BULGARIAN NATIONAL BANK

ANNUAL REPORT · 2019

Bulgarian National Bank

ANNUAL REPORT • 2019

Published by the Bulgarian National Bank
1, Knyaz Alexander I Square, 1000 Sofia
Tel.: (+359 2) 9145 1351, 9145 1209, 9145 1806
Fax: (+359 2) 980 2425, 980 6493
Printed in the BNB Printing Centre

Website: www.bnb.bg

The BNB Annual Report for 2019 employs statistical data as of 3 April 2020.

ISSN 1313-1494 (print)
ISSN 2367-492X (online)

Honourable Chair of the National Assembly,
Honourable People's Representatives,

Under the provisions of the Law on the Bulgarian National Bank Article 1, paragraph 2 and Articles 50 and 51, I have the honour of presenting the Bank's Annual Report for 2019.

Dimitar Radev
Governor
of the Bulgarian National Bank

BNB Governing Council

Sitting from left to right: Lyudmila Elkova, Nina Stoyanova, Lena Roussenova, Elitsa Nikolova.
Standing from left to right: Kalin Hristov, Dimitar Radev, Radoslav Milenkov.

BNB Governing Council

Dimitar Radev
Governor

Kalin Hristov
Deputy Governor
Issue Department

Nina Stoyanova
Deputy Governor
Banking Department

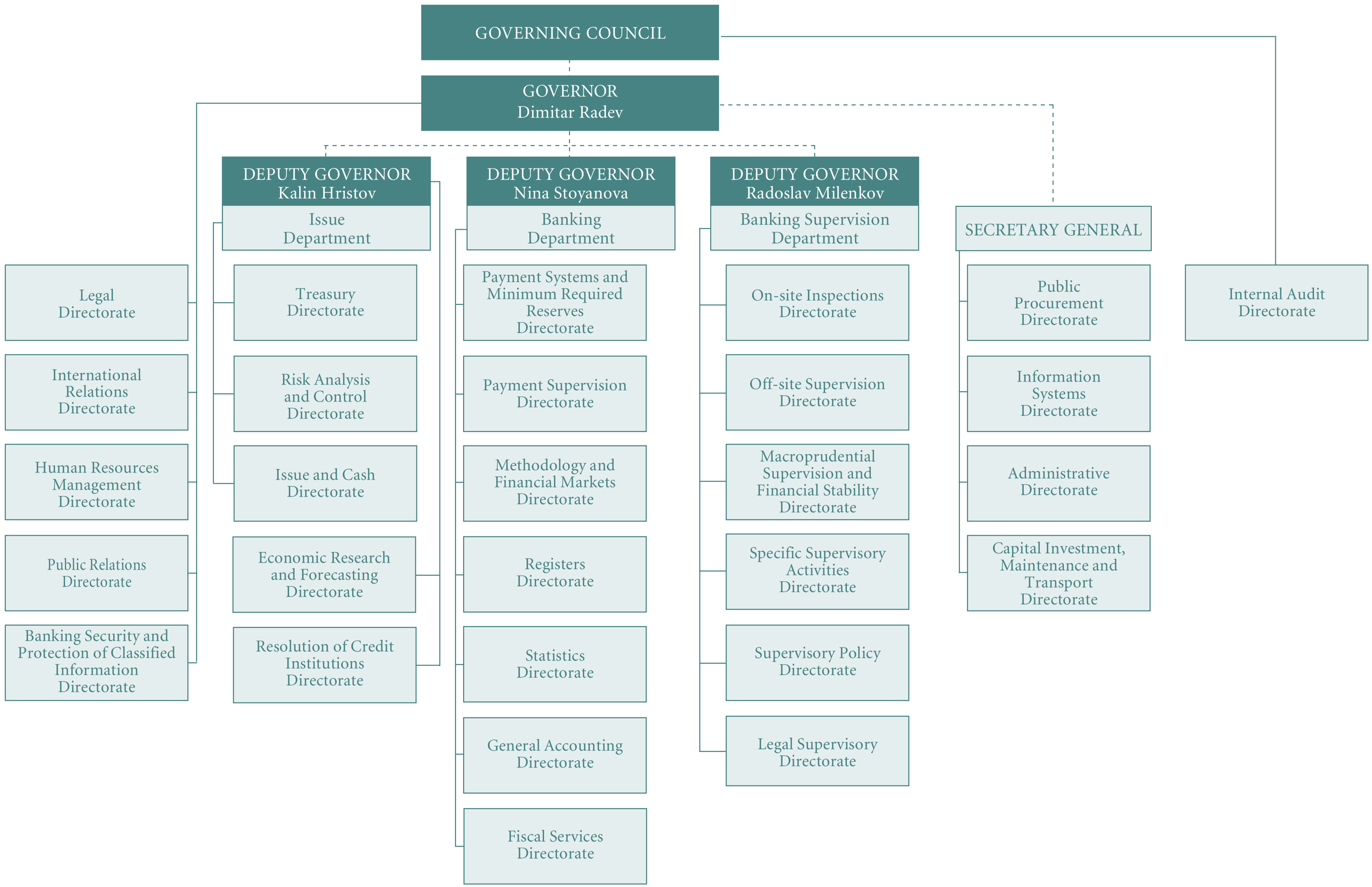
Radoslav Milenkov
Deputy Governor
Banking Supervision Department

Lena Roussenova

Elitsa Nikolova

Lyudmila Elkova

Organisational Structure of the BNB
(as of 31 December 2019)



Contents

Abbreviations

ABSPP	ECB Asset-backed Securities Purchase Programme
AQR	asset quality review
AS ROAD	Automated System for Registration and Servicing of External Debt
ATM	Automated Teller Machine
BIS	Bank for International Settlements
BISERA	Bank Integrated System for Electronic Payments
BNB	Bulgarian National Bank
BORICA	Bank Organisation for Payments Initiated by Cards
BRF	Bank Resolution Fund
CBPP3	ECB's Third Covered Bond Purchase Programme
CCR	Central Credit Register
CHF	Swiss franc
EBA	European Banking Authority
EC	European Commission
ECB	European Central Bank
Ecofin	Economic and Financial Affairs Council of the European Union comprising Member State economics and finance ministers
EDIS	European Deposit Insurance Scheme
EONIA	Euro OverNight Index Average (registered trademark of the European Money Market Institute, EMMI)
ESA 2010	European System of National and Regional Accounts
ESCB	European System of Central Banks
ESRB	European Systemic Risk Board
ESROT	Electronic System for Registering and Servicing Government Securities Trading
EU	European Union
EUR	euro
EURIBOR	Euro InterBank Offered Rate (EURIBOR, registered trademark of the European Money Market Institute, EMMI)
GDP	Gross Domestic Product
GSAS	System for Government Securities Sale and Repurchase Auctions
HICP	Harmonized Index of Consumer Prices
IAS	International Accounting Standards
IASB	International Accounting Standards Board
IFRS	International Financial Reporting Standards
IMF	International Monetary Fund
IOBFR	System for Budget and Fiscal Reserve Information Servicing
KTB	Corporate Commercial Bank AD
LBDG	Law on Bank Deposit Guarantee
LBNB	Law on the BNB
LCI	Law on Credit Institutions
LEONIA	an interest rate on real transactions in unsecured overnight deposits in BGN offered at the interbank market
LPSPS	Law on Payment Services and Payment Systems
LRRCIIF	Law on the Recovery and Resolution of Credit Institutions and Investment Firms
LTROs	Longer-term refinancing operations
MF	Ministry of Finance
MFI	Monetary Financial Institutions
NPISH	Non-profit Institutions Serving Households
NSI	National Statistical Institute
OPEC	Organization of Petroleum Exporting Countries
POS	Point of sale/point of service: a retail trade terminal for credit and debit card transactions
PSPP	Public Sector Purchase Programme
RINGS	Real-time gross settlement system
ROA	Return on Assets
ROE	Return on Equity
SDR	Special Drawing Rights
SEPA	Single Euro Payments Area
SITC	Standard International Trade Classification
SOFIBID	(Sofia Interbank Bid Rate) is an index calculated as the average of the bid quotes for unsecured BGN deposits
SOFIBOR	(Sofia Interbank Offered Rate) is a fixing of the quotes for unsecured BGN deposits offered in the Bulgarian interbank market
SRB	Single Resolution Board
SRF	Single Resolution Fund
SRM	Single Resolution Mechanism
SSM	Single Supervisory Mechanism
TARGET2	Trans-European Automated Real-time Gross settlement Express Transfer system for the euro
TARGET2-BNB	Bulgarian system component of TARGET 2
USD	US dollar
VaR	Value-at-Risk
VAT	Value Added Tax
WB	World Bank
XAU	troy ounce gold
XDR	currency code for special drawing rights

Summary

The Bulgarian National Bank conducts its policy taking into account the international situation and developments in the domestic economy. The BNB pursues its primary objective of price stability through maintaining national currency stability by adhering to the Law on the Bulgarian National Bank and applying its potential and capabilities effectively.

The Report covers the activities relating to the BNB's legal functions and duties as well as other BNB business related to or supporting its functions and duties. The Report also includes BNB budget performance for 2019 and consolidated financial statements as of 31 December 2019 (audited). Information under Article 17, paragraph 5 of the Law on the Bulgarian National Bank concerning resolutions adopted by the BNB Governing Council in 2019 is also included.

Global economic activity slowed down in 2019 in the context of enhanced uncertainty surrounding US trade relations with China and and further worsening of economic situation in advanced economies. Preliminary estimates show that real global economic growth decreased to 2.9 per cent from 3.6 per cent in 2018. Economic activity reported lower growth in all major advanced economies (with the exception of Japan and the United Kingdom) and in emerging market economies. Global industrial production rose 0.7 per cent, while the volume of world trade in goods and services decreased on 2018 by 0.4 per cent. The trend towards a slowdown in euro area economic activity continued driven by a decrease in international trade and high uncertainty regarding the effects of international trade conflicts and Brexit, with real GDP growth accounting for 1.2 per cent (1.9 per cent in 2018). US economic growth also slowed down in real terms to 2.3 per cent (2.9 per cent in 2018). Global inflation was 2.0 per cent at the end of 2019 and remained close to the December 2018's rate. Euro area inflation decelerated to 1.3 per cent on an annual basis at the end of 2019 (1.5 per cent in December 2018), while US annual inflation measured by the personal consumption expenditure price index fell in the fourth quarter of 2019 to 1.4 per cent, remaining below the Federal Open Market Committee (FOMC) target.

Taking into account moderating inflationary expectations, deteriorating economic environment, increasing risks to global economic growth, the European Central Bank and the US Federal Reserve System stated that they may launch monetary stimulus measures in the second half of the year and subsequently they launched the measures. In July 2019 the US Federal Reserve cut the federal funds rate target range for the first time since December 2008 in three steps by 25 basis points to 1.50–1.75 per cent and decided to stop reducing Federal Reserve holdings of debt securities. In September the ECB approved a package of measures, including a 10 basis point deposit facility cut to -0.50 per cent, recovered net purchases under the Asset Purchase Programme, introduction of a two-tier system for reserve remuneration and improved parameters of the new series of targeted longer-term refinancing operations.

The upward trend in global stock market indices recorded in the first nine months of 2019 reflected market participants' expectations of accommodative monetary policy measures of the leading central banks along with expectations of reaching a preliminary trade agreement between the US and China in the last quarter. International government bond markets saw a steady price appreciation until mid-third quarter and a slight downward adjustment through year-end. Lower demand for safe assets and increased government bond yields were affected by the progress in trade negotiations between the USA and China and the reduction in likelihood of the UK leaving the EU without a deal.

In 2019 Bulgaria's real GDP rose 3.4 per cent from 3.1 per cent in 2018. Private consumption contributed most to growth of economic activity, government consumption and fixed capital investment contributing less. Private consumption increased amid low interest rates, enhanced demand for loans and active supply of lending resources by banks along with a further increase in labour income, employment growth and high consumer confidence. Despite the unfavourable international economic situation and demand declines in the major trading partners, exports of goods and services rose mostly due to the exhausted effect of temporary supply side factors. Strong domestic demand boosted goods and services imports. This made net exports' contribution to real GDP growth slightly negative. At the close of 2019 annual consumer price inflation accounted for 3.1 per cent, accelerating on December 2018's 2.3 per cent. Food and services contributed most to the accumulated inflation throughout the year: 1.5 percentage points and 0.8 percentage points, respectively.

The continuous labour income growth and faster gross operating surplus increase in the overall economy favoured the upward dynamics of broad money over 2019 amid economic agents' high propensity to save. The lack of sufficiently safe alternatives to bank deposits was another factor behind M3 growth, which reached 9.9 per cent in December 2019 (8.8 per cent at the end of 2018). At the end of 2019 annual growth of non-government sector deposits accelerated to 9.7 per cent, from 7.3 per cent at the end of 2018. Annual growth of credit to non-financial corporations and households remained comparatively high throughout the year, reflecting the favourable macroeconomic environment, low interest rates and high inflow of funds attracted in the banking system. In December 2019 loans to non-financial corporations rose 5.9 per cent on an annual basis from 5.4 per cent at end-2018, while loans to households reached 9.5 per cent in December. Housing deposits contributed most to this growth.

In 2019 the budget balance on the consolidated fiscal programme was BGN -1148 million (-1.0 per cent of GDP). The budget deficit reflected mainly the expenditure incurred under the investment project for acquiring a new type of fighter aircraft (totalling USD 1.2 billion) after the revision of the 2019 State Budget Law. Fiscal reserve deposit funds decreased BGN 448 million from 2018 amounting to BGN 8565 million, of which BGN 8104 million on deposits with the BNB.

In managing gross international reserves, the BNB maintained a conservative policy to ensure high security and liquidity. By the end of 2019 the book value of gross international reserves was EUR 24,835.6 million: a total decline of EUR 236.6 million on the end of 2018. The BNB continued investing the vast majority of assets into government securities with an average share of 61.77 per cent, while deposits accounted for 34.02 per cent. In 2019 net income from international reserves management was positive and amounted to EUR 265.72 million or 1.16 per cent of total return for the review period. Broken by component, net income comprised: 1) income from gross international reserves investment in the original currency worth EUR -63.99 million, reflecting mainly the negative interest rates on BNB's deposits with first class banks and negative yield of euro-denominated high credit quality bonds in which the BNB has invested; 2) income from foreign currency revaluation amounting to EUR 313.99 million largely attributable to the significant gold price surge in euro; and 3) the net financial result of liabilities which was positive worth EUR 15.72 million.

Implementing, operating, and overseeing efficient payment systems is an important central bank duty. National payment systems functioned effectively, providing payment flow continuity. In 2019 RINGS, a real-time gross settlement system, operated by the BNB, processed 85.2 per cent of payments in Bulgaria. RINGS payments numbered 1,113,790, up 5.1 per cent on 2018, their total value reaching BGN 1,093,955 million (up 17.7 per cent on the prior year). The number and value of payments processed by BORICA and BISERA also rose in 2019. The national system component of the Trans-European Automated Real-time Gross settlement Express Transfer system for the euro run by the BNB – TARGET2-BNB – processed 277,343 payments (down 4.7 per cent on 2018) for EUR 443,087 million (up 0.3 per cent on 2018). The BNB regulates and oversees payment system operators, securities settlement systems operators in payment operations, payment institutions, electronic money institutions, and other payment service providers. In 2019 four inspections of payment service providers licensed by the BNB were completed.

The Bank has a monopoly on banknote and coin issue in Bulgaria. Its currency is mandatorily acceptable as legal tender at face value without restriction. BNB issue and cash operations include: banknote printing, coin minting, accepting, delivering, repaying, processing, authenticity and fitness checking of Bulgarian banknotes and coins and foreign currency, exchanging damaged Bulgarian banknotes and coins, and scrapping unfit Bulgarian banknotes and coins. By the close of 2019, 504.4 million banknotes (up 5.8 per cent), amounting to BGN 18,637.3 million (up 10.3 per cent on 2018) and 2598.7 million coins (up 6.5 per cent on 2018), worth BGN 459.7 million (up 10.5 per cent on 2018) were in circulation. As of 1 November 2019 the BNB put into circulation a new banknote of BGN 50 nominal value, issue 2019. As part of its cash circulation integrity and security functions, in the first half of 2019 the Bank conducted four full checks into credit institutions and service providers to ensure compliance with regulations on quality of banknotes and coins in cash circulation.

The Bank regulates and supervises banks in Bulgaria to maintain banking system stability and protect depositors' interests. In 2019 off-site supervision focused on current monitoring of credit institutions risk profile and assessment of their financial position and on the 2018 supervisory review and evaluation process (SREP) of banks which were launched over the period under review. Supervisors reviewed and assessed banks' Internal Capital Adequacy Assessment Process (ICAAP) and Internal Liquidity Adequacy Assessment Process (ILAAP) reports as of 31 December 2018. The scope and objectives of the nine inspections completed over the review year mainly reflected the review and evaluation of credit and credit concentration risk. Monitoring the implementation of supervisory measures imposed during previous inspections remained an important focus of on-site inspections. As a result of inspection conclusions, recommendations were forwarded to some banks to enhance organisation and credit risk management and to improve internal capital adequacy assessment in view of data quality in conducting stress tests. Macro-prudential supervision activities focused on monitoring the trends in international environment along with the processes and inherent risks affecting banking system stability. In order to strengthen banking sector's resilience to potential adverse developments in the economy, in 2019 the BNB Governing Council consistently increased the countercyclical capital buffer applied to resident credit risk exposures from 0.5 to 1 per cent with effect from 1 April 2020, and from 1.0 to 1.5 per cent with effect from the beginning of 2021. In 2019 the BNB' specific supervisory activities were aimed at preventing the use of the banking sector for money laundering and terrorist financing.

In 2019 the BNB participated in the process related to Bulgaria's request of 18 July 2018 for accession to the Single Supervisory Mechanism by establishing close cooperation with the ECB. The BNB provided expert assistance to ECB concerning Bulgarian banking system specificities with regard to the asset quality review (AQR) and stress tests performed by the ECB of six selected Bulgarian banks. The results for each of the six banks were published on the ECB's website. In the context of close cooperation, work continued on the alignment of BNB's supervisory policies, including the internal rules and processes and information flows between the BNB and the ECB.

In 2019 the banking sector in Bulgaria performed financial intermediation in compliance with the capital and liquidity requirements. The year saw a further increase in banking system asset value (by BGN 8.8 billion to BGN 114.3 billion) and improvements in asset quality indicators. The share of gross non-performing loans and advances in total gross loans and advances continued to decline to reach 6.5 per cent by end-2019 (7.6 by end-2018). The downward trend in residual credit risk measured by the amount of net non-performing loans and advances and fully covered by the capital exceeding minimum regulatory requirement was maintained. Banking capital and liquidity position remained stable. Over the period additional capital requirements were set. All banks had Common Equity Tier 1 above the required minimum and adhered to capital buffer requirements. The liquidity coverage ratio of the banking system in all credit institutions continued to exceed the regulatory level of 100 per cent. In 2019 the banking system reported a BGN 1.7 billion profit, with ROA and ROE declining slightly to 1.47 and 11.64 per cent respectively. In 2019 banking sector consolidation continued with the acquisition of Société Générale Expressbank by DSK Bank and Piraeus Bank Bulgaria AD by Eurobank Bulgaria AD.

In line with the Law on the Recovery and Resolution of Credit Institutions and Investment Firms (LRRCIIF), the Bank focused on preparing, reviewing and developing resolution plans. In this process, work continued on developing and improving the internal methodological framework to ensure a common approach in assessments and analyses used in recovery plans and discharge of other Bank obligations under the LRRCIIF. In accordance with the requirements of this Law, in March 2019 the BNB Governing Council set the total 2019 amount of annual bank contributions to the Bank Resolution Fund at BGN 137,257 thousand. The preparatory work to join the Single Resolution Mechanism (SRM) and consequently the Single Resolution Fund (SRF) continued in 2019 as a direct consequence of establishment of close cooperation with the ECB. Work was performed according to a specific Action Plan based on three pillars: (1) drafting and approving relevant amendments to the LRRCIIF; (2) preparations for joining the SRF; (3) preparing the bank resolution planning process after joining the SRM.

The BNB continued to collect, process, analyse and disseminate the official monetary and interest statistics, the external statistics, the statistics on quarterly financial accounts of all institutional sectors, the government finance statistics, the statistics on non-bank financial institutions, including leasing companies and investment funds, specialised lenders and insurance and reinsurance undertakings. In addition to compilation of statistical data, the BNB was actively involved in a number of national, European and international fora discussing and solving methodological issues in the area of statistics. Over the review period monetary statistics methodological requirements were updated with regard to International Financial Reporting Standard 16 enactment and implementation.

The BNB maintains the Central Credit Register (CCR): an information system on customer debt to banks, financial institutions, payment institutions and electronic money institutions extending loans under Article 19 of the Law on Payment Services and Payment Systems (LPSPS). In 2019 CCR conducted 9311 thousand electronic searches (8232 thousand as of 31 December 2018). Over the same period the average monthly number was 776 thousand, of which 73.8 per cent by banks and 26.2 per cent by other participants.

The BNB maintains the Register of Bank Accounts and Safe Deposit Boxes (RBASDB): an electronic information system on bank account numbers, holders and attorneys, data on account preservation orders, bank deposit box holders and attorneys. As of 31 December 2019 the RBASDB logged 15.6 million active bank accounts, from 16 million in December 2018, and 32.4 thousand safe deposit box hires, from 32.0 thousand in December 2018, including records of 3.0 million new and 3.3 million closed accounts. In 2019 bodies and institutions entitled to Register access conducted searches on 685,645 individuals (608,989 individuals in 2018). There were 2775 applications for RBASDB statements: 2636 by individuals and 139 by legal entities. With effect from 5 June 2019, the BNB started to provide electronic services from the RBASDB and the CCR to natural persons. As of 31 December 2019 electronic statements submitted to the CCR were 913, and to the RBASDB 135 requests for electronic statements from the Register.

Acting as fiscal agent and official depository the BNB maintains, develops and improves electronic systems for budget and fiscal reserve information servicing, auctions, settlement and securities trade servicing, the Register of Special Pledges, and external debt transactions. In 2019 the project of the system for conducting government securities auctions (GSAS) upgrade project was completed, thus ensuring its technological and functional modernisation in line with the agreements reached with the MF). The completion of the project allowed the new version of the system to be launched in April and government securities auctions as announced by the MF in June 2019 to be conducted *via* the upgraded GSAS. The MF issuing policy in 2019 involved six auctions for BGN-denominated government securities *via* the GSAS system.

Economic research and projections support the Bank's management in making decisions and delivering economic policy stance. In 2019 Research Plan implementation addressed developing and expanding BNB instruments used to prepare macroeconomic simulations and designing a satellite model reflecting effects of long-term structural changes in the Bulgarian economy. Honing the basic model for BNB macroeconometric forecasting continued over the year.

In July 2019 the BNB jointly with BIS organised a conference entitled 'The current global and European financial cycle: where do we stand and how do we move forward?' on the occasion of the 140th anniversary of the Bulgarian National Bank.

The BNB competitive human resource management system is developed and maintained by ensuring a favourable working and social environment, attracting appropriate candidates and retaining qualified employees by providing career development opportunities. In 2019 employees numbered 895 from 886 at the end of 2018. University graduates led staff educational attainment structure at 75 per cent, while there were no major changes in the age structure. The year saw substantial changes intended to improve the Bank's organisational structure.

BNB internal audit conforms to the International Standards for the Professional Practice of Internal Auditing, the Code of Ethics of Internal Auditors, ESCB Internal Auditor Committee Rules and Internal Audit Rules approved by the BNB Governing Council. In 2019 there were ten audits: seven under the annual Internal Audit

Directorate Programme approved by the BNB Governing Council and three under the ESCB Internal Auditors Committee Programme.

The BNB budget underpins Bank performance. In 2019 the BNB spent BGN 99,060 thousand or 87.8 per cent of approved budget, including currency circulation costs of BGN 30,779 thousand, materials, services, and depreciation of BGN 29,784 thousand and total staff costs of BGN 32,332 thousand. The Bank's 2019 investment programme cost BGN 8052 thousand or 23.0 per cent of budget.

I. Economic Development in 2019

The External Environment

In the context of increased uncertainty about global trade developments and further worsening of economic situation in advanced economies over 2019 global economic growth slowed down in real terms from 2018 and amounted to 2.9 per cent (3.6 per cent in 2018).[1] Economic activity reported lower growth in all major advanced economies with the exception of Japan and the United Kingdom. In emerging market economies the slowdown in growth was more strongly pronounced as a whole compared with advanced economies, with the economic activity dynamics reflecting the uncertainty triggered by the USA–China trade conflicts and country-specific factors in countries such as India, Mexico and Turkey[2].

In 2019 global industrial production slowed materially over 2019 to 0.7 per cent from 2.9 per cent in 2018.[3] Total industrial production in advanced economies decreased by 0.1 per cent from 2018, Japan and the euro area reporting the strongest fall of -2.4 per cent and -1.1 per cent. The annual growth rate of industrial production in emerging market economies slowed down significantly. The volume of world trade in goods and services decreased on 2018 by 0.4 per cent (against 3.4 per cent growth in 2018) driven mainly by the fall reported by Asia's emerging market economies (with the exception of China).[4]

Major Macroeconomic Indicators

(per cent)

	Average annual real GDP growth			Inflation (end of year)			Unemployment rate (average annual)		
	2017	2018	2019	2017	2018	2019	2017	2018	2019
EU	**2.6**	**2.0**	**1.5**	**1.6**	**1.6**	**1.6**	**7.6**	**6.8**	**6.3**
Euro area	2.5	1.9	1.2	1.3	1.5	1.3	9.1	8.2	7.6
EU – new non-euro area Member States	5.0	4.4	3.8	2.0	1.7	3.2	4.7	3.8	3.3
EC-3	2.0	1.6	1.5	2.7	2.0	1.3	4.7	4.4	4.3
The United States	2.4	2.9	2.3	2.1	1.9	2.3	4.4	3.9	3.7
Japan	2.2	0.3	0.7	1.0	0.3	0.8	2.8	2.4	2.4
China	6.9	6.7	6.1	1.6	2.1	2.9	3.9	3.8	3.6

Notes: New non-euro area Member States are countries joining since 2004 less those now in the euro area. The EU-3 are the United Kingdom, Sweden, and Denmark. New non-euro area Member States and EU3 indicators are calculated by weighing time series by country weights in group GDP for growth, in group labour force for unemployment, and the weights of the EU countries in HICP calculated by Eurostat for inflation. The GDP growth estimate for the euro area in 2019 is preliminary; data on real Luxembourg GDP has not been not published. The unemployment level estimate for EU-3 is preliminary; data on the UK has not been published.

Sources: Eurostat, Bureau of Economic Analysis, Bureau of Labour Statistics, Statistics Bureau of Japan, the National Bureau of Statistics of China, BNB computations.

Over 2019 the euro area economic activity continued to slow down, real GDP growth accounting for 1.2 per cent (1.9 per cent in 2018). Lower economic growth was driven by a decrease in international trade and high uncertainty regarding the effects of international trade conflicts and Brexit. By GDP component, lower economic growth reflected mainly the decreased positive contribution of exported goods and services

[1] Preliminary estimates based on IMF data: World Economic Outlook Update, January 2020.

[2] For further information, see IMF: World Economic Outlook Update, January 2020.

[3] Based on CPB data: Netherlands Bureau for Economic Policy Analysis, 23 February 2020.

[4] Based on CPB data: Netherlands Bureau for Economic Policy Analysis, 23 February 2020.

and the formed negative contribution of net exports. Domestic demand continued to support the euro area economic activity growth amid favourable financing conditions and sustained labour market improvement. By component of domestic demand growth of fixed capital investment and government consumption accelerated, while private consumption growth slightly slowed down. Weaker economic activity compared with 2018 was recorded in all euro area countries except Lithuania and Greece[5]. Unemployment continued falling to reach 7.6 per cent on average for the year from 8.2 cent in the previous year. Greece and Spain had most unemployment at 17.3 and 14.1 per cent. A decrease in the unemployment rate from the previous year was recorded in all euro area Member States with the exception of Lithuania and Luxembourg where it matched the 2018's rate.

In 2019 US economic growth also slowed down in real terms amounting to 2.3 per cent (2.9 per cent in 2018). Slower economic growth reflected worsened global outlook for economic activity, the trade conflict with China and exhausted effects of the 2018 tax reform. By GDP component private investment contributed most strongly to the economic activity slowdown. Unemployment in the USA came to 3.7 per cent on average in 2019 (3.9 per cent in 2018).

The Brent crude oil price fell on 2018 both in US dollars[6] (9.9 per cent) and euro (5 per cent). The decline was more strongly pronounced in the second half of the year, reflecting subdued international trade and market participants' concerns about negative effects of foreign trade conflicts on global economic activity. A temporary rise in oil prices was recorded after the Saudi Arabia oil refinery attack in September and the December agreement of OPEC+ countries to deeper oil production cut in the first quarter of 2020. International non-energy product prices in euro and US dollars moved in opposite directions in 2019 as the US dollar appreciated against the euro. Food and metal prices decreased strongly in US dollars from 2018 as a result of weaker global demand, while in euro both groups posted a rise.

Global inflation was 2.0 per cent at the end of 2019 and remained close to the December 2018's rate.[7] The inflation rate in emerging market economies surged to 2.8 per cent (2.2 per cent at the end of 2018), whereas in advanced economies its rate moderated to 1.3 per cent (1.7 per cent at the end of 2018).

Euro area inflation[8] decelerated to 1.3 per cent on an annual basis at the end of 2019 (1.5 per cent in December 2018) reflecting mainly the downward movement in international prices of energy products. Core inflation (excluding food, energy, alcohol and tobacco products) accelerated to 1.3 per cent (0.9 per cent at the close of 2018). Slovakia led at 3.2, Portugal trailing at 0.4 per cent at the end of the year.

US Consumer Price Index (CPI) inflation[9] accelerated to 2.3 per cent in December 2019 from 1.9 per cent at the end of 2018. Concurrently, annual inflation in the fourth quarter of 2019 measured by the personal consumption expenditure price index fell on 2018 fourth quarter's 1.9 per cent to 1.4 per cent, remaining below the Federal Open Market Committee (FOMC) target.

---

[5] Data on Luxembourg's real GDP growth were not published in 2019.

[6] Referred to as the US dollar below.

[7] Based on World Bank data, Global Economic Monitor Database. The World Bank measures CPI change in country groupings as a weighted average of CPI changes in group countries. Real GDP based on purchasing power parity is used to calculate country weights. Groups include only World Bank Member States. Data are seasonally adjusted.

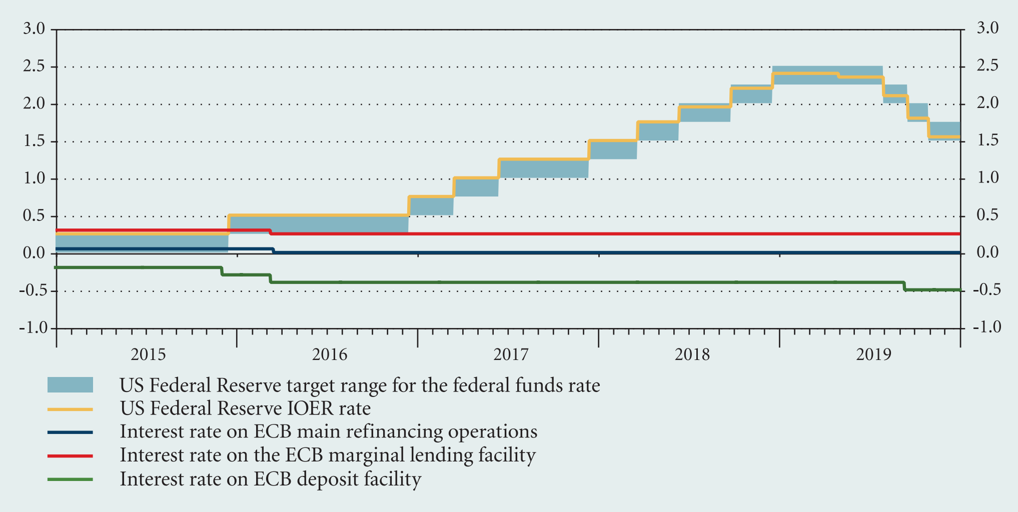
[8] Measured by the Harmonised Index of Consumer Prices.

[9] Non-seasonally adjusted data.

Amid risks for global economic growth to be lower than expected due to the euro area weaker economic activity and the downward trends in inflationary expectations, in 2019 the European Central Bank (ECB) launched accommodative monetary policy measures. In the first eight months of the year the Governing Council of the ECB left unchanged reference interest rates but changed their forward guidance, announced its plans to start a new series of Targeted Longer-term Refinancing Operations (TLTRO III) and possibly to launch monetary stimulus measures. Due to increasing risks to achieving the inflation target, in September 2019 a broad package of measures was approved, including a cut in the deposit facility rate by 10 basis points to -0.50 per cent, a restart of net purchases under the ECB's asset purchase programme (APP), an introduction of a two-tier system for banks' reserve remuneration, as well as a change in modalities of targeted longer-term refinancing operations (TLTRO III) to create more favourable bank lending conditions.[10]

Key Interest Rates of the ECB and the US Federal Reserve System

(per cent)



Sources: the ECB, the Federal Reserve System.

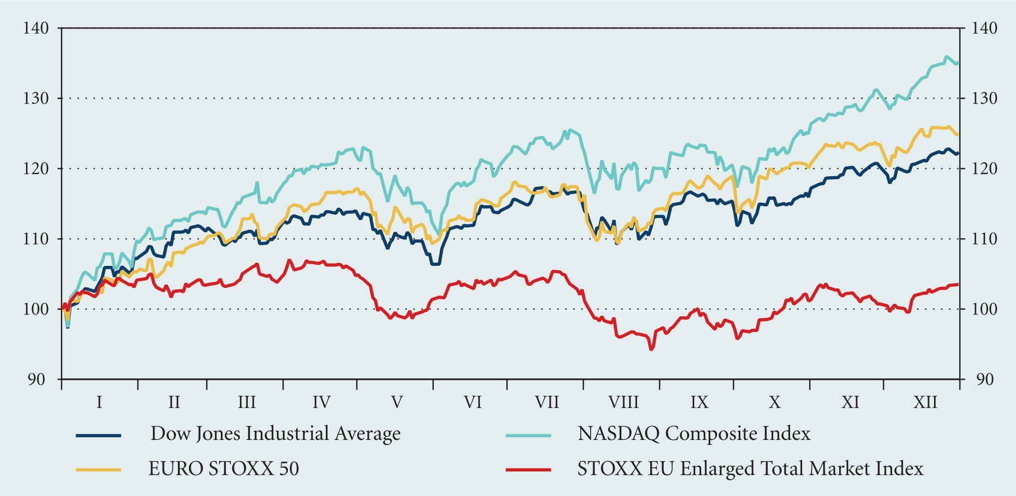
In July 2019 the US Federal Reserve cut the federal funds rate target range for the first time since December 2008, reducing the target range in three steps by 25 basis points. As a result in October 2019 the target range reached 1.50–1.75 per cent. Decisions to cut the target rate were made taking into account the risks for the economic activity to be lower than expected due to moderating growth of the global economy, international trade conflicts and uncertainty over Brexit.

In 2019 international financial market developments were characterised by lower price volatility of shares compared with 2018 and broadly upward trend in stock market indices. Higher stock exchange indices reflected the market participants' expectations that major central banks would launch monetary stimulus measures, with the upward dynamics of indices in the last quarter additionally underpinned by the expected conclusion of a partial trade deal between the USA and China. The increase in US stock exchange indices was comparatively strong in the last quarter as a result of favourable developments of trade negotiations with China. EURO STOXX 50 and STOXX EU ENLARGED to a lesser extent ended 2019 at levels above the average

[10] For details on ECB and US Federal Reserve monetary policies, see Chapter II.

in December 2018. Yields in international bond markets decreased steadily in the first eight months and rose somewhat in the last quarter.[11]

Stock Exchange Indices in the USA and Europe in 2019



Notes: US dollars, 31 December 2018 = 100.
STOXX EU Enlarged Total Market Index is a share price index of companies traded on stock markets of the 13 Member States which joined the European Union after 1 May 2004.

The Bulgarian Economy

In 2019 Bulgaria's real GDP rose 3.4 per cent from 3.1 per cent in 2018. Private consumption contributed most to growth of economic activity, government consumption and fixed capital investment contributing less. Private consumption increased amid low interest rates, enhanced demand for loans and active supply of lending resources by banks along with a further increase in labour income, employment growth and high consumer confidence. Higher gross fixed capital formation was mainly driven by government investment, whereas the amount of private investment remained close to the previous year's level.[12] External demand for Bulgarian goods and services in 2019 slowed down significantly, reflecting mostly weaker demand by Bulgaria's major trading partners such as Turkey, Romania, some euro area countries and China. Despite the unfavourable international economic situation exports of goods and services rose by 1.9 per cent in real terms due mostly to the exhausted effect of temporary supply side factors, limiting exports of petroleum products in 2018[13], and strengthening competitiveness of Bulgarian economy. Strong domestic demand boosted goods and services imports 2.4 per cent. This made net exports' contribution to real GDP growth negative at 0.3 percentage points.

[11] For more information on government bond markets, see Chapter II.

[12] Private and government investment is assessed by available national accounts data on overall investment in the economy, quarterly non-financial accounts data on the general government sector, and NSI reports on consolidated fiscal programme implementation.

[13] The first half of 2018 saw lower production of petroleum products as a result of a key sector company refurbishing its facilities.

GDP Change in Real Terms and Contribution by Component of Final Use

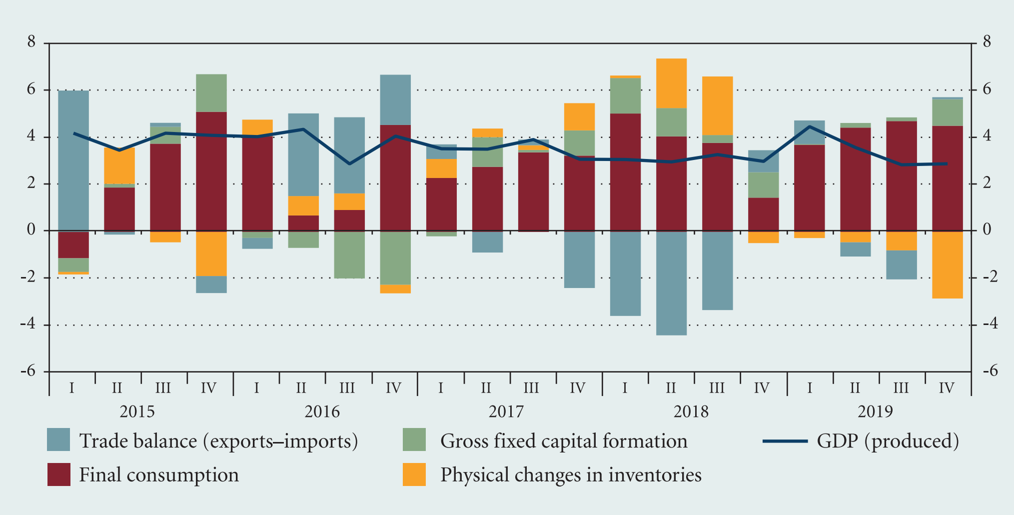
(on corresponding period of the previous year, non-seasonally adjusted data)

	2018		2019	
	Change (per cent)	Contribution, percentage points	Change (per cent)	Contribution, percentage points
GDP	**3.1**	-	**3.4**	-
Final consumption	4.6	3.5	5.7	4.4
Household consumption	4.3	2.5	5.8	3.4
NPISH consumption	13.0	0.1	10.1	0.1
Individual government consumption	6.2	0.5	4.5	0.4
Collective consumption	4.5	0.4	6.5	0.5
Gross fixed capital formation	5.4	1.0	2.2	0.4
Physical changes in inventories	-	1.1	-	-1.2
Exports (goods and services), net	-	-2.4	-	-0.3
Exports (goods and services)	1.7	1.1	1.9	1.3
Imports (goods and services)	5.7	-3.6	2.4	-1.5

Sources: the NSI, BNB calculations.

GDP Change in Real Terms and Contribution by Component of Final Use

(per cent, percentage points on corresponding quarter of previous year, non-seasonally adjusted data)



Sources: the NSI, BNB calculations.

Favourable labour market developments and high consumer confidence in 2019 boosted private consumption growth to 5.8 per cent in real terms from 4.4 per cent in 2018.

Government consumption grew 5.5 per cent in real terms from 5.3 per cent in 2018, reflecting mainly increasing government current wage, healthcare and operating expenditure.

Fixed capital investment growth was 2.2 per cent in real terms in 2019, slowing down from the previous year (5.4 per cent in 2018). Government investment contributed most to investment growth in the economy reflecting simultaneously risen national and EU co-financed capital expenditure. Private investment dynamics remained comparatively subdued throughout the year. Weaker external demand and worsening business expectations of economic activity curbed private investment growth.

Real gross value added growth in the economy slowed to 3.0 per cent from 3.5 per cent in 2018. This was attributable to the lower economic activity in the services sector, where value added rose by 3.0 per cent (5.8 per cent in 2018). In agriculture and industry economic activity was 3.6 and 2.8 per cent. Value added in real estate, finance and insurance, and general government rose comparatively more than in other services sub-sectors[14]. Construction repeated its positive previous years' contribution to industry value added growth as building construction output rose amid rising house prices in Bulgaria.[15] Value added in industry[16] posted growth on 2018 benefiting from the stronger increase in exports of goods and services and higher domestic demand.

