

FINANCIAL INTEGRATION OF BULGARIA AFTER THE DEBT CRISIS

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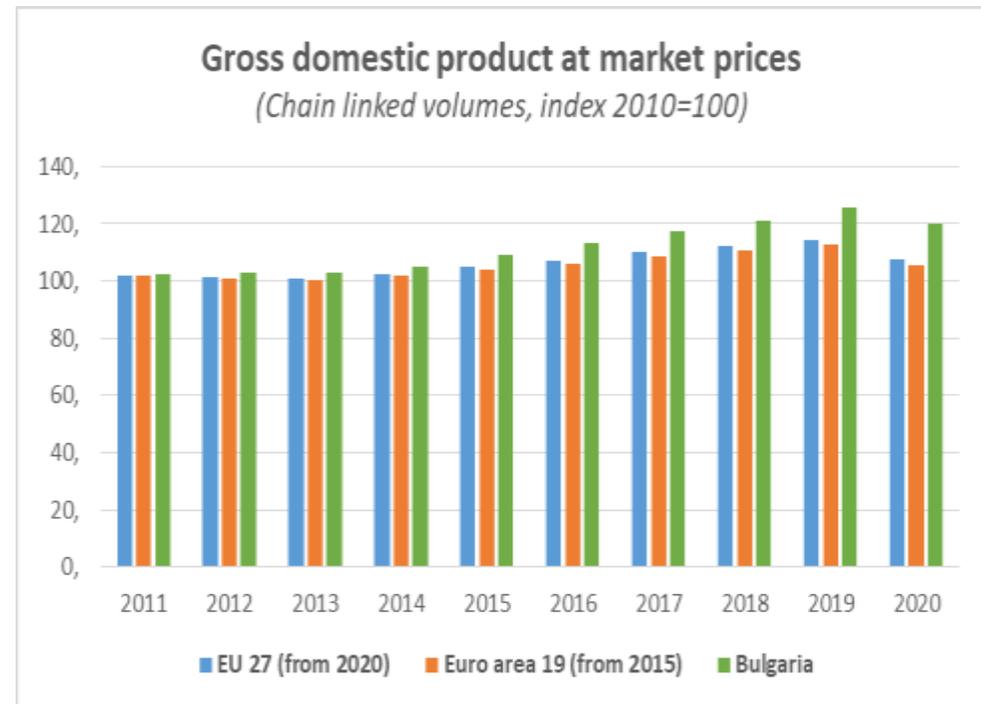
Main points

- Changes in the EU after the crisis in the financial sphere
- Banking policy and adaptation to the new conditions in the EU
- The capital market in Bulgaria after the European debt crisis

