

Petar Chobanov: What to expect for banks and the economy in 2024

Speech by Mr Petar Chobanov, Deputy Governor of the Bulgarian National Bank, at the opening of the "Banks and Business" Conference, organised by the Capital newspaper, Sofia, 5 December 2023.

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First of all, I would like to thank the organisers from 'Capital' for inviting me to take part in today's conference, which over the past decade has established itself as an important event in the area of finance in Bulgaria. The subjects on today's agenda are extremely important and highly topical in the field of banking services.

The new year 2024 is a natural continuation of the macroeconomic and global processes that originated with the onset and spread of the COVID-19 pandemic. Since 2020, we have been faced with a unique situation in the world economy, in which the dynamism of events is predetermined by a series of shock events. The pandemic caused by COVID-19 has created conditions for monetary and fiscal relaxation which made economic agents have unrealistic expectations, and also for inflation comparable with the oil price shocks of the 1970s.

In early 2022, with the start of the military invasion in Ukraine, the cumulating economic shocks intensified, exacerbating the supply chain issues in the global economy and creating pre-conditions for the outbreak of an energy and food crisis, and with recent developments in the Middle East these conditions have the potential to escalate and grow into a much broader humanitarian crisis by its nature.

Turning to the national specifics in Bulgaria, we are meeting the year 2024 confronted with the already mentioned external challenges, and at the same time it should be noted that it seems that one of the safeguards inherent to the economy, which would arise from the declaration and implementation of a clear and consistent fiscal conservatism, will be lacking. On the other hand, in national conditions, especially considering our future entry into the euro area, the most effective macroeconomic policy is precisely the synergistic interaction between monetary and fiscal policies, which is somehow underestimated and sent into the background, while a kind of priority is given to fiscal dominance. The BNB's position on the fisc has always tended towards moderate conservatism, combined with the precise setting and planning of budget buffers that have the potential to provide fiscal space in the realisation of significant economic risks.

For this particular reason, the specified coordination of fiscal and monetary policies is of prime importance so as to ensure the attainment of the medium and long-term objectives of a sustainable and balanced growth and moderate inflation. I am happy to say that for the performance of this task we can count on the cooperation with the banking and financial community, as the banking system is well capitalised and liquid, which, in terms of the mentioned risks to economic development, is both a corrective mechanism and a buffer for a balanced growth of the financial system and the economy as a whole. In this regard, it should be noted that the tendency towards increasing

disposable income will have a positive effect on the capacity of households and businesses to service their loans, which in turn contributes to the stability and capacities of the banking system.

From a European perspective, according to Eurostat's projections, the euro area's annual inflation (HICP) is estimated to be 2.4% in November 2023, falling from 2.9 % in October 2023. In terms of the main components of inflation in the euro area, foodstuffs, alcohol and tobacco registered the highest annual rate in November (6.9% compared to 7.4% in October), followed by services (4.0% compared to 4.6% in October), non-energy industrial goods (2.9% compared to 3.5 % in October) and energy (-11.5 % compared to -11.2 % in October). The data seem to indicate that the periods of high, I would say "frenzied", inflation are passing. As a result of the mentioned dynamics, it is expected that in 2024 the ECB will stop raising key interest rates, which in turn will halt the increase in the interest rate spread of commercial banks and will intensify the pressure for efficiency in their business.

The main question to be answered regards the potential growth drivers in 2024, primarily in a national context, which are relevant to the financial sector and its resilience. First of all, here we should note the importance and role of the investments in infrastructure which, within the current discourse about 2024, will be digital infrastructure. On the one hand, digital infrastructure should ensure an advance from basic information security to promoting complete customer financial literacy that would counter cyber threats more effectively. In 2024, the financial sector is expected to become increasingly dependent on digital technologies in conducting its core business. Digitalisation has the potential to provide serious opportunities, offering a number of solutions to many of the challenges I have listed, while creating the prerequisites for growth and sustainability.

On the other hand, in 2024 the requirements of the Digital Operational Resilience Act (DORA) are going to be transposed into the Bulgarian legislation and thus ensure that the financial sector in Bulgaria will retain and reinforce its resilience in case of serious operational events. The DORA Regulation has already been adopted at the European level and will become mandatory for implementation as of 17 January 2025.