Gross Value Added Change in Real Terms and Contribution by Industry

(on corresponding period last year, non-seasonally adjusted data)

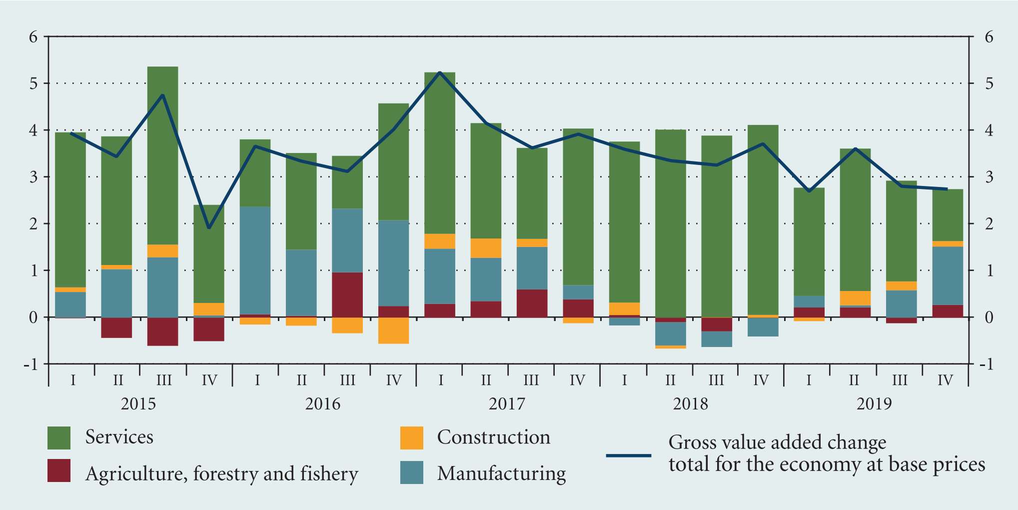
	2018		2019	
	Change (per cent)	Contribution, percentage points	Change (per cent)	Contribution, percentage points
Gross value added	**3.5**	-	**3.0**	-
Agriculture, forestry and fishery	-2.0	-0.1	3.6	0.1
Industry*	-1.1	-0.3	2.8	0.7
Services	5.8	3.9	3.0	2.1

* Industry and construction.

Sources: the NSI, BNB calculations.

Gross Value Added Change in Real Terms and Contribution by Industry

(per cent, percentage points on corresponding quarter of previous year, non-seasonally adjusted data)



Sources: the NSI, BNB calculations.

Labour market developments in 2019 remained favourable. Real wage increased and unemployment fell. The number of employed rose 0.3 per cent from -0.1 per cent in 2018 mainly due to growth in the services sector.

The NSI Labour Force Survey showed average unemployment dropping from 5.2 per cent in 2018 to 4.2 per cent in 2019. Employment Agency data on unemployment registrations show the average unemployment rate continuing to drop to 5.7 per cent from 6.2 per cent in 2018. NSI Labour Force Survey data show that in 2019 the number of people unemployed up to a year fell less than those unemployed for longer. The long-term unemployment share was 56.7 per cent from 58.6 per cent in 2018. The labour force participation rate of the 15–64 age group rose again, to 73.2 per cent

[14] Public administration, education, human health and social work activities.

[15] Construction production index data are used.

[16] Mining and quarrying; manufacturing; electricity, gas, steam and air conditioning supply; water supply; sewerage, waste management and remediation by economic activity groupings (A10).

from 71.5 per cent in 2018. The number of discouraged persons fell to 63,900 from 85,400 on average in 2018.

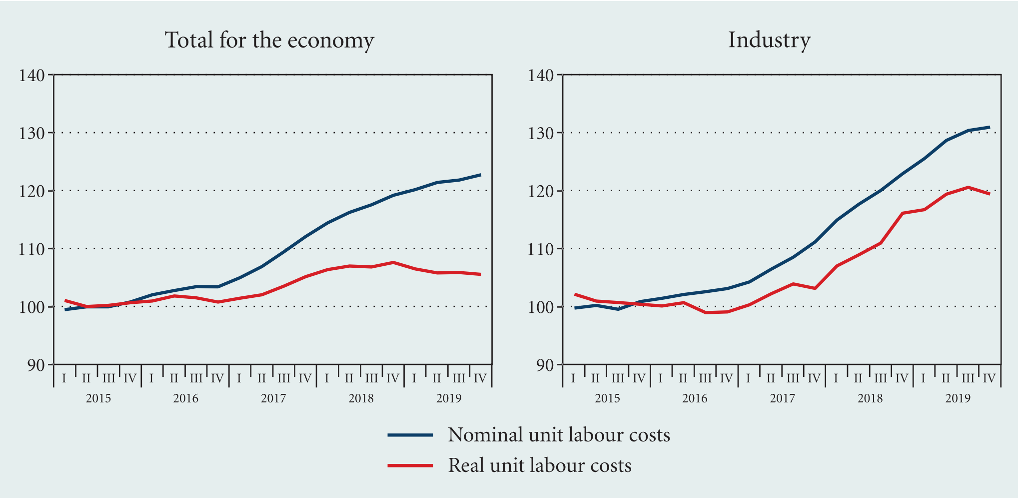
Strong labour demand, minimum pay and insurance threshold rises, and public sector pay rises drove labour costs. Compensation *per* employee in the overall economy rose 7.7 per cent nominally on 10.6 per cent in 2018. Compensation *per* employee rose by 6.1 per cent (9.7 per cent in 2018), with the highest rates reported in the sub-sector of industry (10.3 per cent in manufacturing and 23.1 per cent in construction) and in the public sector (10.9 per cent). The overall economy nominal wage *per* employee rose 5.8 per cent from 9.6 per cent in 2018. Real growth[17] was 3.3 per cent from 6.7 per cent in 2018.

Labour productivity[18] rose 3.0 per cent in 2019 from 3.2 per cent in the previous year. Agriculture and real estate operations exhibited the highest growth rate across subsectors (8.4 per cent and 5.5 per cent), while information and communication posted the strongest fall (-5.1 per cent).

Nominal unit labour cost growth slowed down significantly to 2.9 per cent from 6.3 per cent in 2018 due to slower growth in compensation *per* employee and buoyant labour productivity growth. Growth in manufacturing slowed down to 6.6 per cent from 10.6 per cent in 2018. Real unit labour costs in overall economy decreased 1.6 per cent from 2.2 per cent growth in 2018, with the services indicator dynamics contributing most to this.

Unit Labour Costs

(moving average, 2015 = 100)



Sources: the NSI, BNB calculations.

Gross operating surplus in the overall economy accelerated its growth rate to 7.5 per cent from 5.6 per cent in 2018. The services sector and, to much lesser extent, agriculture contributed most to this, while industry posted a fall. In the sector of services, general government, trade[19] and real estate operations had the largest positive contributions to operating surplus growth.

The GDP deflator was 4.7 per cent in 2019. By final use component all deflators were positive: the private consumption deflator at 2.0 per cent, the government

[17] Real wage is obtained as a result of deflating nominal wage by HICP.

[18] Real GDP measures labour productivity in the overall economy. Labour productivity by sector is calculated based on value added of the sector in real terms.

[19] Wholesale and retail trade; repair of motor vehicles and motorcycles; transportation and storage; accommodation and food service activities sector by A10 breakdown of economic activities.

consumption deflator at 9.3 per cent, the gross fixed capital formation deflator at 2.8 per cent, and the exports deflator at 2.4 per cent and the imports deflator at 0.4 per cent. By economic sector, deflators were positive in industry and services at 5.0 and 4.5 per cent, while the agriculture deflator was negative at -1.1 per cent.

At the close of 2019 annual consumer price inflation accounted for 3.1 per cent, accelerating on December 2018's 2.3 per cent.[20] Food and services contributed most to the accumulated inflation throughout the year: 1.5 percentage points and 0.8 percentage points respectively. As transport fuels contributed negatively to overall Inflation in most months of the year, higher annual international oil prices in euro at the end of 2019 were the major factor behind the positive inflation in this group. By the close of the year the inflation rate in services slowed down materially from December 2018 and accounted for 2.9 per cent reflecting mainly the price fall in insurance connected with travel and telecommunication services, and lower inflation in transport services.

The group of food had the largest contribution to overall inflation in most months of the year, the price index of this group rising in December 6.2 per cent on an annual basis from 2.4 per cent in December 2018. Accelerated food price growth was particularly pronounced in unprocessed food, whose contribution to overall Inflation reached 0.9 percentage points. The higher inflation in the group of unprocessed food was mainly driven by the meat and meat products sub-group. The strong pork price hike reflected the limited supply, higher producer[21] and import[22] prices due to African swine fever spread worldwide and in Bulgaria[23]. The price rise of meat was an important factor also behind higher annual inflation of processed food due to its indirect effect on prices of ready-to-eat foods available in food shops and supermarkets.

Core inflation (excluding food, energy products, goods and services with administratively controlled prices, and tobacco) slowed to 1.8 per cent annually at the close of the year from 2.5 per cent in December 2018. This dynamics was mainly driven by lower services inflation, while non-food goods had a low positive contribution throughout the year. Lower inflation in the services group reflected mostly cheaper transport and telecommunication services in most of 2019, slower inflation of transport services, and exhausted base effects in prices of insurance connected with travel and accommodation services, to a lesser extent. The lower contribution of transport services was due to the inflation slowdown in air transport and the drop in the price index of passenger automobile and other road transport. Concurrently, amid strong consumer demand and upward food price dynamics, the price rise in catering tended to accelerate, the group making the largest positive contribution to overall inflation across services components at the close of the year. In early 2019 industrial goods deflation which had been observed since 2010, was reversed and by the end of the year the price index posted an increase of 0.5 per cent from a fall of 0.5 per cent in December 2018. Following many years of a price fall motor vehicle prices rose, which was the major reason behind the upward price dynamics in the group. Prices of durable goods (excluding motor vehicles) continued to decrease, though at slower rates, while non-durable goods inflation remained low.

Inflation of goods and services with administratively controlled prices and tobacco products slightly fell accounting for 2.0 per cent at the end of 2019 from 2.3 per cent in December 2018. This reflected mainly the lower positive contribution of tobacco products due to the exhausted base effect of increased excise duties on cigarettes in early 2018.

[20] The analysis employs HICP data.

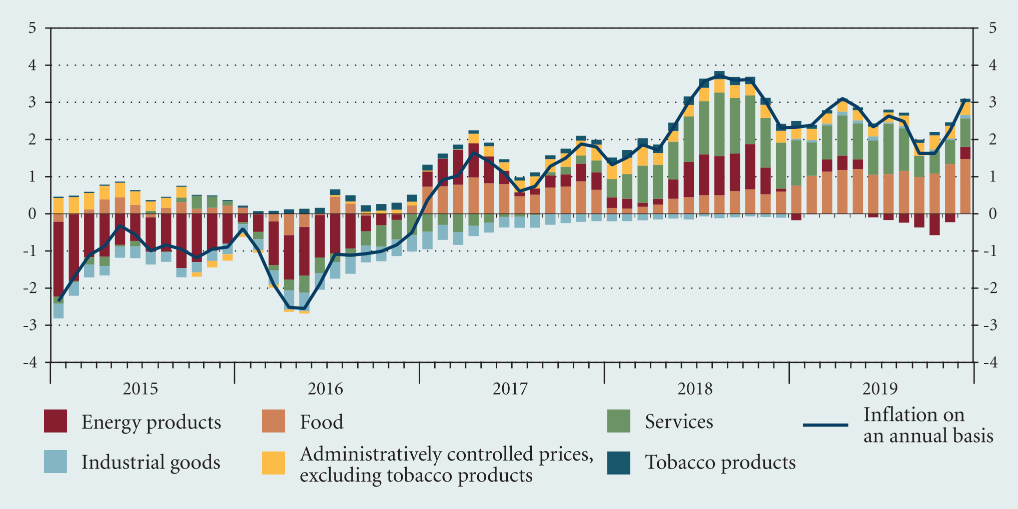
[21] NSI data on prices and producer price indices of agricultural produce.

[22] National accounts data on price deflator for imported goods and BNB calculations.

[23] The disease was registered in Bulgaria in July 2019.

Annual Inflation and Contributions by Major Group of Goods and Services

(per cent, percentage points)



Sources: the NSI, BNB calculations.

HICP Inflation Accumulated since the Year's Start and Contributions by Major Goods and Services Groups

	2018		2019	
Inflation (per cent)	2.3		3.1	
	Rate of inflation by group (per cent)	Contribution (percentage points)	Rate of inflation by group (per cent)	Contribution (percentage points)
Food	**2.4**	**0.60**	**6.2**	**1.47**
Processed food	2.5	0.42	3.4	0.54
Unprocessed food	2.2	0.18	11.8	0.93
Services	**5.0**	**1.24**	**2.9**	**0.77**
Catering	4.3	0.24	5.8	0.31
Transport services	3.6	0.12	1.9	0.06
Telecommunication services	2.4	0.11	-3.4	-0.17
Other services	6.7	0.77	4.4	0.56
Energy products	**1.0**	**0.08**	**4.1**	**0.33**
Transport fuels	-0.4	-0.03	5.5	0.35
Industrial goods	**-0.5**	**-0.11**	**0.5**	**0.09**
Goods and services with administratively controlled prices	**1.9**	**0.32**	**2.0**	**0.34**
Tobacco products	**4.1**	**0.19**	**2.2**	**0.09**

Notes: This structure corresponds to the Eurostat classification; tobacco products and goods and services with administratively controlled prices are shown separately. The index of goods and services with administratively controlled prices is calculated through the elementary aggregates level in the consumer basket.

Sources: the NSI, BNB calculations.

Preliminary balance of payments data show that in 2019 the overall balance on the current and capital accounts was in a EUR 3343.6 million surplus, up EUR 1968.2 million on 2018.

All sub-items added to current account surplus growth, with reduced deficit on the net primary income[24] contributing most due mainly to lower outflows under the reinvested profit item and smaller payment of distributed profit and dividends to

[24] Preliminary data subject to revision.

non-residents. The higher capital account surplus was mainly driven by higher capital transfers received under EU operational programmes.

In 2019 real imports posted stronger annual growth than exports but favourable terms of trade contributed to decreased trade balance deficit compared with 2018. Despite the substantial slowdown of external demand growth exported goods rose from the previous year mainly due to internal one-off factors. Concurrently, real imports of goods continued growing on an annual basis amid strong domestic demand.

Foreign trade figures[25] in 2019 show nominal goods exports rising 4.2 per cent on 2018, with the mineral products and fuels, machines, vehicles, appliances, instruments, and animal and plant products, food, drinks and tobacco groups having the strongest positive contribution. Increased exports of petroleum products reflected mostly the low base from the previous year when production of a key sector company was temporarily stopped due to refurbishing its facilities. Nominal goods imports rose 3.6 per cent, consumer and investment goods contributing most by use.

The higher positive services trade balance in 2019 reflected mostly increased nominal exports of services compared with 2018, while imports of services posted a fall compared with the previous year. The telecommunications, computer and information services subgroup recorded the strongest increase in exported services. The decreased imports of services was mainly ascribable to lower imports of insurance and pension services due to temporary factors.

In 2019 the secondary net income surplus rose from 2018, which reflected to a large extent lower payment of non-life insurance premiums/claims to non-residents.

The balance of payments financial account in 2019 was positive because foreign assets rose more than foreign liabilities. All sectors contributed to foreign assets growth, with long-term debt securities issued by non-residents acquired by other sectors[26] posting the highest increase. Direct investment attracted from other sectors increased foreign liabilities. Based on preliminary balance of payments data direct investment liabilities in the overall economy (reporting direct investment into Bulgaria) amounted to EUR 1348.0 million in 2019.

Net current, capital, and financial account flows cut BNB international reserves by EUR 559.4 million according to the balance of payments data (valuation adjustments and revaluations excluded). Taking into account changes in international foreign reserves on the BNB Issue Department balance sheet, including valuation adjustments and price revaluations, they fell EUR 236.6 million on the end of 2018.

In December 2019 gross external debt rose EUR 956.2 million from the end of 2018 to EUR 34.1 billion or 56.2 per cent of GDP. This was mainly attributable to intercompany loans and banks' increased debt to some extent.

The continuous labour income growth and faster gross operating surplus increase in the overall economy favoured the upward dynamics of broad money over 2019 amid economic agents' high propensity to save. The lack of sufficiently safe alternatives to bank deposits was another factor behind broad monetary aggregate growth. In December 2019 annual M3 growth accelerated to 9.9 per cent compared with 8 per cent at the end of 2018. Historically, low deposit rates were the reason for firms and households to continue to save mostly in the form of overnight deposits. Quasi-money

[25] The analysis employs balance of payments data to the sixth edition of the IMF Balance of Payments and International Investment Position Manual (IMF, 2008): BPM6. BPM6 introduced major methodological changes in reporting goods and services trade to a mismatch between data on them and those on international trade in goods compiled by the NSI.

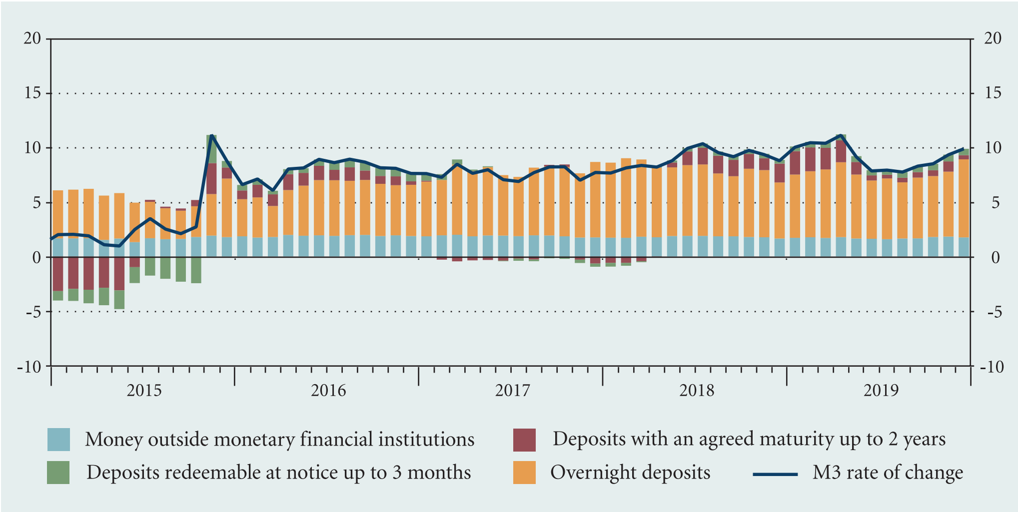
[26] Sectors other than central banks, other monetary financial institutions and general government.

continued to contribute to M3 growth though to a much lesser extent than overnight deposits. Money outside MFI contributed steadily through the year.

In December 2019 non-government sector deposits in the banking sector totalled BGN 85.2 billion, with annual growth accelerating to 9.7 per cent from 7.3 per cent at the end of 2018. Household deposits, totalling BGN 55.6 billion, continued to contribute most strongly to deposit growth. However, the acceleration recorded from the previous year was almost entirely due to the increase in deposits of non-financial corporations to BGN 26.5 billion at end-2019. In terms of currency, both corporations and households continued to save primarily in levs, with such deposits comprising 64.6 per cent of all non-government sector's deposits in December 2019.

Annual Rate of Change in M3 and Contribution by Component

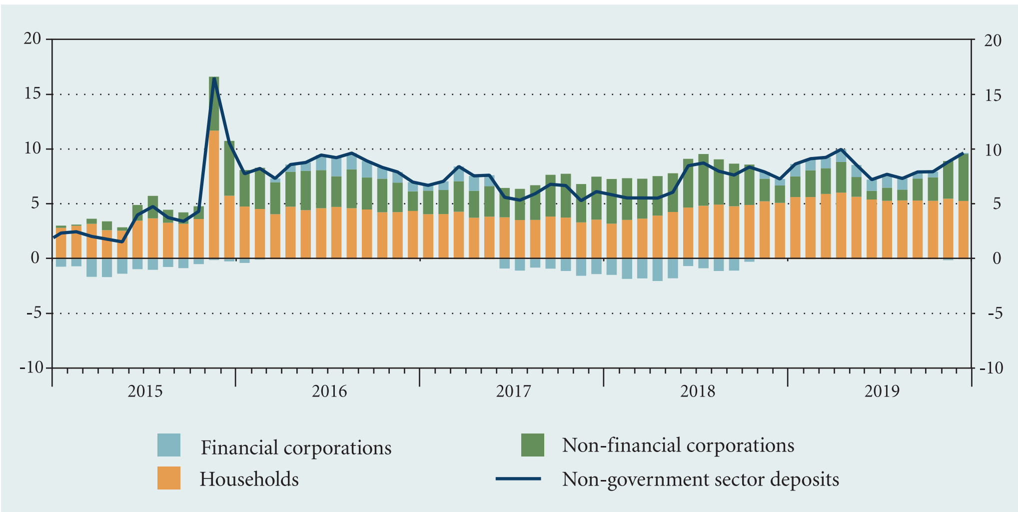
(per cent, percentage points)



Source: the BNB.

Annual Growth of Non-government Sector Deposits and Contribution by Sector

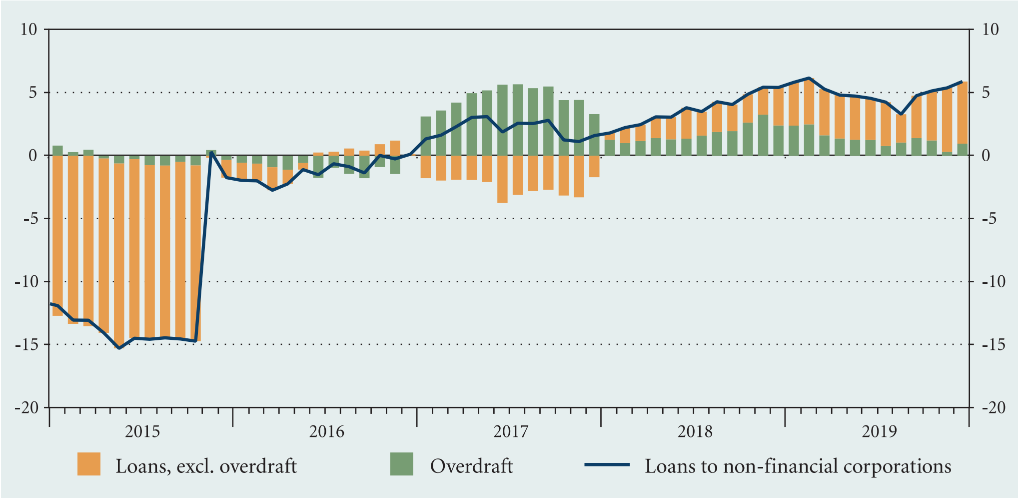
(per cent, percentage points)



Source: the BNB.

Annual Non-financial Corporation Credit Growth and Contributions by Loan Type

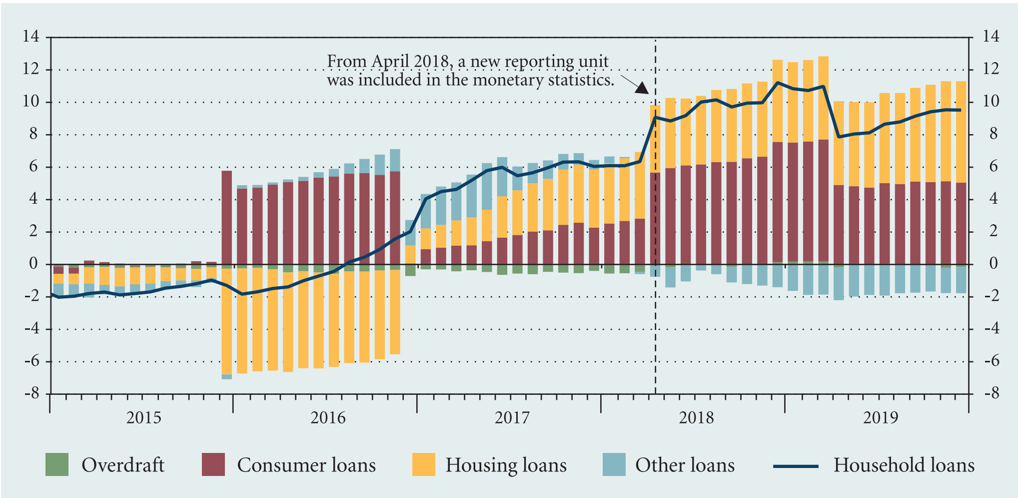
(per cent, percentage points)



Source: the BNB.

Annual Household Credit Growth and Contributions by Loan Type

(per cent, percentage points)



Source: the BNB.

Annual growth of credit to non-financial corporations and households remained comparatively high throughout the year, reflecting the favourable macroeconomic environment, low interest rates and high inflow of funds attracted in the banking system. In December 2019 loans to non-financial corporations rose 5.9 per cent on an annual basis from 5.4 per cent at end-2018. After the base effect of including a new reporting unit in the scope of monetary statistics[27] had been exhausted, an upward trend in loans to households occurred from the beginning of the second quarter, with annual growth reaching 9.5 per cent in December. Housing deposits contributed most

[27] As from April 2018 the other monetary financial institutions sector includes BNP Paribas Personal Finance S.A., Bulgaria branch, with balances reclassified from the other financial intermediaries sector. The reclassification results from BNP Paribas Personal Finance EAD specialised in lending being transformed through merger into the new credit institution. Until March 2018, it was included in the sector of other financial intermediaries for the purposes of monetary statistics.

to this growth, their annual growth rate accelerating to 14.5 per cent at end-2019 from 11.8 per cent in December 2018. Concurrently, the contribution of consumer loans remained relatively stable from April to December. Other loans continued to contribute negatively to the overall household loan dynamics largely as a result of government payment of loans extended under the National Programme for Energy Efficiency of Multi-family Residential Buildings which exceeded the volume of new loans under this programme.

BNB quarterly lending survey data show rising corporation and household credit demand in 2019. Banks' responses suggest that demand for funds for working capital and inventories and for financing investment along with low interest rates were the major factors behind the stronger demand for corporate loans. The overall macroeconomic environment and favourable outlook in the housing market also supported household demand for loans.

On the supply side, banks changed standards for extending corporate loans relatively little and eased somewhat household lending standards mostly in the fourth quarter. Eased lending standards were a result of the enhanced competition and high liquidity in the banking sector, increasing volume and low cost of attracted resources and lowered assessment of risk. In particular, risk assessments reflected the overall macroeconomic environment and business climate in the sectors with a large share in the credit portfolio, favourable housing market outlook and increased assessment of borrowers' solvency. Nevertheless, banks' lower lending risk appetite militated in favour of tighter corporate and household lending.

In 2019 the banking systems retained strong liquidity position, with liquid asset ratio (LCR)[28] accounting for 269.9 per cent from 294.1 per cent at the end of 2018.

In asset management, banks' claims on the non-government sector rose faster, their foreign assets rising less. Foreign liabilities and claims on the general government also slightly rose. Concurrently, banks' reserves with the BNB exhibited a decline reflecting the drop in excess reserves.[29] Stronger growth in foreign assets than foreign liabilities boosted net foreign assets BGN 2.2 billion to BGN 10.8 billion at the end of the year.

Banks' transactions with the BNB in reserve currency (euro) are their main instrument for lev liquidity management under Bulgaria's currency board. This takes advantage of the main currency board function: buying and selling levs for euro at the fixed exchange rate of the lev under the Law on the Bulgarian National Bank[30]. In 2019 the BNB bought EUR 1.7 billion net from banks.[31]

Interbank money market developments at the end of the third quarter of 2019 were impacted by the cut in the ECB deposit facility rate by 10 basis points to -0.50 per cent in September, resulting in a decline in the interest rate on banks' excess reserves with the BNB to -0.70 per cent.[32] In December LEONIA Plus index[33] accounted

[28] The liquidity coverage ratio for the banking system is calculated as the ratio of liquidity buffer to net liquidity outflows. For further information on liquidity reporting requirements, see the BNB quarterly Banks in Bulgaria.

[29] For further details see Chapter Four.

[30] See Chapter Two.

[31] Data refer to all bank transactions in foreign currency, including liquidity management operations related to the transfer of own funds from lev accounts with the BNB to own accounts with the BNB in euro and *vice versa*.

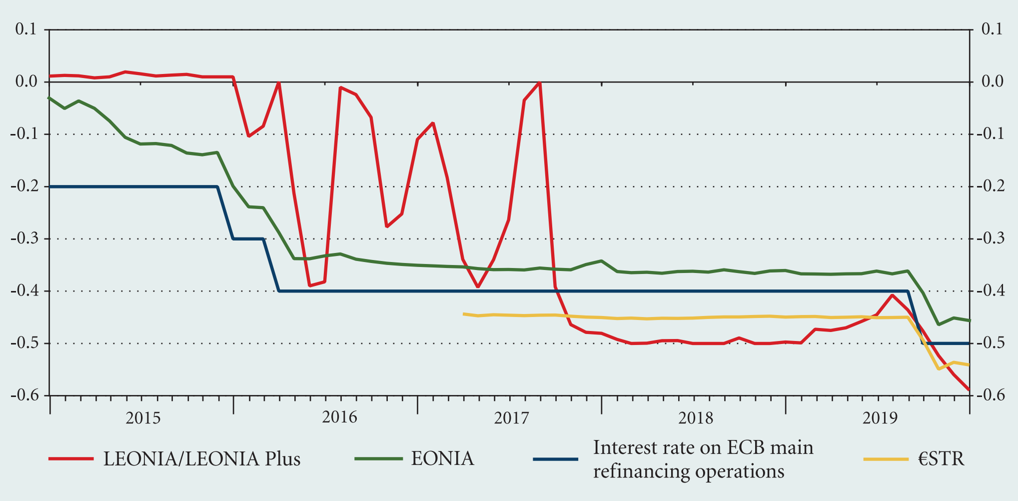
[32] The methodology for calculating interest rates on accounts with the BNB was changed upon a resolution of the BNB Governing Council, effective from 4 October 2017. According to this change the BNB applies on bank excess reserves whichever is lower between 0 per cent and ECB deposit facility rate reduced by 20 basis points.

[33] LEONIA Plus (LEv OverNight Interest Average Plus) is a reference rate of unsecured overnight deposit transactions in Bulgarian levs on the interbank market.

for -0.59 per cent falling by 15 basis points from August. Traded volumes in the lev interbank market rose in the second half-year, mostly in the overnight transactions segment. Interbank money market lev transactions in 2019 totalled BGN 42.1 billion, down 12.3 per cent on the previous year. Deposits comprised 86.9 per cent of the turnover, with government securities repos at 13.1 per cent. Overnight transactions dominated interbank deposit transactions with a share of 77.0 per cent.

Overnight Interbank Money Market Rates

(per cent)



Notes: LEONIA Plus replaced LEONIA on 1 July 2017. LEONIA Plus monthly values are calculated as an arithmetic average for those days when overnight unsecured lending transactions are concluded in the interbank market in levs.
€STR (Euro Short-Term Rate) replaced EONIA on 2 October 2019. EONIA (euro overnight index average) will be computed by applying a fixed spread to the €STR and published until the end of 2021.

Sources: the BNB, the ECB.

Since 2 October 2019 the ECB started publishing a new euro unsecured overnight rate, €STR, which replaced EONIA. Between 15 March 2017 and 30 September 2019 the ECB published preliminary data on the index (the so-called €STR preliminary). Values of LEONIA Plus index are much closer to those of €STR, than to EONIA. In December the spread between LEONIA Plus and €STR was negative, coming to -5 basis points.

In 2019 the budget balance on the consolidated fiscal programme was BGN -1148 million[34] (-1.0 per cent of GDP). The budget deficit reflected mainly the expenditure incurred under the investment project for acquiring a new type of fighter aircraft (totalling USD 1.2 billion) after the revision of the 2019 State Budget Law.[35] The deficit reported under the consolidated fiscal programme was significantly below the government programme BGN-2433 revised target for 2019, mainly through capital spending falling 10.5 per cent and tax revenue exceeding 2.1 the projections.

Consolidated fiscal programme revenue and grants in 2019 grew 11.1 per cent on an annual basis driven mainly by the dynamics of tax revenue and, to a lesser extent, by higher non-tax revenue and grants. Sustainable tax revenue growth was driven by

[34] Based on monthly reports on the implementation of budget, published on the Ministry of Finance website on 31 January 2019.

[35] The Law on Amendment of the 2019 State Budget of the Republic of Bulgaria increased the expenditure on the acquiring a new type of fighter aircraft by the Armed Forces of the Republic of Bulgaria. As a result the 2019 consolidated fiscal programme balance was revised from a deficit of 0.5 per cent to 2.1 per cent of GDP.

strong domestic demand and the upward dynamics of compensation *per* employee, with changes to tax and social security policy and measures to improve tax collectibility also adding to this effect. Social and health contributions up 11.5 per cent annually and VAT revenue up 10.2 per cent annually led to 9.4 per cent tax revenue growth. In 2019 the non-tax revenue growth rate slowed down, reflecting mainly the lower increase in revenue into the Electric Power System Security Fund's budget[36]. A significant drop was reported in the growth rate of revenue from grants *vis-à-vis* the previous year, reflecting a decelerated absorption of funds under EU 2014–2020 operational programmes.

Annual growth in total consolidated fiscal programme expenditure in 2019 amounted to 14.4 per cent and was mainly attributable to higher national budget current and capital expenditure. Public investment (5.6 percentage points), personnel costs (3.2 percentage points) and social payments (3.0 percentage points) contributed most substantially to budget expenditure growth. Capital spending grew 41.7 per cent on an annual basis attributable mainly to higher national capital expenditure related primarily to costs incurred under the investment project for acquiring a new type of fighter aircraft. Increased personnel costs reflected largely higher public sector income and the policy of wage increases in the education sector projected in the budgetary framework. Changes to the pension policy throughout the year were the main driver of social payments growth.

By the end of December 2019 the total amount of the fiscal reserve, including claims on EU funds over certified expenses, advance and other payments reached BGN 8768 million. Fiscal reserve deposit funds decreased BGN 448 million from 2018 amounting to BGN 8565 million, of which BGN 8104 million on deposits with the BNB. Revenue from domestic government securities (BGN 967.3 million) slightly exceeded payments on matured bonds. As a result the positive net financing of the budget with government securities amounted to BGN 47 million.[37] Net external financing on the consolidated fiscal programme was negative at BGN 66 million mainly because of an excess of payments over received new external loans. There were neither new government securities issues, nor payments on matured government securities on international capital markets in the year.

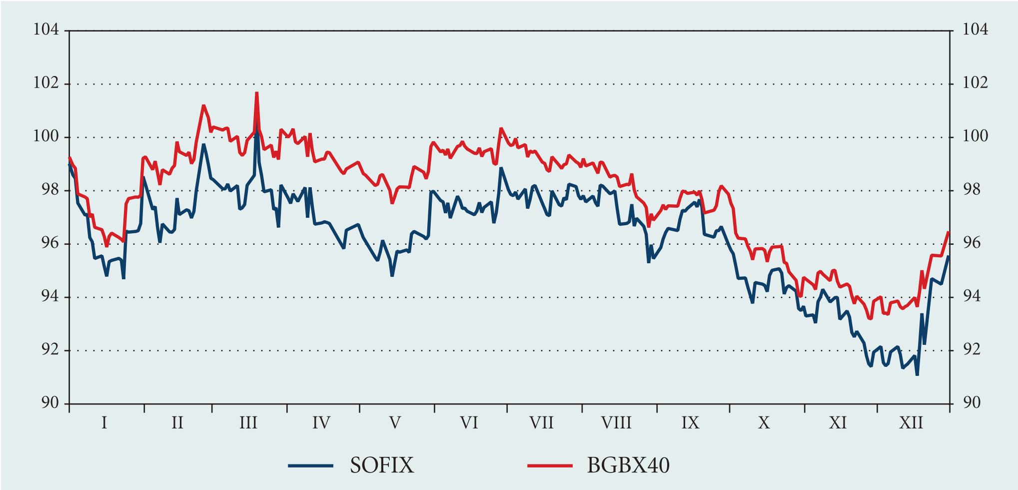
In 2019 Bulgarian Eurobond yields issued in international capital markets followed a downward pattern. The spread between yields of Bulgarian and German government securities declined substantially in the long end of the maturity curve. This was ascribable to Bulgaria's stable fiscal indicators, still higher demand over supply of Bulgarian bonds and Bulgaria's increased credit rating by a leading rating agency in the last quarter.

The leading Bulgarian Stock Exchange SOFIX and BGBX40 indices experienced no serious fluctuations in the first nine months of the year. Both indices decreased somewhat in October and November and recovered in December. By the end of December 2019 SOFIX fell by 4.4 per cent and BGBX40 by 3.5 per cent. December 2019 market capitalisation of the Bulgarian Stock Exchange, Sofia, was BGN 27.9 billion or 23.5 per cent of GDP from 24.4 per cent at end-2018.

[36] Lower growth in Electric Power System Security Fund's revenue over the second half of 2019 reflected a decision of the Energy and Water Regulatory Commission of July 2019 to cut the 'obligation to society' fee from BGN 36.75/MWh in 2018–2019 to BGN 19.57 in 2019–2020.

[37] For more information on government securities domestic market, see Chapter Twelve.

Bulgarian Stock Exchange Indices in 2019



Note: Indices based on 28 December 2018 = 100.

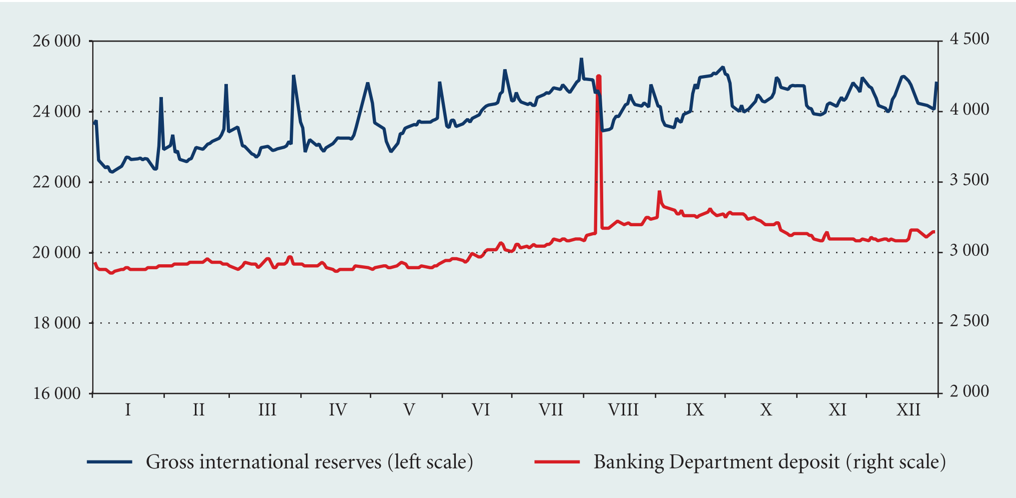
Sources: the BNB, Bulgarian Stock Exchange.

II. Gross International Reserves

The BNB manages its gross international reserves in line with the Law on the Bulgarian National Bank[38], investment constraints, business procedures and methodologies, and opportunities offered by international financial markets. BNB gross international reserves comprise the assets on the Issue Department's balance sheet. Their role is to provide complete cover for monetary liabilities under the fixed exchange rate of the lev to the euro provided for by the Law on the Bulgarian National Bank[39]. The excess of gross international reserves over monetary liabilities forms the Banking Department Deposit item or the net value in the Issue Department's balance sheet[40].

Gross International Reserves and Banking Department Deposit in 2019

(EUR million) (EUR million)



Notes: The chart shows daily movements of the Issue Department balance sheet figure and the Banking Department Deposit in the Issue Department balance sheet. The sharp increase in the value of Banking Department Deposit item on 7 and 8 August 2019 is due to the way of accounting of the funds provided for a customer payment (in the amount of USD 1200 million) from the date of the payment order to the value date of the payment.

Source: the BNB.

---

[38] There were no Law on the BNB amendments of the regulatory framework for gross international reserve management.

[39] The Law on the BNB Article 28, paragraph 2 defines the Bank's monetary obligations as all circulating cash issued by the BNB, and all balances of other entities' BNB accounts, except the IMF. Article 28 paragraph 3 defines what assets may comprise gross international reserves: monetary gold; Special Drawing Rights; banknotes and coins in freely convertible foreign currency; funds in freely convertible foreign currency held by the BNB on accounts with foreign central banks or other financial institutions or international financial organisations with one of the two highest ratings by two internationally recognised credit rating agencies; securities issued by foreign countries, central banks, other foreign financial institutions, or international financial organisations assigned one of the two highest ratings by two internationally recognised credit rating agencies; the balance on accounts receivable and payable on BNB forward or repo agreements with (or guaranteed by) foreign central banks, public international financial organisations or other foreign financial institutions with one of the two highest ratings from two internationally recognised credit agencies; and BNB futures and options which bind non-residents and which are payable in freely convertible foreign currency. The Law on the BNB stipulates that these assets are estimated at market value.

[40] The Law on the BNB Article 28, paragraph 1 states that 'the aggregate amount of monetary liabilities of the BNB shall not exceed the lev equivalent of gross international reserves,' with the lev equivalent calculated on the basis of the fixed exchange rate.

The Amount and Structure of Gross International Reserves

By the end of 2019 the book value of gross international reserves was EUR 24,835.6 million: a total decline of EUR 236.6 million or 0.94 per cent on the end of 2018. This amount includes balances in banks' TARGET2 national system component accounts worth some EUR 297.6 million at the end of 2019 (a decline by EUR 163 million on end-2018) and the two tranches of SDR 611 million in August and September 2009 upon general SDR allocation by the IMF [41].

Major factors affecting the market value of assets include income from reserve management, income from foreign currency revaluation, and external cash flow effects over the review period.

Foreign currency cash flows resulting from EUR 906.5 million withdrawals from commercial banks' accounts with the BNB, on the basis of which minimum required reserves and excess reserves are reported, had a negative contribution to the change in international reserves in 2019. Commercial banks' net purchases of reserve currency worth EUR 394.6 million contributed positively. There are also net receipts into government and other budget organisations' accounts in the amount of EUR 392.7 million mainly due to EC transfers on its account with the BNB and to payments made, the most significant being Ministry of Defence's purchase of a new type of military equipment worth USD 1200 million. By comparison, external cash inflows in the previous 2018 were positive amounting to EUR 1182 million.