Changes in the EU after the financial crisis

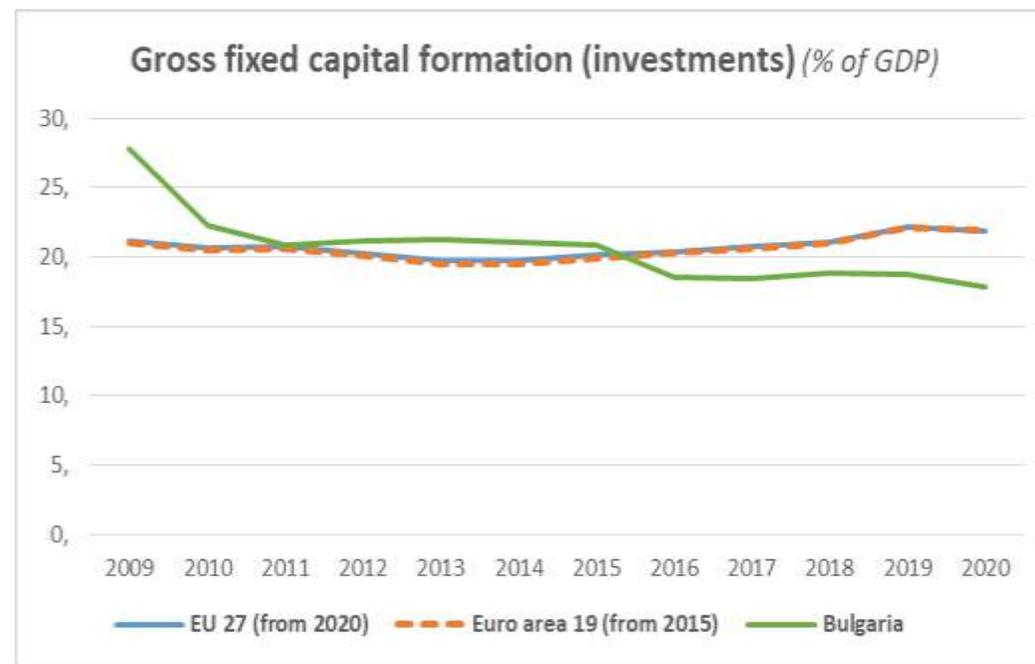
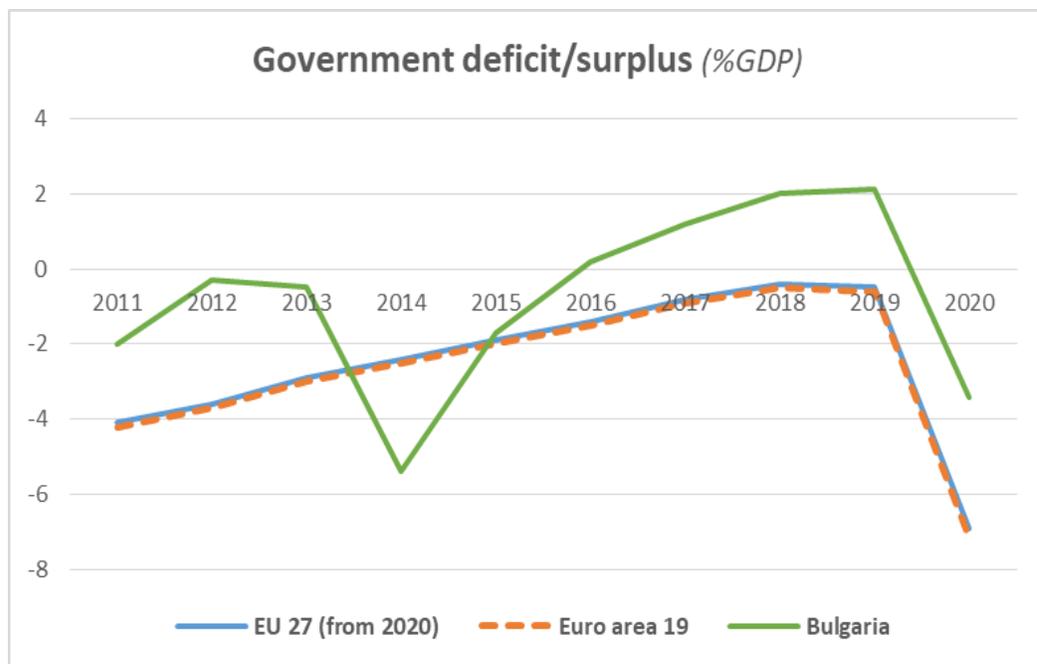
From the broad economic policy guidelines to the EU surveillance framework of the national financial sectors

- The Maastricht Treaty in 1992 – in the monetary union early detection of divergent trend is key for harmonious development (*Art. 121.2 of the EU Treaty*)
- The Commission recommendation for the broad economic policy guidelines to the Council
- The first country-specific guidelines 1998
- Financial crisis in 2008 and introducing the European semester in 2011
- European supervisory authorities 2013
- The EU surveillance framework of the national financial sectors



