Dimitar Radev: Responding to policy volatility – the outlook for public investors

Speech by Mr Dimitar Radev, Governor of the Bulgarian National Bank, at OMFIF-State Street Global Advisors, London, 15 May 2025.

* * *

The defining feature of our current environment is volatility. It dominates economic briefings, investment strategies and global outlooks.

This volatility is not just market noise. It signals deeper, systemic shifts. We are no longer navigating temporary dislocations. We are operating in a fundamentally more uncertain world. Policy itself has become a source of volatility.

This transformation has profound implications for how we think, plan and invest. To navigate this environment, we must rely on a strong conceptual framework – one grounded in economic reality and institutional adaptability.

Five key assumptions

My conceptual framework is based on five key assumptions.

First, policy volatility is structural, not episodic. Geopolitical tensions are intensifying. Trade flows are becoming politicised. Financial sanctions are more frequent and increasingly targeted. These are not temporary disruptions – they are reshaping the global financial system.

Second, in such an environment, strategic resilience must take precedence over tactical prediction. Diversification remains important, but it is no longer sufficient. We must embed optionality into our governance frameworks – ensuring that our policies and processes allow rapid adaptation to shifting conditions.

Third, policy coordination is more essential than ever – both within institutions and externally. Reserve management cannot be isolated from monetary policy or financial stability. Our investment decisions must support, rather than complicate, broader policy objectives – especially during periods of stress. Externally, coordination with fiscal authorities and international institutions is critical. In a fragmented world, shared insight becomes a powerful source of stability.

Fourth, we must re-examine the notion of strategic autonomy – not only at the European level but also nationally. In a climate of geopolitical uncertainty, it is not only what assets we hold, but whether we can access them when needed. This requires a renewed focus on exposures and counterparty risk, along with a serious evaluation of alternative reserve assets – including gold and exchange-traded funds – and a strategic effort to expand and strengthen regional currency arrangements, such as the euro area.

Fifth, despite short-term noise, we must remain focused on the long term. Demographic aging, the climate transition and technological disruption are not distant threats – they are present investment realities. We must integrate these forces into public wealth management to preserve value and foster sustainable economic growth.

Implications for Bulgaria and the CEE region

The implications for Bulgaria may mirror broader trends across central and eastern Europe. While Bulgaria's direct exposure to current trade tensions is limited, indirect effects could be significant. We are deeply integrated into European supply chains and heavily reliant on external demand from major euro area economies. A slowdown in these – driven by weakening global trade – poses real risks to our exports and investment flows.

At the same time, the restructuring of global supply chains introduces uncertainty about future trade routes and production hubs. The full impact is difficult to quantify. But the risks are clearly tilted to the downside, with potential consequences for medium-term growth.

One channel already in motion is commodities. Expectations of softer global demand – driven by trade tensions – have pushed oil prices down. For energy-intensive economies like Bulgaria, this has delivered a short-term disinflationary effect.

However, the broader inflationary and investment implications of trade fragmentation remain uncertain and may evolve rapidly.

Foreign exchange reserve management

The optimal composition of foreign exchange reserves warrants renewed scrutiny. We now operate in an environment marked by heightened geopolitical tensions, weaker global growth, volatile capital flows and increased market instability

Historically, confidence in the US economy and financial system has supported the dominance of the dollar. As of the end of 2024, there has been no major shift in global reserve currency allocations – the dollar remains dominant, underpinned by its liquidity, depth and perceived safety. Yet this may be beginning to change.

Simultaneously, gold has re-emerged as a strategic reserve asset. Several central banks have significantly increased their gold holdings in recent years – not only as a hedge against financial risk, but also as protection against geopolitical shocks.

These trends sharpen the focus on the euro's role as a reserve currency – an increasingly relevant question.

The euro and Bulgaria's strategic path

For Bulgaria, these developments make our long-standing ambition to join the euro area more relevant – and more urgent – than ever. This conclusion is clearly supported by the prevailing conceptual framework outlined here.

Euro adoption will have five sets of repercussions. It will anchor Bulgaria's monetary policy within the European Central Bank framework, and provide credibility, stability and predictability. Furthermore, it will reduce currency risk and protect the economy from speculative pressure; enhance investor confidence and deepen financial integration; and offer access to euro area mechanisms, such as the European Stability Mechanism.

In a world where policy volatility is structural, euro area membership will strengthen Bulgaria's strategic resilience – through institutional alignment and enhanced crisis response tools.

Bulgaria's reserve management strategy

At present, the composition of Bulgaria's foreign exchange reserves is shaped by our legal mandate and the operational logic of the currency board. About 90% of our reserves are held in euros, with the remaining 10% in gold.

Credit and currency risks are tightly constrained. Eligible assets must carry a minimum AA– rating. This conservative, short-duration approach has served us well during periods of market stress.

Looking ahead, euro area accession will mark a new phase in reserve management. The new law on the Bulgarian National Bank introduces greater flexibility. With the euro becoming our domestic currency, we will begin to diversify our foreign exchange reserves into other currencies.

We are already laying the groundwork – developing new operational infrastructure, expanding our network of counterparties and building deeper market expertise.

We will also adjust our risk framework, relaxing the credit threshold of the securities we hold from AA- to A- and extending the investment horizon from short-term to strategic, long-term. These reforms will broaden our investment universe – potentially including instruments such as ETFs. Naturally, any such instruments will be subject to rigorous assessment to ensure alignment with our core objectives: capital preservation and liquidity assurance.

Central banks must adapt

As global fragmentation becomes a defining feature of the international landscape, central banks must adapt. We must continue to uphold the core principles of reserve management – liquidity, safety and return – while increasingly addressing geopolitical and systemic risks.

Strategic positioning will be just as important as financial fundamentals. For the Bulgarian National Bank, this means maintaining resilience under today's currency board – while preparing for a more dynamic, risk-aware reserve management strategy in the very near future.

The reforms ahead will require careful execution. But they also offer a timely opportunity to strengthen our capabilities, increase our adaptability and position ourselves for a more volatile, multipolar world.