External Cash Flows in Foreign Currency

(EUR million)

	2018	2019
I. Euro purchases and sales		
At tills	-66	-113
With banks	1,523	395
purchases from banks	31,257	60,351
sales to banks	-29,734	-59,956
Subtotal I	**1,457**	**282**
II. Currency flows with banks, the MF, *etc*		
Bank reserves (including minimum required reserves)	-1,471	-907
Government and other depositors	1,195	393
Subtotal II	**-276**	**-514**
Total I+II	**1,182**	**-232**

Source: the BNB.

The relative share of gold in gross international reserves rose on 2018 to 7.11 per cent on average from 6.57 per cent in 2018. This was mainly due to the rise in euro gold prices, while net euro cash outflows from the Issue Department balance sheet reduced somewhat the share of euro denominated assets to 92.13 per cent on average for 2019. USD denominated assets increased accounting for 0.21 per cent of gross international reserves.

[41] For further details see BNB Annual Report, 2009, p. 26. Balances in banks' TARGET2 national system component accounts and the two tranches of SDR are not included in the analysis of changes in the BNB gross international reserves below.

Currency Structure of Gross International Reserves

(per cent)

Currency	Issue Department balance sheet assets	
	2018	2019
EUR	92.69	92.13
USD	0.17	0.21
XAU	6.57	7.11
SDR	0.56	0.54
CHF	0.00	0.00

Note: Average values calculated on a daily basis for the period.

Source: the BNB.

In the international reserves structure by financial instrument securities continued to prevail with an average share of 61.77 per cent, while deposits accounted for 34 per cent.

Structure of Gross International Reserves by Financial Instrument

(per cent)

Financial instruments	2018	2019
Vault cash*	3.52	4.21
Deposits**	35.52	34.02
Securities**	60.96	61.77

Note: Average values calculated on a daily basis for the period.
* Account balances, payments and monetary gold.
** Including instruments in foreign currency and gold.

Source: the BNB.

In 2019 most of international reserves continued to be invested in the up to a year maturity sector: current accounts, short-term deposits in foreign currency and gold, and short-term securities, their share averaged 67.15 per cent over the period, slightly higher than in 2018. Investment in the one- to three-year and five- to ten-ten year maturity sectors declined on 2018, while those in the three- to five year-maturity sector rose to 7.08 per cent on average in 2019.

Gross International Reserves by Residual Term to Maturity (per cent)

(per cent)

Maturity sectors	2018	2019
Up to a year	67.12	67.15
One to three years	25.99	25.68
Three to five years	6.67	7.08
Five to ten years	0.22	0.10
Over ten years	0.00	0.00

Note: Average values calculated on a daily basis for the period.

Source: the BNB.

Gross International Reserves Risk and Return

The Market Environment

Market participants' moderating inflation expectations, deteriorating economic environment, slower economic growth and rising geopolitical risks prompted US and euro area central banks to change their monetary policies in 2019. Initially, the institutions signalled a possible move to a monetary accommodative policy in the second half year, if inflation and inflation expectations retain their downward dynamics. Consequently, they introduced changes in their monetary policies to stimulate the economies. The ECB approved a package of monetary stimulus measures, including a 10 basis point deposit facility cut to -0.50 per cent, recovered net purchases under the Asset Purchase Programme (APP), introduction of a two-tier system for reserve remuneration and improved parameters of the new series of targeted longer-term refinancing operations (TLTRO). The US Federal Open Market Committee (FOMC) cut in three steps the federal funds rate range by overall 75 basis points to 1.50–1.75 per cent and decided to stop reducing Federal Reserve holdings of debt securities.

The volatility of international financial markets slightly declined on previous year's level. Global stock market indices rose in 2019 with some of them reaching historically highest levels. The upward trend in the indices recorded in the first nine months of the year reflected market participants' expectations of accommodative monetary policy measures of the leading central banks along with expectations of reaching a preliminary trade agreement between the USA and China in the last quarter.

International government bond markets saw a steady price appreciation until mid-third quarter and a slight downward adjustment through year-end. Government bond yields declined in the first eight months of 2019 as a result of a number of factors behind the increased uncertainty about global economic growth. The main factors included incoming data releases indicating slowing activity in global manufacturing, rising concerns over new protectionist measures in international trade, the uncertainty surrounding Brexit and changing monetary policy stance of leading central banks. Over that period geopolitical risks also increased (the most important being the uncertainty in Middle East surrounding US sanctions against Iran, Hong Kong protests and political fragmentation in the EU) also leading to rising demand for low risk assets. In the last quarter of 2019 government bond yields increased driven by lower demand for safe assets as a result of the progress in trade negotiations between the USA and China, and the reduced in likelihood of the UK leaving the EU without a deal. The decline in uncertainty and the stabilisation of euro area economic data slightly improved market participants' inflation expectations and reduced the probability of ECB and US Federal Reserve undertaking additional expansionary monetary policy measures.

ECB and Federal Reserve Policies

Between January and August 2019 the ECB Governing Council left reference interest unchanged, while changing on several occasions their forward guidance and announcing its plans to launch a new series of Targeted Longer-term Refinancing Operations (TLTRO III). At its monetary policy meeting of 7 March the ECB Governing Council decided to change the forward guidance on interest rates according to which they will remain at their current levels at least until the end of 2019. It was announced that in September 2019 a new series of Targeted Longer-term Refinancing Operations (TLTRO III) would be launched, which would be carried out quarterly, would end in March 2021 and each operation would be with a maturity of two years. ECB credit operations would continue to be conducted as fixed rate tender procedures with full allotment for as long as necessary, and at least until the end of bank reserve maintenance period, starting in March 2021. At its 6 June meeting the ECB Governing Council changed again the forward guidance on key interest rates, and announced its expectations that they would remain at their present levels at least through the end of the first half of 2020, and in any case for as long as necessary to ensure the continued sustained convergence of inflation to the ECB's objective of below, but close to, 2 per cent over the medium term. The third series of targeted long-term refinancing operations TLTRO-III modalities were announced, with the interest rate in each operation set at a level that is 10 basis points above the average rate applied in the Eurosystem's main refinancing operations over the life of the respective TLTRO. For banks whose eligible net lending exceeds a benchmark, the interest rate would be lower and could be as low as the average interest rate on the ECB deposit facility over the life of the operation plus 10 basis points.

The indicators of market participants' inflation expectations in the euro area declined throughout the first half of 2019 reaching historical lows in spite of ECB's readiness to restart monetary stimulus in the second half of the year. To reverse the downward trend in inflation expectations, the ECB President stated in June that the Governing Council would discuss how monetary policy instruments should be adapted commensurate to the severity of the risk to price stability in the euro area. He pointed out that the ECB would look into the possibilities to use all monetary policy instruments, including cuts in reference interest rates and restarting the Asset Purchase Programme.

With a view to increasing risks to the inflation target as set by the ECB, over the third quarter of 2019 the Governing Council launched a series of monetary policy measures intended to stimulate the euro area economy. At its 25 July monetary policy meeting the ECB Governing Council changed the forward guidance on key interest rates, announcing that they would remain at their present or lower levels at least through the first half of 2020, and in any case for as long as necessary to ensure the continued sustained convergence of inflation to its aim over the medium term. At its monetary policy meeting of 12 September the ECB Governing Council approved a package of measures for monetary accommodation of the euro area economy, which is aimed at preserving favourable financial conditions to support euro area economic growth and to further enhance inflationary expectations, and, accordingly, to ensure the continued sustained convergence of inflation to its aim over the medium term. At the meeting the Governing Council took the following decisions:

- the interest rate on the deposit facility will be decreased by 10 basis points to -0.50 per cent. The interest rate on the main refinancing operations and the rate on the marginal lending facility will remain unchanged at 0.00 and 0.25 per cent respectively. The ECB Governing Council expects the key ECB interest rates to remain at their present or lower levels until it has seen the inflation outlook robustly converge to the inflation target, and such convergence has been consistently reflected in underlying inflation.
- net purchases will be restarted under the Governing Council's asset purchase programme at a monthly pace of EUR 20 billion as from 1 November and are expected to end shortly before raising the key ECB interest rates. Purchases of assets with yields below the deposit facility rate are allowed on all APP parts.
- as of 30 October 2019 a two-tier system for reserve remuneration of euro area banks will be introduced. Part of banks' holdings of excess liquidity will be remunerated at a rate of 0.0 per cent. The volume of this part will be equal to the minimum required reserves of each bank and a multiplier initially set at 6 will be

applied. The multiplier and the remuneration rate of this part bank's holdings of excess liquidity are subject to change.

– reinvestments of receipts from maturing securities purchased under the APP will continue in full for an extended period of time past the date of raising the key ECB interest rates.

– the modalities of the new series of targeted longer-term refinancing operations (TLTRO-III) will be changed. The interest rate in each operation will be set at the level of the average rate applied in the Eurosystem's main refinancing operations over the life of the respective TLTRO. For banks whose eligible net lending exceeds a benchmark, the rate applied on TLTRO-III operations will be lower, and can be as low as the average interest rate on the deposit facility over the life of the operation. The maturity of the operations will be extended from two to three years with early repayment option after two years.

In the fourth quarter of 2019 the ECB Governing Council made no changes to the key interest rates and the forward guidance to change them in the future. The Governing Council expected interest rates to remain at their present or lower levels until the robust convergence of inflation outlook to the level close to, but below, 2 per cent, affecting core inflation dynamics. At the monetary policy meeting of 12 December it was announced that a comprehensive review of all aspects of monetary policy strategy would be launched in January 2020, continuing throughout the year.

By 31 December 2019 the Eurosystem balance sheet figure decreased 0.6 per cent to EUR 4.69 trillion on the end of 2018. The amount of the four asset purchase programmes of the ECB increased compared with the end of 2018, as follows: by EUR 0.9 billion under the Public Sector Purchase Programme (PSPP), by EUR 6.5 billion under the Corporate Sector Purchase Programme (CSPP), by EUR 1.4 billion under the third Covered Bond Purchase Programme (CBPP3), and by EUR 0.9 billion under the Asset-Backed Securities Purchase Programme (ABSPP). As of 30 December 2019 excess liquidity in the banking system declined by EUR 74 billion to EUR 1712 billion on the end of 2018. In 2019 the effective Euro Overnight Index Average (EONIA) fell to -0.39 per cent against -0.36 per cent on average for 2018. On 2 October 2019 the ECB started publishing a new euro unsecured overnight rate, €STR, which will replace EONIA. With effect from the same date and until the end of 2021, EONIA will be computed by applying a fixed spread of 8.5 basis points to the €STR. In the fourth quarter of 2019 the average €STR was -0.54 per cent. EURIBOR interest rates on interbank market deposits in the euro area fell. By end-2019 the one-month deposit rate was -0.44 per cent (down 8 basis points on the end of 2018), and six- and twelve-month rates reached -0.32 and -0.25 per cent (down 9 and 13 basis points, respectively, from the end of 2018).

In 2019, the US Federal Open Market Committee decided to cut in three steps the federal funds rate range by 25 basis points reaching 1.50–1.75 per cent by the end of October. FOMC announced that with the decision to cut for the third time the key rate, the monetary policy adjustment process was completed. The Committee presented the decrease in the key rate range by overall 75 basis points as a preventive measure resulting from risks of lower than projected economic growth related to the consequences of trade conflicts, slowdown in global economy growth and continuing uncertainty surrounding Brexit. This signalled that the change was due to a reassessment of monetary policy stance and represents an adjustment in the middle of the economic cycle rather than the beginning of a new cycle of cutting key rates.

At its December 2019 meeting the Committee decided unanimously to maintain the federal funds rate range. The median of FOMC members' individual forecasts about the expected level of the federal funds rate fell by 25 basis points *per* year until the end of 2022 compared to the September 2019 forecast, reflecting the October decision for target range cut. The median showed the expectations of maintaining the target rate at its current level of 1.50–1.75 per cent in 2020 and increasing the key rate by 25 basis points in 2021 and 2022. The estimate of the long-run equilibrium level of federal funds rate remained unchanged at 2.50 per cent.

In the second half of September the Federal Reserve Bank of New York initiated measures to provide additional liquidity to the money market due to the lack of liquidity resulting from specific factors and the completion of the Federal Reserve balance sheet reduction process. On 11 October FOMC announced that effective 15 October 2019 the Federal Reserve will begin purchasing short-term government securities at least into the second quarter of 2020 and will conduct daily overnight repurchase operations and two-week term repurchase operations twice *per* week through January 2020. The press release emphasised that these steps were, in fact, technical measures intended to support FOMC monetary policy and do not change monetary policy stance. The technical modalities of operations include the purchase of short-term government securities with a monthly volume of around USD 60 billion until the end of the second quarter, the volume of daily overnight repurchase operations being at least USD 75 billion and that of two-week term repurchase operations at least USD 35 billion.

Euro Area and US Sovereign Bond Yield Curve

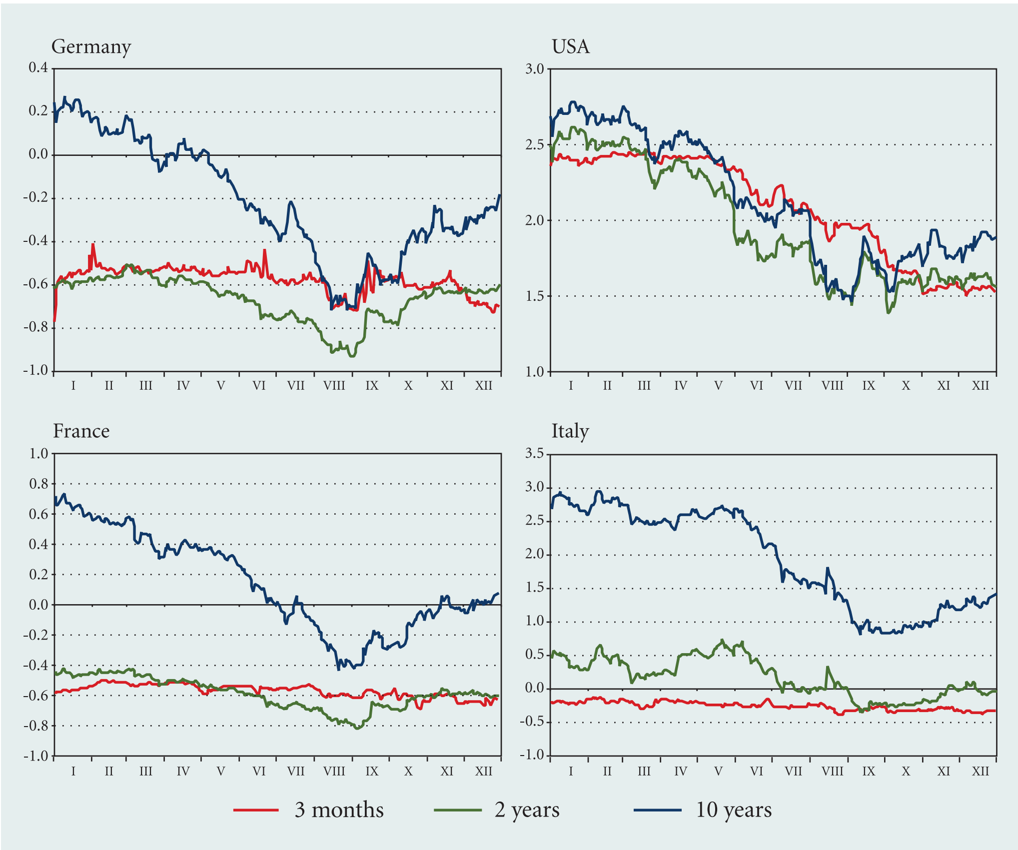
In 2019 German sovereign bond yields fell almost across all maturity sectors with a more significant decline in longer term bonds. Two-year bond yields rose by 1 basis point to -0.60 per cent on end-2018, with ten-year yields falling by 43 basis points to -0.19 per cent. These developments led to a 44 basis point flattening in the German bond yield curve measured by the difference between ten- and two-year yields. By half year's end all German government bonds with under 15-year maturities traded at negative yields. From January to December 2019 German government bond yields followed a downward trend. Major factors behind these developments included market participants' concerns about slowing global economic growth and changing monetary policy stance of leading central banks. Weaker than expected macroeconomic data releases for the euro area in this period and downward revisions of economic growth projections of a number of institutions, such as the EC, the IMF and the ECB, contributed to the decline in German government bond yields. Federal Reserve's more cautious approach in determining monetary policy also exerted downward pressure on German bond yields. Higher demand for German bonds as a safe asset was driven by the intensification of trade disputes between the USA and their major trading partners in the second and third quarters of 2019. Worsening prospects for global trade and economic growth had a negative effect on market inflation expectations in the euro area, resulting in changed market expectations of cuts in euro area's interest rates with enhancing expectations following ECB President's June statement in Sintra. At its monetary policy meeting of 12 September 2019 the ECB Governing Council decided to cut the deposit facility rate and to resume net asset purchases which weakened expectations for future deposit facility rate cuts. This increased German sovereign bond yields, mostly in short-term maturity sectors. The decision to resume trade negotiations between the USA and China along with the reduced likelihood of UK leaving the EU without a deal weakened the demand for safe assets, thus also contributing to German bond yield increase in the fourth quarter of 2019. The decline in uncertainty and the stabilisation of euro area macroeconomic data slightly improved market participants' inflation expectations and reduced the probability of ECB undertaking additional monetary policy measures.

In 2019 spreads between yields on euro area counties and German government securities contracted broadly. In the ten-year maturity sector the largest yield spread declines were recorded by Italy, Portugal, Ireland and Spain by 90, 85, 60 and 52 basis points, respectively. Yield spreads on Belgian and French government securities decreased to a lesser extent by 26 and 16 basis points. The results of European Parliament elections were a common factor for yield spread narrowing. These results were perceived positively by market participants pushing down the political risk premium in the EU. Another common factor for spread contraction involved the change in ECB monetary policy stance and monetary stimulus measures launched by the Bank in September 2019. Yield spreads on bonds of some euro area countries declined also as a result of their credit rating increase. S&P Agency raised Portugal's and Ireland's credit ratings from BBB- to BBB with a stable outlook and from A+ to AA- , respectively, while DBRS and Fitch agencies confirmed Italy's credit rating to BBB (high) with a stable outlook and to BBB with a negative outlook. The weakening of the effect of civil riots in France which affected negatively nation's economic activity at the end of 2018 contributed to French bond spreads decline in the first six months.

In the two-year sector, bond spreads of euro area countries narrowed to a lesser degree compared to those in the longer term sectors. The largest yield spread declines were recorded by Italy, Portugal, Spain and France by 54, 20, 16 and 13 basis points, respectively. Only the yield spread of Dutch two-year government bonds rose by 8 basis points due to technical reasons.

Government Bond Yields in 2019

(per cent)



By the close of 2019 the US government bond yield curve, measured by the difference between ten- and two-year bond yields, increased by 15 basis points on 2018. The change reflected the stronger short-term yield decline (by 92 basis points to 1.57 per cent for the two-year maturity sector) and a smaller decrease in long-term yields (by 77 basis points to 1.92 per cent for the ten-year sector). Decrease in short term maturity sector yields was driven by FOMC decisions to cut the federal funds target rate by overall 75 basis points and the change in market participants' expectations about the global economic outlook and the risk of recession in the USA. Lower decline in US medium and long-term yields was mainly due to the progress in trade negotiations between the USA and China in the fourth quarter. Continuing Eurosystem and Central Bank of Japan asset purchases in line with their monetary policies, development of trade relations between USA and their major trading partners, particularly China and increased geopolitical tensions in the Middle East also contributed to the fall in US medium- and long-maturity bond yields.

Gold and Exchange Rates

In 2019 gold prices rose significantly in both dollars and euro, posting an increase of 17.8 per cent to USD 1522.8 and 17.7 per cent to EUR 1356.0 per troy ounce at year-end. Gold price increase was concentrated mainly in the period June–September 2019 largely driven by investors' growing concerns about slowdown in global economic growth. These concerns arose primarily from the continuing uncertainty surrounding US trade relations with China and growing geopolitical risks, in particular in the Middle East and Hong Kong.

By end-2019 the US dollar appreciated by 1.2 per cent on an annual basis against the euro, ranging from USD 1.09 to USD 1.15 *per* EUR 1 (from EUR 0.87 to EUR 0.92 *per* USD 1). The major factor behind dollar appreciation against the euro was relatively weaker euro area economic data compared to those of the USA, which resulted in a change in ECB monetary policy stance, along with new monetary stimuli launched in September 2019. The dollar appreciation was also due to the continuing uncertainty surrounding US trade relations with China and geopolitical conflicts around the world, which prompted the demand for US dollars and US government securities as a safe asset. In the last weeks of 2019 the US dollar reversed its appreciation trend, slightly depreciating against the euro due to the weakening of trade tensions between the USA and China and the release of mostly positive euro area economic data.

The USD/EUR Exchange Rate in 2019

(EUR)

Troy Ounce Gold Price in US Dollars in 2019

(USD)

Troy Ounce Gold Price in Euro in 2019

(EUR)

Major Types of Risk

Annual net value risk in the Issue Department balance sheet measured by the standard deviation of net return was 7.87 per cent.

In 2019 international reserve **interest rate risk** measured by reserves' average modified duration was 0.86 years. The duration maintained was 0.02 years shorter than the average for 2018. The relative interest risk limit of Issue Department assets was set on the basis of not more than 0.20 per cent relative yield volatility.

The Law on the BNB stipulation that the sum of the absolute values of open foreign currency positions[42] in currencies other than euro, SDR, and monetary gold, should not exceed 2 per cent of the market value of monetary liabilities in these currencies constrained gross international reserve **currency risk.** There were minimal foreign currency open positions in the reporting period, the open position in monetary gold posing the main currency risk to the BNB.

[42] An open foreign currency position is the difference between the value of assets and liabilities in any currency other than euro.

In 2019 the Bank continued its conservative **credit risk** management policy in gross international reserve investment, while complying with temporary bans introduced in 2018 related to particular counterparties and issuers' securities. Covered bonds issued by Norway's financial institutions have been approved as an eligible investment instrument of secured debt class. Due to the upcoming withdrawal of the United Kingdom from the European Union new financial institutions designated by BNB's counterparties established in the UK were included in the lists of BNB counterparties of group I and II and will replace them after Brexit.

To achieve its main objective of very high international reserve liquidity and security, the BNB continued investing the main share of assets into euro area core country government bonds and government guaranteed debt, and into short term deposits with first class foreign banks.

By the end of 2019 some 66.8 per cent of international reserves was invested into assets with the highest AAA long-term credit rating.

Operational risk is managed by strict observance and control over investment constraints and relevant business procedures in managing foreign exchange reserves.

Return and Efficiency

Net income from assets in euro is the sum of three components: 1. income from gross international reserves investment in the original currency; 2. currency imbalance income[43]; and 3. liabilities expenditure and/or income. BNB income from international reserve investment was negative at EUR -63.99 million:- 0.28 per cent yield. This reflects mainly the negative interest rates on BNB's deposits with first class banks and negative yield of euro-denominated high credit quality bonds in which the BNB has invested. The positive income from foreign currency revaluation of assets and liabilities amounting to EUR 313.99 million (1.37 per cent) was largely attributable to the significant gold price surge in euro by 21 per cent over the review period. As a result of BNB interest rate policy on liabilities (applied to funds of the Ministry of Finance and other Bank customers and to banks' excess reserves with the BNB) the net financial result of liabilities was positive at 0.08 per cent in 2019, corresponding to a EUR 15.72 million income. These three components brought net earnings from BNB international reserve management to EUR 265.72 million: 1.16 per cent of total 2019 profitability[44].

International Reserves Income and Return* in 2019

Period	Net income (EUR million)	Net return (per cent)	Income (EUR million)	Return (per cent)	Income (EUR million)	Return (per cent)	Expenditure (EUR million)	Return (per cent)
			on assets		on currency revaluation of assets and liabilities		on liabilities	
	(1)+(2)+(3)		(1)		(2)		(3)	
First quarter	50.95	0.24	1.06	0.10	46.23	0.22	3.66	0.02
Second quarter	126.53	0.56	10.72	0.05	112.05	0.49	3.77	0.02
Third quarter	140.77	0.59	-17.80	-0.08	154.74	0.66	3.84	0.02
Fourth quarter	-52.54	-0.23	-57.97	-0.25	0.98	-0.01	4.45	0.02
Total	**265.72**	**1.16**	**-63.99**	**-0.28**	**313.99**	**1.37**	**15.72**	**0.08**

* Return between time T_0 and time T_N is calculated by chain linked returns for this period. The formula is: $R(T_0,T_N) = (1+r_1)(1+r_2)\ldots(1+r_N)-1$. This formula for calculating investment returns complies fully with the Global Investment Performance Standards (*GIPS*).

Source: the BNB.

[43] Currency imbalance income is the result of the effects of exchange rate movements on asset and liability open foreign currency positions.

[44] Total return is obtained as a product, rather than a sum, of the return of relevant components.

For the purpose of operational management international reserves are split into separate portfolios by currency and investment goal. Each portfolio has a benchmark, investment objectives and limits. The table below shows major BNB portfolios and the results from their management.

Portfolio Return and Risk in 2019

Portfolio	Return		Volatility (risk)		Information ratio[3]
	Absolute (per cent)	Relative[1] (basis points)	Absolute (basis points)	Relative[2] (basis points)	
Investment 1, EUR	-0.29	14	14	9	1.57
Investment 2, EUR	-0.30	14	14	10	1.43
External manager A, EUR	-0.01	35	77	11	3.18
External manager B, EUR	-0.30	7	78	8	0.82
Liquid, EUR	-0.44	11	1	1	-
Liquid, XAU	0.07	-	1	-	-
Liquid, USD	2.44	29	5	5	-

[1] A portfolio's positive relative return is attained profit against benchmark return. Relative returns with a negative sign are interpreted as opportunity cost in portfolio management.
[2] Relative volatility (relative risk) against benchmark indicates the degree of deviation of portfolio risk characteristics from benchmark through active portfolio management. The risk is on an annual basis.
[3] Information ratio is the ratio between relative portfolio return and relative portfolio risk on an annual basis.

Source: the BNB.

To diversify management styles and reduce operational risk, most euro-denominated assets continued being distributed into two investment portfolios with identical benchmarks and limits, but managed by different BNB teams. By the end of 2019 around 3 per cent of gross international reserves was managed by external managers that were international financial institutions. Beside additional diversification, using external managers helped exchange expertise in international market investment management. Liquid portfolios were intended mainly to assist liquidity management objectives and BNB foreign currency payment needs.

III. Payment Systems and Payment Oversight

The Law on the Bulgarian National Bank tasks the Bank with payment system organisation, support, and development by assisting the implementation, operation, and oversight of efficient payment mechanisms. The Bank's major goals are curbing systemic risk and integrating Bulgarian payment systems into the European payment infrastructure.

Bulgaria's lev payment systems are:

- RINGS, a real-time gross settlement system operated by the BNB;
- RINGS has these transaction settlement ancillary systems:
  - BISERA, for settling customer transfers at a designated time, operated by BORICA AD;
  - BORICA, for servicing bank card payments in Bulgaria, operated by BORICA AD.

Bulgaria's euro payment systems are:

- the TARGET2 national system component, TARGET2-BNB, run by the BNB;
- the TARGET2-BNB ancillary system:
  - BISERA7-EUR, a system for servicing customer transfers to be settled at a designated time, operated by BORICA AD.

Bulgaria's securities settlement systems, where the cash leg is settled in payment systems run by the BNB, are:

- the book-entry government securities settlement system, run by the BNB;
- the book-entry securities registration and servicing system, run by the Central Depository AD.

Lev Payment Systems

In 2019 the RINGS real-time gross settlement system processed most lev payments in Bulgaria. On 31 December 2019 the BNB and 24 banks participated in RINGS.

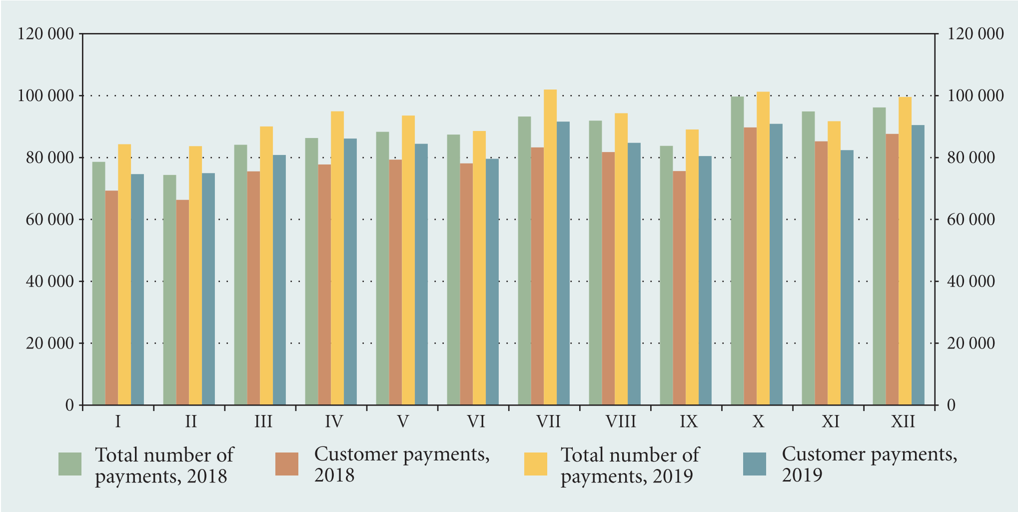
In 2019 RINGS processed payments worth BGN 1,093,093 million, up 17.7 per cent on 2018, their number reaching 1,113,790 or 5.1 per cent higher than in the prior year. There were 1,001,719 customer payments (89.1 per cent) of total payments for BGN 245,807 million (22.5 per cent of the total).

The daily average value of payments *via* the system was BGN 4393 million and their daily average number was 4473. The daily value peak was BGN 10,185 million, with a daily number peak of 8611.

In 2019, 73 per cent of payments by value were processed by noon and 87.7 per cent by 2.30 pm. The balance of 12.3 per cent went through by 5:30 pm. As regards system traffic, 83 per cent of RINGS payments were effected by 2.30 pm. RINGS offered 100 per cent availability[45] in the period under review.

[45] The ratio of time when the system is operational to scheduled operating time.

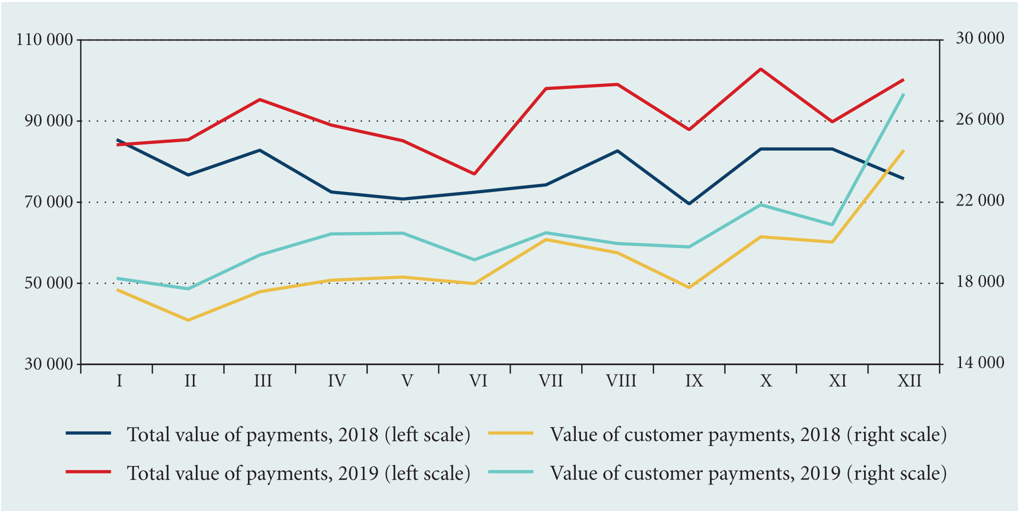
RINGS Payment Number in 2018 and 2019



Source: the BNB.

RINGS Payment Value in 2018 and 2019

(BGN million) (BGN million)



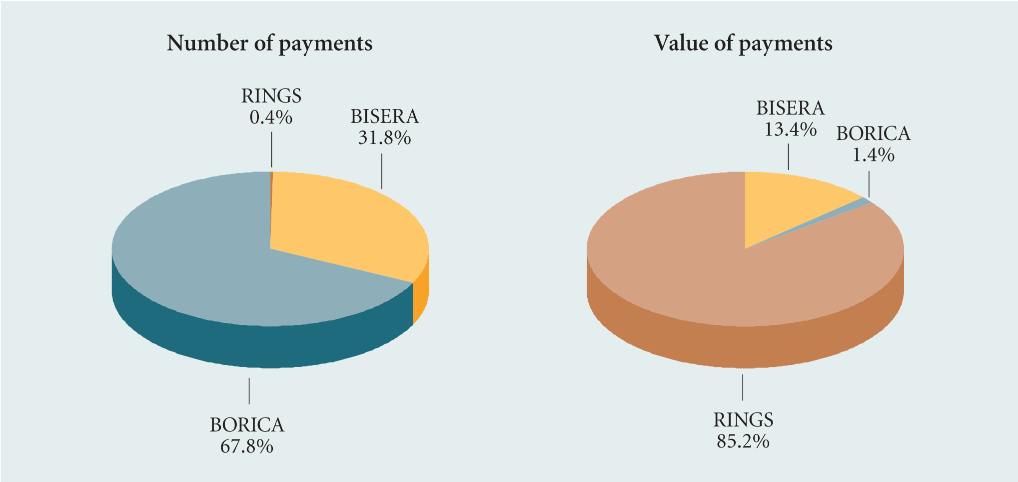
Source: the BNB.

Lev payment distribution in Bulgaria by payment system saw no changes from 2018. RINGS processed 85.2 per cent of the payments effected in Bulgaria. Values around 80 per cent are deemed optimal for the operation of real-time gross settlement systems. RINGS processed 0.4 per cent of the total number of lev non-cash payments.

In 2019 BORICA processed 179.5 million of ATM and POS terminal payments, totalling BGN 17,357.2 million: a 21.4 per cent numerical and 18.5 per cent value rise on 2018.

In 2019 BISERA processed 84.2 million of payments totalling BGN 172,608.8 million. Processed payments rose 8.4 per cent and 9.5 per cent in number and value.

Distribution of Lev Payments in Bulgaria by Payment System in 2019

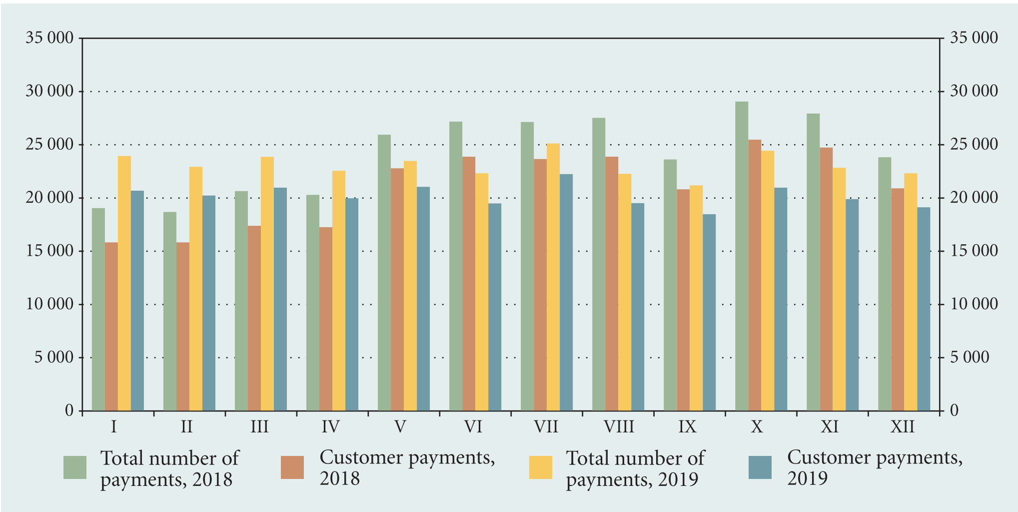


Source: the BNB.

Euro Payment Systems

TARGET2 settles gross euro payments in real time with central bank money. It is a Single Shared Platform (SSP) system, each participating and connected central bank responsible for its system component. From 1 February 2010, the BNB operates the TARGET2-BNB national system component and is responsible for the business relations of its participants and coordination with the European Central Bank and participant banks.

TARGET2-BNB Payment Number in 2018 and 2019



Source: the BNB.

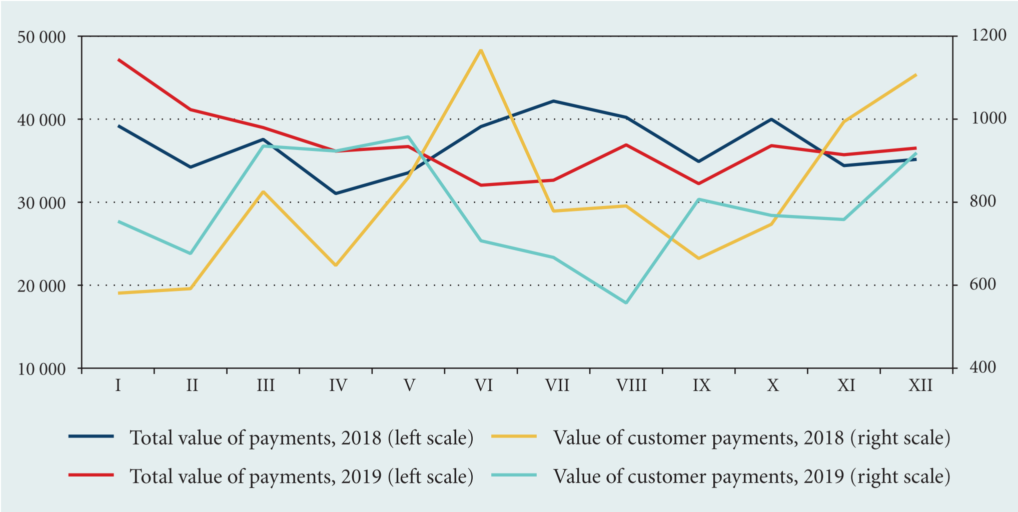
As of 31 December 2019 the system included the BNB, 18 direct participant banks, four addressable BIC holders, and three ancillary systems: the BISERA7-EUR for settling customer transfers in euro at a designated time; the securities settlement system run by Central Depository AD and the BNBGSSS for government securities settlement at the BNB.[46]

[46] For a current list of TARGET2 participants in TARGET2-BNB, see the BNB website: http://bnb.bg/PaymentSystem/PSTARGET2/PSTARGETList/index.htm?toLang=_EN

In 2019 TARGET2-BNB processed 277,343 customer and interbank payments for EUR 443,087 million. Customer payments numbered 242,653 (87.5 per cent of the total number of payments) accounting for EUR 9430 million (2.1 per cent of the total value of payments). Payment number fell 4.7 per cent and value rose 0.3 per cent on 2018.

TARGET2-BNB Payment Value in 2018 and 2019

(EUR million) (EUR million)



Source: the BNB.

Payments by other system components to banks were 94.7 per cent of the number and 85.5 per cent of the value of national component payments. The daily average number of system payments was 1088, their average value reaching EUR 1738 million. The daily number peak of payments ordered by TARGET2-BNB participants was 2013 with a daily transaction value peak of EUR 5048 million.

The BISERA7-EUR ancillary system processes designated time customer euro transfers. As of 31 December 2019, 14 banks participated in BISERA7-EUR. The system processed 20,553 payments for EUR 179 million, down 56.4 per cent in number and 49.9 per cent in value from 2018.

To meet the requirements of Regulation (EU) No 260/2012 of the European Parliament and of the Council the BISERA7-EUR payment system for small payments in euro processes SEPA payments and offers interoperability with the SEPA Clearer, Equens and EuroELIXIR systems, allowing SEPA credit transfers between banks in Bulgaria and other EU Member States.

Developing the Payment Services and Payment Systems Regulatory Framework

Over 2019 the BNB amended Ordinance No 3 of 18 April 2018 on the Terms and Procedure for Opening Payment Accounts, Executing Payment Transactions and Using Payment Instruments. Amendments mainly concern: regulation of the possibility of concluding a framework contract for off-site payment services through qualified electronic signature under the Electronic Document and Certification Services Law; alignment of the requirements to all payment service providers (banks, payment institutions and electronic money institutions) to use International Bank Account Number (IBAN) for payment accounts held with them, and implementation of Commission Delegated Regulation (EU) 2018/389 of 14 September 2019 supplementing

Directive 2015/2366 of the European Parliament and of the Council on regulatory technical standards for strong customer authentication and common and secure open standards of communication.

Over the review period the Governing Council of the BNB adopted amendments to Ordinance No 16 of the BNB of 29 March 2018 on Granting Licenses and Approvals, Entry into the Register under Article 19 of the Law on Payment Services and Payment Systems (LPSPS), and Requirements to the Activity of Operators of Payment Systems with Settlement Finality. Changes include improvement of provisions related to the information on the required minimum own funds of an electronic money institution in compliance with the requirements of LPSPS, and the obligation of an operator of a payment system with settlement finality to immediately notify the BNB in the event of incidents occurring to the operation of the payment system or to additional activities performed by the operator. A fee for examining applications on supplementing a license to operate as a payment institution was introduced.

Payment Systems Oversight

In line with the Law on the BNB and the Law on Payment Services and Payment Systems, the Bank regulates and oversees payment system operators with settlement finality, payment service providers and electronic money issuers in Bulgaria. The BNB grants licences and oversees compliance with national and European statutory requirements and relevant international principles, standards, and recommendations.