Eurostat

Changes in the EU after the crisis in the financial sphere



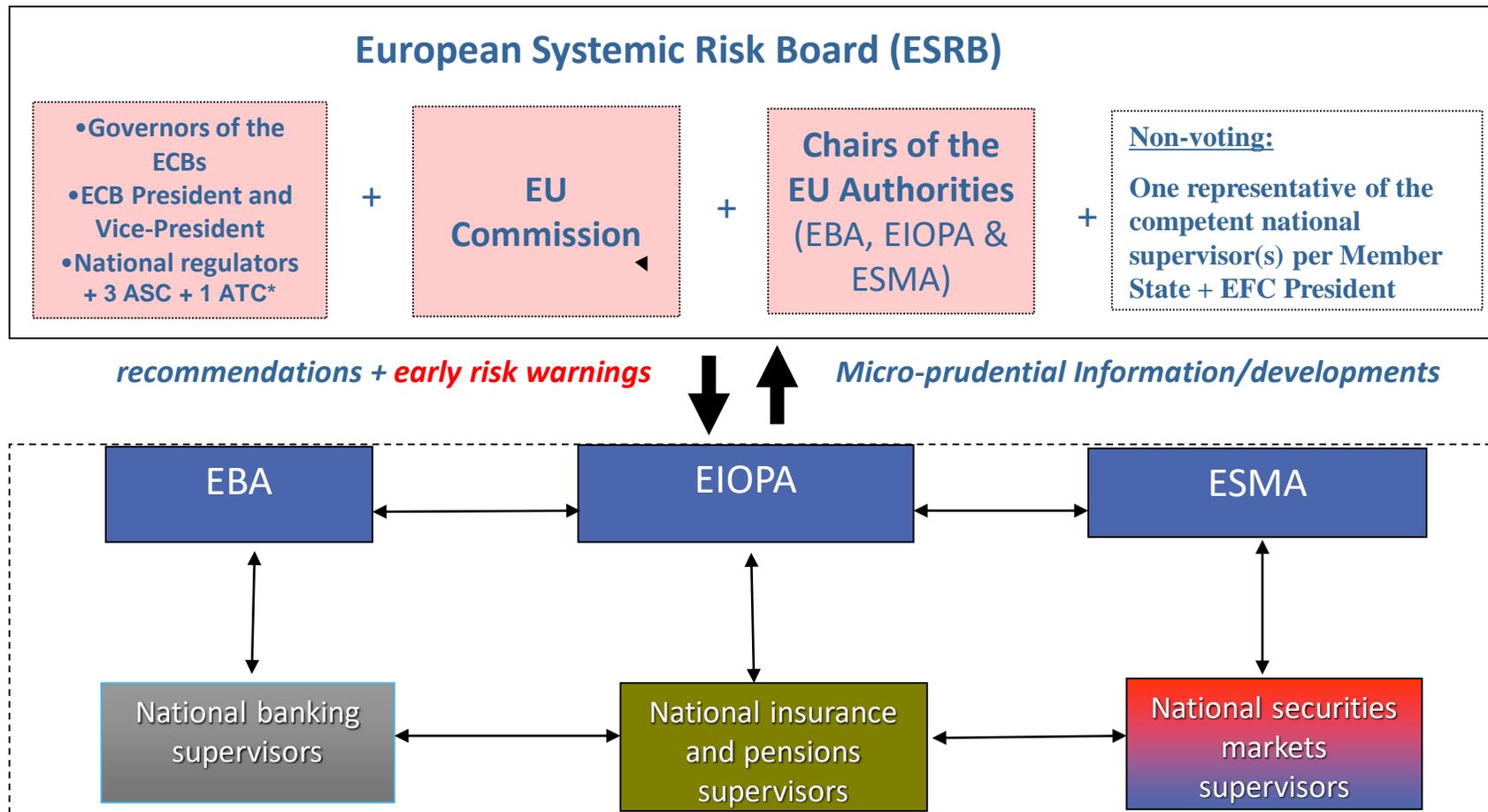
Eurostat

Changes in the EU after the crisis in the financial sphere

SUPPORT FOR ECONOMIC AND MONETARY UNION

- Banking Union
 - Uniform rules
 - Unified supervisory mechanism
 - Unified restructuring mechanism
- Capital markets union
 - provide businesses with a greater choice of funding at lower costs
 - support the economic recovery post-Covid-19
 - new opportunities for savers and investors

