Jorgovanka Tabaković: Annual Financial Stability Report for 2015

Speech given by Dr Jorgovanka Tabaković, Governor of the National Bank of Serbia at the presentation of the Annual Financial Stability Report for 2015, Belgrade, 27 July 2016.

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Ladies and gentlemen, esteemed members of the press and fellow economists,

Welcome to the presentation of the *Annual Financial Stability Report for 2015*. If we call last year's presentation of this Report history or our firstborn, then today's press conference can be regarded as the start of tradition and continuation of good international practice. Macroprudential policy or the policy of safeguarding financial stability has been the focus of almost all economic discussions since the outbreak of the global financial crisis. The National Bank of Serbia does not lag behind other central banks in this respect. Quite to the contrary, we are keeping up with them. The depth of our analyses and the expert approach place us among the most efficient central banks in terms of achieving the financial stability mandate.

We have been witnesses to turbulences in the international environment for quite some time already. The ripple effects of these turbulences did not by-pass Serbia as an open and small economy. However, we did not stand by and wring our hands, waiting to be hit by the waves of uncertainty from different continents. In coordination with the Government of the Republic of Serbia, we responded with timely action, carefully assessing the intensity of all influences. Through synchronisation of monetary easing and consistent fiscal consolidation, we have maintained price stability, reduced external and internal imbalances significantly and improved further the conditions for sustainable economic growth. As a result, the key policy rate is at its historical low since the introduction of the inflation targeting regime and the fiscal deficit is at its lowest level since 2008.

I will take the liberty of saying that the monetary policy easing of the National Bank of Serbia has paved the way for a sharp drop in interest rates on dinar loans in the last three years. To put this into numbers – from May 2013 until today, the key policy rate was cut 17 times by a total of 7.75 pp to 4%. That the interest rate channel is working in the dinar segment of the market is confirmed by the concurrent decline in interest rates on dinar loans to households and corporates by almost 10 pp to the lowest levels on record. Interest rates on government dinar securities also declined. Since November 2014 we have also reduced the FX required reserve ratios by a total of 9 pp, with a view to unlocking the credit potential of banks. Lower costs of borrowing and the funds released as a result of reduced FX required reserves, together with a pick-up in economic activity, supported the recovery in lending activity in the second half of 2015, and we all know that lending is an important prerequisite for a sound financial system.

There is no particular need to underscore that in euroised economies such as ours the relative stability of the exchange rate and increased use of the national currency are the cornerstone of financial stability. The implementation of the Dinarisation Strategy therefore remains one of our priorities. It is exactly in the area of macroeconomic stability, which represents the first and most important pillar of the Strategy, that we have achieved significant results. Household dinar savings are now around 3 times higher than at end-2012. More than two-thirds of new household loans in 2015 were in dinars, while the figure is even higher this year (over 70%). We are pleased to see that the results of the National Bank of Serbia – low inflation, relative stability of the exchange rate and the sharp fall in interest rates in the dinar market – have kickstarted the process of dinarisation.

The committment and effectiveness of the National Bank of Serbia in maintaining financial stability is reflected also in easing the pressures from strong international turbulences and averting them from our financial market. You will allow me once again to step out of the time frame covered by the *Report* presented today and to touch upon the present. This is a way to show that time has not stopped and that we are discussing and monitoring stability all the time, without limiting ourselves to the span of one year.

After persistent pressures in the foreign exchange market late last year and in the first half of 2016, it took another huge shock, such as Brexit, to clearly demonstrate to everyone the importance of the National Bank of Serbia, its commitment, role and contribution to stability. The National Bank of Serbia, with the huge support of the President of the Government of the Republic of Serbia, took a proactive, efficient and impartial approach. The quality of our presence in the market improved, our interventions became more efficient, our communication with all market participants enhanced, as did our coordination with the Government. International portfolio investors confident in the central bank and the Government, that is confident in financial and political stability, show they are prepared to make long-term investments in dinar government securities.

And just what amount of FX reserves was spent in 2015 and 2016 to preserve this stability? In those 19 months, the dinar weakened by 2%, while in cumulative terms, foreign exchange interventions drove up the level of FX reserves by EUR 25 million. We managed to do this by intervening in the foreign exchange market proactively, cost-efficiently and effectively (I dare say, with filigree precision).

You will hear from my colleagues today that our banking sector has remained stable and resilient to shocks from the international and domestic environment despite the numerous challenges it faced. The results of macroprudential stress tests we carry out on a quarterly basis confirm that the banking sector remains well-capitalised and highly liquid even in the case of extremely pessimistic assumptions which did not materialise even at the height of the global financial crisis.

High capital adequacy of the Serbian banking sector was re-affirmed by the special diagnostic studies of the quality of bank assets in Serbia. It gives me great pleasure to repeat once again that no capital shortfall was identified in any of the 14 in-scope banks which account for 88% of banking sector assets.

Still, like in most regional peers, resolving the high level of NPLs remains a priority. For this reason, the National Bank of Serbia took an active part in developing a comprehensive Strategy for NPL Resolution and adopted an Action Plan for the implementation of that Strategy. The first results are already visible as the share of NPLs in total loans decreased during the first five months of the year by 1.3 pp to 20.3%. Let me remind you that during this year's ministerial dialogue the European Commission and the ECB commended the systematic and comprehensive approach of the NBS and the Serbian Government to NPL resolution, and recommended the implementation of our NPL resolution process to other candidate countries.

Ladies and gentlemen, esteemed members of the press and fellow economists,

The policies pursued by central banks nowadays and ten years ago are not the same. They change and adjust to market conditions, specificities of local economies, capital flows...but almost invariably they have the same goal – to maintain stability, both price and financial.

Confucius said, "The superior man is modest in his speech, but exceeds in his actions." We will therefore let others speak about us, those others being unbiased appraisers such as the ECB, the European Commission, the IMF…

And yet, we will not let their praises lull us into a false sense of security, but will as so far remain vigilant and ready to take proactive measures and preserve the stability achieved.

Thank you for your attention. I now give the floor to Vice Governor Diana Dragutinović.