In 2019 four inspections of payment service providers licensed by the BNB were completed. The inspections were aimed to establish whether the activities of payment service providers and electronic money institutions complied with the requirements of the LPSPS, its implementing acts, EU legal framework, as well as with the requirements of the Law on the Measures against Money Laundering and the Law on Measures against Terrorist Financing. In two cases supervisory measures were imposed. Over the review period the Bank started an inspection of a payment service provider which continued into the new year. The Bank inspected a payment service provider on applying the requirements of Article 50, paragraph 2 of the LPSPS on providing preliminary information in providing currency exchange services. The Bank inspected four institutions to see whether they had provided payment services and/or had issued electronic money without due licence.

In 2019 the Bank launched a spot supervisory inspection to establish compliance with the statutory requirements on determining the amount of fees charged for services on payment accounts with basic features, as well as on measures launched to increase public awareness related to this type of account. The correspondence with BNB licensed payment service providers continued consistent with the spot inspection establishing compliance with the provisions of Regulation (EU) 2015/751 on interchange fees for card-based payment transactions. In 2019 the BNB started two spot supervisory inspections of payment service providers licensed by the BNB to establish compliance with the requirements of Regulation (EU) No 260/2012 establishing technical and business requirements for credit transfers and direct debits in euro, and on applying the requirements of the Opinion of the European Banking Authority on the deadline for the migration to strong customer authentication (SCA) for e-commerce card-based payment transactions (EBA-Op-2019-11). The inspections continued into the new year.

In accordance with LPSPS Article 33 paragraph 6 data and information were requested on all payment institutions and electronic money institutions operating in Bulgaria and licensed by other EU Member States to check the volume of their operations.

Under LPSPS requirements the BNB Governing Council decided on four applications on issuing a payment institution license and on three applications on supplementing a license to operate as a payment institution.

The Governing Council licensed Iris Solutions OOD to provide payment services under Article 4, items 7 and 8 of LPSPS: payment initiation services and account information services. The Bank refused to license two payment institutions to operate as payment institutions and another payment institution licensing procedure was terminated at the applicant's request.

In 2019 the license of Transcard Financial Services AD was supplemented by payment services in accordance with LPSPS Article 4, item 3c and item 4c: execution of credit transfers, including standing orders. In the review period the license of Diners Club Bulgaria AD was supplemented by payment services in accordance with LPSPS Article 4, item 3c: execution of credit transfers, including standing orders. The license of BORICA AD was supplemented by payment services under LPSPS Article 4, items 7 and 8: payment initiation services and account information services.

In 2019 the BNB withdrew the licence of Euromoney Transfer OOD to operate as a payment institution following its application.

By the end of the reporting period there were five payment institutions and five electronic money institutions licensed by the BNB.

Under LPSPS requirements the BNB Governing Council decided on seven notifications filed by service providers under LPSPS Article 2, paragraph 3 in relation to payment instruments provided by them, which may be used as limited network, and on three notifications filed by service providers under LPSPS Article 2, paragraph 4 in relation of transactions conducted under LPSPS Article 2, paragraph 1, item 12.

The past year saw these entries and deletions in/from registers under the LPSPS and BNB Ordinance No 16 of payment institutions and electronic money institutions licensed by the BNB:

– 226 agents were listed and 147 agents were delisted in the public register of licensed payment institutions and electronic money institutions operating in Bulgaria;
– nine agents were listed and five agents delisted in the public register of licensed payment institutions and electronic money institutions operating elsewhere in the EU.

The period saw EU Member States competent authorities notifications of the payment institutions, electronic money institutions and registered account information service providers licensed elsewhere in the EU and eligible to operate in Bulgaria:

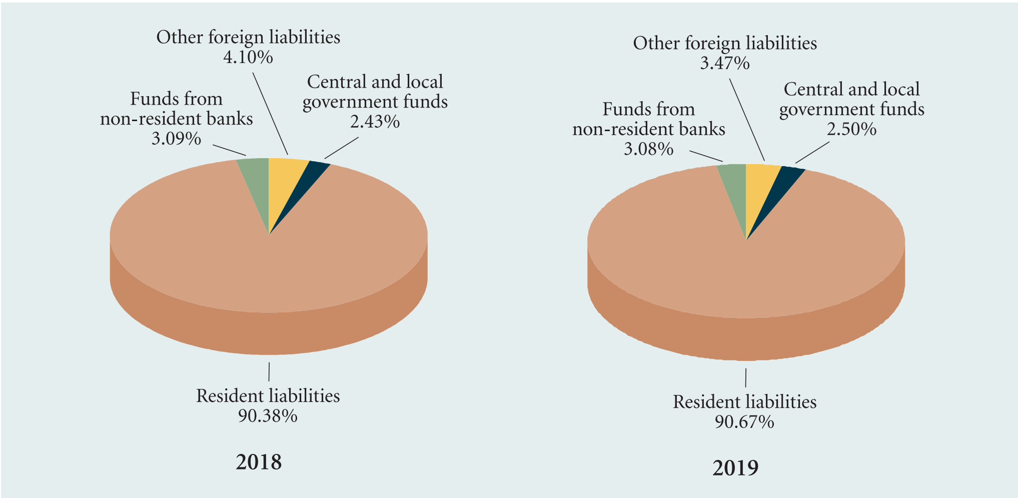
– for listing 154 payment institutions, electronic money institutions and account information service providers, established elsewhere in the EU and eligible to directly operate in Bulgaria, and for delisting 29 payment institutions and electronic money institutions operating directly in Bulgaria;
– for listing two branches of payment institutions and electronic money institutions licensed elsewhere in the EU and eligible to operate in Bulgaria;
– for listing 416 and delisting 434 agents of payment institutions and electronic money institutions licensed elsewhere in the EU and eligible to operate in Bulgaria;

The BNB enquired into 306 complaints submitted by members of the public and corporate payment service users. In 15 of them the Bank issued instructions. The other cases involved no breaches of the Law on Payment Services and Payment Systems and its statutory instruments, or were resolved in favour of payment service users through correspondence.

IV. Banks' Reserves at the BNB

In 2019 the average daily value of banks' attracted funds for minimum reserve calculation purposes (excluding central and local government budget accounts) rose by 7.5 per cent on 2018. The average daily value of funds attracted from residents (excluding central and local government budget funds) increased by 8.0 per cent, and those from non-residents by 2.3 per cent, with funds attracted from non-resident banks growing by 7.5 per cent. Funds attracted by banks from central and local budgets posted 10.8 per cent growth. The effective implicit ratio of minimum reserve requirements remained unchanged from the previous year at 9.4 per cent.[47] Reserve assets held by banks to cover this ratio include funds in banks' BNB accounts (8.3 per cent) and half of cash balances designated as reserves (1.1 per cent).

Structure of Attracted Funds in the Banking System*



* Average daily value of attracted funds for reserve calculation purposes.

Note: The sum may differ from 100 per cent due to rounding.

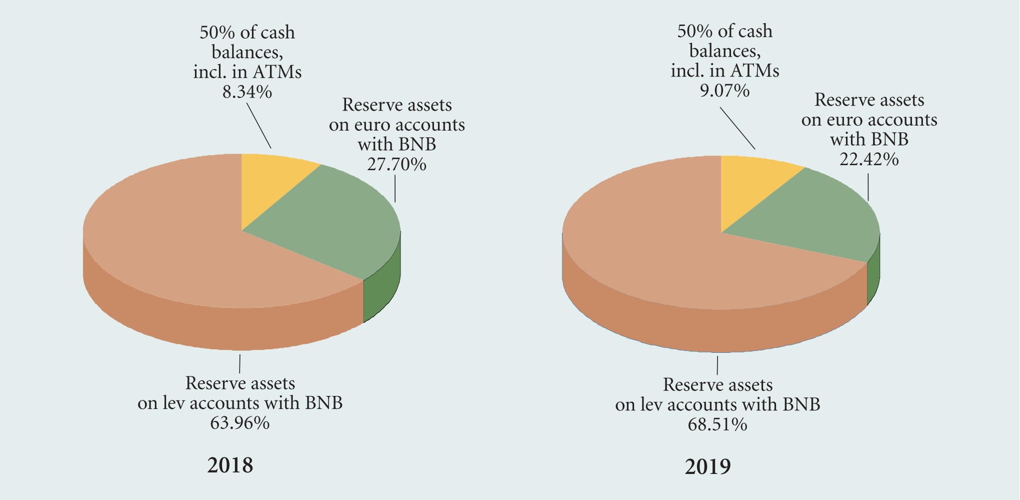
Source: the BNB.

Banks keep reserves in their own assets: BNB lev and euro accounts and half their cash balances, including in ATMs.[48] In 2019 the share of lev-denominated reserve assets was 68.5 per cent on an average daily basis, from 64.0 per cent a year earlier, while the share of euro reserve assets decreased to 22.4 per cent, from 27.7 per cent a year earlier. The share of cash balances designated as reserve assets, including in ATMs, rose from 8.3 per cent in 2018 to 9.1 per cent in 2019.

[47] BNB Ordinance No 21 on the Minimum Required Reserves Maintained with the BNB by Banks has left reserves on funds attracted from residents at 10 per cent of the deposit base, those from non-residents at 5 per cent, and those from central and local government budgets at nil since 4 January 2016.

[48] Article 4 of BNB Ordinance No 21.

Bank Reserve Asset Structure under Article 4 of Ordinance No 21

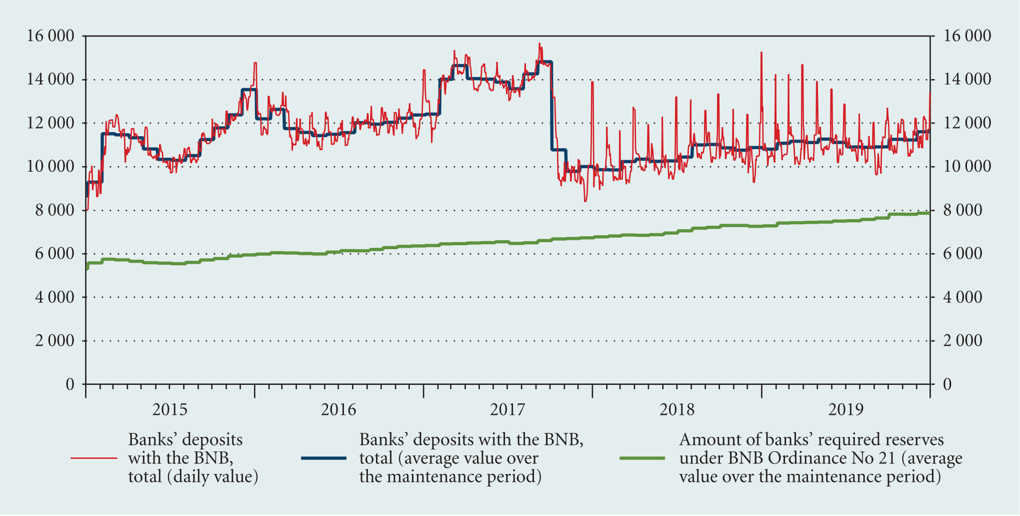


Source: the BNB.

Effective from 18 September 2019, the BNB applied -0.70 per cent interest on banks' excess reserves[49] under Ordinance No 21, reflecting the 10 basis point deposit facility cut to -0.50 per cent[50] approved by the ECB. Excess reserves on the BNB accounts continued to decrease over the period. Compared to 2018, the average daily amount of bank excess reserves declined by BGN 546.3 million. Funds in banks' BNB Ordinance No 21 accounts exceeded minima by 27.2 per cent on an average daily basis, against an excess of 36.8 per cent in 2018.

Banks' Reserves at the BNB

(BGN million)



Source: the BNB.

[49] Article 5, paragraph 1 of Ordinance No 21 defines excess reserves as funds exceeding the reserve requirement by more than 5 per cent holdings.

[50] According to the interest rate methodology for BNB accounts, effective since 4 October 2017, banks' excess reserves attract the lower of: 0 per cent or the ECB deposit facility rate reduced by 20 basis points.

V. Currency in Circulation

The Bulgarian National Bank has a monopoly on banknote and coin issue in Bulgaria. Its currency is mandatorily acceptable as legal tender at face value without restriction[51]. The Bank prints banknotes, mints coins, and keeps and scraps uncirculated or withdrawn currency.

In 2019 the BNB Governing Council adopted new BNB Ordinance No 18 on the Control over Quality of Banknotes and Coins in Circulation (published in the Darjaven Vestnik, issue 80 of 2019). This Ordinance specifies the classification of machines for servicing circulating cash in order to ensure that functionalities of existing machines in operation comply with the legislation. A procedure for submitting, upon request of banks, samples of new issues of banknotes/coins before their launch is introduced with the aim to adjust sorting and/or customer-operated machines with deposit function. The procedure for machine testing is amended. A rule provides for banks and service providers to submit test sets of genuine Bulgarian banknotes and coins, while tests with non-genuine banknotes/coins to be conducted by BNB officers. Added provisions point out that banks and service providers shall use in their business such models and types of machines which are included in the list on the BNB website, without requesting additional testing by the BNB, and are obliged to stop using the models/types of machines which have been removed from the BNB list. The Ordinance lays down the explicit obligation for banks to ensure that the immediate exchange of mutilated or damaged Bulgarian banknotes and coins is performed in all their branches and offices where cash operations are carried out, without charging fees or commissions for the exchange.

General Terms and Conditions and Tariff of Rates of the BNB for providing test sets and samples of banknotes and circulating coins and for testing of sorting machines and customer-operated machines were adopted and entered into force on 7 October 2019.

As of 1 November 2019 the BNB put into circulation a new banknote of BGN 50 nominal value, issue 2019. Its general appearance and main features are almost unchanged from the 1999 and 2006 BGN 50, but with new security features.

Pursuant to Article 26 of the Law on the BNB, the BNB Governing Council withdrew from circulation commemorative coins issued in 2013 which ceased to be legal tender on 8 February 2019. They may be exchanged at BNB tills at face value with no limit to amounts and no charge until 31 December 2020.

Banknotes and Coins in Circulation (Outside BNB Vaults)

At the end of 2019 currency in circulation[52] reached BGN 19,104.9 million, up BGN 1779.4 million or 10.27 per cent on 2018. The share of banknotes was 97.55 per cent, that of coins 2.41 per cent, and that of commemorative coins 0.04 per cent.

By the close of 2019 circulating banknotes numbered 504.4 million worth BGN 18,637.3 million. In a year, their number rose BGN 27.8 million or 5.83 per cent, and their value BGN 1735.7 million or 10.27 per cent. Previous periods' currency

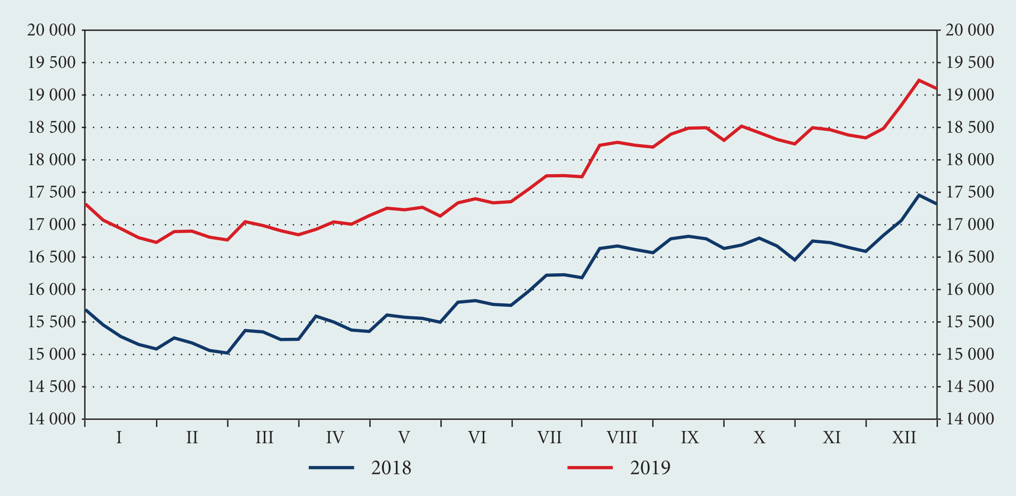
[51] Article 2, paragraph 5 and Article 25, paragraph 2 of the Law on the BNB.

[52] Banknotes and circulating coins issued after 5 July 1999, including those withdrawn from circulation with no time restriction on exchange, and commemorative coins issued after 5 July 1999, including those withdrawn from circulation whose exchange deadline have not fallen due.

circulation trend towards faster annual growth in the number of high value banknotes (BGN 50 and BGN 100) continued. Compared to the end of 2018, the number of BGN 50 banknotes increased BGN 20.4 million or 15.46 per cent and that of BGN 100 banknotes BGN 6.9 million or 10.85 per cent. The BGN 50 and 100 banknotes contributed most to the annual rise in the number of circulating banknotes.

Banknotes and Coins in Circulation (Outside BNB Vaults)

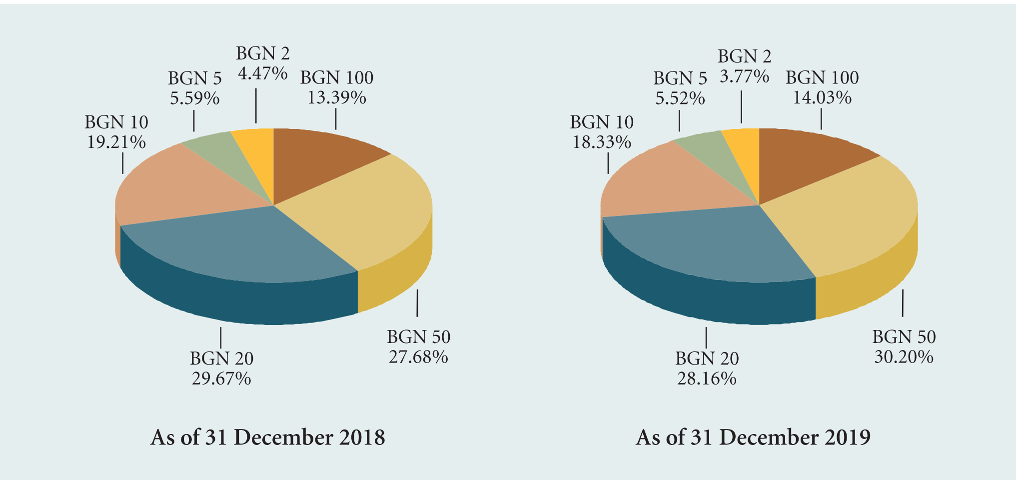
(BGN million)



Source: the BNB.

The BGN 50 banknote continued to hold the largest 30.20 per cent share in the total number of circulating banknotes. Recent years' upward trend in the shares of highest value banknotes by number continued. The shares of BGN 50 and 100 rose by 2.52 and 0.64 percentage points over the year. As a result, the share of BGN 20 banknotes fell 1.51 percentage points and that of BGN 5 and 10 banknotes by 0.07 and 0.88 percentage points. In a year, the share of BGN 2 banknotes fell 0.70 percentage points due to the BGN 2 bill's rollover with a coin.

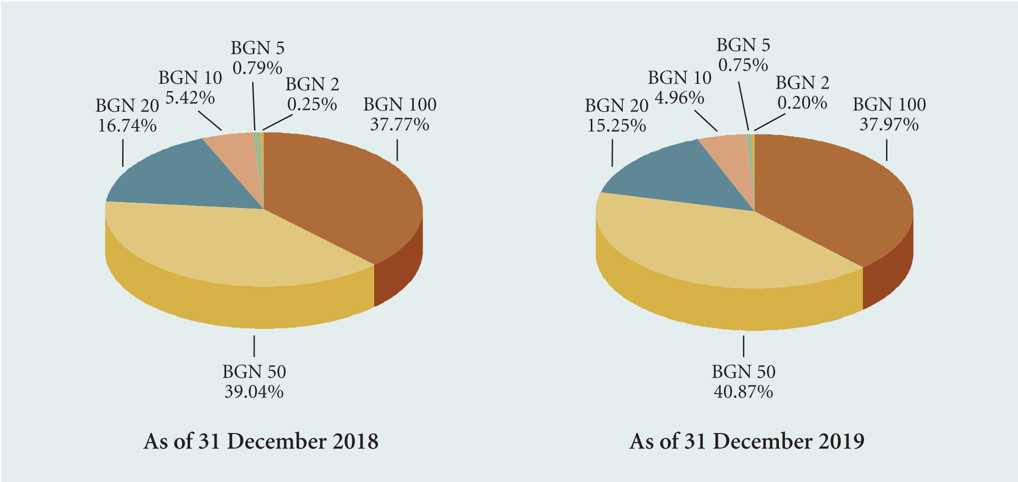
Individual Denomination Shares in the Total Number of Circulating Banknotes



Source: the BNB.

At the end of 2019 the BGN 50 and 100 banknotes held the largest value share of 40.87 and 37.97 per cent in the structure of circulating banknotes. Their share by value rose 1.83 and 0.20 percentage points from the end of 2018. Compared to the same period the shares of the other banknotes fell, that of the BGN 20 dropping most by 1.49 percentage points: from 16.74 to 15.25 per cent. The share of the BGN 10 declined by 0.46 percentage points: from 5.42 to 4.96 per cent. In a year, the BGN 5 banknote posted the smallest decline of 0.04 percentage points.

Individual Denomination Shares in the Total Value of Circulating Banknotes

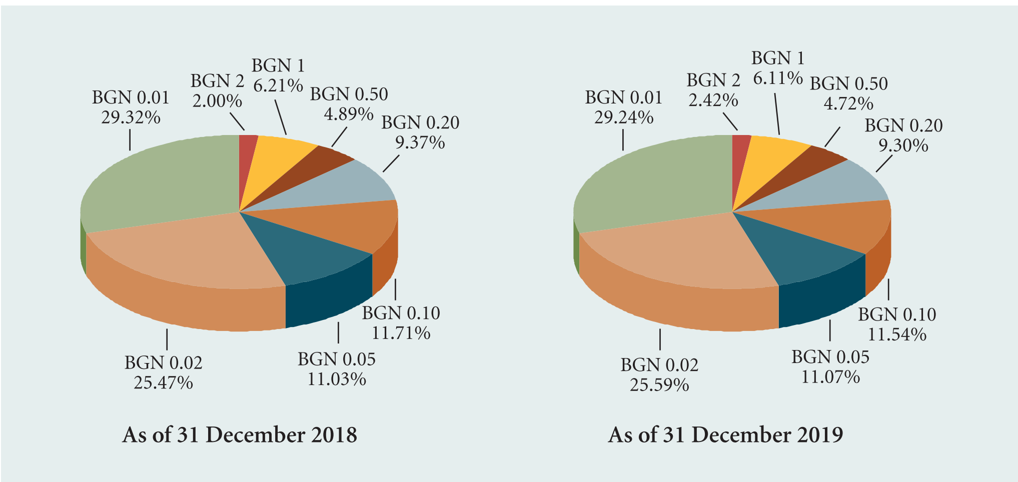


Source: the BNB.

The average circulating banknote was worth BGN 36.94 at the close of 2019, up BGN 1.49 or 4.20 per cent from 2018, reflecting higher BGN 50 and BGN 100 growth in currency in circulation.

In late 2019, 2598.7 million coins worth BGN 459.7 million circulated. Year on year, their number rose 159.2 million (6.53 per cent), and their value BGN 43.6 million (10.48 per cent). The general rising trend in the number of circulating coins continued. The numbers of BGN 0.01 and 0.02 coins rose most by BGN 44.5 million (6.22 per cent) and 43.7 million (7.03 per cent). The number of BGN 2 coins continued growing fast by 14.1 million or 28.93 per cent to 62.9 million at the end of the year. The number of BGN 0.05, 0.10, 0.20, 0.50 and 1 coins rose from 3.4 to 18.6 million (2.86 per cent to 6.93 per cent).

Individual Nominal Value Shares in the Total Number of Circulating Coins



Source: the BNB.

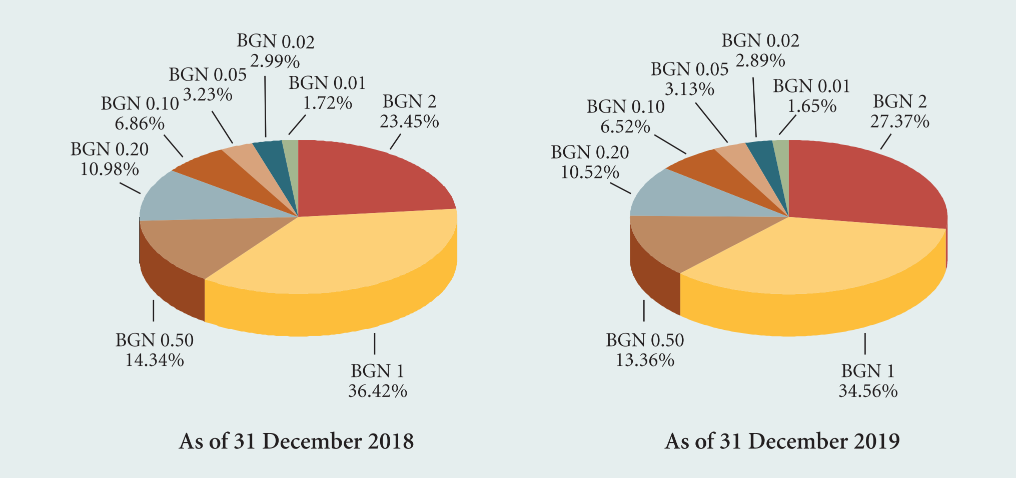
Circulating BGN 0.01 coins had the greatest 29.24 per cent share of circulating coins, with 759.8 million coins circulating outside BNB vaults by 31 December. The BGN 2 coin held the smallest share at 2.42 per cent. The numerical shares of BGN 0.02, 0.05 and 2 coins rose on the end of 2018. Over the same period, the share of other denominations fell.

At the end of 2019 the BGN 1 coin occupied the largest share at 34.56 per cent in the structure of circulating coins by value.

Developments in the structure of circulating coins by value reflected mainly the new BGN 2 coin entering currency circulation. It is the only coin whose share grew on an annual basis by 3.92 percentage points reaching 27.37 per cent. The shares of other denominations in the total value of circulating coins fell on the end of 2018, with BGN 1 and 0.50 coins posting the sharpest declines of 1.86 and 0.98 percentage points.

The average coin circulating at the end of 2019 was worth BGN 0.18: up BGN 0.01 in a year as a result of the new BGN 2 coin entering currency circulation.

Individual Nominal Value Shares in the Value of Circulating Coins



Source: the BNB.

Non-genuine Banknotes and Circulating Coins

In 2019 the BNB National Analysis Centre retained 1314 non-genuine Bulgarian banknotes which had entered into circulation, 533 more than their number in 2018. The share of retained non-genuine banknotes remained very low at 0.00026 per cent of total circulating banknotes.

The BGN 20 banknote had the largest share of all retained non-genuine banknotes at 69.71 per cent, followed by the BGN 50 at 16.51 per cent and the BGN 10 at 11.64 per cent. Non-genuine BGN 100, 5 and 2 banknotes' shares were 1.37, 0.53 and 0.23 per cent.

There were 452 non-genuine retained coins: 181 BGN 2s, 71 BGN 1s and 200 BGN 0.50s. The share of retained circulating non-genuine Bulgarian coins compared to the number of coins in circulation was also very low at 0.000017 per cent by the end of 2019.

Performing its duty to evaluate suspect foreign banknotes and coins, in 2019 the BNB retained: 2348 euro banknotes, 550 US dollar banknotes, and 156 assorted foreign non-genuine banknotes.

BNB Issue and Cash Operations

BNB issue and cash operations include: banknote and coin production, accepting, delivering, repaying, processing, authenticity and fitness checking of Bulgarian banknotes and coins and foreign currency, exchanging damaged Bulgarian banknotes and coins, and scrapping unfit Bulgarian banknotes and coins.

In 2019 producers supplied 136.6 million new banknotes and 204.1 million new coins worth BGN 4664.3 million. The BNB launched four commemorative coins as provisioned in Article 25, paragraph 1 of the Law on the BNB and the 2019 Minting Programme.[53]

In 2019 banks deposited BGN 17,170.6 million of cash, up BGN 616.5 million or 3.72 per cent on 2018. Over the same period, Bulgarian banknotes and coins worth BGN 18,949.1 million were withdrawn from the BNB: up BGN 771.2 million or 4.24 per cent in a year.

In 2019 banknotes recirculated through BNB tills an average of 1.7 times. Highest and lowest value banknotes returned less often, from 0.1 to 1.2 times; BGN 10 and BGN 20 banknotes returned more often at 3.4 and 2.6 times.

In 2019 banknote processing machines tested 781.1 million banknotes and 78.3 million coins. These numbers fell 1.48 and 5.75 per cent on last year. BGN 20s and 10s and BGN 0.20s, 0.50s and 1s had the largest nominal value shares at 43.36 and 35.62 per cent and 13.92, 16.22 and 21.40 per cent.

Cash quality and integrity checks identified some 48.3 million banknotes as unfit for circulation, down 7.3 million (13.18 per cent) on 2018. BGN 10 and 20s had the largest shares of unfit banknotes at 36.87 per cent and 35.20 per cent. The share of unfit banknotes processed in 2019 was 6.18 per cent. In a year, processing and fitness checks revealed 1.3 million unfit coins, up 10.64 per cent from the previous year. The share of unfit coins processed in 2019 was 1.72 per cent.

In 2019 the BNB bought EUR 0.6 million of reserve currency, including EUR 0.5 million from budget organisations and EUR 0.01 million from individuals. At the same time, the Bank sold EUR 113.1 million of reserve currency, including EUR 7.5 million to budget organisations and EUR 105.6 million to individuals.

The Bank conducted four full checks into credit institutions and service providers to ensure compliance with Ordinance No 18 on the Control over Quality of Banknotes and Coins in Currency Circulation and instructions on its implementation. The BNB conducted initial tests, tests for putting into operation and control and functionality tests of 451 sorting machines and customer-operated machines in line with identification and fitness standards into seven credit institutions, five service providers, and six machine manufacturers under Ordinance No 18.

[53] See the BNB website for new banknote and circulating and commemorative coin issues.

VI. Maintaining Banking System Stability and Protecting Depositor Interests

Assessment of the State of the Banking System[54]

In 2019 credit institutions operated in compliance with the capital and liquidity requirements and at levels of profitability allowing them to improve their capital position. In the context of accelerated growth of loans and total banking assets, the downward trend in residual credit risk measured by net non-performing loans and advances continued.

Banking capital position remained stable, with indicators further exceeding minimal regulatory and prudential requirements. Over the period additional capital requirements were set. All banks had Common Equity Tier 1 above the required minimum and adhered to capital buffer requirements.

Banking liquidity position remained sustainable, with the liquid coverage ratio in all credit institutions further exceeding the regulatory level of 100 per cent.

In 2019 the amount of non-performing loans and advances and their share in total loans and advances decreased.

As of 31 December 2019 banking system profit remained close to that reported in 2018. By the end of 2019 *ROA* and *ROE* declined to 1.47 and 11.64 per cent.

In 2019 banking sector consolidation continued with the acquisition of Société Générale Expressbank (hereinafter 'Expressbank') by DSK Bank and Piraeus Bank Bulgaria AD by Eurobank Bulgaria AD. As a result, one-off operations were reported over the year impacting the dynamics of balance sheet indicators and banking sector's regulatory capital.

In 2019 banking system assets increased by BGN 8.8 billion (8.3 per cent) to BGN 114.3 billion, their growth rate rising by 8.0 per cent or BGN 7.8 billion on 2018. Loans and advances also grew to reach 65.7 per cent of total banking assets. The share of the most liquid item of cash, cash balances at central banks and other demand deposits remained at a comparatively high level of 15.9 per cent at the end of the year.

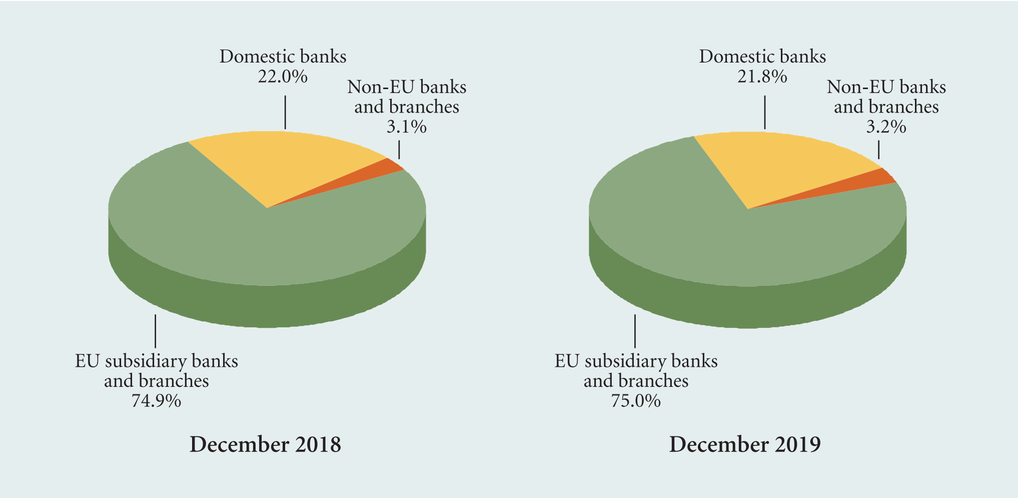
The asset share of the five largest banks rose to 62.2 per cent at the end of 2019 (against 59.4 per cent by end-December 2018). The year saw no significant changes in the market share of credit institutions: the share of local equity banks fell to 21.8 per cent, that of EU subsidiary banks and branches rising to 75.0 per cent. The market share of non-EU banks and branches reached 3.2 per cent.

In 2019 gross loans and advances rose by 6.1 per cent or BGN 5.4 billion to BGN 94.4 billion. Claims on all sectors, excluding those on central banks increased. In the currency structure of gross loans and advances, the share of lev loans grew to 59.4 per cent, from 58.3 per cent by end-2018, and the euro share fell from 36.5 per cent by end-2018 to 35.4 per cent. Exposures denominated in other currencies remained at 5.2 per cent close to the level reported by end-2018 (5.3 per cent).

Resident and non-resident claims occupied 84.3 and 15.7 per cent of total loans and advances, from 85.3 and 14.7 per cent at the end of 2018.

[54] Based on supervisory statements on an individual basis as of end-December 2019 and end-December 2018 submitted by 3 April 2020 and 7 March 2019.

Domestic and Foreign Bank Market Shares by Asset Size



Source: the BNB.

Banking system's credit portfolio (excluding loans and advances to central banks and credit institutions) rose by 8.8 per cent or BGN 5.4 billion to BGN 66.3 billion over the review period. In absolute terms, household loans increased most significantly (by BGN 2.1 billion or 9.6 per cent). Loans to non-financial corporations occupying the largest share in the credit portfolio grew by BGN 1.7 billion (4.9 per cent), those to financial corporations by BGN 1.4 billion (42.7 per cent), and credit to the general government by BGN 191 million (25.8 per cent).

In 2019 banking system deposits picked up BGN 7.5 billion (8.4 per cent) to BGN 97.2 billion. The strongest growth was recorded in household deposits by BGN 4.2 billion (7.9 per cent), their share prevailing in total attracted funds. The growth rate of non-financial corporations' deposits was BGN 2.9 billion (11.4 per cent). Funds from credit institutions and other financial corporations also increased on the previous year, while government sector deposits fell (by BGN 32 million or 1.2 per cent).

The currency structure shows lev-denominated items growing from 59.0 to 60.4 per cent and euro deposits falling from 33.2 to 32.1 per cent. Exposures denominated in other currencies also decreased, from 7.8 per cent to 7.4 per cent. Within the residence structure the share of domestic sources' deposits rose to 91.5 at the expense of non-resident deposits falling to 8.5 per cent, from 91.1 and 8.9 per cent at the end of 2018.

Balance sheet equity rose by 3.5 per cent to BGN 14.4 billion on an annual basis. Other reserves, accumulated other comprehensive income and retained earnings contributed positively to growth.

In 2019 asset quality indicators continued improving. Gross non-performing exposures were BGN 6.1 billion by end-December 2019, their share declining to 5.7 per cent, from 6.7 per cent by end-2018.

Total gross loans and advances grew by BGN 5.4 billion or 6.1 per cent, while gross non-performing loans and advances[55] declined by BGN 663 million or 9.8 per cent to BGN 6.1 billion, which helped reduce their share by 1.1 percentage point to 6.5 per cent by end-2019. The share of non-performing loans to non-financial corporations

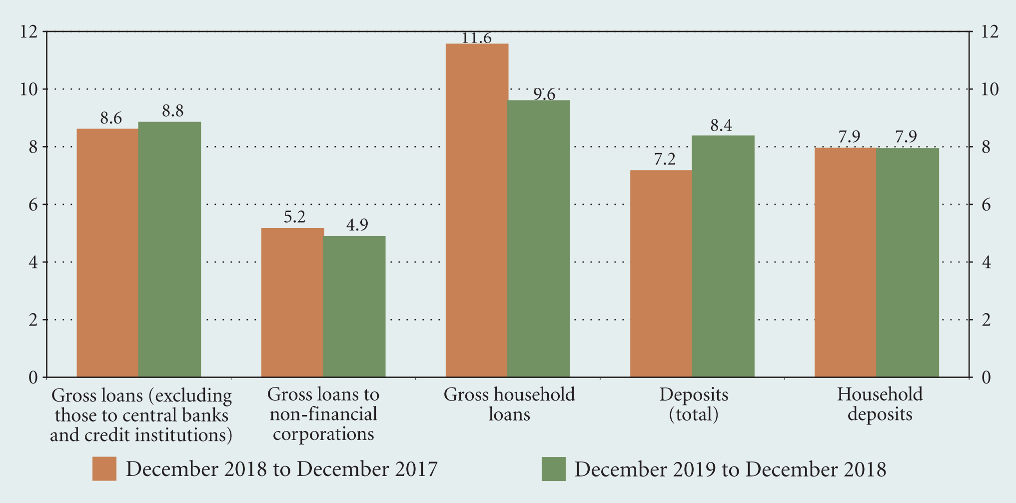
[55] Non-performing exposures are based on the broadest definition under the EBA methodology including both gross loans and advances and debt securities other than those held for trading.

decreased to 11.5 per cent, from 13.3 per cent at the end of 2018, while that of non-performing loans to households contracted to 7.3 per cent, from 8.9 per cent a year earlier.

Dynamics of Selected Balance Sheet Indicators

(on an annual basis)

(per cent)

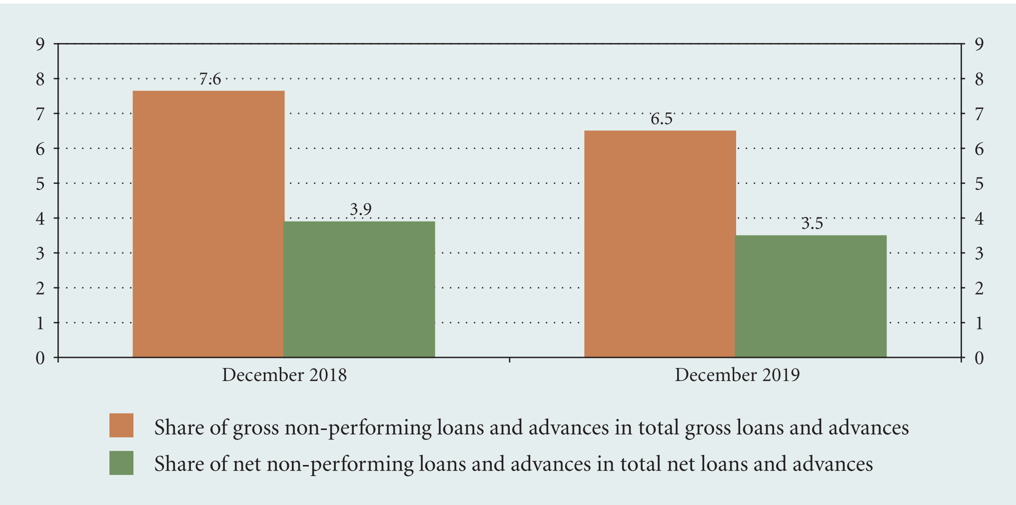


Source: the BNB.

Net non-performing loans[56], representing a potential credit risk in bank balance sheets, fell by 4.5per cent to BGN 3.2 billion by end-2019, their share in net loans and advances improving to 3.5 per cent. The volume of residual risk remained entirely covered by the capital exceeding the regulatory minimum.

Non-performing Loans and Advances in Total Loans and Advances

(per cent)



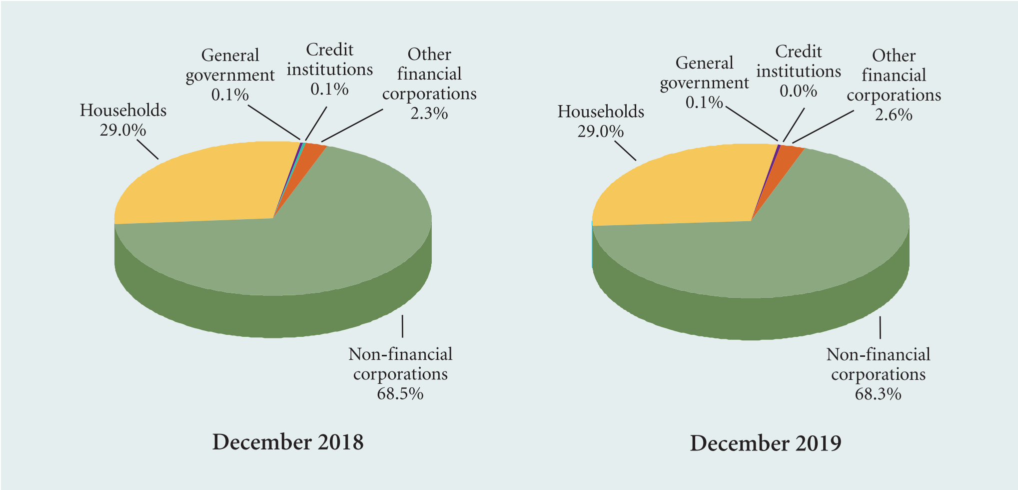
Source: the BNB.