All financial service providers will fall within the scope of DORA, and of the relevant national legislation respectively, such as banks, payment service providers, electronic money issuers, investment intermediaries, crypto-asset service providers, as well as critical ICT service providers acting as outsourcing companies for the regulated participants in financial markets.

The transposition of DORA into the Bulgarian legislation will create a regulatory framework for the operational resilience of digital technologies, through which all companies falling within the specified regulatory scope should ensure that they are able to withstand, react and recover from any type of ICT-related disruption and threats. The Bulgarian National Bank is actively involved as a partner of the Ministry of Finance regarding the transposition of DORA by contributing its expertise on technical and supervisory issues so that the best and most effective supervisory practices can be implemented with a focus on the stability, sustainability and continuity of the ICT processes.

Also, at an advanced stage of implementation in the Bulgarian legislation is the Regulation on the markets of crypto-assets (MiCA) that will introduce uniform market rules in the EU for the supply and trading of crypto-assets. The Regulation covers crypto-assets that are not currently regulated by the existing financial services legislation. The transposition of the Regulation will regulate the scope of the issuance and trading of crypto-assets (including asset-backed tokens and e-money tokens) ensuring transparency, disclosure, authorisation and supervision of transactions. The new legal framework will support market integrity and financial stability by regulating public offerings of crypto-assets while creating legal certainty that consumers will be better informed about the risks involved.

The MiCA Regulation entered into force in June 2023 and national legislation should define and specify the implementation of the new regime, which will take place within 12 to 18 months.

During the implementation phase of MiCA, ESMA (in close cooperation with EBA, EIOPA, ECB and BNB respectively) will consult the public and businesses on the creation and implementation of technical standards, which will be subsequently published. The goal of this effort is to prepare measures as soon as possible to include stakeholder feedback. The date of entry into force of these measures will depend on their adoption by the European Commission and their subsequent approval by the European Parliament and the Council of the EU.

In parallel with these processes, the BNB is working with the European supervisory authorities on supervisory convergence, the aim here being to ensure compliance of supervisory expectations related to entities offering services related to e-money tokens in EEA jurisdictions and to encourage, from the outset, consistent practices to be used after the final entry into force of MiCA, particularly in relation to licensing regimes.

It should also be noted that in the coming year, topics related to Environmental, Social and Governance (ESG) activities will be important for the BNB and the banking community. With regard to ESG, the BNB adheres to compliance with European legislation in this area (such as SFDR – the Sustainable Finance Disclosure Regulation), as well as to the EBA policies, which recommends the incorporation of ESG risks by credit and financial institutions. The EBA has put into practice a number of definitions, processes, mechanisms and supervisory practices in relation to credit and financial institutions with the aim of identifying and managing ESG risks. Among them are the requirements for the mentioned companies related to the disclosure policies of the incorporation of the ESG factors, which we should consider through the overall political discourse of the Green transition.

In the current year, we can report significant progress in terms of projects in the field of payments related to the preparation for the country's entry into the euro area, the effects of which will be fully felt in 2024. This progress was achieved with the help and active participation of the banking community in Bulgaria.

In March of this year, the migration to the Eurosystem's new consolidated TARGET Services platform took place. The new platform has become a stable foundation of the financial market infrastructure of the euro area. In October of this year, another important project in the field of payments was completed – this is the project for the

migration of budget payments to the Single Euro Payments Area (SEPA) standards. Next, we should note the development of instant credit transfers in BGN. Currently, we report that through the BORIKA AD Blink Service practically 100% of customer bank accounts in the country are accessible for instant payments in BGN, which are executed within 10 seconds, 24 hours a day, 365 days a year.

As I already said, in the coming year a number of challenges are expected on various fronts, but then again they provide opportunities for the sustainable development of the financial sector as a whole, with which the payment systems in the country will be integrated into the corresponding systems and infrastructures of the euro area. The mentioned projects are essential for the country's financial infrastructure, especially in terms of digitisation and cyber resilience processes, as they will become a foundation for further development of innovations in the sector. The realisation of the stated goals and the prevention of the analysed risks could not be possible without the joint efforts of the regulator and market participants through fruitful cooperation, smooth communication and strong motivation to achieve results.

I wish you success in the new, challenging year 2024, as well as fruitful discussions in a spirit of partnership and cooperation.