European system of financial supervisors (ESFS)



Changes in Bulgarian **banking policy** and adaptation to EU conditions

- ❑ In the post-global financial crisis (GFC), the European sovereign debt crisis (2010) - Banks in Bulgaria take on the old and new risks in an unfavorable economic and financial environment.
- ❑ Bulgarian banks face a number of challenges:
 - ❖ Fall in bank profits;
 - ❖ Growth of interest expenses suppresses banks' net interest income.
 - ❖ Banks' profitability was also affected by lower net income from fees and commissions and higher administrative costs.
- ❑ The stabilization of the banking sector is due to lower impairment charges and higher net income from financial instruments.
- ❑ Other factors with negative impact on banks' balance sheets:
 - ❖ slow recovery of the Bulgarian economy;
 - ❖ difficulties in servicing the liabilities of enterprises and households.

Changes in Bulgarian banking policy and adaptation to EU conditions

- ❑ After 2012 rise in banks' liquidity .
- ❑ Foreign-owned banks transfer the liquidity accumulated from household savings to foreign credit institutions (mainly parent banks).
- ❑ Credit risk management - a positive sign is the amelioration of the coverage ratio of NPLs overdue for more than 90 days.
- ❑ The capital base of the banking system is maintained at levels higher than the minimum capital requirements.
- ❑ The zero levels interest rates and the fall in banks incomes is compensated by the increase of the prices of the different financial services, provided by the commercial banks.

Dynamics of selected balance indicators of Bulgarian banks by years,

1. Banking system assets in billion BGN,
2. Gross loans and advances in billion. BGN, excluding loans to credit institutions
3. Deposits in billion BGN
4. Share of bank nonperforming loans (NPLs) and advances in total loans and advances (%)
5. Liquidity assets ratio under the BNB Ordinance 11

Indicators	2012	2013	2014	2015	2016	2017	2018	2019	2020
Assets (1)	82,42	85,75	85,14	87,5	92,1	97.8	105.6	114.2	124.0
Loans (2)	64,7	68,1	55.6	74.5	77.5	81.6	89	94.5	76.7
Deposits (3)	70.7	73.9	73.5	74.4	78.6	83.7	90	97.2	105.7
NPLs (4)	16.63	16.88	16.75	14.61	13.17	10.42	7.80	6.62	5.6
Liquidity ratio (5)	26.0	27.07	30,12	26.1	38.24	38.97	22.39	18.11	29.23
ROE (7)	5.3	4.9	7.1	7.80	10.4	9.32	12.11	11.63.	5.31
ROA (8)	0.71	0,70	0,8	1.03	1.37	1.20	1.59	1.47	0.66
Net profit (9)	0,57	0,59	0,51	0.90	1.26	1.17	1.68	1.68	0.82
Capital adequacy (10)	16.7	16.9	21.95	22.18	22.15	22.08	20.16	20.22	22.74
leverage ratio (%)	13.2	13.0	11.53	10.84	10.89	10.55	10.55	10.55	10.74

Changes in Bulgarian banking policy and adaptation to EU conditions

- ❑ Close cooperation ECB - BNB a comprehensive assessment in 2018-2019 has been conducted of 6 banks in Bulgaria, required for EU Member States whose currency is not the euro.
- ❑ ECB Banking Supervision methodology has been applied for the AQR and the ST in Bulgaria.
- ❑ In 2019, new regulatory measures were introduced – the EBA internal regulation of commercial banks. <https://meet.google.com/swy-ahfw-gnm>
- ❑ The application of the definition of default and the alignment of its definition with the Single Supervisory Mechanism's approach was transposed by amendments of BNB Regulation 7 on the bank's risk management process.
- ❑ Ordinance 37 on the internal exposures of banks (from July 2018), the BNB laid down the internal procedures for forming, calculating, monitoring, and reporting internal exposures for banks.
- ❑ The application of IFRS 9 led to changes in the banks loan-loss provisioning model and capital ratio.
- ❑ In July 2018 Bulgaria announced its intention to join simultaneously the Exchange Rate Mechanism II and the Banking Union.