The downward trend in gross non-performing loans was accompanied by the decline in their coverage ratio to 48.6 per cent by year's end (51.4 per cent by end-2018).

[56] Net non-performing loans and advances are calculated using EBA methodology: gross non-performing loans and advances less accumulated impairment for this category. In calculating the share of net non-performing loans and advances, their net value is used along with that of total loans and advances.

The 68.3 per cent share of non-financial corporations continued to dominate the structure of gross non-performing loans (68.5 per cent in 2018).

Non-performing Loans and Advances by Sector



Source: the BNB.

Gross non-performing loans past due over a year continued to post the largest annual decline, occupying 47.4 per cent of total non-performing loans by the close of the year (54.4 per cent a year earlier).

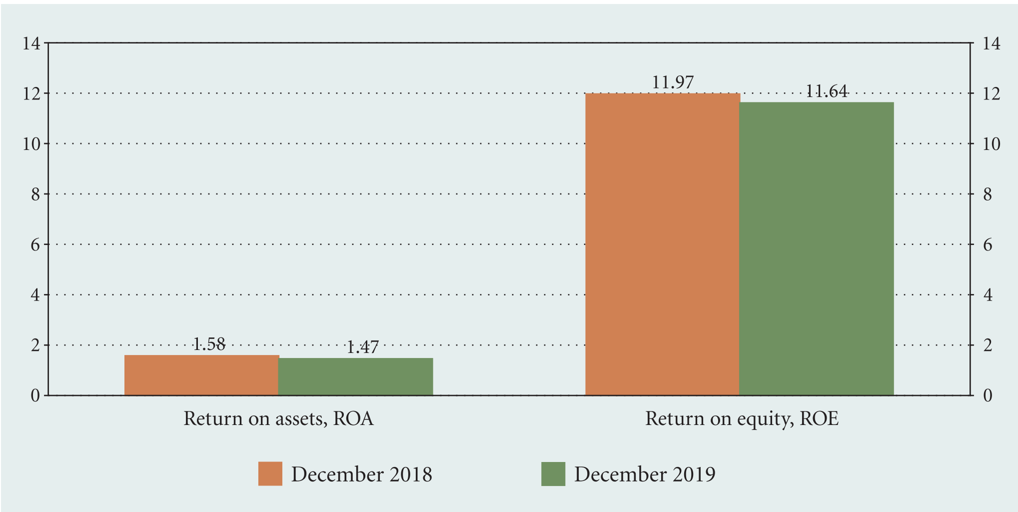
Balance sheet assets other than loans retained their good quality and helped maintain the high share of liquid assets.

Banking system profitability was affected by keeping interest rates low for an extended period.

By the end of 2019 banking system profit was BGN 1.7 billion, remaining similar to that reported in 2018. Reflecting higher growth rates of assets and balance sheet equity, ROA and ROE decreased to reach 1.47 and 11.64 per cent at the end of December, from 1.58 and 11.97 per cent in 2018.

Return on Assets and Return on Equity

(per cent)

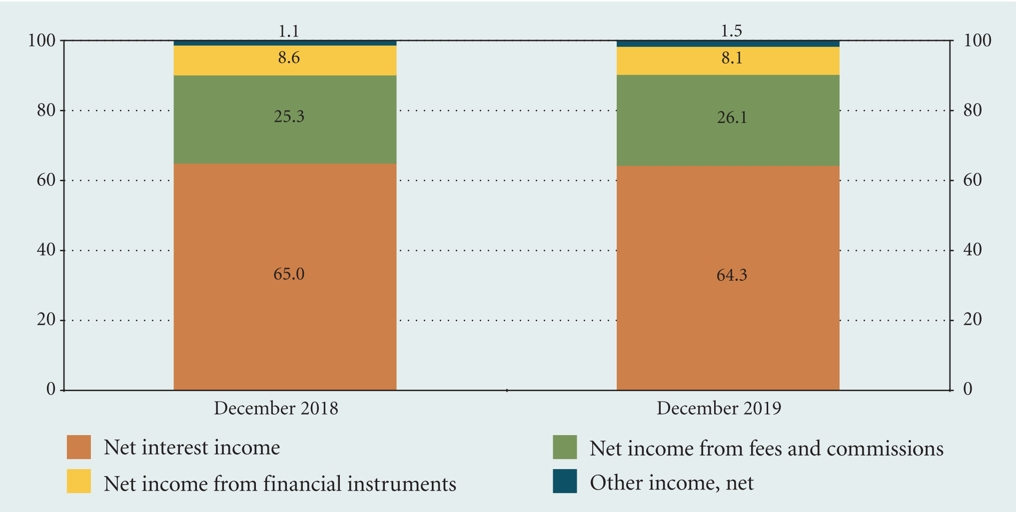


Source: the BNB.

Net operating income rose by 0.5 per cent or BGN 21 million on 2018. Its key component, net interest income reported a slight fall over the year, its share in total net operating income declining by end-December 2019 to 64.3 per cent, from 65.0 per cent in 2018. Concurrently, net fee and commission income rose, its share in the structure of total net operating income reaching 26.1 per cent at the end of December 2019, from 25.3 per cent in 2018.

Net Operating Income Structure

(per cent)



Source: the BNB.

Compared to the end of 2018, interest income went down by 0.4 per cent or BGN 12 million, while return on interest bearing positions rose. As a result, return on interest bearing assets declined to 3.18 per cent (3.50 per cent in 2018). Over the year interest bearing assets declined further to 0.19 per cent (0.22 per cent at the end of 2018). Over the same period, interest expenditure rose by 0.9 per cent (BGN 3 million) against the background of significantly higher growth rate of attracted funds.

Cost-to-income ratio (administrative expenditure and depreciation costs to net operating income) grew to 45.6 per cent, from 44.9 per cent by end-2018. This was attributable to depreciation expenditure dynamics, picking up by 53.1 per cent under the influence of the change in finance lease accounting according to International Financial Reporting Standard 16 (IFRS 16). In the same period administrative expenditure also fell to 3.2 per cent.

In 2019 banks' impairment charges of financial assets amounted to BGN 0.4 billion, down 6.6 per cent on the previous year. By end-year the impairment loss to net total operating income ratio fell to 10.5 per cent, from 11.3 per cent by end-2018.

Banking capital indicators remained sustainable throughout the year, their levels remaining within the range of 19 to 20 per cent. By end-2019 all banks reported sufficient common equity amount to meet the requirements for capital conservation buffers.

Capital indicators were influenced by one-off technical factors related to banking system consolidation process, regulator changes[57], in force since the

[57] As of early 2019 a higher risk weight to exposures to Member States' central governments or central banks should apply where exposures are denominated in a currency other than the domestic one (under Articles 114, 136 and 138 of Regulation (EU) 575/2013), and a 4 per cent capital requirement for foreign exchange risk (Article 354 of the same Regulation). On 1 January 2019 higher other systemically important institutions (O-SII) buffer rates became effective. Since October 2019 the countercyclical capital buffer rate of 0.5 per cent has been applied.

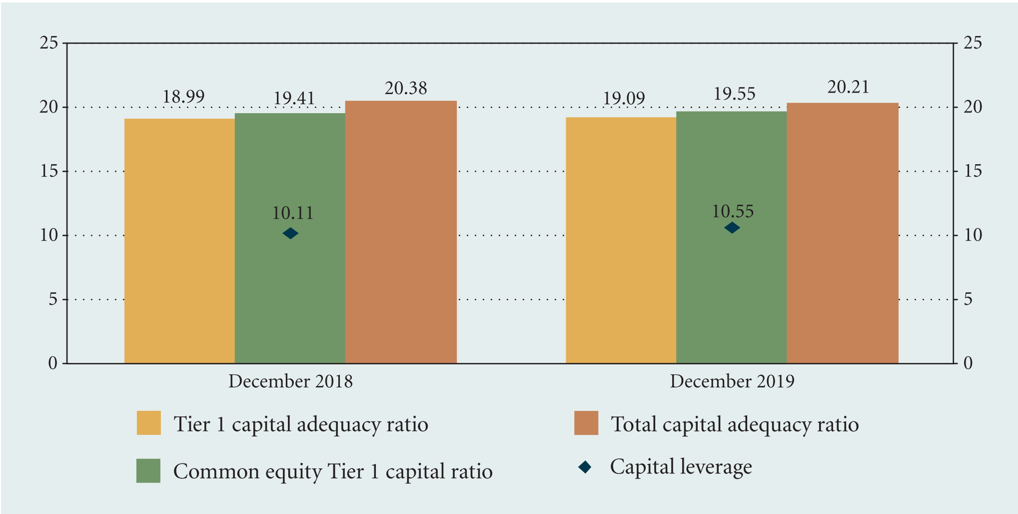
beginning of the year and the determination of additional capital requirements[58] under Pillar 2.

On an annual basis, banks' regulatory equity grew by BGN 1.6 billion (13.8 per cent) to reach BGN 13.3 billion by end-2019. Common equity Tier 1 capital increased by BGN 1.7 billion to BGN 12.5 billion and Tier 1 capita reached BGN 12.8 billion.

Total risk exposures picked up BGN 8.5 billion (14.8 per cent) to BGN 65.6 billion by end-2019. The share of credit risk weighted exposures rose to 90.4 per cent at the end of 2019, from 89.3 per cent at end-2018. Operational risk exposures grew also, but their share dropped to 8.8 per cent, from 9.8 per cent by end-2018. Despite the reported growth of exposures to position, currency, and commodity risks, they contributed insignificantly by 0.7 per cent of total risk exposures (0.8 per cent a year earlier).

Selected Capital Indicators

(per cent)



Source: the BNB.

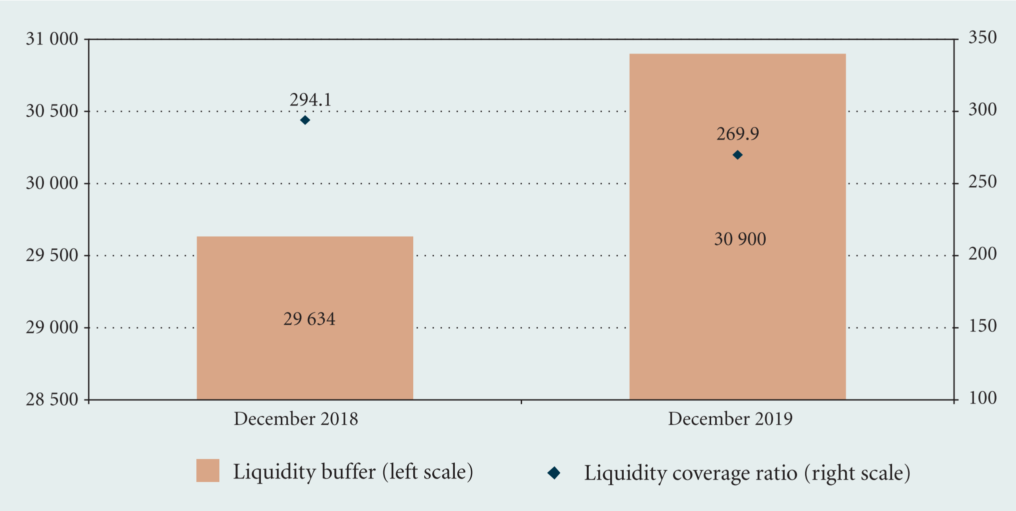
Common equity Tier 1, Tier 1 capital and total capital adequacy ended the year at 19.09, 19.55 and 20.21 per cent. The capital exceeding the regulatory minimum under Pillar 1 amounted to BGN 8.0 billion or BGN 0.9 billion more than in the prior year. The surplus above the regulatory requirements and capital buffers fell by BGN 0.6 billion to BGN 3.3 billion driven by the growth in risk exposures and required capital and buffers calculated on this basis, as well as the additional requirements, which were introduced in 2019.

In 2019 banking liquidity position remained stable, with all credit institutions exceeding the minimum required level of 100 per cent. The liquidity coverage ratio of the banking system fell to 269.9 per cent at the end of 2019, remaining significantly above the regulatory requirement. Compared to the end of 2018, the liquidity buffer (ratio numerator) increased by BGN 1.3 billion (4.3 per cent) to BGN 30.9 billion. Over the same period, net liquidity outflows (denominator) posted a growth of BGN 1.4 billion (13.6 per cent) to BGN 11.5 billion, which triggered the lower rate of the ratio.

[58] In March 2019 based on the completed supervisory review and evaluation process (SREP) and according to the EBA methodology, the BNB Governing Council set an additional capital requirement under Pillar 2 of the regulatory framework (in force from the second quarter of 2019).

Selected Liquidity Indicators under Commission Delegated Regulation (EU) 2015/61[59]

(BGN million) (per cent)



Source: the BNB.

Banks continued investing liquid assets in the central government, coming to BGN 16.3 billion or 52.9 per cent of liquidity buffer at the end of the period. The reserves in the central bank with an option for withdrawal item dropped to BGN 12.0 billion, their share to 38.9 per cent, while coins and banknotes accounted for BGN 2.3 billion, or 7.3 per cent of liquid assets, and the share of assets in the central bank underwent no significant changes.

The loan-to-deposit ratio[60] (LTD) of banking system remained almost unchanged at 72.2 per cent by end-2019 (72 per cent by end-2018).

Overview of Financial Institutions Recorded in the BNB Register under Article 3a of the LCI

In 2019 financial institutions recorded in the Register under Article 3a of the LCI operated in the context of a further growing number of recorded institutions and increasing balance sheet figure of this sector. The BNB recorded 13 new companies and deleted six due to termination or non-compliance with the Law on Credit Institutions and Ordinance No 26 on Financial Institutions. Six companies were denied registration due to unclear origins or unproven own funds in generating the contributions to company's capital. By end-2019 the total number of financial corporations reached 208, including 10 financial institutions from EU Member States conducting activities on the territory of the Republic of Bulgaria *via* a branch or directly (Articles 24 and 27 of the LCI) and a fund established under the procedure of the Law on the Bulgarian Development Bank.

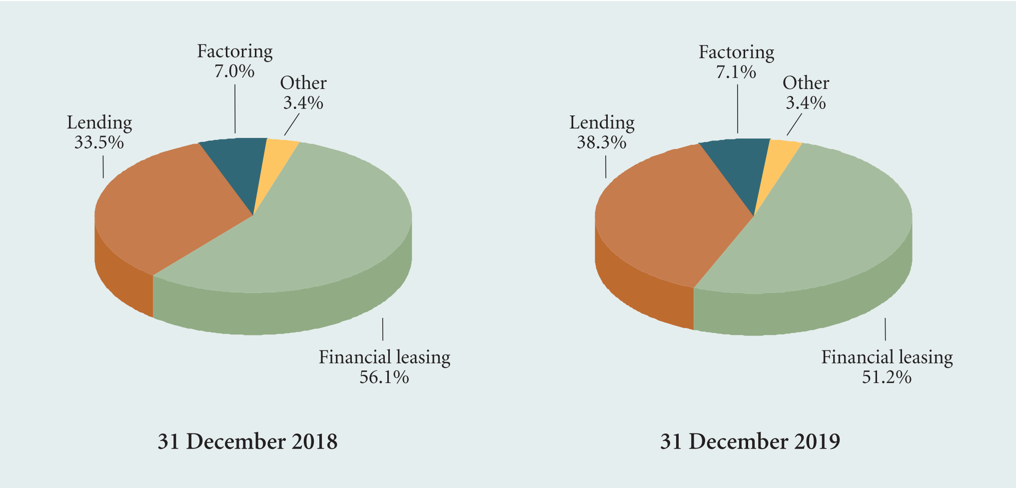
Total assets of financial institutions reached BGN 9.2 billion, retaining their share in banking system assets (8.1 per cent). Balance sheet figure rose by 12.2 per cent on the end of 2018 (BGN 8.2 billion) entirely due to the higher consumer lending and

[59] Commission Delegated Regulation (EU) 2015/61 of 10 October 2014 to supplement Regulation (EU) No 575/2013 of the European Parliament and of the Council with regard to liquidity coverage requirement for credit Institutions.

[60] The ratio has been calculated excluding central banks and credit institutions sectors.

progressively rising volume of receivables under lease agreements. Leasing companies (46) had the highest market share, followed by lenders (129), whose credit portfolio increased by 28.4 per cent to BGN 3.5 billion outpacing the total growth of sector's credit portfolio and financial leasing. The 20 largest financial institutions' assets retained their large market share at 76.1 per cent held mostly by leasing companies (11).

Breakdown of Financial Institutions' Assets by Type of Business



Source: the BNB.

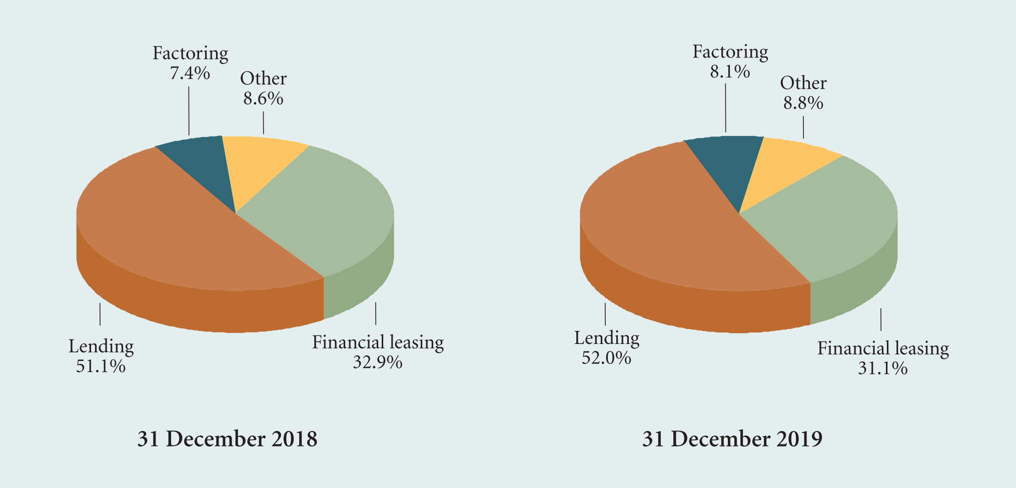
The gross credit portfolio, including claim on loans and financial leasing, rose by 9.9 per cent on an annual basis to BGN 7.8 billion. By end-2019 the share of performing loans of financial institutions registered under Article 3a of the LCI occupied 74.3 per cent. As regards impaired claims, leasing agreement comprised 56.2 per cent. The 20 financial corporations reported 81.1 per cent of all performing loans and 71.5 per cent of all impaired claims. Consumer loans rose at the highest rate of 18 per cent, followed by lease portfolio at 9.7 per cent. The share of loans and receivables in foreign currency continued dropping to 38.6 per cent of the item's balance sheet value in levs and currency.

Sector's attracted funds increased 12.9 per cent year on year to BGN 6.7 billion. Funds attracted from banks reported the most significant increase (15.7 per cent). Attracted resources from domestic banks (BGN 3.8 billion) retained its prevailing share (56.7 per cent) in all attracted funds. Foreign institutions (83 per cent) dominated attracted resources from other financial institutions, mainly with long-term funding in foreign currencies.

2019 profit was BGN 357 million, up 3.2 per cent. Net interest income contributed most to sector's profits. The 20 top companies achieved 58.7 per cent of sector's profits. Return on assets (ROA) dropped to 3.9 per cent, from 4.2 per cent at end-2018. Return on equity (ROE) decreased also to 17.2 per cent, from 17.9 per cent in 2018.

Total sector equity rose by 7.8 per cent on an annual basis to BGN 2.1 billion, reflecting both the increase in financial institutions' equity and new institution registrations under Article 3a of the LCI. The 20 top financial institutions continued to comprise more than half of sector's equity, though declining to 54.9 per cent (59.2 per cent for 2018).

Breakdown of Financial Institutions' Equity by Type of Business



Source: the BNB.

Banking Supervision's Activity

Off-site Supervision

Current Monitoring of Credit Institutions' Risk Profile

In 2019 current monitoring of credit institutions' risk profile and assessment of their financial position remained the major focus of off-site supervision. Dynamics of key risk indicators was monitored within individual quarters, along with analyses of the level and trends of risks assumed by banks including their effects on credit institutions' viability. On this basis, quarterly analytical reports on each bank were drafted. They focused on quarterly changes in the financial position, the level and degree of risks to the capital: credit and concentration risks, market and operational risks, including liquidity and funding risks. Quarterly Supervisory Review of Banks Report described analysis findings and conclusions on financial parameters of banks and across bank groups and the whole banking system. Daily monitoring of all credit institutions' liquidity positions was an aspect of regular supervision, tracking changes in both liquidity assets and attracted funds.

Supervisory Review and Evaluation Process (SREP)

In the first half of 2019 the supervisory review and evaluation process (SREP) of banks with a reference date as of 31 December 2018 and additional capital determination process for credit and credit concentration risk were launched. By end-year in order to reach joint decisions on subsidiaries of European bank groups, the BNB Governing Council decided to approve them. The assessment of institutions' viability based on the adequacy of sources, size, equity structure and liquidity, governance, controls, business model and strategy to cover the risks is based on the on-going monitoring of banks, on the conclusions and findings of supervisory inspections and checks under the special supervision concerning various aspects of the activity and financial performance of credit institutions, and on the outcomes of annual stress-test simulation in line with the macroprudential supervision.

Supervisors carried out annual reviews and assessments of banks' Internal Capital Adequacy Assessment Process (ICAAP) and Internal Liquidity Adequacy Assessment Process (ILAAP) reports as of 31 December 2018. Conclusions were therefore based on the assessment how ICAAP and ILAAP have been integrated into the internal corporate governance framework and to what extent the results are part of capital planning, liquidity needs forecasting and institutions' budgeting. Assessments and conclusions related to the reliability, efficiency, and comprehensiveness of ICAAP and ILAAP in line with the EBA requirements were taken into account in determining the capital and liquidity adequacy ratings as part of the overall rating of the institutions.

The BNB reviewed also banks' funding plans with a reference date as of 31 December 2018 covering projections of assets, liabilities and capital dynamics in a three-year horizon (2019–2021) to ensure that all short and long-term objectives are realistic in line with EBA Guidelines on harmonised definitions and templates for funding plans of credit institutions and European Systemic Risk Board Recommendation.

In 2019 supervisors continued their work on reviewing and assessing updated recovery plans of local banks under Article 6, paragraph 1 of the Law on the Recovery and Resolution of Credit Institutions and Investment Firms (LRRCIIF). The main conclusions, findings and recommendations for removing weaknesses, improving quality and plan applicability were discussed, and assessments were taken into account in determining the internal (corporate) governance rating of each credit institution.

Work on Drafting Opinions and Follow-up of Supervisory Measures

In 2019 opinions were drafted on the pre-approval issued by the BNB to include 2018 annual profits in banks' capital before a decision to that end is made by the relevant General Shareholder Meeting. The BNB sent notices of non-objections to banks willing to pay dividends provided that these institutions maintain a capital adequacy ratio above the minimum regulatory levels. A number of opinions were drafted: on the actions taken by two banks regarding outsourcing notification; on three banks regarding capital increases by contributions in fact and one bank by contribution in kind; with regard to Société Générale Expressbank acquisition by DSK Bank, and on transformation of Piraeus Bank Bulgaria AD through merger into Eurobank Bulgaria AD.

Follow-up of the implementation of supervisory measures imposed to remove regulatory framework breaches and recommendations resulting from on-site inspections continued. It was established that credit institutions took proper actions to implement most of the recommendations and eliminate infringements. The monitoring found a potential non-compliance with the provisions of the measure at one bank. In this connection, a legal opinion was sought.

Meetings Held With Audit Firms' Representatives

In the first half-year meetings with audit firms' representatives took place implementing the Guidelines on communication between competent authorities supervising credit institutions and the statutory auditor(s) and the audit firm(s) carrying out the statutory audit of credit institutions (EBA/GL/2016/05). Discussions dealt with the control environment, bank processes efficiency, audit committee commitment, key questions to the management, Bank challenges, and the model for applying IFRS 9. Within the framework of this dialogue, a subsequent meeting was held at the end of 2019 with one of auditing companies on its own initiative to provide information on audit process initiated in five banks and one branch.

On-site Inspections

In 2019 on-site inspections were consistent with the approved annual on-site inspection plan. The scope and objectives of the nine inspections completed over the year were focused on several streams related mainly to the review and evaluation of credit and credit concentration risk. The risk impact was additionally assessed in the ICAAP with a view to the current and foreseen effects within the period of time to which the ICAAP relates. There were assessments of operational risk management and its impact on the ICAAP at some of the inspected banks, and of liquidity position management in terms of placements within the banking group.

The main aspects of risks' review and assessment included internal management framework quality, including existing processes and systems for managing specific risk categories, control mechanisms, reporting. Inspections examined the organisation, rules and methodology the respective credit institutions use to identify their internal capital needs in the ICAAP. Assessments pointed the extent to which internal bank systems were comprehensive and to which the strategies and processes were proportionate to the nature, scale and complexity of banks' activities. During on-site inspection, the quality of supervisory reporting of the respective bank is reviewed. The implementation of supervisory measures imposed during previous inspections, involving supervisory prescriptions to overcome weaknesses in operational activities and internal control mechanisms, was also assessed.

Inspection findings show that recommendations from previous inspections have been implemented and actions have been undertaken to improve internal governance and committees' work, compliance with supervisory requirements, internal rules, etc. As a result of inspection conclusions, recommendations were forwarded to the inspected banks' managements to enhance credit risk organisation and management. In particular, continual credit risk monitoring brought recommendations to increase frequency and quality of borrowers financial condition analyses along with treating eligible security when determining credit exposure risk weights. Other recommendations involved enhancing internal capital adequacy assessment in relation to data quality in stress testing and documenting the process and the need of developing or supplementing internal methodologies associated with this process.

Breaches found related mainly to incorrect treatment of credit risk exposures from a risk classification perspective and inaccurate identification of risk weights in reporting for regulatory purposes. Analyses in all these banks suggest that breaches had no major impact on their capital adequacy. In the ICAAP inspections found weaknesses at some banks in reflecting inherent risks into their own internal capital adequacy and planning assessments.

Based on inspection findings, supervisory measures in force demanded the respective credit institutions to undertake corrective actions concerning the credit risk assessment, internal capital adequacy assessment, capital position strengthening and other measures to enhance business model sustainability. Following the inspection, actions taken by the bank concerned with the aim to address shortfalls in the operations and limit the risks were taken into account.

Over the review period the approval of internal models developed by banks for regulatory purposes was focused on documentary checks in three banks upon their request. Supervisory analyses and assessments were prepared in order to obtain a regulatory approval of significant changes in internal approaches for measuring the regulatory capital with regard to the credit risk in two banks and operational risk in one bank. The results of internal model checks in these banks were used in the joint decisions made by supervisory colleges. These decisions entitle the respective banking group and in particular the domestic subsidiary bank to implement the intended changes for the purposes of Pillar 1 of the regulatory framework. Documentary checks were performed in one bank and statements of opinion were drawn up in view of its notification of insignificant changes in internal models used for evaluating credit risk.

In order to implement single procedures for the fulfilment of its operational tasks in relation to the SREP, the Banking Supervision developed a comprehensive On-site Inspections Manual draft. The document provides for implementation of single inspection standards, which comply with the relevant procedures carried out by the ECB.

Macroprudential Supervision

In 2019 effective fulfilment of the BNB macroprudential mandate was based on regular and comprehensive review of banking system trends. Systematic monitoring involved banking intermediation and its interdependence between financial system and economic development in Bulgaria, along with the influence of international environment.

Macroprudential instruments were supported by periodic monitoring of cyclic and systemic risks measured by established methodologies, trends and best practices.

- Regular assessments of eight credit institutions were conducted using the methodology for identifying systemically important institutions and their O-SII buffer rates were set.
- In assessing structural risks in the banking sector, systemic risk buffer level was confirmed at 3 per cent.
- From October 2019 a positive level of the countercyclical capital buffer applied to resident credit risk exposures at 0.5 per cent entered into force[61]. In order to strengthen banking sector's resilience to potential adverse developments, the BNB Governing Council gradually increased the countercyclical capital buffer applied to resident credit risk exposures from 0.5 to 1 per cent, with effect from 1 April 2020, and to 1.5 per cent from early 2021.

Transparency principle was applied by publishing the main indicators of the banking system state and a risk assessment in monthly press-releases and Banks in Bulgaria quarterly. Over the year a number of analytical materials were drafted, including an analysis of real estate mortgage-backed loans to households and the Annual Banking Business Aspects Survey. Research topics dealt with various key areas, specificities of bank portfolios and financial stability issues. The Bank continued improving methodologies and techniques for analysis and quantitative assessments.

Specific Supervisory Activities

The transposition of Directive (EU) 2015/849 of the European Parliament and of the Council on the prevention of the use of the financial system for the purposes of money laundering or terrorist financing in 2018 was followed by an update of the national legislation to meet the requirements laid down in Directive (EU) 2018/843.

Over the review year work continued on finalising the National Risk Assessment (NRA) in line with the requirements under Article 7 of Directive (EU) 2015/849. Planned supervisory inspections checked nine banks, while applying a risk-based approach. The inspections at three of them were completed over the first quarter of 2020. Specific supervision focused on risk evaluation procedures, internal rules

[61] For more information on capital buffers, see the BNB website: http://www.bnb.bg/BankSupervision/BSCapitalBuffers/?toLang=_EN.

for control and prevention of money laundering, and achieved compliance of policies and procedures with the revised regulatory framework. The 11 breaches found were insignificant and related to isolated cases. Twenty-nine recommendations were forwarded to supervised entities to improve due diligence of customers and administrative capacity of the specialised unit. Over the review period one inspection was performed jointly with the State Agency of National Security Financial Intelligence Directorate. In addition to the planned inspections, 15 *ad hoc* off-site inspections were conducted in seven banks, the result of which ascertained banks' compliance with statutory requirements. Increased statutory requirements have caused banks to apply more stringent rules for clients. As a result, relationship with clients which have not submitted information and documents legally required for risk assessment was terminated. The comprehensive assessment of the banking sector based on the supervisory inspections indicates that systems preventing bank use for money laundering and terrorist financing and adequacy of practices used by banks are credible.

In November the BNB took part in the supervisory college on money laundering prevention organised by De Nederlandsche Bank. The supervisory college discussed the implementation of the new legal framework and convergence of supervisory approaches regarding the entities in the bank group.

The Law on Bank Deposit Guarantee adherence on reporting guaranteed deposits was subject of two inspections. Breaches in calculating deposit bases and guaranteed deposit amounts were found and recommendations to the inspected banks for removing them made. The Bulgarian Deposit Insurance Fund was notified of the findings. Follow-up to the measures taken by the inspected banks was conducted to remove the deficiencies.

Supervisory attention focused closely on the requirements of the Law on Real Estate Loans for Consumers (LRELC) in order to apply prudent standards in housing lending to individuals and to strengthen market discipline. The aim was to enhance resilience of banks and borrowers to adverse economic and financial shocks. The control focused on establishing statutory compliance of borrower creditworthiness rules adopted and applied by creditors, professional training systems and remuneration policies of the staff engaged in the LRELC implementation. Three checks into credit institutions under the LRELC, four into financial institutions granting housing loans and three spot on-site checks into credit intermediaries were completed in 2019.

Results of the LRELC inspections show that banks apply adequate control rules and mechanisms to assess consumer creditworthiness, professional staff training and individual remunerations complying with statutory requirements. It finds that banks comply with safer housing credit standards, unlike financial institutions. The BNB established breaches of statutory provisions of the LRELC in four inspected financial institutions and issued administrative infringement notices to three of them.

The LRELC Register listed 15 new Bulgarian and three EU Member State intermediaries. One applicant company was denied registration under the LRELC due to non-compliance with the requirements of the law. There were 46 local entities and nine EU Member State credit intermediaries. The BNB continued taking measures against entities suspected of acting as credit intermediaries. Forty-seven companies suspected of non-listed credit intermediation were inspected.

Isolated cases of non-transparent capital origins were established in registration and change in ownership of financial institutions under Article 3a of the LCI. In order to take an informed decision, the competent national and international institutions were contacted.

Signals for bad practices used by financial institutions were checked by competence. Most of the signals were referred to the Consumer Protection Commission, the Commission on Personal Data Protection or claimants were instructed to submit the relevant information to the law enforcement authorities.

One financial institution was imposed a pecuniary sanction for infringement of BNB Regulation No 26 on Financial Institutions over the review year.

Issue of Licences, Permits, and Approvals

There were no new credit institution operations licences or bank licensing procedures in the Republic of Bulgaria over the past year.

Following the application procedure by DSK Bank EAD for direct acquisition of 99.7352 per cent and by OTP Bank AD, Budapest, Hungary for indirect acquisition of Société Générale Expressbank AD paid-up equity, the BNB Governing Council approved the acquisition in February (Resolution No 57 of 28 February 2019) after assessing compliance with the criteria under Article 28a, paragraph 3 of the LCI.

Subsequently, in December 2019 DSK Bank EAD and Expressbank AD filed a new application under Article 29, paragraph 1 of the LCI to transform Expressbank AD through merger into DSK Bank EAD.

In February 2019 the BNB opened an approval procedure at the request of D Commerce Bank AD under Article 29, paragraph 1 of the LCI for bank capital increase by non-monetary contribution of its shareholder Fortera AD. The BNB Governing Council approved by Resolution No 131 of 4 April 2019 bank capital increase of D Commerce Bank AD by non-monetary contribution of its shareholder Fortera AD, acquiring property rights on immovable property of the shareholder.

The February procedure to transform Piraeus Bank Bulgaria AD through separation of single-person limited liability company under Article 29, paragraph 1 of the LCI, the BNB Governing Council ended with the BNB Governing Council approval (Resolution No 107 of 28 March) for Piraeus Bank Bulgaria AD to transform by separating single-person limited liability company under Article 262d of the Commercial Law.

Following the application procedure by Eurobank Bulgaria AD for direct acquisition of 99.9819 per cent and by Eurobank Ergasias SA for indirect acquisition of Piraeus Bank Bulgaria AD paid-up equity, the BNB Governing Council approved the acquisition in March (Resolution No 107 of 28 March 2019) after assessing compliance with the criteria under Article 28a, paragraph 3 of the LCI.

Subsequently, in August 2019 Eurobank Bulgaria AD and Piraeus Bank Bulgaria AD filed a new application under Article 29, paragraph 1 of the LCI to transform Piraeus Bank Bulgaria AD through merger into Eurobank Bulgaria AD. By Resolution No 346 of 15 October 2019 of the BNB Governing Council and given the previous approval of Eurobank Bulgaria AD application for direct acquisition of 99.9819 per cent and by Eurobank Ergasias SA for indirect acquisition of Piraeus Bank Bulgaria AD paid-up equity, the BNB Governing Council approved the acquisition by merging Piraeus Bank Bulgaria AD into Eurobank Bulgaria AD pursuant to Article 262 of the Law on Commerce.

In April 2019 the BNB opened a preapproval procedure at the request of Fairfax Financial Holdings Limited, Toronto, Canada, and its subsidiaries and shareholders under Article 28, paragraph 1 of the LCI for indirect acquiring 33.33 per cent of Eurobank Bulgaria AD and Piraeus Bank Bulgaria AD equity. The BNB issued an approval to Fairfax Financial Holdings Limited, Toronto, Canada, and its subsidiaries and shareholders by Resolution No 277 of 6 August 2019, as a result of the merger of Grivalia Properties REIC into Eurobank Ergasias SA, currently a shareholder of Eurobank Bulgaria AD, to acquire over 33 per cent without reaching the threshold of 50 per cent of Eurobank Bulgaria AD and Piraeus Bank Bulgaria AD capital.

At the request of Chimimport AD, in August 2019 the BNB opened a preapproval procedure under Article 28 of the LCI for acquisition by Armeec Insurance Jsc of 6.4 per cent of Central Cooperative Bank AD equity.

In November 2019 the BNB opened an approval procedure at the request of Eurobank Bulgaria AD under Article 29b, paragraph 2 of the LCI for a merger of ERB Leasing Bulgaria EAD into Eurobank Bulgaria parent company, thereby the subsidiary being dissolved without going into liquidation.

At the request of Central Cooperative Bank AD, in November 2019 the BNB opened a new application procedure under Article 25, paragraph 1 of Ordinance No 2 on the Licenses, Approvals and Permissions Granted by the BNB according to the LCI for extending the scope of license granted to the Central Cooperative Bank AD by the activities under Article 2, paragraph 1, item 13 of the LCI on the issuance of electronic money.

In 2019, following the BNB Governing Council resolutions, three banks were allowed to include 2018 profits into Common Equity Tier 1. Three other banks increased their Common Equity Tier 1 through issue of shares and conversion of bonds into shares.

In 2019 five banks obtained approvals by the BNB Governing Council under Article 71, paragraph 3 to amend their statutes.

Over the past year the BNB Governing Council imposed supervisory measures on five banks for supervisory framework breaches.

There were management and supervisory board changes at: United Bulgarian Bank AD (a new management board member and executive director and a new supervisory board member), UniCredit Bulbank AD (three new executive directors, three new supervisory board members and management board member), Tokuda Bank AD (a new supervisory board member and two new management board members), DSK Bank EAD (a new management board member, three new management board members and executive directors and two new supervisory board members), Expressbank AD (two new management board members and executive directors, a new management board member and two new supervisory board members), Piraeus Bank Bulgaria AD (three new board of directors members and three new board of directors members and executive directors), Allianz Bank Bulgaria AD (a new supervisory board member), T.C. Ziraat, Sofia Branch (a new branch manager), Investbank AD (a new management board member and a new management board member and executive director), ProCredit Bank (Bulgaria) EAD (a new supervisory board member and a new management board member and executive director), TBI Bank EAD (a new management board member).

Between January and December 2019, 29 new EU Member State credit institutions exercised the freedom to provide services under the mutual recognition of single European passport through notices to the BNB from their licensing authorities, bringing the number of received direct services notices in Bulgaria to 338.

Following the notice of intent by TBI Bank EAD to provide services directly in Poland, in July 2019 the BNB notified the Polish supervisory authority.

The BNB Banking Supervision Department registered and handled 198 complaints from bank customers.

Regulatory Framework Activity

Banking supervision activities continued to be based on the effective European regulatory framework applicable to credit institutions focused on the consistent implementation of EC delegated acts, as well as EBA guidelines and ESCB recommendations.

Preparations to amend the regulatory framework on the operation and supervision of credit institutions continued. Amendments to the Law on Accountancy concerning the applicable accounting basis for banks and financial institutions in relation to the application of International Accounting Standards were adopted.

In April the BNB Governing Council adopted Ordinance No 20 on Issuance of Approvals to Members of the Management Board (Board of Directors) and Supervisory Board of a Credit Institution and Performance Requirements for Their Duties. Concurrently, the BNB Governing Council also adopted Ordinance No 10 on the Organisation, Governance and Internal Control of Banks. The Ordinance is based on the current regulations concerning the internal control of banks extending the requirements to banks' internal organisation in accordance with the provisions of the LCI and Guidelines on internal governance issued by the EBA.

The adopted amendments to Ordinance No 4 of 2010 on the Requirements for Remunerations in Banks provide that the obligation to set up a remuneration committee applies only to significant banks where the number of board members is higher and efficient distribution of committee's functions between its members is possible.

The amendments to Ordinance No 7 of 2014 on Organisation and Risk Management of Banks lays down the requirements on the repute, qualification and professional experience to the head of risk management function. Again, banks' obligation to establish a risk committee applies only to significant banks. The ordinance lays down the minimum number of committee members and a requirement for independent members.

In the first half of 2019, along with the amendments to ordinances, the BNB Governing Council adopted resolutions to implement a number of guidelines issued by the EBA. Within the compliance procedure, the EBA was informed of decisions taken.

Standing committees and working groups of the EC and EBA jointly with BNB experts continued their work on the discussion and elaboration of common oversight policies and standards, the assessment and convergence of national practices on the introduction and implementation of the EU prudential and supervisory framework.

BNB experts helped in the coordination of Bulgarian language versions of the amendments to the Capital Requirements Directive and Capital Requirements Regulations (CRD and CRR), to the Bank Recovery and Resolution Directive (BRRD) and to the Regulation on the Single Supervisory Mechanism (SRMR), collectively known as 'risk mitigation measures'.

In the second half of 2019, the EBA *via* the Subgroup on Own Funds assessed three Bulgarian banks' capital instruments issued before the entry into force of Regulation (EU) No 575/2013 and included into Common Equity Tier 1. This assessment is conducted in accordance with Article 80 of the same Regulation to analyse and check the extent to which banks' capital instruments included into CET1 comply with the prudential requirements. The inspection included both relevant national legislation (the Law on Commerce, the LCI, the Law on Bank Bankruptcy) and banks' statutes.

Checks were performed in three banks: Raiffeisenbank, UniCredit Bulbank and United Bulgarian Bank (UBB). Inspection findings show that both national legislation and banks' statutes complied with the requirements of Article 28 of Regulation (EU)

575/2013, Commission Delegated Regulation (EU) No 241/2014 of 7 January 2014 supplementing Regulation (EU) No 575/2013 of the European Parliament and of the Council with regard to regulatory technical standards for Own Funds requirements for institutions, EBA report on CET1 instruments, and all published EBA replies and questions relevant to CET1 instruments. Instruments of the other five banks, which were determined as other significant institutions, are expected to be assessed in 2020.

