ensure the banking community that the institution I govern is open for an institutionalised co-operation with the banking system by channeling it through the Albanian Association of Banks. We have a great consideration on this Association and we hope that its role will further be enhanced in the future, particularly on the principled topics that will characterize the development of the banking system and that of the financial system in general in the years to come.

Honored bankers,

I hope you share the same opinion with me that we become recently witnesses of a qualitative development of the Albanian banking system. I use the opportunity to express that positive assessments on the banking system have been given also in the report prepared by the World Bank and International Monetary Fund after the completion of their assessment made on the Albanian financial system (FSAP-Financial System Assessment Program). **Of course, this is good news.**

Conclusions of FSAP, of this important international passport, are an indication of our earliest conclusions that the Albanian financial system is characterized by a supervised and effective banking system and by other segments that are still in the first development stages where regulation and supervision remain a priority. Regardless of what I mentioned above, **sincerely feeling myself as a part of the banking system I would envisage that it needs better and faster motivation to reach higher contemporary standards in all the aspects of the banking activity.**

The banking system has experienced remarkable developments recently. After the licensing of Popular Bank, with Albanian capital, the number of banks increased from 15 to 16, and a preliminary license is granted to Union Bank (Albanian capital), which is expected to raise the number of banks to 17 over 2005. The system assets have further increased by 14 percent while there was an increase of banking products and an expansion of their network. During this year there will be sold the public shares of both the Italian Albanian Bank and United Bank of Albania, which will lead to an increase of effectiveness and banking competition, paving the way to the processes of selling, merging and acquisitions towards a new consolidation of the banking system.

The lending activity increased by 38 percent where one can distinguish, inter alia, the significant growth of medium-term and long-term loans compared to short-term loans.

The map of coverage of the country with the banking system has further expanded, including new areas ever covered before. At the end of 2004, the total number of branches reached 88, or 11 branches more than the end of the previous year, while the number of agencies recorded for the first time a full three-digit number, 100 and the number of the employed people increased by 26 percent.

The high increase of the number of branches relative to that of agencies shows that banks are not interested only in providing the service of collecting deposits but also in providing other products like crediting to the economy. **These developments, besides their positive contribution in enhancing the financial intermediation, speak for a better perception of investing potential from banks in Albania.**

An outstanding development is mainly related to the client service, which is accompanied through electronic terminals by the increasing number of electronic cards in circulation. Banks offer already debit and credit cards in co-operation with international companies such as Visa and MasterCard. **Six banks provide the ATM service and the number of ATMs reached 108 by the end of February 2005.**

The banking system results to have a profit level, which has been increasing to Lek 5.1 billion. Return on equity (ROE) was estimated at 21 percent while credit quality is only 4.2 percent from 4.6 percent in the previous year. In any case, we must say that credits are still new and do not have adequate history to show their performance.

However, problems and challenges, which the system is facing, are still enormous and in this context the role of the association of banks, I think, will be important to overcome them.

Credit to the economy and credit register

Credit to the economy has recently known a great development. High growth rates impose us to be prudent in the other direction, that is portfolio quality. Enhancing competitiveness and consequently, enhancing the credit level is bringing about a rising trend of weighted risk assets and some banks are already close to the minimum level of 12 percent.

The client's identification on receiving and using the credit and other obligations he/she has to the banking market is vague, incomplete without giving the opportunity the banking system to have a history on the client's activity. That's why I believe that a centralized register, which unlike the previous years became now a necessity, is needed.

I would like to highlight that Bank of Albania has included the project of establishing the credit register in its short-term plans and we are deeply committed to execute it within the next year. I use the opportunity to emphasize that this register will be under the administration of Bank of Albania and the participation of banks member of the system will be compulsory. Only in this way, **evasion in the statistical information will be avoided, its integrity will be ensured and at the same time available for each bank member of the system.**

On the other hand, we are aware of the fact that issues dealing with credit are more complex. They have to do with many other obstacles that arise from lack of collateral register, inaccuracy of mortgage, lack of knowledge and the non-functioning on a correct basis of the judiciary system and law, particularly with regard to technical problems that relate to the knowledge and execution of collateral.

For this purpose, we shall take the initiative to set up an ongoing communication with the judiciary system, with the intent to organise an open conference in autumn of the current year.

The main objective remains enforcing legal initiatives that would bring about the modification of legal and sub-legal basis.

Modification of regulatory basis of Bank of Albania

I have stated even previously that Bank of Albania aims at reviewing its regulatory basis with the sole intent to simplify it and to ease its implementation.

For this purpose I have insisted on a continuous basis that the first contacts among mutual technical staffs to raise the banking system concerns on the regulatory framework enforcement should be established.

After several discussions we come to the conclusion that the group of the following regulations should be subject of necessary modifications, and I would ensure you that work at the Bank of Albania has already started for this purpose.

Methodical guideline on “foreign exchange risks”

Observations: inclusion in the calculation of the open position of off-balance guarantees which include as unused credit limit, the financing commitments made and received, and registering of collateral estimated in foreign currency and received for guaranteeing the credit (all banks in the matrix). These are commitments that remain in force and for which, according to the current regulatory framework interpreting, the bank is required to create a real position (within the balance).

