Dimitar Radev: Positive trends in the banking sector are expected to continue in 2019, however with possible increased challenges

Publication by Mr Dimitar Radev, Governor of the Bulgarian National Bank, in the Quarterly Bulletin of the Association of Banks in Bulgaria, issue 56, January 2019.

In 2018 the banking sector continued to maintain high level of capital adequacy and liquidity, also generating historically high annual profit. Deposits in the banking system increased, lending grew, and the share of nonperforming loans dropped. We expect these positive dynamics in the sector to continue altogether through 2019.

Loan portfolios are a primary source of operating income for the banks in Bulgaria, but credit growth is by definition associated with assumption of new risk. At this stage of credit expansion, banks should continue making adequate efforts to manage the credit risk accumulating on their balance sheets.

Large part of the central bank’s recent activities, in our capacity as a regulator and supervisor of the banking system, is focused on the risk associated with bank lending. The BNB Governing Council decided to activate the countercyclical capital buffer from this year. In December 2018, the National Assembly passed new legislative amendments, proposed by the BNB, which provide us with an additional macro-prudential toolbox of measures regarding bank lending. It includes for example BNB’s new powers to require enforcement of limiting the loan-to-value ratio or the debt-to-borrower’s income ratio.

The probability of realization of credit risk would grow particularly in an economic slowdown or a situation less favourable than the one observed in the recent years. Presently, we see growing indications of possible problems and increased uncertainty – globally and in the euro area – which could, through certain channels, bring negative effects domestically.

From the perspective of the sector, 2019 will also be dominated by the asset review and stress test in several banks. We are at the stage of finalising the preparations for the practical implementation of these processes. They are under the lead of the European Central Bank, but with the active cooperation of the BNB.

The asset review, stress test and synchronization of our supervisory practices with the European Central Bank are a very important, though not the only, element of the efforts associated with Bulgaria’s plans for entry of the Bulgarian Lev in the Exchange Rate Mechanism (ERM II) and Bulgaria’s accession to the Single Supervisory Mechanism. These strategic steps should be made simultaneously, according to the plan and the agreements reached with our European partners.

In 2019 we expect the positive trends in the banking sector to continue altogether, however with possible increased challenges associated with the general economic environment banks operate in. Concurrently, in the coming months we will evidence processes of potentially long-term consequences directly impacting the sector, aimed at achieving a qualitatively higher degree of integration of Bulgaria into the European financial and institutional infrastructure.