Activities Related to the Comprehensive Assessment of the ECB in the Context of Bulgaria's Request for Establishing Close Cooperation between the ECB and the BNB in View of Bulgaria's Integration into the Single Supervisory Mechanism

In 2019 the BNB participated in the process related to Bulgaria's request of 18 July 2018 for accession to the Single Supervisory Mechanism by establishing close cooperation with the ECB. The BNB provided expert assistance to the ECB concerning Bulgarian banking system specificities with regard to the Asset Quality Review and stress test performed by the ECB of six selected Bulgarian banks: UniCredit Bulbank AD, DSK Bank EAD, United Bulgarian Bank AD, First Investment Bank AD, Central Cooperative Bank AD and Investbank AD. The ECB carried out a comprehensive assessment of the selected banks based on its methodology and macroeconomic scenarios for the stress test purposes. The results for each of the six banks were published on 26 July 2019 on the ECB's website. In the context of close cooperation, work continued on the alignment of BNB's supervisory policies with those of the ECB, including the internal rules and processes and information flows between the two institutions. In 2019 the BNB participated in meetings with ECB's representatives in the context of the AQR. The submitted information on the six banks, subject to the review, covered main risk assessments, financial position data and specific information on each bank. The following stages of the AQR process included both on-site visits to banks, and data verification and confirmation, as requested by the ECB. The following topics were discussed at the meetings: prioritisation, supervisory activities planning, resources allocation based on risk assessment; stages of the ongoing supervisory activities, including SREP, ICAAP and ILAAP review and assessment, recovery plans and interaction of the off-site supervision with the resolution authority of credit institutions within the BNB. The activity on issuance of approvals for bank acquisition and merger was also presented. Experts exchanged views on the structure, organisation, processes and regulatory framework of the supervisory policy of both parties, including the supervisory reporting and data quality assessment process. The meeting between the BNB and ECB representatives focused on mechanisms for information exchange between the regulatory authorities on the prevention of money laundering and terrorist financing.

VII. BNB Activities on Resolution of Credit Institutions

The Bulgarian National Bank is a resolution authority for credit institutions in compliance with the Law on the Recovery and Resolution of Credit Institutions and Investment Firms (LRRCIIF).

In 2019 the BNB as a resolution authority focused on preparing, reviewing and developing resolution plans. In the beginning of each year, the BNB collects from credit institutions information required for drafting resolution plans. In the first half of 2019 BNB reporting templates were brought into line with implemented Regulation (EU) No 2018/1624[62] to enable credit institutions to collect standardised information required for assessing resolvability and preparing resolution plans. With entry into force of Commission Delegated Regulation (EU) 2019/348, [63] specifying a generally applicable combination of certain quantitative and qualitative criteria for applying simplified requirements under Article 25 of the LRRCIIF, internal rules were adopted to specify relevant conditions and criteria for credit institutions licensed in Bulgaria and the content of simplified requirements for developing resolution plans.

As part of the overall process of building and improving the internal methodological framework, while complying with the LRRCIIF and Delegated Regulation (EU) 2016/1450,[64] a methodology was developed and adopted in the first half year to set out the minimum requirement for own funds and eligible liabilities (MREL) of credit institutions for which the BNB is the resolution authority. This methodology will establish a uniform approach to the main MREL components, *i.e.* the amount of losses which a credit institution would normally incur in taking a resolution action and the amount of capital needed to meet ongoing prudential requirements after resolution in order for this credit institution to still meet licensing conditions, carry on its activities and maintain market confidence. The methodology also sets out a requirement for liabilities with equal ranking as part of the MREL to ensure a fair treatment of creditors.

Given the comprehensive critical functions methodology in preparing resolution plans for 2019, 20 credit institutions licensed in Bulgaria were assessed during the first six months of the year. Results of implementing the methodology identified less than ten critical functions at eight credit institutions, ten to 20 critical functions at seven, and over 20 critical functions at two credit institutions. Three credit institutions did not provide functions that could be reasonably assessed as critical. In the second half of the year results of calculations were comprehensively implemented in the assessment for 2019, which involves choosing from resolution or liquidation under insolvency proceedings at an individual institution level, according to the methodology for considering actions on resolution and liquidation under insolvency

[62] Commission Implementing Regulation (EU) 2018/1624 of 23 October 2018 laying down implementing technical standards with regard to procedures and standard forms and templates for the provision of information for the purposes of resolution plans for credit institutions and investment firms pursuant to Directive 2014/59/EU of the European Parliament and of the Council, and repealing Commission Implementing Regulation (EU) 2016/1066.

[63] Commission Delegated Regulation (EU) 2019/348 of 25 October 2018 supplementing Directive 2014/59/EU of the European Parliament and of the Council with regard to regulatory technical standards specifying the criteria for assessing the impact of an institution's failure on financial markets, on other institutions and on funding conditions, effective from 23 March 2019.

[64] Commission Delegated Regulation (EU) 2016/1450 supplementing Directive 2014/59/EU of the European Parliament and of the Council with regard to regulatory technical standards specifying the criteria relating to the methodology for setting the minimum requirement for own funds and eligible liabilities.

proceedings. Results of applying the methodology justified initiation of resolution actions in 17 credit institutions with regard to their effect on the following areas: (1) functioning of the financial market and market confidence; (2) financial market infrastructures; (3) other financial institutions; and (4) the real economy. In three credit institutions, initiation of resolution actions is not justified given the insignificant impact of their possible liquidation on the above areas.

In reviewing internal rules for application of simplified requirements adopted in early 2019, the BNB did not designate any credit institutions to which the simplified requirements under Article 25 of the LRRCIIF should apply in 2019.

In the second half of 2019 the BNB calculated MREL for all credit institutions licensed in Bulgaria, while applying the approved MREL methodology and data disclosures as of 31 December 2018 on an individual and consolidated basis, where appropriate.[65] Obtained results are provided for information purposes only with a view to pending transposition of amendments to the regulatory framework of loss-absorbing and recapitalisation capacity of credit institutions into national law.[66] To provide timely and up-to-date data and apply transparency and equal treatment principles, all credit institutions were in due time informed of calculated MREL levels in order to raise their awareness of the BNB approach in determining MREL in compliance with Delegated Regulation (EU) 2016/1450. In addition, MREL levels calculated for information purposes enable credit institutions at a subsequent stage of resolution planning to comply in advance their business plans and objectives with MREL measurement.

Based on 31 December 2018 data, calculated MREL levels for 2019 moved within 8.6–25.6 per cent of total liabilities and own funds or 15.0–36.5 per cent of risk weighted assets on an individual basis. On a consolidated basis, these ranges were 9.8–25.5 and 15.0–36.5 per cent, respectively.

As a resolution authority of subsidiary banks of parent companies from the EU, the BNB participated in international resolution colleges for EU cross-border banking groups. In the first half of 2019 the BNB, jointly with the group-level resolution authority and other resolution authorities of EU subsidiary companies (resolution colleges), continued its work on assessing the opportunities for resolution and reviewing resolution plans of seven banking groups and their subsidiaries licensed in Bulgaria. Reflecting changes in the structure of some banking groups due to sales of their subsidiaries in Bulgaria,[67] the BNB terminated its participation in two of resolution colleges. In the second half year joint decisions on resolution plans for 2018 and assessments of resolvability were taken within four of the remaining five colleges in which the BNB is represented as a resolution authority. All updated resolution plans for 2018, adopted by joint decisions, included assessments of banking group resolvability, significant corporations in relevant banking groups and business model analyses, identified critical functions of significant corporations, and their preferred resolution strategy and instrument. Subsidiaries that are licensed in Bulgaria and included in these banking groups were determined as significant with identified critical functions.

---

[65] Credit institutions applying consolidation under Regulation (EU) No 575/2013 of the European Parliament and of the Council on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012, excluding subsidiaries licensed in the Republic of Bulgaria, part of EU cross-border banking groups subject to international resolution colleges.

[66] Directive (EU) 2019/879 of the European Parliament and of the Council of 20 May 2019 amending Directive 2014/59/EU as regards the loss-absorbing and recapitalisation capacity of credit institutions and investment firms and Directive 98/26/EC.

[67] Direct acquisition by DSK Bank EAD of shares representing 99.7352 per cent of the capital of *Société Générale Group* making it a subsidiary of DSK Bank and part of the OTP Group; direct acquisition by Eurobank Bulgaria AD of 99.9819 per cent of Piraeus Bank Bulgaria AD paid up equity, making it a subsidiary of Eurobank Bulgaria and part of *Eurobank Ergasias* Group.

With regard to all banking groups having subsidiaries licensed in Bulgaria, the group-level resolution authority initiates adoption of a joint decision on the MREL on a consolidated basis for the respective parent undertaking for 2018. Reflecting its formal policy, the Single Resolution Board (SRB)[68] as a group-level resolution authority within four of the five resolution colleges set binding MREL targets for 2018 not only on a consolidated but on an individualised basis for significant subsidiaries within the framework of the Single Resolution Mechanism. Over the second half of 2019 relevant joint decisions were adopted within four resolution colleges. The BNB, in its capacity as a resolution authority of subsidiaries in Bulgaria falling within the scope of resolution colleges, calculated MREL on an individual basis, while applying the approved MREL methodology and employing data as of 31 December 2017, given the reference date of groups' resolution plans. According to the BNB approach, MREL calculations for subsidiaries are not subject to a joint decision with the rest resolution authorities, and are not therefore binding for the institutions but are used for information purposes only.

In the second half year, reflecting 2019 results of implemented methodologies involving key resolution plan elements, the BNB began systemising resolution plans of the rest credit institutions falling within the scope of BNB powers as a resolution authority.

Under the LRRCIIF requirements, in March the Governing Council set the total 2019 amount of annual bank contributions to the Bank Resolution Fund (BRF) at BGN 137,257 thousand. In April this sum was apportioned to individual banks depending on their risk profile. All banks paid their due contributions into the Fund within the term set in the LRRCIIF, with accumulated funds exceeding BGN 548 million.

Following a formal letter sent on 29 June 2018 by the Minister of Finance and the BNB Governor with regard to Bulgaria's participation in the SSM by establishing close cooperation with the ECB, the preparatory work to join the SRM and consequently the Single Resolution Fund (SRF) continued in 2019 as a direct consequence of establishment of close cooperation. Participation in the SRM and the SRF stems from the direct application in the Republic of Bulgaria of Regulation (EU) No 806/2014,[69] with effect from the date of establishing close cooperation.

The BNB as a resolution authority jointly with SRB representatives continued working on a joint action plan with a timetable based on three individual pillars: (1) drafting and approving relevant amendments to the LRRCIIF; (2) preparations for joining the SRF; (3) developing bank resolution planning after joining the SRM.

On 24 April 2019 the National Assembly adopted a draft law amending the LRRCIIF (published in the Darjaven Vestnik, issue 37 of 7 May 2019) introducing provisions for enforcement of Regulation (EU) No 806/2014. These provisions are essentially projected to enter into force upon establishing close cooperation with the ECB with the aim to ensure legal certainty, completeness and clarity in national legislation in compliance with Regulation (EU) No 806/2014. In preparations for SRM participation, a transitional provision to the LRRCIIF provides for an exchange of information, prior to Bulgaria's joining the SRM, between the BNB and the SRM, on the one hand, and between credit institutions and the SRB, on the other, at the request of the BNB acting in its capacity as a resolution authority. With the adoption of LRRCIIF amendments, the work on the first pillar of the action plan was completed.

[68] *MREL – 2018 SRB Policy for the second wave of resolution plans,* published on 16 January 2019.

[69] Regulation (EU) No 806/2014 of the Council of 15 July 2014 establishing uniform rules and a uniform procedure for the resolution of credit institutions and certain investment firms in the framework of a Single Resolution Mechanism and a Single Resolution Fund and amending Regulation (EU) No 1093/2010.

The BNB role in the second pillar of the action plan focused on technical and expert support to the SRB in terms of establishing the amount of the first contribution of Bulgaria to the SRF under the ratified[70] agreement on the transfer and mutualisation of contributions to the SRF in establishing close cooperation with the ECB and joining the SRM. In 2019 the BNB contributed actively to the SRB in ensuring required financial information from credit institutions with a view to setting the first Bulgaria's computation to the SRF.

Work on the third pillar of the action plan was intended to encompass joint actions with the SRB for participation in the SRM related to identification of credit institutions falling within the scope of direct responsibilities and tasks of the SRB, familiarising with SRB procedures and division of responsibilities and tasks between the SRB and national resolution authorities within the SRM.

[70] Law on Ratification of the Agreement on the Transfer and Mutualisation of Contributions to the Single Resolution Fund (adopted on 8 November 2018, published in the Darjaven Vestnik, issue 96 of 2018).

VIII. Participating in the ESCB and EU Bodies

BNB experts sat on discussions and negotiations on EU institutions and bodies activities aimed at building a deeper Economic and Monetary Union (EMU), implementing measures to complete the Banking Union, establish a well functioning and integrated capital market union and enhance confidence in the financial system.

Bank representatives were involved in the negotiations on measures to reduce risk in the EU banking sector as part of the EC 2016 package on prudential supervision and resolution of credit institutions, on which agreement has been reached. In the context of building the Capital Markets Union, measures were proposed to strengthen the European Supervisory Authorities (ESA) powers and the convergence of supervisory practices, and to enhance the EBA role. The BNB's representatives made an expert contribution to the negotiations on reforming EBA's mandate and reviewing the ESRB's mission and organisation.

The European System of Central Banks

The BNB Governor sits on the ECB General Council with EU central bank governors and the ECB President and Vice President. The four ECB General Council sessions in 2019 looked at important issues of economic development, EU financial development and performance, as well as key ECB documents including the ECB report on the outlook and monetary policies in non-euro area EU countries, the report on central bank observance of the prohibition of monetary financing, and the report on public finance.

BNB representatives sat on 12 ESCB committees[71], 50 working groups, and the Human Resource Conference and Heads of Administration Conference. Through representatives in ESCB bodies, committees and working groups, the Bank helped elaborate ECB legal instruments on monetary and banking policy, payment and settlement systems, statistical reporting and research, and other central banking issues. The Bank helped coordinate ECB standpoints in written consultations with EU Member States on legislative bills within ECB purview.

During the review period Bulgaria consulted the ECB in writing on the draft Law amending the Law on the Recovery and Resolution of Credit Institutions and Investment Firms. The draft law introduces provisions implementing Regulation (EU) No 806/2014 of the European Parliament and of the Council establishing uniform rules and a uniform procedure for the resolution of credit institutions and certain investment firms in the framework of a Single Resolution Mechanism and a Single Resolution Fund and amending Regulation (EU) No 1093/2010.

Bulgaria also carried out a consultation on the draft Law on amending the Law on payment services and payment systems. The draft law aims to transpose Directive (EU) 2015/2366 of the European Parliament and of the Council into national legislation and to implement certain measures provided for in other EU legal acts adopted in connection with Directive (EU) 2015/2366, and to introduce measures for the application of Regulation (EU) 2019/518 of the European Parliament and of the Council.

---

[71] The Accounting and Monetary Income Committee (AMICO), the Financial Stability Committee (FSC), the Banknotes Committee (BANCO), the Eurosystem/ESCB Communications Committee (ECCO), the Information Technology Committee (ITC), the Internal Auditors' Committee (IAC), the International Relations Committee (IRC), the Legal Committee (LEGCO), the Market Operations Committee (MOC), the Monetary Policy Committee (MPC), the Market Infrastructure and Payments Committee (MIPC), and the Statistics Committee (STC).

The European Systemic Risk Board, the European Banking Authority, and Colleges of Supervisors

The BNB Governor and BNB Deputy Governor are members of the ESRB General Board. The debate at the four General Board meetings in 2019 focused mainly on the assessment of financial stability risk in the context of the existing geopolitical uncertainty, at both global and European level. Reassessment of risk premia in global financial markets, deteriorating economic outlook including vulnerability of financial institutions' balance sheets and unsustainable levels of indebtedness were identified as the main risks to the EU financial stability. It was emphasized that slower growth would have negative effects on EU financial institutions' profitability and would affect private and public sector debt sustainability. The General Board discussed the mid-term risks arising from vulnerabilities in the residential real estate (RRE) sector in the European Economic Area and found that in eleven countries, which do not include Bulgaria, the observed vulnerabilities could be a source of systemic risk to the financial stability in the medium term. As a result, recommendations or warnings were issued to those countries to take measures aimed at remediating the weaknesses identified. In the context of the 2018 annual review of major trends, the General Board members noted that in implementing EU macroprudential policy Member States' measures are mostly restrictive, with the countercyclical capital buffer, systemic risk buffer and limited loan-to-property-value ratio being the most frequently used instruments.

At the March General Board meeting two reports were considered: the first discussing the contribution of regulatory complexity to systemic risk, and the second the channels through which the exchange-traded funds (ETFs) market may affect systemic risk. The General Board adopted a Recommendation amending the Recommendation on closing real estate data gaps in order to include a new sub-recommendation addressed to Eurostat, to align the definitions used with those included in the EU legislation, and to change the deadlines for reporting on the implementation of the Recommendation. It approved the adverse scenarios for the stress tests of the occupational retirement institutions, central counterparties and money market funds. The results of the 2018 insurance sector stress tests were discussed, highlighting the importance of publishing individual results in view of improving transparency and achieving a level playing field.

The June meeting looked at systemic risks and vulnerabilities related to non-bank financial intermediation, including those related to interconnectedness, liquidity and leverage as well as the second-round effects of EU banks' stress tests.

The issues examined at General Board's September meeting included the vulnerabilities in the residential real estate sector and the possible approach allowing the ESRB to assess the weaknesses in the commercial real estate sector and the adequacy of macroprudential policies to address these weaknesses. Among the major topics were the collection and exchange of information on branches of credit institutions for the purposes of macroprudential policy.

The December meeting put an emphasis on the vulnerabilities in the EU financial system, including the indebtedness of non-financial corporations, the liquidity of assets in investment funds, and the misconduct costs facing financial institutions. General Board members also took note of the risks to the financial stability which might result from climate change and disruptions in critical financial infrastructures. They highlighted the importance of the global financial cycle and that the developments in the core non-EU economies, particularly the United States and China, may be transmitted to EU countries, affecting their domestic financial conditions. In line with its strategy for expanding macroprudential policy beyond banking, possible tools for preventing and mitigating risks in the insurance sector were discussed, thereby ensuring cross-sectoral consistency of macroprudential policy. The Board also noted the main areas, where financial instruments, which prove difficult to be measured at fair value (due to lack of data or incomplete data) may affect financial stability and macroprudential decisions. It underlined the need for greater transparency in this regard in line with the Recommendation of ESRB adopted in 2016 on closing data gaps in the residential and commercial real estate sectors, addressed to the national macroprudential authorities, the European Supervisory Authorities (ESAs) and the European Commission.

In addition to the ESRB General Board, Bank representatives were active in the Advisory Technical Committee, working group meetings and task forces, and prepared positions on topics discussed at meetings, including on written procedures and consultations. In 2019 the BNB experts continued to sit on the supervisory colleges of European banking groups and their subsidiaries, and resolution colleges. Supervisory colleges discussed risk scores as of end 2018 resulting from the Supervisory Review and Evaluation Process (SREP) and signed Joint Decisions on Capital and Liquidity of the banking groups with subsidiaries in Bulgaria. Discussions on banking group recovery plans for 2019 began in the second half of the year.

Under the special supervisory actions the BNB experts continued to participate actively in committees and working groups of the EBA and EC on anti-money laundering and combating financing of terrorism, consumer protection and financial innovations. The topics discussed contributed to updating the methods of supervision in the areas concerned.

With regard to the regulatory framework, standing committees and working groups of the EC and EBA jointly with BNB experts continued their work on the discussion and elaboration of common supervisory policies and standards, the exchange, the assessment and convergence of national practices on the introduction and implementation of the EU prudential and supervisory framework.

The Ecofin Council and Economic and Financial Committee (EFC)

In 2019 the EU Council continued strengthening the Economic and Monetary Union and establishing a regulatory framework to complete the Banking Union. In the first six months of the year the legislative package of measures to reduce risk in the EU banking sector (the banking package[72]) was finally approved. As a result, amendments were made to the legislation on prudential requirements for credit institutions and strengthening the framework for their recovery and resolution. BNB representatives took part in the negotiations on new measures aimed at improving the resilience of EU credit institutions and strengthening financial stability.

The experts were involved in intensive discussions within the Working Group on Financial Services to the EU Council on the 2018 package of measures to tackle non-performing loans in the EU. The progress on the package consisting of a proposal for a Regulation amending Regulation (EU) No 575/2013 as regards minimum loss coverage for non-performing exposures and a proposal for a Directive on credit servicers, credit purchasers and the recovery of collateral, is directly related to the achievement of the main objective of reducing risks in the banking sector and completing the

[72] For further details see BNB January–June Report 2019, p.72.

Banking Union. The regulation introducing a backstop for NPLs was finally approved by the EU Council on 9 April 2019 and published subsequently in the Official Journal of the European Union[73]. In the course of negotiations the proposal for a directive was split in two separate directives the final adoption of which is subject to negotiations with the European Parliament.

In 2019 the work continued on the legislative proposal for a regulation of the European Parliament and of the Council amending Regulation (EU) 806/2014 in order to establish a European Deposit Insurance Scheme (EDIS). Discussions on the proposal which is part of the measures for further risk sharing in the banking system and building Banking Union's third pillar in the euro area continue within the high-level working group set up by Eurogroup decision. In line with the mandate given to the group additional steps should be undertaken to reach an agreement on a roadmap for political negotiations on the legislative proposal. BNB provides its expertise to the Ministry of Finance's representatives in the subgroups to the High-Level Working Group on matters falling within the competence of the central bank.

In 2019 the legislative package of measures to improve the efficiency of the European System of Financial Supervision[74] was endorsed, aimed at enhancing the supervisory convergence and strengthening the capacity of the European supervisory authorities and the ESRB. The measures adopted, which were discussed with the participation of BNB's experts, include amendments intended to strengthen the powers and increase the efficiency of ESA and ESRB management as well as to mitigate the risks to the EU financial sector stemming from activities of money laundering or financing of terrorism.

In 2019 the Bank continued its intensive work on transposing European requirements into national legislation. BNB experts were involved in drafting the Law on amending the Law on payment services and payment systems introducing amendments resulting from both the application of the Directive on payment services in the internal market[75], and the need of national measures to implement the Regulation on cross-border payments in euro[76] as regards certain charges on cross-border payments in the Union and currency conversion charges which came into force at the end of 2019. BNB representatives participated in the inter-service task force, which drafted the Law amending the Law on measures against money laundering adopted in November 2019, which introduced in the national legislation the requirements of Directive

[73] Regulation (EU) 2019/630 of the European Parliament and of the Council of 17 April 2019 amending Regulation (EU) No 575/2013 as regards minimum loss coverage for non-performing exposures (OJ L 111, 25.04.2019, p. 4).

[74] Regulation (EU) 2019/2175 of the European Parliament and of the Council of 18 December 2019 amending Regulation (EU) No 1093/2010 establishing a European Supervisory Authority (European Banking Authority), Regulation (EU) No 1094/2010 establishing a European Supervisory Authority (European Insurance and Occupational Pensions Authority), Regulation (EU) No 1095/2010 establishing a European Supervisory Authority (European Securities and Markets Authority), Regulation (EU) No 600/2014 on markets in financial instruments, Regulation (EU) 2016/1011 on indices used as benchmarks in financial instruments and financial contracts or to measure the performance of investment funds, and Regulation (EU) 2015/847 on information accompanying transfers of funds (OJ L 334, 27.12.2019, p. 1), Regulation (EU) 2019/2176 of the European Parliament and of the Council of 18 December 2019 amending Regulation (EU) No 1092/2010 on European Union macro-prudential oversight of the financial system and establishing a European Systemic Risk Board (OJ L 334, 27.12.2019, p. 146).

[75] Directive (EU) 2015/2366 of the European Parliament and of the Council of 25 November 2015 on payment services in the internal market, amending Directives 2002/65/EC, 2009/110/EC and 2013/36/EU and Regulation (EU) No 1093/2010, and repealing Directive 2007/64/EC.

[76] Regulation (EU) 2019/518 of the European Parliament and of the Council of 19 March 2019 amending Regulation (EC) No 924/2009 as regards certain charges on cross-border payments in the Union and currency conversion charges.

(EU) 2018/843 amending Directive (EU) 2015/849 on the prevention of the use of the financial system for the purposes of money laundering or terrorist financing[77].

A Deputy Governor represents the BNB on the Economic and Financial Committee. Discussions focused on overcoming challenges in the banking sector, the operational preparation for the withdrawal of the United Kingdom from the EU and cases related to the fight against money laundering involving EU credit institutions. Committee's participants examined also the progress in building the Capital Markets Union, and in particular the sustainable financing, the technological innovations used in financial services (fintex) and the resulting challenges to financial sector's functioning and structure. In the context of establishing the Banking Union, further improvement of the supervision framework and the framework for resolution of credit institutions were debated. Progress was achieved by adopting the banking package in April 2019 and implementing the Action Plan to tackle the non-performing loans in the EU. New challenges included increased geopolitical risk, risk of abandoning reforms already implemented in the financial sector, slower economic growth, reassessment of risk premia, risks related to changes in the non-banking sector and in the business models of banks. Within the meetings held Committee's members looked also at the effects of low interest rates for an extended period on EU financial sector. In view of this, discussions focused on banks' resilience, risks stemming from relations with non-banking financial sector and deterioration of unfavourable interdependence between banking and sovereign risk. Committee's members regularly reviewed the actions aimed at building the Capital Markets Union, the expected impact on it as a result of Brexit and the effects of reducing carbon emissions, climate changes and technological developments. They also prepared the annual assessment of capital movement and freedom of payments. Topics discussed included the economic situation review, risks to financial stability, EU financial sector trends, EU government debt markets and opportunities and risks related to the so-called anti-volatile crypto-assets. The international role of the euro, the 15th General Review of IMF Quotas as well as the proposals included in the Report of the G20 Eminent Persons Group on Global Financial Governance concerning the international dimension of financial sector reforms, including key issues arising in regulatory dialogues with third-countries were examined.

Finance and economy ministers and central bank governors took part in the informal EU ECOFIN Council in April and September. The BNB Governor and a Deputy Governor attended the meetings. During the first working session in Bucharest in April participants debated the priorities in the next institutional cycle in order to reach consensus on the steps to ensure an inclusive growth and convergence between EU Member States. In the context of building the Capital Markets Union and the steps undertaken to achieve its objectives, participants considered the benefits and challenges in an increasingly digitalised and greener economic environment framework. The September informal meeting focused on the resilience of financial market infrastructures and the role of the financial sector in counteracting hybrid threats. Consideration was also given to EU priorities on capital markets for the next institutional cycle in view to identify them and to reach an agreement on a series of practical measures which should foster cross-border integration of European capital markets, including measures to be undertaken by Member States.

At the Council of Ministers' Council for European Affairs the BNB helped formulate Bulgarian standpoints on key economic governance areas and the financial sector.

---

[77] Directive (EU) 2018/843 of the European Parliament and of the Council of 30 May 2018 amending Directive (EU) 2015/849 on the prevention of the use of the financial system for the purposes of money laundering or terrorist financing, and amending Directives 2009/138/EC and 2013/36/EU.

IX. International Relations

The Law on the Bulgarian National Bank entitles the Bank to participate organisationally and contribute financially to international financial organisations furthering currency, monetary, and credit policy cooperation. Where Bulgaria participates in international financial institutions, the BNB acts as government's fiscal agent and depository.

The Bulgarian National Bank holds equity in the Bank for International Settlements (BIS). The BNB Governor sat on BIS central bank governors' regular meetings: a major forum for cooperation and debate on world economic developments and prospects, and international financial markets. The BIS Governors allocated net profit at the Annual General Shareholder Meeting in late June 2019, the BNB receiving EUR 2.4 million dividend for its 8000 shares.

The Governor represents Bulgaria as member on the IMF Board of Governors. Bulgaria's IMF quota is SDR 896.3 million or 10,428 voting shares: 0.21 per cent of IMF voting shares.

In January 2019 the BNB signed a Memorandum of Cooperation with the People's Bank of China. Its aim is to strengthen relations and enhance cooperation between the two central banks.

On 26 March 2019 the central bank of Germany jointly with the BNB, other national central banks of the ESCB and the ECB officially launched a technical cooperation programme with central banks and supervisory authorities of countries in the Western Balkans – EU candidates and potential candidates: Albania, Bosnia and Herzegovina, Montenegro, North Macedonia, Serbia and Kosovo. This is a two-year programme financed by the EU *via* the Instrument for Pre-Accession Assistance and managed by the Deutsche Bundesbank. It is intended to further strengthen the capacity of beneficiary institutions and improve policy instruments by applying the best international and European standards in various areas of central bank activities. Over the review period BNB experts delivered lectures to beneficiaries on consumer financial protection, statistics, financial inclusion, statistics, banking supervision, payments systems and European integration. Preparatory meeting with the central bank of the Republic of Kosovo was held on bilateral activities on preventing money laundering and terrorist financing.

BNB experts took part in a forum of central banks on internal audit organised by the central bank of the Republic of Turkey within the framework of bilateral cooperation.

In October 2019 the BNB held an international conference on the fight against euro counterfeiting in the Black Sea region funded by the Pericles 2020 EC programme. The aim of the event was to strengthen cooperation between national competent authorities and exchange of experience and best practices to protect the euro and other currencies against counterfeiting.

In April 2019 the BNB contributed USD 10,000 to the Group of Thirty, an Advisory Group on International Economic and Financial Issues.

In October 2019 the BNB became a member of the European Money and Finance Forum (SUERF) and contributed EUR 1750. This allows the Bank to be more widely represented in the international dialogue on topical issues of importance to the central banks such as the global economic policy, and to participate in the ongoing research activities.

Helping step up regional cooperation, the Bank also participated at summit level in the Central Banks Governors' Club of Central Asia, Black Sea Region and Balkan Countries.

On 18 November 2019 the BNB as a competent supervisory authority signed a Memorandum of Understanding with the Central bank of England and the Financial Conduct Authority (FCA). The Memorandum's structure and contents are entirely based on the EBA template which has been developed for that purpose, its final wording being coordinated with the Bank of England in writing. It regulates information sharing and cooperation between the competent authorities in the performance of their supervisory functions in authorisation (information sharing on representatives and managers, owners and persons exercising control in case of related parties) and in individual aspects of ongoing supervision. The Memorandum covers supervisory colleges and exchange of supervisory assessments, cooperation in supervisory inspections, implementation of supervisory measures and interventions at micro level, implementation of macroprudential measures, recovery plans assessment and cooperation in emergencies and crisis management, in information sharing on the implementation of measures and data sharing in financial crimes.

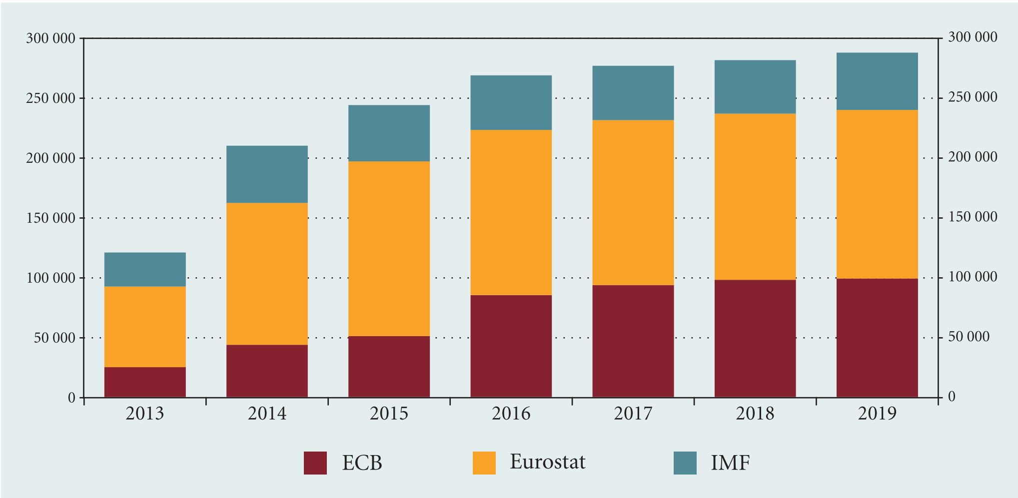
X. Statistics

The BNB compiles statistical information under Article 42 of the Law on the Bulgarian National Bank and as ESCB member under Article 5 of the Statute of the ESCB and the ECB. The Bank adheres to harmonised European standards based on international statistical methodology of relevant leading institutions (the ECB, Eurostat, the IMF, the BIS, the OECD, the UN, and the World Bank).

The BNB collects, processes, analyses and disseminates official monetary[78] and interest[79] statistics, external statistics[80], quarterly financial account statistics for all institutional sectors[81], government finance statistics[82], and statistics on non-bank financial institutions, including leasing companies and investment funds[83], specialised lenders and insurance and reinsurance undertakings[84].

Unique Time Series Sent to the ECB, Eurostat and IMF

(number)



Source: the BNB.

In 2019 the Bank continued to disseminate up-to-date data on its website and by regular communications with the ECB, Eurostat, the ESRB, the IMF, the BIS, and other national and international institutions. The volume of statistics sent to international

---

78 Pursuant to Regulation (EU) No 1071/2013 of the European Central Bank of 24 September 2013 concerning the balance sheet of the monetary financial institutions sector (recast).

79 Pursuant to Regulation (EU) No 1072/2013 of the European Central Bank of 24 September 2013 concerning statistics on interest rates applied by monetary financial institutions (recast).

80 Pursuant to Regulation (EC) No 184/2005 of the European Parliament and of the Council of 12 January 2005 on Community statistics concerning balance of payments, international trade in services and foreign direct investment and Guideline of the ECB of 9 December 2011 on the statistical reporting requirements of the European Central Bank in the field of external statistics (ECB/2011/23).

81 Under the European System of Accounts (ESA 2010) provided for in Regulation (EC) No 549/2013 of the European Parliament and of the Council of 21 May 2013, Guideline of the European Central Bank of 25 July 2013 on the Statistical Reporting Requirements of the European Central Bank in the Field of Quarterly Financial Accounts (ECB/2013/24) and subsequent amendments.

82 Pursuant to ESA 2010 Guideline of the ECB of 25 July 2013 on government finance statistics (ECB/2013/23) and subsequent amendments.

83 Pursuant to Regulation (EU) No 1073/2013 of the ECB of 18 October 2013 concerning statistics on the assets and liabilities of investment funds.

84 Pursuant to Regulation (EU) No 1374/2014 of the European Central Bank of 28 November 2014 on statistical reporting requirements for insurance corporations (ECB/2014/50).

institutions continued to grow, the number of unique time series provided to the ECB, Eurostat and IMF reaching 289,000 in 2019 (282,000 in 2018).

Compiled statistical data are also used for economic research and forecasting, financial stability analyses, major BNB operations, and a number of foreign publications and reports like the ECB and Eurostat statistical database, the ECB Annual Report, the Convergence Report, and the Macroeconomic Imbalance Procedure Scoreboard. In 2019 all statistical data were published on the BNB website as scheduled.

In addition to the compilation of statistical data, the BNB was active in a number of national, European and international fora discussing and solving statistics methodological issues. All statistical data published by the BNB were accompanied by the relevant metadata which were periodically revised where necessary. In early 2019 monetary statistics methodological requirements were updated with regard to IFRS 16 enactment and implementation.

The statistical database continued developing and improving to match ESCB priorities and objectives and amended ECB guidelines on the Register of Institutions and Affiliates Data (RIAD), including BNB reference individual data (the Register of Domestic Economic Agents and the Bulgarian Securities Database). Along with analytical options at the national level, these databases allow the BNB to fulfil its commitments to the ESCB in managing the data for Bulgaria in the Register of Institutions and Affiliates Database and the Centralised Securities Database (CSDB)[85]. This contains reference information on credit institutions, money market funds, financial vehicle corporations, investment funds and their management companies, payment service providers and payment system operators, insurance and reinsurance companies, and holding companies and head offices. In 2019 domestic pension funds and Bulgarian non-financial corporations which had issued securities became RIAD reported units in stages. This allows RIAD issuer reference data to link with CSDB securities data.

The Bank continued volunteering to help ESCB national central banks identify and supplement RIAD reference information on resident institutional unit parties to credit relations as part of the AnaCredit project[86] on granular credit and credit risk data. The BNB actively participated in the ECB Securities Holdings Statistics project (SHS)[87], important for gathering various statistical data and analysing financial stability.

In 2019 the Bank continued developing and elaborating the Integrated Statistical Information System (ISIS) and the Information System for Monetary and Interest Rate Statistics (ISMIRS). They automate management, improve the reliability and high quality of statistical information the BNB receives, processes and disseminates, and greatly reduce the administrative burden on individuals and legal entities by offering electronic submission of statistical reports and declarations. Early 2019 changes to ISIS improved electronic submission and signature of access applications, declarations, change requests and statistical reports. In line with this, BNB guidelines for providing electronic statistical information were updated. The BNB attaches great importance to the quality of the statistical data compiled by it. It follows the principles of the Public Commitment on European Statistics by the European System

[85] Pursuant to Guideline and Recommendation of the ECB of 26 September 2012 on the data quality management framework for the Centralised Securities Database (ECB/2012/21 and ECB/2012/22).

[86] Pursuant to Regulation (EU) No 2016/867 of the European Central Bank of 18 May 2016 on the collection of granular credit and credit risk data (ECB/2016/13).

[87] Pursuant to Regulation (EU) No 1011/2012 of the European Central Bank of 17 October 2012 concerning statistics on holdings of securities (ECB/2012/24) and subsequent amendments, Guideline of the ECB of 22 March 2013 concerning statistics on holdings of securities (ECB/2013/7) and subsequent amendments, Recommendation of the ECB of 2 August 2016 on the data quality management framework for statistics on holdings of securities (ECB/2016/24).

of Central Banks, based on the fundamental principles of UN official statistics. The Bank took part in ESCB and European Statistical System reports on quality assessment measuring compliance with these principles of central bank statistical products and national statistical institutes through set indicators: accessibility and clarity, punctuality, reliability, comparability, and coherence. The published reports ensure transparency and allow for a comparative analysis of the quality of these statistical products for all EU Member States.

At the end of June 2019 the ECB and Eurostat published their fifth Annual report on the quality of statistical data underpinning the indicators used in the macroeconomic imbalances procedure, including BNB statistics on the balance of payments, the international investment position, and quarterly financial accounts. The BNB as coordinator for Bulgaria also adheres to the requirements of the IMF Data Quality Assessment Framework, part of the Special Data Dissemination Standard Plus (SDDS Plus) which Bulgaria has joined.

In statistics, the BNB cooperates with the NSI and the Ministry of Finance, national and international statistical authorities, and central banks. As a result of the joint work between the Bank and the NSI, a revision aiming at data comparability (benchmark revision) between international investment position and balance of payments statistics, and quarterly and annual financial accounts was carried out over the year.

XI. The Central Credit Register and the Register of Bank Accounts and Safe Deposit Boxes

The Central Credit Register

The Bulgarian National Bank maintains an information system on customer debt to banks, financial institutions, payment institutions and electronic money institutions extending loans under Article 19 of the Law on Payment Services and Payment Systems (reporting units). BNB Ordinance No 22 on the Central Credit Register establishes the operation, scope, procedure, and timeliness of information flows to and from the CCR. The Register maintains data on all loans, irrespective of their amount, extended by reporting units. The CCR provides information on credit indebtedness of customers in real time. This includes loan status, arrears, and repaid loans for five years back.

In view of CCR system development and the need of improving quality of the information provided by the Register, since 20 November 2019 the system has been providing additional information on entities, which are co-borrowers and guarantors on extended loans. Additional data allow CCR participants to assess customers creditworthiness better.

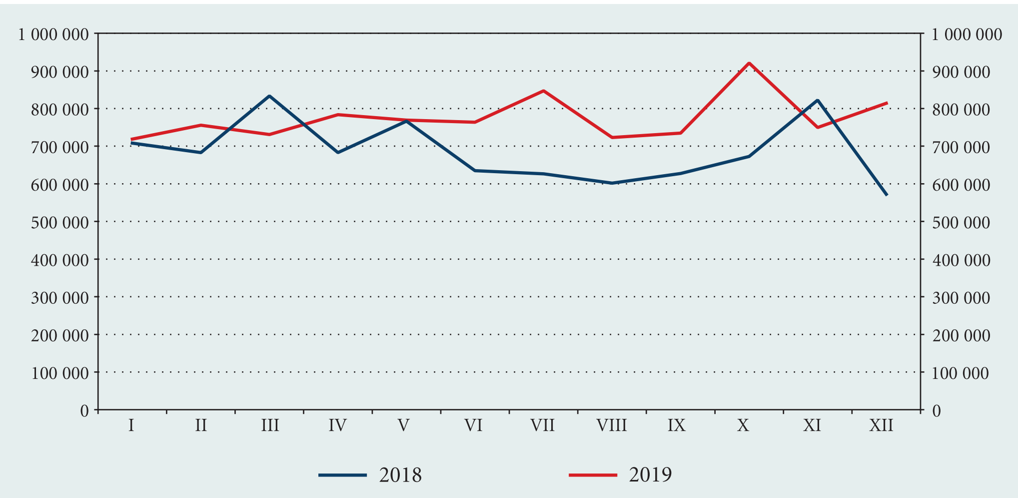
On 31 December 2019 the CCR had 215 participants: 26 banks, 186 financial institutions, two payment institutions and an electronic money institution. Over the year 13 new financial institutions and an electronic money institution enrolled and five financial institutions and a bank left.

As of 31 December 2019 the CCR listed 5844 thousand loans, from 5433 thousand a year earlier, with a balance sheet exposure of BGN 83,718 million (BGN 75,866 million a year earlier). Borrowers numbered 2547 thousand, of whom 2319 thousand natural persons, 101 thousand legal entities, 119 thousand non-residents not registered at Bulgarian addresses or BULSTAT/PIK coded, and 8000 self-employed persons practising liberal professions or crafts.

As of 31 December 2019 residual debt of up to BGN 5000 predominated with natural persons (59.5 per cent), while debts of BGN 5000 to 50,000 predominated with legal entities (34.1 per cent).