The development of the Bulgarian **capital market** during three decades since 1990: main features

- The decade 1991-2001: the re-birth and the market failures by 1995-1997

The start up of the regulation of the organized capital market;

The second decade: 2000-2010 - preparation for the EU accession: transposition of the EU law for the banking and non-banking sector regulation

- Ac 2000, BSE introduced the completely automated trading system RTS Plaza, the same year it launched the stock index SOFIX, and in 2003 the Stock Exchange set up an Internet-based application for on line access to the BSE – COBOS.
- Since 2007 Bulgaria's entry in the EU a new "wave" of a regulation of the financial sector in Bulgaria followed. Since 2007, the electronic trading system of Deutsche Boerse Xetra® is in operation, functioning as a trading platform of the BSE that creates new functionalities for the investment intermediaries and their customers. CD also introduces a new trading system, allowing the clearing and settlement of transaction in securities and it continues to function also as the primary register of transactions and ownership of dematerialized securities.
- Since July 2021 Bulgarian Stock Exchange introduced a new market segment - BSE International. It trades 90 stocks and exchange traded funds from Europe, the United States and Canada. Among them are iconic companies such as Apple, Microsoft, Amazon, Tesla, Deutsche Bank, Siemens and many others.

Bulgarian capital market in 2020-2021: the impact of the EU membership

- Further institutionalization of market regulation
- Inflow of foreign capital and market restructuring

The favourable factors for the gradual and progressive development of the Bulgarian capital market in the subsequent years.

- *favourable tax regime,*
- *The Bulgarian legislation synchronized with *acquis communautaire* of the European Union in the field of financial market regulation,*
- *the high regulatory and supervisory requirements applicable to investment intermediaries and other market participants, as well as*
- *the established state-of-the art market infrastructure of the BSE and CD*

Market capitalization has been increased in 2016-2020

Market Capitalisation (BGN)

Market/Segment	Market Capitalisation (BGN)		Change	
	31.12.2019	31.12.2020	%	Absolute value (BGN)
Equity (REITs excluded)	26 701 997 825	27 043 058 506	-1,28%	-341 060 681
REITs	1 202 538 971	1 311 447 727	9,06%	108 908 756
Total capitalisation	27 904 536 796	28 354 506 233	1,61%	449 969 437

Market Capitalisation (BGN)

Пазарен сегмент	Market	Market Capitalisation (BGN)		Change	
		31.12.2018	31.12.2019	%	Absolute value (BGN)
Premium Equity Segment	BSE	1 796 413 436	1 329 406 818	-25,99%	-467 006 618
Standard Equity Segment	BSE	6 314 927 201	6 671 968 123	5,65%	375 040 922
REITs Segment	BSE	786 013 126	783 336 673	-0,34%	-2 676 453
Equity Segment	BaSE	18 590 657 188	19 041 683 565	2,43%	451 026 377
REITs Segment	BaSE	416 525 845	528 111 054	26,79%	111 585 209

Market Capitalisation/ Gross Domestic Product (GDP)

	31.12.2016	31.12.2017	31.12.2018	31.12.2019	31.12.2020
Market Capitalisation (BGN million)	9 682,52	23 620,97	26 765,34	27 904,54	28 354,51
GDP (BGN million)	92 635	98 631	107 925	118 669	11 789 9
Market Capitalisation / GDP	10,45%	23,95%	24,80%	23,51%	24,05%

* GDP for the current period is estimated by the Bulgarian National Bank as of the date of publication of this report. For the remaining periods the GDP is according to final data for the respective year.

