

## **Ardian Fullani: Competition versus risk-taking in the banking sector in SEE countries**

Speech by Mr Ardian Fullani, Governor of the Bank of Albania, at the conference on “Competition versus risk-taking in the banking sector in SEE countries”, organized by the Central Bank of the Republic of Kosovo, Prishtina, 5 October 2012.

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Honourable Governors,

Dear participants,

Regular regional meetings are a good opportunity to discuss economic and financial developments in our countries. They help identify the similarities and differences among us, and the economic and financial policies we need for solving the problems we encounter.

The geographic position and economic relations with the same trade partners are factors that have led to similar economic and financial developments across our countries. They have determined the nature and size of contamination from the global economic crisis, in general, and the euro area crisis, in particular.

The impact of the crisis on our countries has often been the main topic of discussion in such meetings. Macro-financial difficulties and uncertainties in the euro area render the actual European crisis the main focus of this meeting as well.

Actual operations and commitments of the European Central Bank consist in a wide range of instruments that European authorities may use to support financial markets and institutions. Investors, however, are still waiting on additional decisions which will be more harmonised and stronger politically. The economic situation, especially in Greece and Spain, remains difficult, whereas Portugal and Italy have undertaken additional fiscal consolidation programmes. Unemployment in the EU and the euro area has reached historic levels, especially amongst the youth. Economic growth is weak and is mainly concentrated in central countries of the euro area.

Our countries have been affected by this situation for objective reasons. Trade relations, movement of capital and workers, and the financial system are channels that pass these problems on to our economies. The form, size and extent of this impact have evolved over the past four years.

At present, the situation is reflected in the decrease of domestic demand, decline of economic growth, reduction of available income, loss of confidence and deterioration of optimism; this is, in turn, reflected in higher savings.

Consequently, these developments have placed the focus of economic policies towards economic activity and revitalisation of optimism in order to boost investments and consumption. On the other hand, maintaining financial stability becomes a necessity, creating thus a binomial of priorities that condition each other and require a simultaneous solution.

The Albanian economy is increasingly facing the challenge of economic growth. Although the Albanian economy enjoys consolidated macroeconomic stability and sound financial foundations, aggregate demand has been weak during the first nine months of 2012. Both domestic and foreign demand suffer from high uncertainty, relatively tight lending standards, and limited space for discretionary and stimulating policies.

In the domestic context, the economy continues to face relatively low consumption and private investments and an absent stimulus by the public sector resulting from the orientation of the fiscal policy towards maintaining long-term stability of the public debt.

On the other hand, the banking and financial system remains sound and liquid and capital indicators are at relatively satisfactory levels. The activity of the banking sector continues to be strongly supported by the increase of public's deposits. Banks have reinforced their capital position to boost resilience against risks arising from banking operations. As at the end of June 2012, the capital adequacy ratio stood at 15.6%. Credit developments, however, remain a problem that is subject to the performance of economic activity and expectations for the future.

Slowdown of economic activity and decline of demand for investments and consumption by businesses and households are determinants of private sector credit and credit quality performance. On their side, banks have evidently increased their prudence as regards lending.

Periodic stress tests show that the banking sector is resilient and can withstand any adverse events to economic performance. However, we are aware that the banking industry is facing difficult challenges. Besides recovery of economic activity and confidence for the future, improvement of credit quality requires also the completion of legal issues to enable and facilitate collateral execution. Selling impaired assets at their real market value is the starting point of the process for making financial correction and enriching the private sector's balance sheets and the financial system a whole. Cleaning up balance sheets would promote economic activity through consumer investments, by ensuring a constantly improved credit quality.

Currently, the mutual influence of economic activity and credit quality is the main concern to monetary policy. Efficiency of successive interventions by lowering the key interest rate is overshadowed by negative expectations.

Consequently, the effects of business and household consumption and investments on domestic demand are not at the desirable level. In spite of these problems, economic growth remains in positive territory, but below the potential. According to our estimates, it will remain positive even in the future. Economic and financial operators' inflation expectations remain anchored around the Bank of Albania's target.

Good liquidity condition and capitalization of the banking sector, and stability of macroeconomic indicators have led to harmonised economic policies for maintaining the status quo. If this situation remains as such in a predictable time horizon, the monetary policy may remain accommodative over the same period. The recovery of the domestic demand and economic growth is further related to expectations, which are also affected and contaminated by our trade partners' condition.

The fiscal policy has aimed at fiscal consolidation and has continued making efforts to prudentially provide necessary fiscal stimuli.

Currently, if the privatization process is successfully completed, then the fiscal opportunities for promoting economic growth and for revering any negative expectations are significant. The way of using privatization receipts should not only support the short-term economic growth objectives, but should also affect the economic operators' expectations for stable economic growth in the future. The latter can be achieved by using additional revenues to reduce debt levels and support reforms for structural changes in the economy.

Dear participants,

Currently, we are of the opinion that the concept of long-term development strategies of a deeply national character is an important issue for the stable long-term growth in our region. Lacking a regional perspective does not favour the individual success of small economies in the global economy.

The process of connectivity and integration of transport infrastructure should continue with the integration of development strategies, capital markets, the labour and primary commodities, and energy infrastructure. Our economies are vulnerable and contaminable

from global developments because they are small economies in an economic region fragmented and dependent on foreign inflows in the form of investments, exports and remittances.

Increase in the market share, ease in production factors mobility (capital, labour, and raw materials), integration of financial and payment systems, integration and coordination of scientific and educational curricula and addressing of challenges from a regional perspective would make the region an attractive and integrating economic place. This integration would identify the comparative regional advantages, enhancing at the same time the competitiveness of each of our economies.

Consequently, it would convert the tendency of the region to be negatively contaminated from global developments into an opportunity, a positive impact, in order to achieve high and stable economy growth in the long run.

Thank you!