Searches by Participants in the CCR Information System (Monthly)

(number)



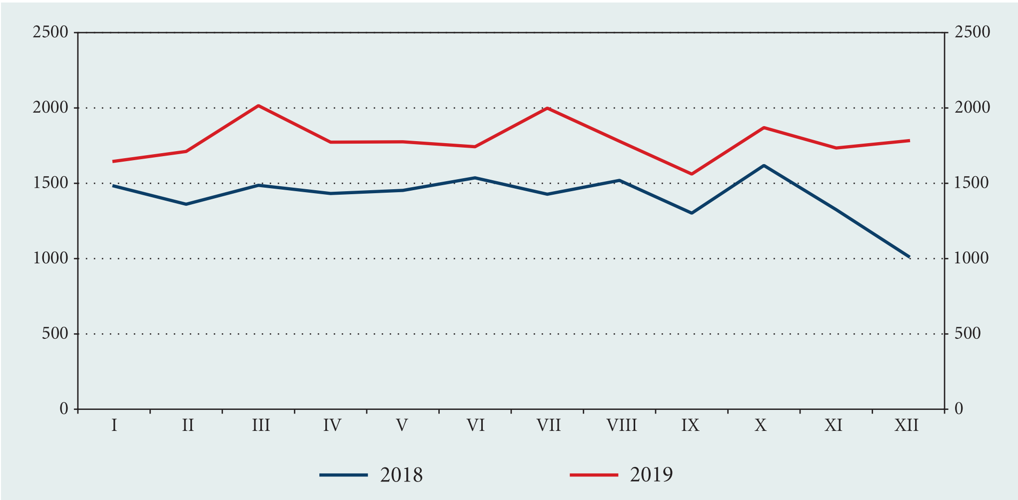
Source: the BNB.

CCR information was essential for creditors to assess borrower creditworthiness before lending. Historical data on arrears and repaid loans added an important aspect to this. In 2019 CCR conducted 9311 thousand electronic searches (8232 thousand as of 31 December 2018). The average monthly number was 776 thousand, of which 73.8 per cent by banks and 26.2 per cent by other participants.

Articles 21–23 of Ordinance No 22 grant natural persons (including for probate purposes) and legal entities access to debt information. In 2019 there were 21,385 applications for CCR hard copy statements (16,953 as of 31 December 2018).

CCR Searches Based on Applications /Letters Submitted to the BNB by Month

(number)



Source: the BNB.

With effect from 5 June 2019, requests for electronic statements from the Register may be submitted by natural persons holding a qualified certificate for electronic signatures issued by a certification service provider under the Electronic Document and Certification Services Law. Fees charged for electronic services account for 50 per cent of those submitted on paper. As of 31 December 2019 electronic statements submitted to the CCR were 913.

The CCR adheres to state of the art information use requirements *via* three user interfaces based on new data processing technologies. The Register exchanges information with other European credit registers to improve its technological and methodological performance. CCR information compiling and maintenance follows relevant best practice.

The CCR provides research, statistical analyses, and annual information to the World Bank under the Doing Business project, the ECB, the IMF, and other international bodies.

The Register of Bank Accounts and Safe Deposit Boxes (RBASDB)

The BNB maintains an electronic information system on bank account numbers, holders and attorneys, data on account preservation orders, bank deposit box holders and attorneys. Banks and foreign bank branches in Bulgaria, and the BNB submit information to the Register. BNB Ordinance No 12 on the Register of Bank Accounts and Safe Deposit Boxes establishes the operation, scope, terms, procedure and timeliness of information flows to and from the CCR. The information on bank accounts and safe deposit box hires is provided in real time, with banks submitting weekly data to the BNB.

As of 31 December 2019 the Register logged 15.56 million active bank accounts, from 16 million in December 2018, and 32.40 thousand safe deposit box hires, from 32.04 thousand in December 2018, including records of 3.03 million new and 3.33 million closed accounts.

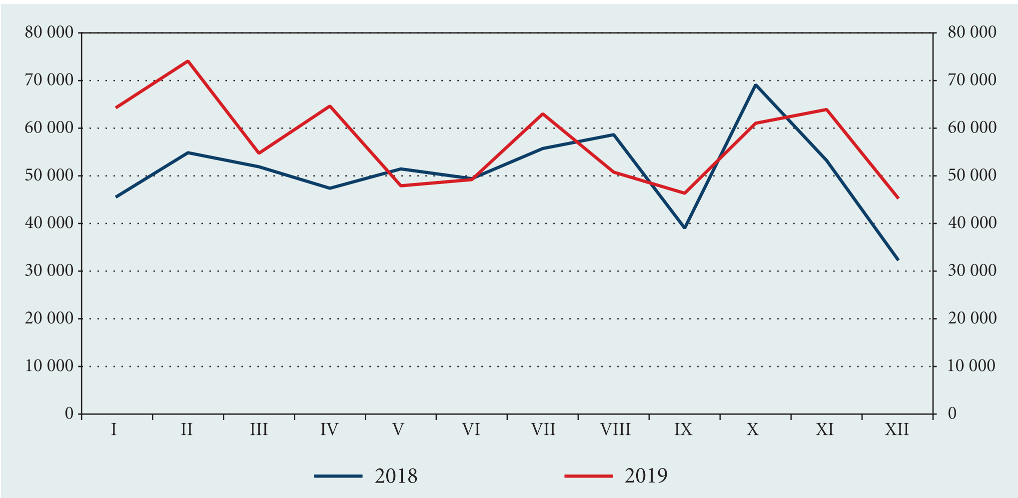
As of 31 December 2019 the Register held details of 1.3 million account preservation orders and 362 thousand accounts with rescinded preservation orders. The two consolidations resulting from mergers of banks in 2019 led to a transfer of 338.2 thousand records of accounts to the Register.

The Law on Credit Institutions grants Register information access to judicial authorities (Courts, the Prosecutor's Office, and criminal investigation authorities), the Ministry of the Interior National Police General Directorate, the General Directorate for Combating Organised Crime and Ministry of Interior regional directorates, the State Agency for National Security, the National Revenue Agency, the Committee for Combating Corruption and Withdrawal of Illegally Acquired Property, the Customs Agency, the Financial Supervision Commission, private and state bailiffs in enforcement proceedings, and other bodies listed in the Law on Credit Institutions Article 56a. Facilities offering electronic access to the system to authorised bodies are available. By 31 December 2019 electronic statements accounted for 98.5 per cent of all statements for the year. Their relative share for 2018 was 98.3 per cent.

In 2019 bodies and institutions entitled to Register access under Article 56a, paragraph 3 of the Law on Credit Institutions conducted searches on 685,645 individuals. The average monthly number of searches was 57,137. In 2018 the total number of searches was 608,989 and the average monthly number 50,749.

RBASDB Searches by Bodies and Institutions under Article 56a, Paragraph 3 of the Law on Credit Institutions by Month

(number)

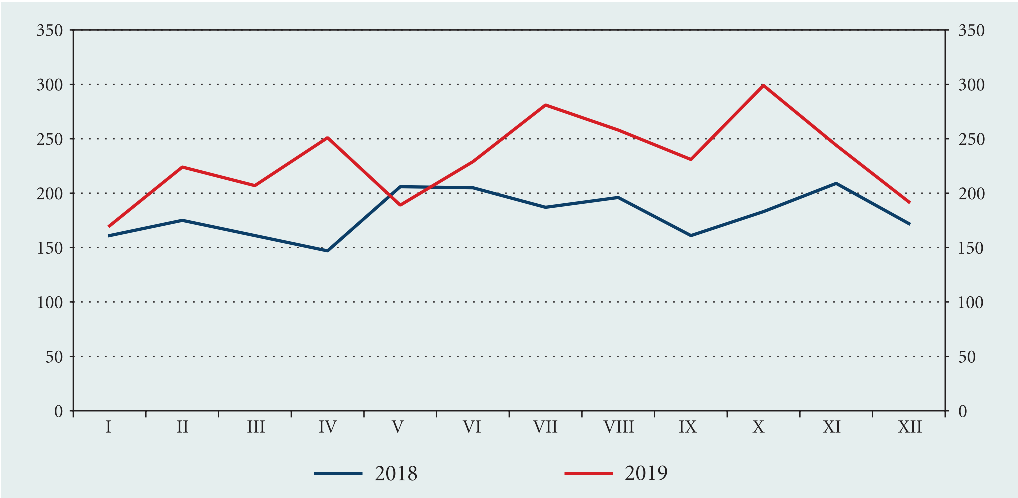


Source: the BNB.

BNB Ordinance No 12 on the Register of Bank Accounts and Safe Deposit Boxes grants natural persons (including for probate purposes) and legal entities access to information on available bank accounts and safe deposit boxes. In 2019 there were 2775 applications for RBASDB statements: 2636 by individuals and 139 by legal entities. In 2018, 2163 applications for RBASDB statements were submitted, of which 2059 by individuals and 104 by legal entities.

RBASDB Searches Based on Submitted Applications (Monthly)

(number)



* Based on hard copy applications submitted by natural persons and legal entities.

Source: the BNB.

With effect from 5 June 2019, requests for electronic statements from the RBASDB may be submitted by natural persons holding a qualified certificate for electronic signatures issued by a certification service provider under the Electronic Document and Certification Services Law. Fees charged for electronic services account for 50 per cent of those submitted on paper. As of 31 December 2019 electronic statements submitted to the RBASDB were 135.

The RBASDB continuously improves and develops using the best EU practices in creating and operating bank account registers. To boost data quality and reliability, incoming information is constantly analysed and the RBASDB changed and improved. New functionalities are being created following amendments to the European Union law and national legislation.

XII. The Fiscal Agent and State Depository Function

In line with the Law on the BNB, the Bank acts as the fiscal agent and official depository pursuant to contracts concluded with the Ministry of Finance. These commitments call for a continuing improvement of the GSAS system for conducting government securities auctions; the ESROT electronic system for registering and servicing government securities trading; the GSSS government securities settlement system; the Register of Special Pledges; and the IOBFR system for budget and fiscal reserve information servicing.[88]

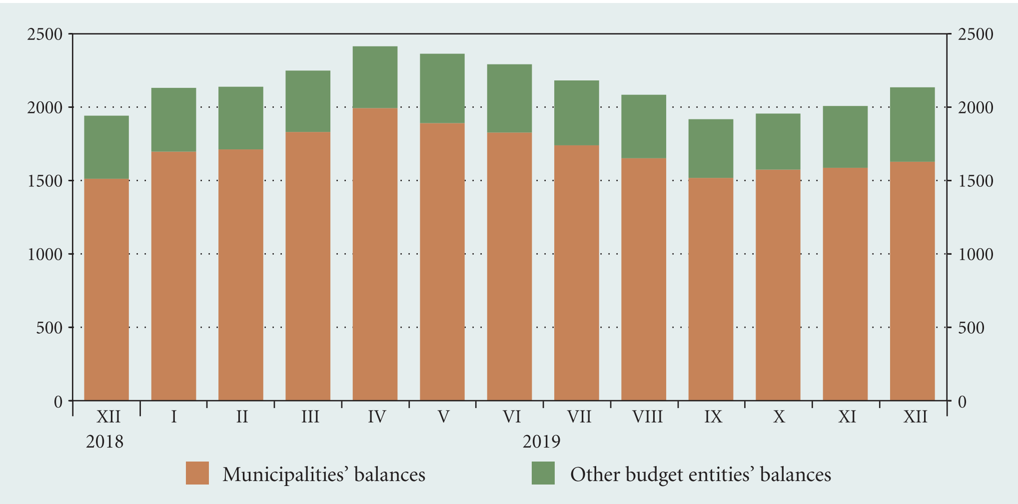
Revenue raised in 2019 from system participants under the Tariff of Fees and Commissions Charged on Processing Government Securities Transactions and from the MF under LBNB Article 43 was BGN 2121.6 thousand, from BGN 1712.8 thousand last year.

Information Service

Providing state budget information under the MF contract involved issuing 987 summarised standard statements on budget entity operations and balances at the BNB and Bulgarian banks. Summarised information sets the overall balance of budget entities' accounts (including municipalities) at BGN 10,245.4 million[89], down 3.0 per cent on 31 December 2018. At end-2019, BGN 8104.4 million or 79.1 per cent was in BNB accounts and the rest (BGN 2141.0 million) with 17 domestic banks.

Budget Entities' Accounts with Domestic Banks (BNB Excluded)

(BGN million)



Source: the BNB.

Budget entities' account balances outside the central bank rose by 9.9 per cent on end-2018, of which 74.5 per cent at five banks.

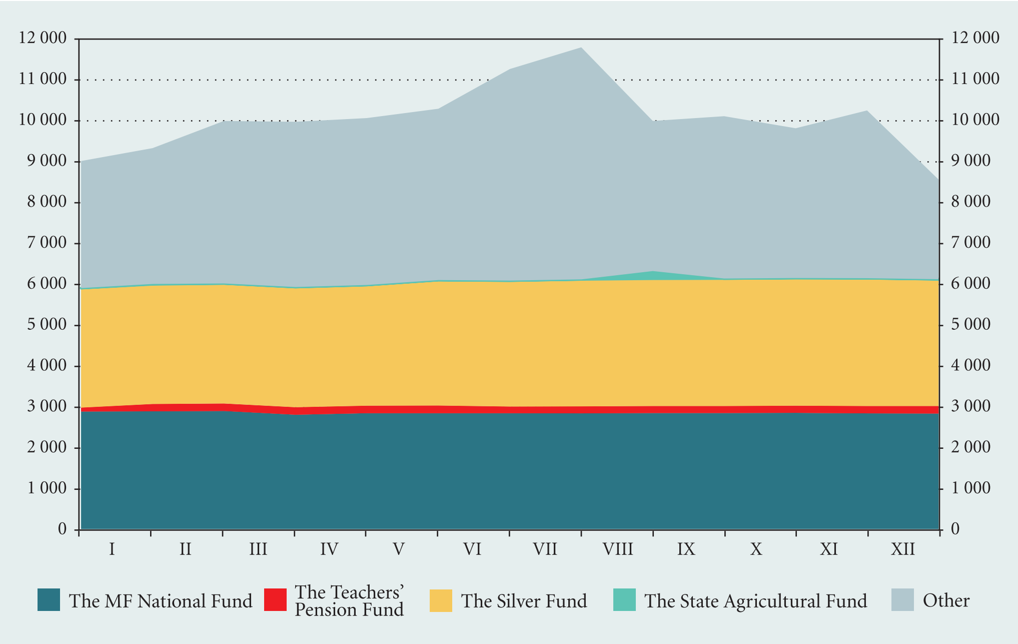
[88] Since 1 September 2019, the AS ROAD system for registering and servicing external debt has been completely phased-out, with all system activities technologically backed by other information systems of the BNB and the MF.

[89] Foreign currency account balances are recalculated in levs at the BNB exchange rate as of the end of the period.

Over the year 83.4 per cent of total budget funds at the BNB and other domestic banks formed the fiscal reserve's[90] liquidity portion[91]: BGN 8543.3 million on 31 December 2019. Of this, BGN 6110.1 million was allocated to earmarked funds: the State Fund for Guaranteeing the Stability of the State Pension System (the Silver Fund), the MF National Fund, the State Fund Agriculture – Paying Agency, and the Teachers' Pension Fund.

Structure of Bank Account Balances within the Fiscal Reserve Scope

(BGN million)



Source: the BNB.

Standing Minister of Finance and BNB Governor joint instructions task the Bank, on behalf of the Ministry of Finance, to monitor security pledged by banks under the Law on Public Finance and tally it with balances on budget entities' accounts on a daily basis.

Servicing Government Securities Trading

The MF issuing policy in 2019 involved six auctions for BGN-denominated government securities *via* the GSAS system. They offered two long-term issues denominated in levs: a 10.5-year issue at 0.5 per cent annual interest and a 20-year issue at 1.5 per cent annual rate.

The total nominal value of government securities offered for sale was BGN 1095 million. Over 54 per cent of bids were by banks (BGN 916.2 million) with BGN 769.0 million by non-bank institutions. The total volume of government securities sales reached BGN 969.8 million, or 88.6 per cent of the scheduled auction volume. Banks (including primary dealers[92] of government securities) bought nearly 49 per cent of

[90] The Law on Public Finance Additional Provisions §1, item 41 defines the fiscal reserve as comprising the balances of all budget entities' bank accounts (excluding municipalities and their budget spending units) and other assets and claims on EU funds.

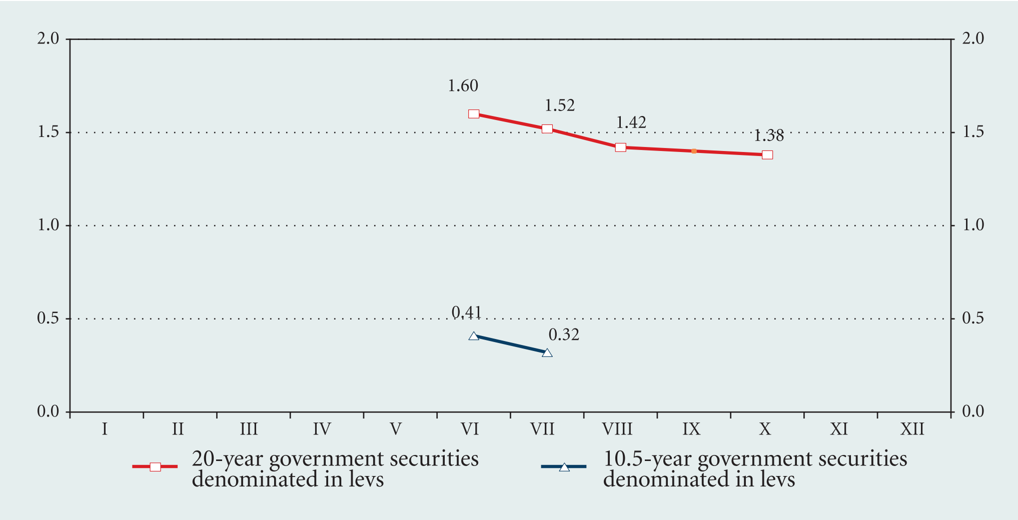
[91] Comprises the balances of all Bulgarian budget entities' bank accounts, excluding municipalities and their budget spending units.

[92] Nine primary dealers were selected under MF and BNB Ordinance No 15 as of 31 December 2019.

all sold bonds. Average annual yields of 10.5-year and 20-year issues were 0.37 and 1.48 per cent, respectively.

Average Annual Yields Attained at Domestic Government Securities Auctions in 2019

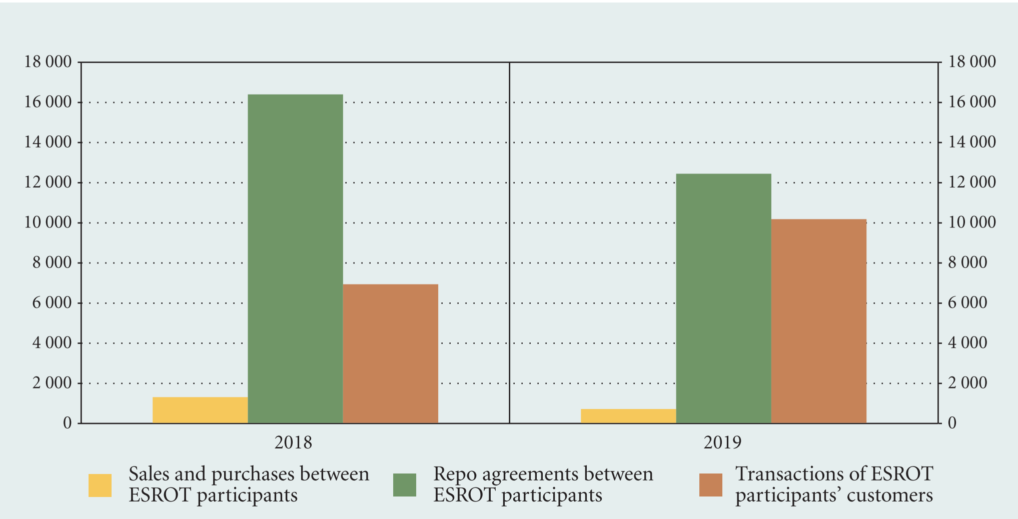
(per cent)



Source: the BNB.

Volume of Transactions in Tradable Government Securities

(BGN million)



Source: the BNB.

ESROT registered corporate event payments on behalf and for the account of the issuer to a total amount of BGN 1116.5 million[93], down BGN 347.7 million (23.7 per cent) against the same period of 2018. The 17 circulating MF issues had an overall nominal value of BGN 5479.5 million[94] or 0.5 per cent more than on 31 December 2018. Bond currency structure changed due to the last bonds issued for structural reform (ZUNK bonds) maturing in January 2019 and denominated in euro and USD

[93] The lev equivalence of payments on foreign currency denominated government securities issues was calculated at the BNB rate on the date of payment.

[94] The lev equivalence of government securities issues denominated in foreign currency was calculated on the basis of the BNB rate for 31 December 2019.

redeemable in levs. BGN-denominated government securities redeemable in levs occupied the largest relative share of 80.6 per cent, followed by EUR-denominated government securities redeemable in euro at 19.4 per cent. The maturity structure underwent no changes from end-December 2018, medium and long-term bonds comprising 10.9 and 89.1 per cent.

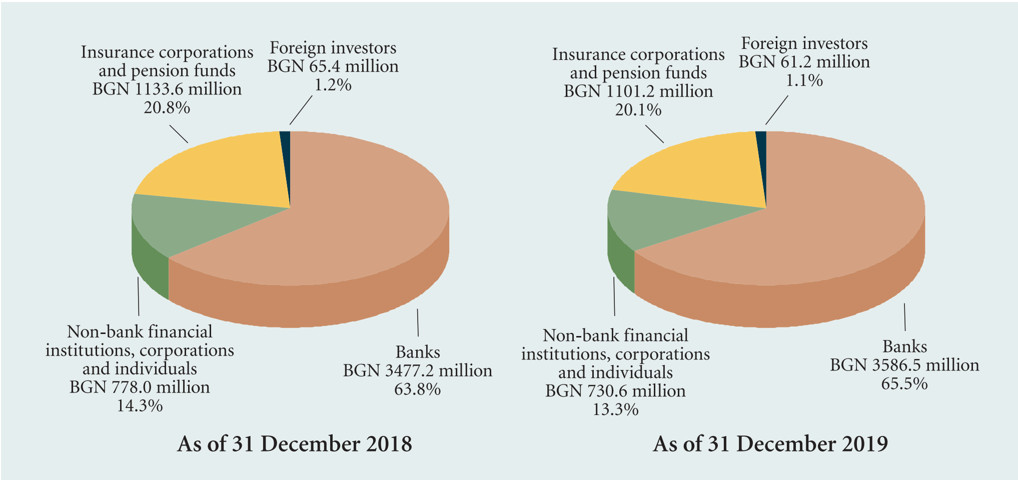
The nominal value of government securities registered in ESROT came to BGN 23,431.2 million, down 5.3 per cent on 2018.

Repos had the largest share at 91.3 per cent, including one-day ones (45.6 per cent), mostly in lev-denominated government securities. Government securities sale and purchase transactions totalled BGN 1457.1 million. Of this, transactions between ESROT participants were BGN 696.5 million, those between participants and their customers amounting to BGN 760.6 million. Transactions between ESROT participants' customers[95] accounted for BGN 575.5 million.

Reflecting government securities trade, secondary government bond market liquidity ratio[96] was 4.3 per cent against 4.5 in the previous year. In 2019 ESROT participants encountered no problems and provided government bonds and cash in levs and euro for the delivery *versus* payment (DvP) settlement of government securities transactions, with the averaged settlement ratio[97] reaching 100 per cent.

Over the review period ESROT blocking and unblocking operations in domestic government securities related to securing funds in budget entities' bank accounts under the Law on Public Finance and the Law on Special Pledges totalled BGN 4498.0 million, from BGN 6916.3 million for 2018.

Holders of Government Securities Issued in the Domestic Market



Notes: According to BNB and ESROT participants data. The lev equivalence of government securities issues denominated in foreign currency is calculated on the basis of the BNB exchange rate valid for the last business day of the relevant period.

Source: the BNB.

The end of 2019 saw a year-on-year increase of government securities investments in bank portfolios (by BGN 109.3 million) and a decline of those in the rest categories

[95] The ESROT system registered no transactions between customers of the same participant.

[96] The liquidity ratio is the ratio between the volume of secondary market government bond transactions concluded over a year and the volume of circulating government securities by that year's end.

[97] Settlement ratio is the ratio of the number of transactions settled on a specific date to all transactions subject to registration and settlement within the system for the reporting period.

of holders, *i.e.* insurance corporations and pension funds (by BGN 32.4 million), non-bank financial institutions, corporations and individuals (by BGN 47.4 million) and foreign investors (by BGN 4.2 million). This changed the shares of government bond holder categories as of 31 December 2019 to: 65.5 per cent with banks; 20.1 per cent with insurance corporations and pension funds, 13.3 per cent with non-bank financial institutions, corporations and individuals, and 1.1 per cent with foreign investors, from 63.8, 20.8, 14.3 and 1.1 per cent as of 31 December 2018.

Over the review period the ESROT offered 99.9 per cent availability[98] with no call for contingency rules for interaction between systems operated by the BNB.

On 31 December 2019 there were 679 accounts in the government securities settlement system under BNB Ordinance No 31 on Government Securities Settlement. Of them, 17 were for government securities of the issuer (the MF), 277 for participants' own government securities portfolios, 152 for encumbered bonds, and 233 for participants' customers. Account nominals tallied with the amount of outstanding issues at BGN 5479.5 million.[99]

Projects and System Development

In 2019 the GSAS upgrade project was completed, thus ensuring system technological modernisation and its migration to new hardware, software, and application architecture in line with the agreements reached with the MF. Project finalisation in April allowed the new version of the system to be launched and government securities auctions as announced by the MF in 2019 to be conducted *via* the upgraded GSAS.

Over the review period the Bank completed its work on drafting a new instruction on the implementation of Article 152 of the Law on Public Finance to replace the current instruction DDS No 09 of 31 July 2015 on banks' periodic statements of budget entities' operations and funds and daily securing of funds in these accounts. The new instruction was consulted with banks *via* the Association of Banks in Bulgaria.

Jointly with the MF, the BNB drafted an instruction for information collection and submission with a view to regulate and control registration of government bond transactions in the secondary market, optimise provision of information by sub-depositories of government securities and define data scope.

In line with the CPSS/IOSCO Principles for Financial Market Infrastructures and the Standards of the ESCB and the CESR for Securities Clearing and Settlement Systems, to ensure a fair, effective and transparent market of government securities, protect investors' interests and reduce to a minimum risks in registration and settlement systems:

– a meeting was held to establish the User Committee of the Government Securities Registration and Settlement System at the BNB under Article 28 of Regulation (EU) No 909/2014[100] for the period 12 February 2019 to 12 February 2021. According to the operating rules of the User Committee, a regular meeting was organised in the second half year to discuss pending amendments stemming from Regulation (EU) No 909/2014 and regulatory technical standards for settlement discipline along with certain technical aspects of the services provided by the Government Securities Registration and Settlement System at the BNB;

[98] The ratio of time when the system is operational to scheduled operating time.

[99] The lev equivalence of government securities issues denominated in foreign currency is calculated on the basis of the BNB rate for 31 December 2019.

[100] Regulation (EU) 909/2014 of the European Parliament and of the Council of 23 July 2014 on improving securities settlement in the European Union and on central securities depositories and amending Directives 98/26/EC and 2014/65/EU and Regulation (EU) No 236/2012.

– work started on analysing and defining changes in business procedures of the Government Securities Registration and Settlement System at the BNB, stemming from the project for accession of the BNB and TARGET2-BNB participants to the consolidated platform of TARGET services;
– a consultation was held with MF representatives and market participants with regard to the ECB project on the integration of European financial markets through developing harmonised collateral management rules, corporate actions and invoicing, given the need for establishing a National Group for Bulgaria and follow up to the project development.

XIII. Research

Economic research, Bulgarian economic development analyses, and macroeconomic forecasts prepared by BNB experts support the Bank management decisions and economic policy formulation. Specialised research under the 2019–2020 BNB Research Plan supported Bank operations by analysing specific economic processes and issues and improving available forecasting and modelling tools.

In 2019 Research Plan implementation addressed developing and expanding BNB instruments used to prepare macroeconomic simulations and designing a satellite model reflecting effects of long-term structural changes in the Bulgarian economy. Honing the basic model for BNB macroeconometric forecasting continued over the year. Research results featured in technical reports and seminars and conferences held for experts from relevant bodies and academia.

In July 2019 the BNB jointly with BIS organised a conference entitled 'The current global and European financial cycle: where do we stand and how do we move forward?' on the occasion of the 140th anniversary of the Bulgarian National Bank. The Conference discussed issues related to the concept of financial cycle and its role in applying macroprudential instruments to safeguard financial stability, the challenges in applying various approaches for its measurement, and global financial cycle's phases and influence on euro area financial cycle and hence on non-euro area countries' financial cycle.

In 2019 the BNB continued to encourage the research potential of Bulgarian economic science and practice in the area of macroeconomics and finance through its Discussion Papers research series. The BNB Publications Council reviewed five new submissions, of which three were published: *Financial Cycle in the Bulgarian Economy and Its Interaction with the Business Cycle* by Tania Karamisheva, Gergana Markova, Boyan Zahariev and Svilen Pachedzhiev; *Labour Market Functioning and Matching Efficiency in Bulgaria over the Period 2004–2017: Qualification and Regional Aspects* by Ventsislav Ivanov, Desislava Paskaleva and Andrey Vassilev; *Transmission of ECB's Monetary Policy in Bulgaria: Insights from a Large Macro-econometric Model* by Mariella Nenova-Amar, Evgeni Ivanov, Neli Ivanova, Daniel Kasabov, Boyan Zahariev, Gergana Markova, Kristina Karagyozova-Markova.

The BNB quarterly Economic Review presents information and Bulgarian economic forecasts, analyses of the balance of payments flows dynamics, monetary aggregates, their link with the development of the real economy, and their bearing on price stability. It also analyses external developments directly affecting the Bulgarian economy. The Economic Review also carries quantitative assessments of anticipated short-term developments in a set of key macroeconomic indicators. The Review also carries the results of BNB analyses of particular economic issues as highlights and topical research. The year saw publication of a topical research paper on methods for assessing the cyclical position of the Bulgarian economy and two analyses featuring the Key Characteristics of the New Euro Unsecured Overnight Rate (€STR) and Basic Parameters of the 2019–2021 Budgetary Framework.

XIV. Human Resource Management

The policy and activities on human resources management enable the BNB to make full use of staff capabilities and knowledge: the major factor for successful fulfilment of the BNB objectives, functions and tasks. Maintaining and developing competitive human resources continued to be a key Bank policy in 2019.

New labour legislation related to recruiting disabled people changed aspects of human resource management. In line with statutory changes applicable internal acts were supplemented and updated. In view of the Law on Personal Data Protection amendments, the relevant changes in personal data processing of employees and candidates were made in 2019.

The year saw some changes intended to improve the Bank's organisational structure. Fiscal Services Department was transformed into a Directorate under the Banking Department. The Issuing Policy and Control Directorate within the Issuing Department was closed.

To effectively fulfil BNB functions and tasks, it is vital to employ and retain qualified and motivated staff. Key priorities in human resources were related to attracting appropriate candidates, retaining highly qualified employees by providing professional and career development, while applying a supportive and fair remuneration system, and ensuring a favourable, well organised and dynamic working and sociable environment.

At the end of 2019 the BNB staff numbered 895 compared to 886 a year earlier. Of them, 72 were new recruits (64 in 2018), seven covering long term absences. During the period under review five employees covering long-term absence were appointed to permanent positions. The bank advertised 37 vacancies (29 in 2018), attracting more than 800 applicants. Vacancies were usually published on the BNB website and specialised media, including career centres of Bulgarian and foreign higher education institutions. Employees were recruited in compliance with the approved internal rules and procedures for recruitment.

Sixty-one employees left (57 in 2018), including 22 retired (15 in 2018). Staff turnover rose by 0.4 percentage points to 6.8 per cent compared with the previous year.

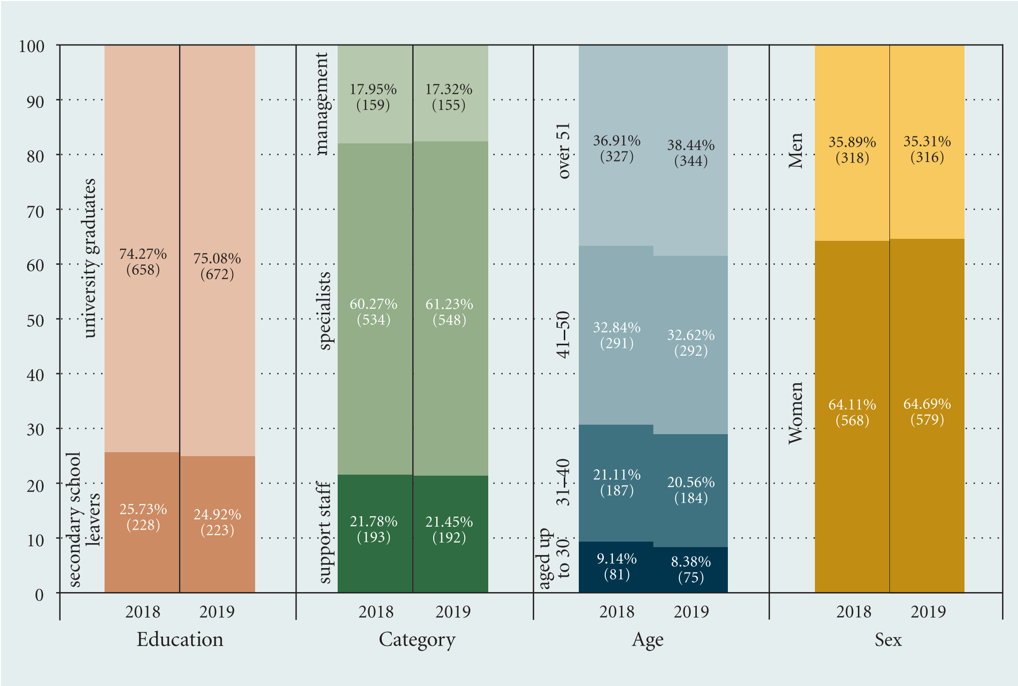
University graduates again led staff educational attainment structure at 75.0 per cent (74.3 per cent a year earlier), of them 85.9 per cent with master's degrees and 9.8 per cent with bachelor's degree. Twenty-nine employees had doctorates (26 in 2018). By category, specialists held the largest share at 61.2 per cent, followed by support staff (21.5 per cent) and management (17.3 per cent). Age structure remained almost unchanged compared to 2018.

In 2019 the shares of employees aged up to 30 and from 31 to 40 years and from 41 to 50 years declined slightly. Only the share of employees aged over 51 years rose by 1.5 percentage points reaching 38.4 per cent compared to 2018.

By the end of 2019 women made up 65 per cent of total employees and men 35 per cent, the shares of these groups changing slightly.

Staff Structure on 31 December

(per cent, number)



Source: the BNB.

Employees' career development through internal mobility ensured an efficient experience exchange across business areas and knowledge and skill acquisition. The number of employees moving to other units or positions increased from 26 in 2018 to 74 in 2019 including 44 who were redeployed as a result of the structural changes. Three BNB employees worked on ECB short-term assignments.

In 2019 the BNB remuneration policy continued to be based on competitive remuneration levels and to be directly dependent on employees' individual contributions, taking into account their professional qualities including skills and abilities to fulfil Bank's tasks and goals.

Most of the activities on human resources management in the Bank were related to employees' training and qualification and their professional and career development. The annual schedule offered employees plentiful opportunities to take a variety of training boosting programmes like distance learning, professional courses and seminars in Bulgaria and abroad, language courses, information technology courses, and courses for specific responsibilities.

Courses and practical seminars enriched employees' theoretical knowledge and developed their technical skills to perform the functions and tasks assigned. Supplemented programs and widened training including intra bank refreshers helped new employees perform sooner and spread knowledge, skills, and information increasing further sense of belonging and sharing a common mission and values at national and European level.

Induction training familiarised new employees with the corporate culture, Bank's history and traditions, topical tasks and challenges, internal rules, and general administrative procedures. A number of internal bank training sessions were carried out, covering new functional areas and groups of employees, on topics like market infrastructure development, implementing measures against money laundering and terrorist financing, identifying suspicious operations, transactions and customers, servicing currency in circulation, *etc*.

Over the year 22 employees, of whom six reading for doctors', nine for masters', and seven for bachelors' degrees, boosted their educational attainments without discontinuing work. Career guidance distance learning and certification programmes drew attention from employees in specific functional units, participating in international programmes on reserve management, information security and internal audit.

BNB's employees took inland specialised courses and seminars in law and public procurement, accounting and internal audit, human resource management, public procurement, security, facilities management, *etc*.

Information systems training focused on presenting innovations in network and communication technologies and in making, implementing and administering security policies, arrangements and rules and development of cloud technologies.

The BNB continued cooperating with ESCB central banks and international financial institutions and Single Supervisory Mechanism national authorities, as well as a number of international financial institutions and training centres. Employees attended international courses, seminars, practical training, expert group meetings, and conferences. These focused on banking supervision, financial stability and macroprudential policy, statistics, financial markets, asset management and market operations, monetary policy and financial programming and economic research. Bank employees continued to take specialised courses, seminars, and working meetings on ESCB committees and working groups and European supervisory bodies.

The Bank carried out foreign language courses aimed at acquiring language knowledge and skills, maintaining the level achieved, mastering specific vocabulary and improving conversation and communication skills.

Activities related to health and safety at work focused on prevention of occupational hazards and accidents at work, employees awareness and training in order to perform safely their duties.

The BNB continued providing career development opportunities, encouraging students to acquire advanced academic knowledge and carry out research. In 2019 the Bank participated in four career student and young professional fora, presenting its career development programmes, traineeships, scholarships, guest researcher programmes, recruitment procedures, and employment conditions. Twenty-seven applicants enquired into the annual postgraduate scholarship programme: 11 for doctors' and 16 for masters' degrees. The Bank awarded two doctor's degree scholarships. Seven applicants were approved for the traineeships programme.

XV. BNB Internal Audit

BNB internal audit conforms to the International Standards for the Professional Practice of Internal Auditing, the Code of Ethics of Internal Auditors, ESCB Internal Auditor Committee Rules and Internal Auditor Rules approved by the BNB Governing Council.

In 2019 there were ten audits: seven under the annual Internal Audit Directorate Programme approved by the BNB Governing Council and three under the ESCB Internal Auditors Committee Programme.

Audits sought assurance of risk management, control and management of inherent risks to provide:

– effective attainment of objectives and tasks;
– reliability and completeness of financial and operational information;
– effective and efficient operations and programmes;
– safeguarding assets;
– legal, regulatory, internal rule, policy, procedure, and contractual observance.

Audits under Annual Internal Audit Directorate Programme

BNB Functions	Audits
Internal services	Procurement organisation and procedures in the BNB
Information and communication technologies	Foreign Exchange Reserve Management System: TREMA
Implementation of monetary policy and asset management	Auditing international reserves management by the Treasury Directorate to the Issue Department
Financial accounting and financial statements	BNB Consolidated Financial Statements as of 30 June 2019
Information and communication technologies	BNB Cash Reporting, Control and Management System
Supervision and financial stability	Comprehensive review of adequacy and efficiency of the activity carried out by the Specific Supervisory Activities Directorate.
Tracking performance	Follow up on recommendations from past audits under the annual BNB Internal Audit Directorate programme
Supervision and financial stability	Comprehensive review of adequacy and efficiency in conducting on-site inspections of credit institutions
Follow-up process	Follow up on recommendations from past audits under the annual Internal Audit directorate programme

Source: the BNB.

ESCB Internal Auditor Committee programme audits focused on operational risk management and information and communication technologies. Implementation of past audit recommendations was monitored.

XVI. BNB 2019 Budget Implementation

The Governing Council adopted the BNB budget by Resolution No 299 of 28 November 2018. This report on the Bank's budget comprises two sections pursuant to the Governing Council Internal Rules on Drafting, Implementing, and Reporting the BNB Budget: BNB Operating Expenditure and Investment Programme. The Bank adheres to environmental protection requirements.

Operating Expenditure

In 2019 the BNB spent BGN 99,060 thousand or 87.8 per cent of budget.

Currency circulation cost BGN 30,779 thousand or 88.3 per cent of budget and 31.1 per cent of Bank operating expenditure. New banknotes cost BGN 15,743 thousand and minting BGN 14,466 thousand, of which BGN 13,969 thousand on circulating coins. The BNB Governing Council 2019 Commemorative Coin Programme cost BGN 497 thousand. New banknote and coin design accounted for BGN 19 thousand. This included four 2020 commemorative coin design competitions. Expenditure on machines for servicing circulating banknotes and coins was BGN 79 thousand and on cash processing consumables BGN 92 thousand. Premise rentals for Bank issue and cash operations cost BGN 379 thousand.

Materials, services, and depreciation cost BGN 29,784 thousand: 79.4 per cent of budget and 30.2 per cent of operating expenditure.

Materials expenditure was BGN 1042 thousand: 78.3 per cent of approved annual budget and 1.1 per cent of all operating expenditure. Expenditure on inventories (BGN 272 thousand) and specialised fleet fuel and spares (BGN 254 thousand) occupied the largest share in this group. The Bank spent BGN 227 thousand on office consumables.

External services cost BGN 18,278 thousand or 82.4 per cent of budget and 18.5 per cent of Bank operating expenditure. Software maintenance subscriptions at BGN 4068 thousand, Bloomberg, Reuters, and other systems at BGN 1171 thousand, mandatory TARGET2 modules at BGN 1105 thousand, and BORICA AD subscriptions at BGN 535 thousand were notable in this group. Equipment maintenance subscriptions cost BGN 2334 thousand. Property and refuse collection levies cost BGN 1345 thousand. Mail, telephone and fax cost BGN 609 thousand. Electric bills were BGN 883 thousand and heating and water cost BGN 243 thousand. Property insurance expenses were BGN 108 thousand. Security and fire protection cost BGN 2860 thousand. Major building maintenance cost BGN 1104 thousand for the reporting period. Judicial protection and other legal services cost BGN 320 thousand and health and safety at work and special clothing BGN 206 thousand. Consultancy services cost BGN 801 thousand, including IT infrastructure and system analysis and banknote handler preventive maintenance.