NEGATIVE IMPACT OF COVID-19 IN 2020 ON THE BSE INDICES

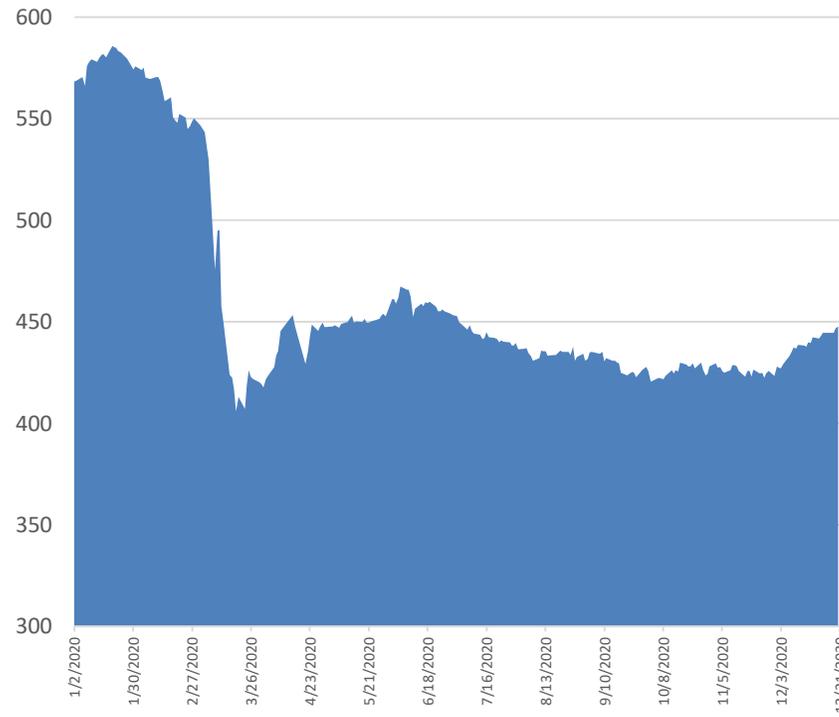
- The beginning of the pandemic was in March, and it was characterized by extremely high volatility on international stock exchanges and increased activity of investors in order to rebalance their portfolios. The impact of the crisis on companies' performance and investor expectations can be measured through changes in leading stock indices.
- At the end of 2020, compared to the beginning of the year, there was a decrease in the values of SOFIX, BGBX40 and BGTR30 and only BGREIT increased its level. The movement in the values of SOFIX and BGBX40 was similar, and the change in BGREIT has a different form, due to the type of companies that make up the index. The downward trend in the dynamics of the indices began at the end of the first and the beginning of the second quarter and made the transition to albeit incomplete recovery in the third and fourth quarters of 2020, with the exception of BGREIT, whose value increased.
- In 2020, the value of SOFIX decreased by 21.23% to 447.53 points, and that of BGBX40 decreased by 9.34% to 101.38 points, and the BGTR30 decreased by 3.31% to 499.17 . The value of BGREIT increased by 7.66% to 137.69 points.

STRATEGIC GOALS OF THE CAPITAL MARKET DEVELOPMENT IN 2019 - 2021

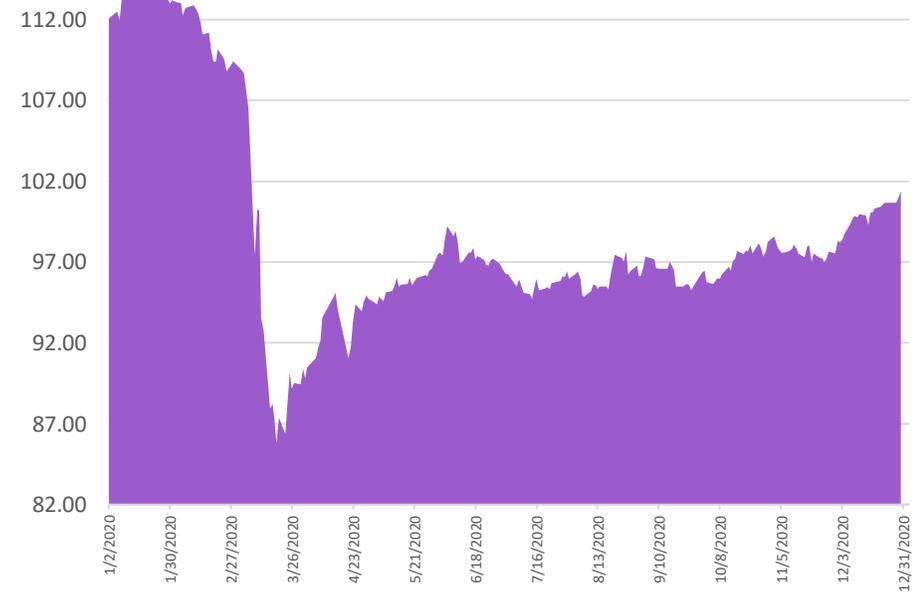
- Making consistent, transparent and foreseeable regulatory activity of the Financial Supervision Commission
- Effective implementation of risk-based supervision and maintaining stable financial markets
- Improving the way of functioning of markets
- Protection of consumers of financial services
- Organizational improvement and development of human capital

