

Ardian Fullani: Achievements and challenges facing the Albanian banking sector

Address by Mr Ardian Fullani, Governor of the Bank of Albania, at the year-end event with the Albanian Association of Banks, Tirana, 20 December 2012.

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Dear bank managers,

At the end of this calendar and financial year, I take this opportunity to share with you some of the achievements and challenges facing the banking sector, confident that they will serve to guide our actions in the future.

As expected, the year 2012 was a very challenging year for the financial and economic activity of the country and of various economic agents. Very likely, this year's economic growth will remain positive, but significantly lower than last year. This economic performance is dictated by the weakening of the fiscal and monetary stimuli, as well as the slowdown of private investment and consumption. The slowdown in the latter is, however, accompanied by a reduction of imports. On the other hand, foreign demand has supported higher growth of exports, especially of energy products. This has led to an improved trade balance during 2012, hence marking a decrease in the deficit-to-GDP ratio. The impact of the global economic crisis continues to be present and its prospects to overcome it in 2013 remains our hope, which is not supported by the expectations of international financial institutions and public authorities, especially with regard to the economic situation in the euro area.

During 2012, the banking sector marked a positive financial result, overall. Net interest income was stable but provisions on credit risk reduced the size of profit. Generally, the banking sector maintained control over other costs of the activity. Liquidity indicators, short-term and structural ones, stand at satisfactory levels. All banks complied with the requirements set out in the regulatory framework regarding the size of liquid assets, both in the lek and in major foreign currencies. Deposits continued to grow at good rates, although at lower levels than in the last year.

Due to the credit growth slowdown, the credit/deposit ratio appears at very suitable levels to support the liquidity needs of the sector. Indicators of activity capitalization stood at good levels, due to capital increase by some banks and slowdown in risk-bearing assets growth. In the course of the year, the Bank of Albania applied tighter requirements for liquidity and capitalization of banks in accordance with the risk profile of their activities.

In the interbank market, trading volumes and participation increased in the 2012. This performance is influenced by structural liquidity movements, banks demand and market operations of the Bank of Albania to support them.

Market interest rates were downward, reflecting the trend of policy interest rate and banks' actions to control operations costs and profit margins. The foreign exchange market has been stable, despite increasing trading volumes and higher number of participants in the market. Banks were active and prudent in servicing their clients' demand for foreign currency.

Dear bank managers,

Let me now focus on a number of issues of concern to the banking industry and the Bank of Albania, which we believe should be addressed carefully during the next year.

I would like to start with lending as the activity that has the main impact on the banks' financial result. We find that lending growth rates decreased and credit quality continued to deteriorate, particularly for foreign-currency denominated loans. This performance is due to the fall of demand for loans; however, it also reflects a persistent reluctance of banks to lend.

This trend needs to be reversed by addressing problems related to the pace of lending and non-performing loans.

The stable growth of deposits as well as the significant increase in non-residential investments show that banks have sufficient financial resources to lend at higher growth rates. These resources should be used to lend mainly to the private sector in Albania, acting in accordance with the established regulatory framework and your policies for investment diversification. On the other hand, efforts to address the non-performing loans should multiply, in terms of both prevention and addressing them properly. Your focus should be placed on the cautious process of loan restructuring, especially before such loans are transformed into non-performing loans. Further, you should act discreetly, but consistently, for the execution of collateral. We are all aware of the problems that exist in this area. Nonetheless, also thanks to your work, I find that the awareness of decision-making public authorities in this regard has improved significantly. I had the opportunity to communicate about these issues today to the parliamentary, Commission of Economy and Finance. I am confident that the work started by the Ministry of Justice for the revision and improvement of some important legal acts, including the Code of Civil Procedures, will be finalized, incorporating and approving some concrete proposals for amendments submitted by the banking industry and the Bank of Albania in order to enhance the process of collateral execution.

In addition, upon the conclusion of legal processes, it is pivotal to proceed swiftly to write-off loss loans from the bank's balance sheets, in accordance with the requirements of the regulatory framework. We would kindly ask you and your shareholders for dedication in this process, not only to find the necessary human and financial resources, but also the most appropriate forms for a quick, transparent, and consistent handling of non-performing loans.

We need to bear in mind that lending carries along risks that are difficult to identify at the time of disbursement. These risks are determined not only by the quality of bank lending procedures, but also by significant external factors, including the performance of the economy. This uncertainty permeates the current phase our banking sector is going through. Therefore, it is indispensable that bank management structures and their shareholders commit the necessary financial resources to cope with the possible additional costs in the future. For shareholders, this implies not only retention of profits in the bank, but also adding new capital in case of need. Remember that it also represents a more general trend in the banking industry globally, with a number of new forthcoming standards that provide for improving the quality of bank capital and increase of its size. Our banks should gradually begin to adapt to these new standards.

For senior managers, strengthening the control systems of the bank activity remains a primary objective, especially for those activities that generate the main revenues and expenses arising from the activity. Risk management structures should be really empowered and have a stronger voice in decision-making. Banks should continue to further improve the efficiency of their operations, including the establishment of a better control over the costs of the activity. Setting priority activities for your institution will allow you to identify new investment needs as well as those activities that use bank resources inefficiently; they should, in turn, be restructured. This process will positively affect the financial performance of the institution, and will allow the implementation of other active policies in areas that benefit the activity of the bank.

We all know that banking is an activity based on trust. For this reason, the bank's services to customers should be "first class" across the entire bank network. This means that customers should be served correctly, timely and transparently. Banking services should be provided in accordance with the clients' financial literacy, in any case highlighting, the benefits and the risks that customers may incur as they use your bank products.

In the context of its role as the supervisory and regulatory authority of banking operations, the Bank of Albania will continue to carefully monitor and address the challenges facing this

activity. Our regulatory framework and supervisory and operational activities will be adapted to provide all the necessary support for the banking activity to be safe and have multiple benefits for the banking industry, customers, and the economy in general. The professional and continuous communication with you will be at the basis of our activity, to identify together the best solutions that address your needs and those of other interest groups.

Dear bank managers,

In conclusion, I would like to bring to your attention one of the biggest lessons learned from the crisis of the latest global financial system, which I think remains applicable for Albania: concentration on short-term time horizons is counterproductive to both individual financial institutions that engage in them, and the overall financial system and economy of a country. In this context, I invite you all to be farsighted in your analyses and decision-making processes with regard to the future of the economy of Albania and its banking industry.

In my view as well as in the conclusions by all the analyses that focus on this issue, Albania has huge potential, to a large extent unutilised, to support a sustainable economic growth, convergent to the economies of our trade partner countries in the euro area. Despite short-term difficulties, originating largely from external sources, the fundamentals of Albania's economic development remain sound. The macroeconomic stability, natural resources, structure and cost of the labour force, render the long-term investment in the Albanian economy an investment with a guaranteed return.

I invite you all to partake in this vision; engage even more intensively in supporting the Albanian economy with loans and financial services; and explore new areas and directions for the country's economic development. I am confident that this is not only the best service you may provide to Albania, but also the best strategy to ensure sustainable and profitable development of the banking industry in Albania.

In unison, we should not allow short-term problems to be transformed into weaknesses and lost opportunities in the long run.

You will always find in the Bank of Albania an institution that is fully determined to comply with its objective on price and financial stability; a fair and farsighted regulator on banking supervision; an efficient administrator of liquidity and financial markets; and a profoundly professional institution and provider of useful macroeconomic analyses.

Finally, I would like to make my most sincere wishes for a successful New Year 2013 in your professional career and personal life!

Thank you.