It is proposed: to reformulate the methodical guideline, excluding the guarantees.

Guideline “on bank regulatory capital”

Observations: To make clearer systemization for the items being deducted from the additional capital, explaining that on which size deductions are to be calculated. To make clearer in the regulation even the inclusion of yearend profit in the regulatory capital only after confirmation from the certified public accountant and by approval from the Audit Committee.

It is proposed: to take into consideration both observations and submit a draft-decision for changing the regulation.

Regulation “on capital adequacy”

Observations: Classification of countries where reference is made to OECD member countries is a bit confused and another time, a list of 29 members is presented, while collateral in cash is not taken into consideration as a deductive element in the calculation of weighted risk assets. Concept of mortgaged credits that are weighted by 50 percent is very restrained and subject of confusion.

It is proposed: to take into consideration the observations and submit a draft-decision for changing the regulation.

Regulation “on market risk”

It is proposed: to review it in the framework of new recommendations of Basel II.

Focusing again on the problem of banking supervision I would like to underline that we, Bank of Albania as a supervisory institution, are determined to have at a possible maximum level a simple and easy supervision for being implemented, associated with a significant improvement of the on-site inspection. We shall intend that expectation and prevention power of our supervision gains new dimension. To this end we are in a process of finalising the negotiations with European partner institutions for launching a twinning project for the further consolidation of supervisory capacities of the Bank of Albania.

Anti cash campaign

Recent developments have impacted cash reduction in the economy. On the other hand, we have carried out an intensive public activity, of clarifying and promoting nature where meetings of another

nature were held too, in which we, all of us as a banking system, have been concretely engaged. Allow me to remind you the meetings we have organized with business and utility services business and also that on the primary market of Treasury bills.

Using this opportunity I would like to bring again to your kind attention the problems raised even beforehand. I hope that now, on the eve of finalising the Automated Electronic Clearing House project, each bank separately and the Association itself are seriously thinking to raise the profit level from this facility that Bank of Albania offers in this moment. **I would appreciate if from the Association will have some comments or potential reactions on the system preparations and the possible assistance and co-operation of Bank of Albania in this direction.**

After the completion of this project, I deem that we must think more seriously about the numerical and qualitative addition of electronic payments. For this purpose I would envisage to start thinking from now about future projects in the payment infrastructure. I personally will insist that even in this direction all of us as a banking system look forward to the European Union directives, in order that each future step is oriented toward the country integration in the European Union.

Few times ago, I have been informed about a new EU initiative, which requires to set up, within a certain period of time, among others a unified payment system within the euro area, including payments with cards. Presently, small and medium businesses in the euro area have not the same payment opportunities as they have in their respective countries on a national scale. Such a case includes credit cards, which cannot be employed equally across the borders. For this purpose I would suggest that respective experts from the Association and Bank of Albania be as soon as possible informed about this project, making the relevant suggestions in this direction. **I personally remain consistent in my position that in Albania we have to adopt the most advanced solutions in all the infrastructure projects that we are going to implement.** I believe that we do not need to examine old-fashioned models, which, in addition to the initial cost, will continuously require other funds for maintenance and modification.

Besides the developments in the field of payments I would welcome from you a broader commitment even in other directions. **I think that the system must further expand its geographical coverage, aiming at including also areas, which, though having at first sight the appearance of being inactive, have large financial potentials in the form of thesaurised savings outside the system.**

Also, the service level should be further improved. **Now the public administration has become a client of the system and I think that there are real opportunities to resolve the utility services payments through the banking system.**

Also, **I hope that the system will be aggressive and will keep promises to the public to put its windows at the service of selling Treasury bills directly to the interested public.** We, as Bank of Albania, have kept our promises and very soon **we will introduce as a first step a commission that is presumed to cover the transaction cost while we will accompany this move by the ban of cash flows receipt at the windows of Bank of Albania.** We shall request the individuals that their participation in the auctions, through windows of Bank of Albania, will become possible only upon presentation of a banking document, which certifies that the client has deposited a certain amount as a guarantee in one of the banks pertaining to the system.

Another direction on which banks must further focus relates to an aggressivity of broader propaganda and clarification. I think that still the majority of common people show a certain hesitation to refer to banks. I believe that they have a feeling of non-confidence that the bank shall not resolve their problems. Many individuals, though in an absurd way, are still in search of a "friend" to negotiate with the bank.

As mentioned above, I understand that above all the reason behind might be our poor tradition in addition to the high degree of informality and a lot of other objective and subjective reasons. However, I think that the cause might be even the lack of detailed clarifications, and lack of informative publications, and lack of the propaganda in the public environment as well as in media.

I think that in the propaganda spaces in the media more space should be given to the clarifications of special products, while launching of new products should be accompanied by standard advertising campaigns.

Dear participants,

Allow me that before closing my speech to express again my high appreciation on the Albanian Association of Banks, ensuring that Governor of Bank of Albania will always be its decent partner in the long path of institutional co-operation.

I sincerely hope that this meeting of banking associations is an important step towards establishing a fruitful regional co-operation.

I am personally committed, in future contacts with my colleagues of the region's countries, to dedicate a special room to this co-operation, hoping that I will find on them a well-understanding and full support.

I again wish you successful and fruitful proceedings of this meeting.

Thank you.