BSE INDICES IN 2020

SOFIX



BGBX40



BSE is licenced to operate as a benchmark administrator of financial instruments

- On June 16, 2020 the Bulgarian Stock Exchange is licenced to operate as a benchmark administrator of financial instruments and financial contracts or to measure the performance of investment funds following the requirements of Regulation (EU) 2016/1011. In this way, BSE is part of the EU benchmark administrators, among which are the stock exchanges in Austria, Germany, Greece, Ireland, Slovenia, Hungary and Croatia as well as the groups of NASDAQ and Euronext.
- The benchmark administrators' licensing in EU aims at requirements unification for their activity to provide a guarantee of the accurate, continuous and trustworthy process of indices determination as well as the protection of clients and investors by elimination of possible errors, manipulations and conflicts of interests.
- This implies the proper functioning under the conditions of the internal capital market and is of high importance for cross-border transactions in the European Union.

The Bulgarian capital market in 2021: dynamic and differentiated by listed companies trends

- On the Bulgarian capital market there is a tendency of selectivity: half of the companies fall and the other half has a sharp rise in the share price. But this is not a negative feature of the market, as it shows the role of the market for the transfer of capital from losing industries to fast-growing industries.
- The SOFIX index does not show significant fluctuations, as the risk is distributed between $\frac{1}{2}$ losing companies and $\frac{1}{2}$ growing companies. Even losing companies provide an opportunity for the speculating investors to invest by looking for undervalued stocks in anticipation of their price growth.

CONCLUSIONS (I)

- The Bulgarian capital market has 30% growth, which is extremely high. This can be seen in the results of both funds and investors.
- The investors no longer look at the market as a basket, but choose stocks that pay dividends from different sectors, stocks that perform well in the long run.

There is a serious interest in the initial public offerings, but in the smaller segment - up to 3 million euros. This is an average amount for the Bulgarian market and we see that there is a market in this segment and the initial public offerings were a great success

There is almost no market for a segment of BGN 20-30 million or EUR, because there are not so many companies to achieve such results.

CONCLUSIONS (II)

- The average profitability of large and liquidly traded companies this year is 3.28%, which is a decrease compared to 4.44% in the previous year, but is still slightly higher than the average for the last five years. The income of the various shares varies from 1.14% to 6.27%.

INVESTMENT RISKS REMAIN

- Industrial companies, as a typical example of cyclical business, have been hit hard by the crisis last year. Their revenues fell by 20-30% in the second quarter, but their results are now offset.
- Capital gains are much more important for profitability than dividends, which should be seen as a bonus to their performance and as an indicator of the stability of financial results. Moreover, the profits from the rise in prices are exempt from taxes, and the tax on dividends for individuals is withheld even before their distribution

Most traded are SHARES WITH DIVIDENDS

- The payment season for this year is almost over, with only a few companies partially paying dividends in the fall or early next year. Therefore, investment must now be part of a long-term strategies. They can be divided into two components. The first, as already mentioned, are the strategies of companies with a special investment purpose due to the stability of the results and the dividend yield.
- The second category includes the other companies on the stock exchange, that have recently paid dividends These are stocks with mostly price growth in the last year and they attract not so much with a dividend of 1-4%, but with their capital gains and the ability to beat inflation and to raise higher capital gains

Thank you for your attention !