Currency circulation expenditure was BGN 10,464 thousand or 74.6 per cent of annual budget and 10.6 per cent of operating expenditure.

Payroll, including social and healthcare, costs were BGN 32,332 thousand or 99.5 per cent of approved budget and 32.26 per cent of all operating expenditure. The BNB reported BGN 1411 thousand of current retirement obligations and unused paid leave under IAS 19 'Employee Benefits'.

Social expenditure was BGN 2174 thousand: 92.5 per cent of budget and 2.1 per cent of Bank's operating expenditure.

Miscellaneous administrative expenditure was BGN 1610 thousand: 62.3 per cent of budgeted funds and 1.6 per cent of total operating expenditure. Inland travel worth BGN 45 thousand involved mainly regional cash centre logistics and checks. Foreign travel unrelated to BNB participation in the ESCB and other EU bodies cost BGN 313 thousand. The annual BNB Staff Education and Professional Training Programme cost BGN 823 thousand. Employees took part in professional courses and seminars held by EU central banks and international financial institutions. They participated in distant learning, language, information technology, and other training at home.

The BNB spent BGN 2381 thousand: 78.7 per cent of budget and 2.4 per cent of operating expenditure on ESCB participation. European Banking Authority annual membership cost BGN 1450 thousand. BNB representatives sat on ESCB committees and working groups and other EU bodies, travel costing BGN 697 thousand and training BGN 34 thousand. The annual contribution of the Centralised Securities Database was BGN 173 thousand. The Bank hosted an extraordinary supervisory college at BGN 7 thousand.

The BNB Investment Programme

The Bank invested BGN 8052 thousand or 23.0 per cent of annual budget.

New construction, refurbishment and modernisation cost BGN 3398 thousand: 23.9 per cent of budget and 42.2 per cent of investment programme.

The design and construction of Plovdiv Cash Centre cost BGN 3398 thousand, including BGN 1829 thousand on construction works, BGN 1034 thousand on vault reinforcement, protective equipment and vault doors; BGN 516 thousand on joining the power network; BGN 14 thousand on consultancy to ensure compliance with main construction requirements; BGN 5 thousand on incidental author's supervision over investment design of general purpose sites.

Machine and equipment, vehicle, and other equipment investment cost BGN 120 thousand: 15.9 per cent of budget and 14.9 per cent of investment programme expenditure.

Cash operations equipment cost BGN 386 thousand. Upgrading of security systems in the BNB premises cost BGN 420 thousand. The BNB spent BGN 102 thousand on purchasing other equipment, including: BGN 37 thousand on office equipment and BGN 34 thousand on ventilation and air-conditioning systems and BGN 31 thousand on equipment for the BNB canteen. The BNB Transport Development Programme for 2018–2020 cost BGN 293 thousand on five new vehicles.

Information system and communication development cost BGN 3453 thousand: 26.0 per cent of budget and 42.8 per cent of investment programme.

Software cost BGN 2053 thousand, including BGN 1027 thousand for licence purchases. The Bank spent BGN 1026 thousand on updating and upgrading the existing systems and on developing and implementing an information system for collection and processing of reporting forms under the Law on Payment Services and Payment Systems.

Hardware cost BGN 1400 thousand, mainly for updating and expanding existing computer and communications equipment.

There was no investment spending on ESCB membership.

BNB budget implementation and fund takeup under both sections were continuously monitored.

The investment programme involved public tendering, contractor selection, and project implementation. Some procurement procedures ended, were suspended, or postponed. The investment programme was bigger than the previous year's one.

Unspent funds under this section were largely due to deferred design and construction at the Plovdiv Cash Centre. Due to appeal against the public procurement contractor award and terminastion of the procedure in 2019 the budgeted BGN 10,222 thousand for designing and construction of the Plovdiv Cash Centre, BGN 3137 thousand for security systems and BGN 640 thousand for vault equipment and internal transport were not disbursed as the equipment tender started after the contractor selection for construction of the Plovdiv Cash Centre and had not been completed until the end of 2019.

Some 51.9 per cent of the underspend amount was thus down to Plovdiv Cash Centre deferrals.

Concurrently, the Bank analysed and replanned budget funds for the two essential investment expenditure groups of information systems and new construction, refurbishment, and modernisation. The constructor selection contract for the Plovdiv Cash Centre was objectively signed at the end of the first half-year, and construction works started in the second half of the year, and therefore the implementation of some projects was to be postponed for 2020.

BNB Budget Implementation as of 31 December 2019

Indicator	Report 31 December 2019 (BGN thousand)	Budget 2019 (BGN thousand)	Implementation (per cent)
Section I. Operating expenditure	**99,060**	**112,849**	**87.8**
Currency circulation expenditure	30,779	34,858	88.3
Materials, services, and depreciation expenditure	29,784	37,534	79.4
Staff expenditure	32,332	32,496	99.5
Social expenditure	2,174	2,351	92.5
Other administrative expenditure	1,610	2,585	62.3
BNB expenditure on ESCB membership	2,381	3,025	78.7
Section II. Investment programme	**8,052**	**35,024**	**23.0**
Expenditure on construction, refurbishment, and modernisation	3,398	14,200	23.9
Machines, equipment, vehicles, and other equipment	1,201	7,541	15.9
Expenditure on BNB computerisation	3,453	13,279	26.0
Investment related to ESCB membership	0	4	0.0

Source: the BNB.

XVII. BNB Consolidated Financial Statements for the Year Ended 31 December 2019

Building a better working world

Ernst & Young Audit OOD
Polygraphia Office Center
47A, Tsarigradsko Shose Blvd., floor 4
1124 Sofia, Bulgaria

Tel: +359 2 81 77 100
Fax: +359 2 81 77 111
ey.com

Independent auditor's report

To the Governing Council of The Bulgarian National Bank

Report on the Audit of the Consolidated Financial Statements

Opinion

We have audited the accompanying consolidated financial statements of Bulgarian National Bank and its subsidiaries, which comprise the consolidated statement of financial position as at 31 December 2019, and the consolidated statement of comprehensive income, consolidated statement of changes in equity and consolidated statement of cash flows for the year then ended, and notes to the consolidated financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying consolidated financial statements give a true and fair view of the consolidated financial position of the Bulgarian National Bank as at 31 December 2019, and of its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union (EU).

Basis for Opinion

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Consolidated Financial Statements* section of our report. We are independent of the Bulgarian National Bank in accordance with the International Ethics Standards Board for Accountants' International Code of Ethics for Professional Accountants (including International Independence Standards)(IESBA Code) together with the ethical requirements of the Independent Financial Audit Act (IFAA) that are relevant to our audit of the consolidated financial statements in Bulgaria, and we have fulfilled our other ethical responsibilities in accordance with the requirements of the IFAA and the IESBA Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

A member firm of Ernst & Young Global Limited

Ernst & Young Audit OOD,
seat and address of management in Sofia
Polygraphia Office Center
47A, Tsarigradsko Shose Blvd., floor 4
UIC: 130972874, VAT # BG130972874
BGN IBAN: BG48 UNCR 7000 1520 6686 91
BIC: UNCRBGSF with Unicredit Bulbank AD

EY
Building a better working world

Information Other than the Consolidated Financial Statements and Auditor's Report Thereon

Management is responsible for the other information. The other information comprises the consolidated management report, prepared by management in accordance with Chapter Seven of the Accountancy Act, but does not include the consolidated financial statements and our auditor's report thereon.

Our opinion on the consolidated financial statements does not cover the other information and we do not express any form of assurance conclusion thereon, unless and to the extent explicitly specified in our report.

In connection with our audit of the consolidated financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the consolidated financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact.

We have nothing to report in this regard.

Responsibilities of Management for the Consolidated Financial Statements

Management is responsible for the preparation and presentation of the consolidated financial statements that give a true and fair view in accordance with IFRS as adopted by the EU and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the consolidated financial statements, management is responsible for assessing the Bulgarian National Bank's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting.

Auditor's Responsibilities for the Audit of the Consolidated Financial Statements

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial statements.

EY
Building a better working world

As part of an audit in accordance with ISAs, we exercise professional judgment and maintain professional skepticism throughout the audit. We also:

— Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
— Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Bulgarian National Bank's internal control.
— Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
— Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Bulgarian National Bank's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report.
— Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves true and fair presentation.
— Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Bulgarian National Bank to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the Bulgarian National Bank audit. We remain solely responsible for our audit opinion.

We communicate with management regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

Report on Other Legal and Regulatory Requirements

Additional Matters to be Reported under the Accountancy Act

In addition to our responsibilities and reporting in accordance with ISAs, described above in the *Information Other than the Consolidated Financial Statements and Auditor's Report Thereon* section, in relation to the consolidated management report, we have also performed the procedures added to those required under ISAs in accordance with the Guidelines on New and Expanded Auditor's Reports and Auditor's Communication of the professional organisation of certified public accountants and registered auditors in Bulgaria, i.e. the Institute of Certified Public Accountants (ICPA). These procedures refer to testing the existence, form and content of this other information to assist us in forming an opinion about whether the other information includes the disclosures and reporting provided for in Chapter Seven of the Accountancy Act applicable in Bulgaria.

Opinion in connection with Art. 37, paragraph 6 of the Accountancy Act

Based on the procedures performed, our opinion is that:

a) The information included in the consolidated management report referring to the financial year for which the consolidated financial statements have been prepared is consistent with those consolidated financial statements.
b) The consolidated management report has been prepared in accordance with the requirements of Chapter Seven of the Accountancy Act.

Audit Firm Ernst & Young Audit OOD:

Nikolay Garnev
Legal Representative and
Registered Auditor in charge of the audit

Milka Natcheva-Ivanova
Legal Representative and
Registered Auditor in charge of the audit

Sofia, Bulgaria

27 April 2020

Translation in English of the official Auditor's report issued in Bulgarian.

Statement of Responsibilities of the Governing Council of the Bulgarian National Bank

The Governing Council of the Bulgarian National Bank is responsible for preparing and approving financial statements to present the Bank's financial position and performance for the period.

The financial statements of the Bulgarian National Bank approved by the its Governing Council are prepared in accordance with the International Financial Reporting Standards adopted by the European Commission.

The Governing Council of the Bulgarian National Bank is responsible for maintaining proper accounting records to disclose with reasonable accuracy at any time the financial position of the Bulgarian National Bank. It has overall responsibility for taking such steps as are reasonably open to it to safeguard the assets of the Bulgarian National Bank and to prevent or detect fraud and other irregularities.

Dimitar Radev
Governor of the Bulgarian National Bank

Consolidated Statement of Comprehensive Income for the Year Ended 31 December 2019

(BGN'000)

	Note	2019	2018
Interest income	7	259,637	264,908
Interest expense	7	(74,527)	(71,167)
Net interest income		**185,110**	**193,741**
Fee and commission income		8,354	7,909
Fee and commission expense		(4,797)	(4,535)
Net fee and commission income		**3,557**	**3,374**
Net (losses)/gains from financial assets and liabilities reported at fair value in the profit or loss or measured at amortised cost, incl.	8	380,529	(181,812)
Provisions for expected credit loss		*(5,961)*	*(8,012)*
Other operating income	9	48,951	36,554
Total income from banking operations		**618,147**	**51,857**
Administrative expenses	10	(128,032)	(110,720)
Profit/(loss) for the period		**490,115**	**(58,863)**
Other comprehensive income			
Other comprehensive income that can be reclassified into profit or loss at a future point in time		-	-
Other comprehensive income that cannot be reclassified into profit or loss at a future point in time		*2,019*	*(605)*
Other comprehensive income, total		**2,019**	**(605)**
Total comprehensive income for the period		**492,134**	**(59,468)**
Profit attributable to:			
Equity holder of the Bank		489,787	(58,979)
Non-controlling interest		328	116
Profit/(loss) for the period		**490,115**	**(58,863)**
Total comprehensive income attributable to:			
Equity holder of the Bank		491,806	(59,584)
Non-controlling interest		328	116
Total comprehensive income for the period		**492,134**	**(59,468)**

The accompanying notes on pages 115 to 151 form an integral part of the Consolidated Financial Statements.

Consolidated Statement of Financial Position for the Year Ended 31 December 2019

(BGN'000)

	Note	2019	2018
ASSETS			
Cash and deposits in foreign currency	11	14,546,049	19,833,248
Gold, instruments in gold, and other precious metals	12	3,535,690	2,884,283
Financial assets at fair value through profit or loss	13	30,333,703	26,120,165
Financial assets at fair value through profit and loss in other comprehensive income	14	2,215,901	2,182,608
Tangible assets	15	150,771	154,065
Intangible assets	16	6,229	5,323
Other assets	17	92,847	84,871
Total assets		**50,881,190**	**51,264,563**
LIABILITIES			
Banknotes and coins in circulation	18	19,104,920	17,325,475
Liabilities to banks and other financial institutions	19	14,462,625	15,267,214
Liabilities to government institutions and other borrowings	20	8,853,715	10,719,427
Borrowings against Bulgaria's participation in international financial institutions	21	3,394,229	3,349,973
Other liabilities	22	265,627	294,432
Total liabilities		**46,081,116**	**46,956,521**
EQUITY			
Capital	23	20,000	20,000
Reserves	23	4,774,773	4,283,069
Non-controlling interest	24	5,301	4,973
Total equity		**4,800,074**	**4,308,042**
Total liabilities and equity		**50,881,190**	**51,264,563**

The accompanying notes on pages 115 to 151 form an integral part of the Consolidated Financial Statements.

Consolidated Statement of Cash Flows for the Year Ended 31 December 2019

(BGN'000)

	Note	2019	2018
OPERATING ACTIVITIES			
Net (loss)/profit		490,115	(58,863)
Adjustments			
Dividend income	9	(4,701)	(4,573)
Depreciation	15, 16	13,970	13,678
Profit/(loss) on disposal of tangible assets		(2)	(238)
(Profit)/loss on financial assets and liabilities arising from market movements		(623,043)	(48,617)
(Profit)/loss of associates		(4,063)	(2,869)
Other adjustments		6,014	3,282
Net cash flow from operating activities before changes in operating assets and liabilities		**(121,710)**	**(98,200)**
Change in operating assets			
(Increase) in gold, instruments in gold and other precious metals		(4,209)	(2,397)
(Increase)/decrease in financial assets at fair value through profit or loss		(4,226,730)	(3,789,624)
(Increase)/decrease in other assets		(2,249)	(3,517)
Change in operating liabilities			
Increase in banknotes and coins in circulation		1,779,445	1,622,278
Increase/(decrease) in due to banks and other financial institutions		(804,589)	1,374,718
Increase/(decrease) in due to government institutions and other liabilities		(1,865,712)	(274,190)
Increase/(decrease) in other liabilities		(28,805)	62,765
Net cash inflow/(net cash outflow) from operating activities		**(5,274,559)**	**(1,108,167)**
INVESTMENT ACTIVITIES			
Acquisition of tangible and intangible assets		(11,614)	(12,469)
Dividends received		4,701	4,573
Net cash inflow from/(net cash outflow) from investing activities		**(6,913)**	**(7,896)**
FINANCING ACTIVITIES			
Payments to the state budget		-	-
Net cash inflow from/(net cash outflow) used in financing activities		-	-
Net increase/(net decrease) in cash and cash equivalents		**(5,281,472)**	**(1,116,063)**
Cash and cash equivalents at beginning of period		**19,881,661**	**20,997,724**
Cash and cash equivalents at end of period	11, 17	**14,600,189**	**19,881,661**
Cash flows from interest and dividends			
Interest received		240,465	263,112
Interest paid		(73,415)	(63,224)

The accompanying notes on pages 115 to 151 form an integral part of the Consolidated Financial Statements.

Consolidated Statement of Changes in Equity for the Year Ended 31 December 2019

(BGN'000)

	Capital	Revaluation of non-monetary assets	Special and other reserves	Total capital and reserves	Non-controlling interest	Total equity
Balance as at 1 January 2018	**20,000**	**134,463**	**4,208,260**	**4,362,723**	**4,857**	**4,367,580**
Profit/(loss) for the period	-	-	(58,979)	(58,979)	116	**(58,863)**
Other comprehensive income:						
other income	-	819	(1,424)	(605)	-	**(605)**
Other comprehensive income, total	-	819	(1,424)	(605)	-	**(605)**
Total comprehensive income for the period	-	819	(60,403)	(59,584)	116	**(59,468)**
Contributions by and distributions to owners:						
contribution to the budget of the Republic of Bulgaria	-	-	-	-	-	-
dividend paid by subsidiaries to minority shareholders	-	-	(70)	(70)	-	**(70)**
Transactions with owners, total	-	-	(70)	(70)	-	**(70)**
Balance as at 31 December 2018	**20,000**	**135,282**	**4,147,787**	**4,303,069**	**4,973**	**4,308,042**
Balance as at 1 January 2019	**20,000**	**135,282**	**4,147,787**	**4,303,069**	**4,973**	**4,308,042**
Profit/(loss) for the period	-	-	489,787	489,787	328	**490,115**
Other comprehensive income:						
other income	-	(95)	2,114	2,019	-	**2,019**
Other comprehensive income, total	-	(95)	2,114	2,019	-	**2,019**
Total comprehensive income for the period	-	(95)	491,901	491,806	328	**492,134**
Contributions by and distributions to owners:						
contribution to the budget of the Republic of Bulgaria	-	-	-	-	-	-
dividend paid by subsidiaries to minority shareholders	-	-	(102)	(102)	-	**(102)**
Transactions with owners, total	-	-	(102)	(102)	-	**(102)**
Balance as at 31 December 2019	**20,000**	**135,187**	**4,639,586**	**4,794,773**	**5,301**	**4,800,074**

The accompanying notes on pages 115 to 151 form an integral part of the Consolidated Financial Statements.

Notes to the Consolidated Financial Statements

1. Statute and Principal Activities

The Bulgarian National Bank (the 'Bank') is 100 per cent owned by the Bulgarian state and is the central bank of the Republic of Bulgaria. The operation of the Bank is governed by the Law on the Bulgarian National Bank (LBNB), which has been effective since 10 June 1997.

Under this Law, the principal activities of the Bank may be summarised as:

- Maintaining price stability through ensuring national currency stability;
- Exclusive right to issue banknotes and coins;
- Regulation and supervision of other banks' activities in the country with a view to banking system stability maintenance;
- Establishment and operation of efficient payment systems;
- Regulation and supervision of the activity of payment system operators, payment institutions and electronic money institutions in the country;
- The Bank shall not extend credit and guarantees in any form whatsoever, including through purchase of debt instruments, to the Council of Ministers, municipalities, as well as to other government and municipal institutions, organisations and enterprises;
- The Bank may not provide credit to banks except in the case of liquidity risk threatening to affect the stability of the banking system;
- The Bank may not deal in Bulgarian government securities;
- The Bank may not issue Bulgarian levs in excess of the Bulgarian lev equivalent of the gross international reserves;
- The Bank acts as the fiscal agent and depository for the state.

The Governing Council of the BNB approved the Consolidated Financial Statements, set out on pages 105 to 151, on 27 April 2020.

2. Applicable Standards

These consolidated financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Commission.

3. Basis of Preparation

The consolidated financial statements are presented in Bulgarian lev rounded to the nearest thousand (BGN'000), which is the functional currency of the Bank. They are prepared on a historical cost basis, except for the following items, which are measured on an alternative basis as at each reporting date:

Items	Measurement basis
Derivative financial instruments	Fair value
Non-derivative financial instruments at fair value through profit or loss	Fair value
Tangible non-current assets	Revalued amount, which is the asset's fair value at the revaluation date less subsequent depreciation and impairment loss
Defined benefit liability	Present value of the defined benefit liability

Use of estimates and judgements

In preparing these consolidated financial statements, the Bank has made judgements, estimates and assumptions that affect the reported amounts of assets and liabilities, incomes and expenses, and the disclosure of contingent receivables and payables as at the financial statements date. These estimates, judgements and assumptions are based on data available as at the date of the consolidated financial statements; therefore actual future results may differ from these estimates.

The estimates and main assumptions are revised on an ongoing basis and are recognised prospectively.

Judgements

The Bank has estimated and classified cash in circulation as a financial liability (ref. note 18).

Assumptions and estimation uncertainties

Measurements of the present value of long-term obligations to retiring staff (following a defined benefit plan) use certified actuarial calculations based on mortality assumptions, rate of staff turnover, future level of salaries and discount factor, which assumptions may lead to adjustments in the next financial year; management however considers them to be reasonable and appropriate for the Bank (ref. note 10).

Bank assumptions and estimates are based on the existing parameters at the time of preparation of the financial statements. Existing circumstances and assumptions about future developments may change due to market changes or circumstances beyond the Bank's control. Such changes are reflected in assumptions when they occur.

Determination of expected credit losses on financial assets with a low credit risk

Instruments with a low credit risk are those for which the risk of default is low, the capacity of a counterparty to perform its contract obligations in a short term is stable, long-term negative changes in economic conditions are unlikely to change the capacity to repay obligations. For its short-term receivables from banks and debt instruments reported at amortised value or at fair value in 'other comprehensive income', the Bank accepts at the reporting date that the possibility of default is unlikely, so it determines for them 12-month credit losses. In case that the low credit risk criteria are no longer met in subsequent reporting periods, the Bank conducts an analysis of the changes in credit risk compared to the initial recognition to assess the need for an adjustment instrument on losses over the life of the instrument. Definition of instruments as such with a low credit risk requires judgement. In developing this judgement, the Bank uses all reasonable and supportable information accessible to it.

Determination of expected credit losses on deposit receivables

As reported in ref. note 6(b) Credit risk, the Bank has developed a Policy to Assessing Changes in Credit Quality and Determining Expected Credit Losses on Financial Instruments. The Bank classifies its risky assets into three risk phases depending on changes in credit risk after initial recognition of the asset and, accordingly, assesses the expected credit losses on the basis of 12-month probability of default if there is no changed credit quality (phase 1) and based on the probability of default for the expected lifetime of the instrument (phase 2 and phase 3) where there is a significant increase in credit risk. When determining how much the credit risk is increased compared to the initial recognition of the asset, the Bank uses all reasonable and supportable information that is available.

Loss on non-performance is a judgement for damages that the Bank would suffer in the event of default. It is based on the difference between the contractual cash flows and the cash flows that the Bank expects to receive. Significant judgement is needed in determining the time and amount of expected cash flows. The management uses judgements based on historical experience of losses on assets with an inherent credit risk and on objective circumstances of impairment similar to those in the portfolio in calculating future cash flows.

In determining the amount of expected credit losses, the Bank uses forward-looking information on expected future changes in certain economic conditions and indicators, as well as assumptions about how changes in these indicators would affect the probability of default.

The 'probability of default' parameter is key for calculating the amount of expected credit losses and reflects the probability that the counterparty will not fulfil its contractual obligations on a certain time horizon. The Bank has developed internal models to determine the probability of default on loans, based mainly on historical information for the period for which such is available. The assessment of the correlation between historical indicators of default and projected economic indicators is a significant approximate estimate. Bank's historical experience in credit losses and expectations of economic conditions may also not be representative of real losses in the future.

Fair value of financial instruments

When fair values of financial assets and liabilities in the statement of financial position cannot be obtained from active markets, they are determined by using various valuation methods, which include the use of mathematical models. Basic data on these models are derived from indicators that are observed in financial markets where possible. Otherwise, assumptions about establishing fair values are made. Assumptions take into account factors related to liquidity, volatility of longer-term derivative and discount rates, early payments and default assumptions related to asset-backed securities.

Some of the Bank's accounting policies and disclosures require fair value measurements of financial and non-financial assets and liabilities. For information on fair value measurements see note 6(e) and note 15.

New and amended standards and clarifications as of 1 January 2019

The following new clarifications and amendments to the existing standards issued by the International Accounting Standard Board (IASB) and accepted by the EU are in force throughout the reporting period:

IFRS 16 Leases

IFRS 16 Leases issued in January 2016, approved by the EU in October 2017, is effective since 1 January 2019, replaces IAS 17 Leases, IFRIC 4 Determining Whether an Arrangement Contains a Lease, SIC-15 Operating Leases - Incentives, SIC-27 Evaluating the Substance of Transactions Involving the Legal Form of a Lease. IFRS 16 sets out the principles for recognition, measurement, presentation and disclosure of leases and requires lessees to account all lease contracts based on uniform balance method, that is similar to accounting treatment of finance lease in accordance with IAS 17. According to the Standard, a lease contract is a contract that conveys the right to control the use of an identified asset for a period of time. The Standard provides two exemptions from recognition of lease contracts – leases of low value assets (*e.g.* laptop computers) and short-term leases (*e.g.* lease with a lease term of 12 months or less). At the initial date of the lease the lessee recognises a liability to make lease payments (*i.e.* the lease liability) and an asset representing the right to use the underlying asset during the lease term (*i.e.* the right-of-use asset). The lessees will be required to recognise separately interest expenses on the lease liability and depreciation expense on the right-of-use asset. Adoption of these amendments does not have a significant impact on the financial position or performance of the Bank.

IAS 28 Investments in Associates and Joint Ventures (Amendments): Long-term Interest in Associates and Joint Venture:

The amendments are effective for annual periods beginning on or after 1 January 2019 with earlier application permitted. The Amendments clarify that an entity applies IFRS 9 Financial Instruments to long-term interests in an associate or joint venture that, in substance, form part of the net investment in the associate or joint venture but to which the equity method is not applied. An entity applies IFRS 9 to such long-term interests before it applies IAS 28. In applying IFRS 9, the entity does not take account of any adjustments to the carrying amount of long-term interests that arise from applying IAS 28. These amendments issued on 12 October 2017, adopted by the EU on 8 February 2019, are published in the EU's Official Journal on 11 February 2019. These amendments have no material effect on the financial position or the performance of the Bank.

IFRIC 23 Uncertainty over Income Tax Treatments

The interpretation was adopted by the EU on 23 October 2018 and is effective for annual periods beginning on or after 1 January 2019 with earlier application permitted. This interpretation addresses the accounting for income taxes when tax treatments involve an uncertainty that affects the application of IAS 12. The interpretation provides guidance on considering uncertain tax treatments separately or together, examinations by tax authorities, the appropriate method to reflect uncertainty and accounting for changes in facts and circumstances. The interpretation has no effect on the financial position or performance of the Bank.

IFRS 9 Financial Instruments: Classification and Measurement (Amendments): prepayment features with negative compensation

The amendments were adopted by the EU on 22 March 2018 and are effective for annual periods beginning on or after 1 January 2019 with earlier application permitted. They propose an amendment to IFRS 9 for particular financial assets that would otherwise have contractual cash flows that are solely payments of principal and interest but do not meet the eligibility requirement as a result of prepayment features with negative compensation. Specifically, for a financial asset that contains a prepayment option that may result in the payment of a reasonable negative compensation amount, the amendments require the financial asset to be measured at amortised cost or at fair value through other comprehensive income, subject to the assessment of the business model in which it is held. It is not expected that these amendments would impact the financial position or performance of the Bank.

IAS 19 Employee Benefits (Amendments): plan amendments, curtailments or settlements.

The amendments are effective for annual periods beginning on or after 1 January 2019 with earlier application permitted. They require entities to use updated actuarial assumptions to determine current service cost and net interest for the remainder of the annual reporting period after a plan amendment, curtailment or settlement has occurred. The amendments also clarify how the accounting for a plan amendment, curtailment or settlement affects applying the asset ceiling requirements. The purpose of the amendments is to clarify that after amendment or reduction of the plan with defined income the entity should apply the updated assumptions about the net asset or liabilities revaluation under a defined income plan for the remainder of the reporting period. These amendments issued on 7 February 2018, have been endorsed on 13 March 2019 by the EU, and are published in the EU's Official Journal on 14 March 2019. The Bank has analysed the process of assessing the impact of these amendments on its financial position or performance and considers that the amendments have no significant effect on the Bank's performance.

Annual Improvements to IFRSs 2015–2018 Cycle

The annual improvements are effective for annual periods beginning on or after 1 January 2019, with earlier application permitted. A summary of amendments and related standards are provided below:

- IFRS 3 Business Combinations and IFRS 11 Joint Arrangements: clarification of the accounting for previously held interests in joint operations;
- AS 12 Income Taxes: clarification of income tax consequences of payments on instruments classified as equity;
- IAS 23 Borrowing Costs: clarification of borrowing costs eligible for capitalisation.

The Improvements to IFRSs 2015–2018 Cycle issued in December 2017, are approved by the EU on 14 March 2019 and published in the EU's Official Journal on 15 March 2019. These improvements have no material effect on the financial position or performance of the Bank.

Adoption of the new standards, improvements and amendments to the existing standards did not result in changes in the BNB accounting policy. The effect of IFRS 9 Financial instruments is disclosed in note 5(m).

4. Basis of Consolidation

Subsidiaries

Subsidiaries are the entities controlled by the Bank. Control over an entity exists when the Bank is exposed to or has rights over the variable return from its participation in that entity, and is able to influence that return through its powers. The financial statements of the subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases. The share in the net assets of the Bank's subsidiaries, which corresponds to the minority shareholders' proportionate share, is disclosed separately from Capital and Reserves under the Non-controlling Interest item.

The Bulgarian National Bank holds a majority of the BNB Printing Works AD and Bulgarian Mint EAD. The accounts prepared for the group contain the accounts of the parent company and subsidiaries. The BNB consolidated report eliminates all receivables and payables, incomes and expenses, as well as intragroup balances and transactions, including sales.

Associates

Associates are those entities in which the Bank has significant influence, but which are neither a subsidiary enterprise, nor a joint venture. Investments in associates are accounted for in the Bank's Consolidated Financial Statements using the equity method as an amount corresponding to the Bank's share in the associates' own funds as of the end of the reporting period. The Bank's share of associates' net results subsequent to acquisition is disclosed in 'profit or loss' as investment income/expenses and is added to/subtracted from the carrying value of the investment.

The BNB participation in other associated companies is accounted at the price of acquisition. The Bank consolidates on an annual basis the accounts of associated companies in which its share is 20 per cent or more than 20 per cent on the basis of the equity method.

Transactions eliminated on consolidation

All receivables and payables, incomes and expenses, as well as intragroup profits, resulting from inter-company transactions within the group, are eliminated except where these are immaterial.

5. Significant Accounting Policies

a) Income recognition

Interest income and expense are recognised on an accrual basis in accordance with the Bank's interest rate policy and in accordance with concluded agreements with international financial institutions and customers of the Bank. Interest income and expense are recognised in the statement of comprehensive income. Interest income and expense also include the amortisation of the discount and premium calculated on the basis of the effective interest rate.

Interest income on foreign securities held in the BNB portfolio includes interest rates on interest coupons of securities issues.

Interest income on deposits includes interest income on deposits in foreign currency and in gold.

Income from and expenses on fees and commissions from financial services of the Bank are recognised in the income statement of the Bank at the moment of provision of the respective service.

In accordance with IFRS 15, revenue from contracts with customer is recognised when the Bank has fulfilled its performance obligations by transferring the promised services to the customer. Revenue is recognised at an amount reflecting the consideration expected to be received in return. No changes in the valuation and recognition of fees and commissions have occurred since the entry of IFRS 15 Revenue from contracts with customers on 1 January 2018.

Other financial income/expenses include income and expenses from sales and changes in the fair value of financial assets and liabilities held for trading and assets available for sale.

Interest income and expense are recognised in the 'profit or loss' using the effective interest rate method. The effective interest rate is the rate which precisely discounts the estimated future cash payments and income over the term of the financial asset or liability to the carrying amount of the asset or liability. The effective interest rate is determined on the initial recognition of the financial asset or liability and does not change thereafter.

The calculation of the effective interest rate includes all commission, received or paid, as well as discounts and premiums that are an integral part of the effective interest rate. Transaction costs include incremental costs directly attributable to the acquisition, issue or derecognition of a financial asset or liability.

Interest income and expense presented in the statement of profit or loss include:

- interest on financial assets and financial liabilities measured at amortised cost calculated on an effective interest basis;
- interest on available-for-sale investment securities calculated on an effective interest basis.

Dividend income is recognised when the Bank establishes the right to receive a dividend.

Fee revenue is deferred and recognised in each of the separate financial periods.

Profits and losses arising from changes in the fair value of financial instruments reported at fair value through profit or loss are recognised in the statement of comprehensive income.

Revenue from a grant related to depreciable assets is recognised as income for future periods upon receipt of the grant and subsequently recognised in the statement of comprehensive income over the relevant periods, systematically over the useful life of assets and proportionate to the depreciation charge for the same assets. Expenses related to depreciable assets incurred during the current period are deferred over the useful life of the assets.

Revenue from a grant related to non-depreciable assets is recognised as income for future periods upon receipt of the grant and is then recognised in the statement of comprehensive income for the periods in which the relevant expenses are accounted for

Foreign currency differences arising from available-for-sale investments are recognised in profit or loss.

Net gains/losses from financial assets and liabilities at fair value through profit or loss include net gains from operations in securities, net gains from operations in foreign currency, net revaluation gains on securities, net gains from gold revaluation, net gains from revaluation of futures, and net gains from revaluation of assets and liabilities denominated in foreign currencies.

b) Recognition of assets and liabilities

Bank's assets and liabilities are stated in their initial cost or fair value. Subsequent revaluations are carried out by evaluating different types of assets and liabilities in different periods in order to determine their fair value. Adjustments to the accounting records, as well as the relevant recognition records in the revaluation reserve are reported in accordance with International Financial Reporting Standards. Where it is not possible to determine the fair value, the historical cost of acquisition less the losses resulting from the impairment of the asset is taken.

International Financial Reporting Standards do not require presentation of assets in a specified balance sheet format and may be designated as underlying assets (tangible fixed assets, intangible assets, inventories, investment property, borrowing costs for asset acquisition, impairment of assets) and assets that are classified as financial instruments.

c) Financial instruments

The Bank may recognise a financial asset or liability in its balance sheet if, and only if it becomes a party to the contractual terms of the financial instruments used. The Bank derecognises a financial asset from its balance sheet:

- when it loses control over the contractual rights that constitute the financial asset;
- when the obligation stated in the contract is extinguished, cancelled or expired.

i) Classification

For the purposes of subsequent measuring of financial assets the BNB uses the following business models:

- financial assets held to collect contractual cash flows;
- financial assets held to collect contractual cash flows and for sale.

The business model of the financial assets held to collect the contractual cash flows includes all current accounts of the Bank with foreign correspondents, and the cash flows under the model used for these assets represent only principal and interest payments. These financial assets are measured at amortised cost.

The business model financial assets held to collect contractual cash flows and for sale includes: deposits, securities and investment. The assets in this group are measured as follows:

- deposits: at amortised cost;
- securities: at fair value through profit and loss;
- investment: at fair value in other comprehensive income.

ii) Recognition

The Bank recognises trading financial assets and investments, the Bank's loans and receivables, and financial liabilities at amortised cost from the settlement date. All other financial assets and financial liabilities are accounted when the Bank becomes a party to the financial instruments contracts.

Financial assets and liabilities are recognised in off-balance-sheet accounts from the trade date to the date of their settlement and are recorded in the BNB statement of financial position at the settlement date (value date). The initial recognition is at acquisition cost, i.e. the fair price paid on acquisition. Transaction costs are included in the acquisition cost of all assets and liabilities. From that moment on, any changes in their fair value are recognised by the Bank as income or expense.

iii) Amortised cost measurement

Assets measured at amortised cost are initially recognised at acquisition cost, then measured at amortised cost, which is the initial measurement of the asset adjusted for the amortised premium or discount using the effective interest rate method. Premium and discount is amortised for each individual item and is recognised in the Bank's income statement. Interests are calculated or recognised on a daily basis in the Bank's statement of comprehensive income.

iv) Fair value measurement and disclosure principles

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants in the principal market or, if no such market is available, then in the most advantageous and accessible market on the measurement date. The fair value of a liability reflects the effect of non-performance risk.

Whenever possible, the Bank measures the fair value of an instrument using quoted prices in an active market of that instrument. A market is considered as active if transactions for the asset or liability take place with sufficient frequency and volume to provide pricing information on an ongoing basis.

If no quoted price in an active market is available, the Bank uses the most relevant observable inputs and makes minimum use of unobservable data. The aim of using a valuation technique is to estimate the price that would be obtained in an orderly transaction between market participants. The chosen valuation technique makes maximum use of market inputs, relies as little as possible on estimates specific to the Bank, incorporates all factors that market participants would consider in determining a price, and is consistent with accepted economic methodologies for pricing financial instruments.

Inputs to valuation techniques reasonably represent market expectations and measures of the risk-return factors inherent in the financial instrument. The Bank calibrates valuation techniques and tests them for validity using prices from observable current market transactions in the same instrument or based on other available observable market data.

The best indicator of the fair value of a financial instrument at initial recognition is the transaction price, i.e. the fair value of the consideration given or received. When the Bank finds a difference between the fair value at initial recognition and the transaction price, and the fair value is neither evidenced by a quoted price in an active market for identical assets or liabilities, nor based on a valuation technique based only on data from observable markets, then the financial instrument is initially recognised at fair value adjusted with the difference between the fair value at initial recognition and the transaction price. This difference is subsequently recognised in profit or loss on an appropriate basis over the life maturity of the instrument but not later than when the valuation is supported wholly by observable market data or the transaction is closed out.

The Bank recognises assets and long positions at a bid price and liabilities and short positions at an ask price when assets or liabilities measured at fair value have a bid and an ask price.

Where the Bank has positions in a group of financial assets and financial liabilities, it is exposed to market risk and credit risk. On the basis of the net exposure to either market or credit risks, the Bank measures them at fair value on the basis of a price that would be received to sell a net long position or paid to transfer a net short position for a particular risk exposure. These portfolio-level adjustments are allocated to the individual assets and liabilities on the basis of the relative risk adjustment of each of the individual instruments in the portfolio.

Where the Bank has positions with offsetting risks, mid-market prices are used to measure them and a bid or ask price adjustment is applied only to the net open position as appropriate. Fair values reflect the credit risk of the instrument and include adjustments to take account of the credit risk of the Bank entity and the counterparty where appropriate. Fair value estimates obtained from models are adjusted for any other factors, such as liquidity risk or model uncertainties, to the extent that the Bank believes a third-party market participant would take them into account in pricing a transaction.

The Bank recognises transfers between levels of the fair value hierarchy as of the end of the reporting period during which the change has occurred.

v) Derecognition

The Bank derecognises a financial asset when the contractual rights to the cash flows from the financial asset expire, or when it transfers the rights to the receipt of the contractual cash flows from the financial asset in the transaction in which substantially all the risks and rewards of ownership of the financial asset are transferred. Any holding in transferred financial assets, which has been originated or kept by the Bank, is recognised as a separate asset or liability.

The Bank derecognises a financial liability when its contractual obligations are discharged or cancelled or expired. The Bank enters into transactions whereby it transfers assets recognised in its statement of financial position, but retains either all or the substantial risks and rewards of the transferred assets or a part of them. If part of or all of the substantial risks and rewards are retained, then the transferred assets are not derecognised from the statement of financial position. Transfers of assets with retention of a part of or all substantial risks and rewards are, for instance, securities lending or repurchase agreements.

In transactions where the Bank neither retains nor transfers all substantial risks and rewards of ownership of a financial asset, it derecognises the asset if it does not retain the control of that asset. The rights and obligations retained in the transfer are recognised separately as assets and as liabilities respectively. In transactions where control of the asset is retained, the Bank continues to recognise the asset to the extent of its continuing involvement, determined by the extent to which the Bank is exposed to changes in the value of the transferred asset.

In certain transactions the Bank retains the obligation to service the transferred financial asset for a fee. The transferred asset is derecognised if it meets the derecognition criteria. An asset or liability is recognised for the servicing contract, depending on whether the servicing fee is more than adequate (asset) or is less than adequate (liability) for performing the servicing.

vi) Offsetting

Financial assets and liabilities are offset and the net amount is presented in the statement of financial position when the Bank has a legal right to offset the recognised amounts and intends to settle the asset or the liability on a net basis. Accounting for assets, net of adjustments is not considered to be offsetting.

Income and expenses are presented on a net basis only when permitted by the accounting standards or for gains and losses arising from a group of similar transactions such as in the Bank's trading operations.

vii) Impairment of assets

Approach applied until 1 January 2018

Financial assets which are not carried at fair value through profit or loss are reviewed at each reporting date to determine whether there is evidence of impairment. Financial assets are impaired if there is objective evidence of impairment as a result of a loss event that occurred after the initial recognition of the asset and that the loss event had an impact on the future cash flows which can be reliably estimated.

Objective evidence of impairment loss from financial assets, including equity instruments, is a default or a borrower's inability to repay his obligations, restructuring of loans under unfavourable financial conditions for the Bank, indications that a borrower or the issuer of a financial instrument would go out of business, the disappearance of an active security market, or other public information. Furthermore, in case of a continuous or significant fall in the market value of an investment in equity instruments there is objective evidence of impairment of these equity instruments.

The Bank considers the need of impairment of loans or investments held to maturity at both individual and group level. All individually significant loans and investments held to maturity are evaluated for specific impairment. All individually significant loans and investments held to maturity on which no specific impairment losses have been charged are evaluated on a portfolio basis. Loans and held-to-maturity investments that are not individually significant are collectively assessed for impairment by grouping together loans and held-to-maturity investment securities with similar risk characteristics.

Approach applied after 1 January 2018

In assessing collective impairment the Bank uses statistical modelling of historical trends of the probability of default, timing of recoveries and the amount of loss incurred, adjusted for management's judgement as to whether current economic and credit conditions are such that the actual losses are likely to be greater or less than suggested by historical modelling. Default rates, loss rates and the expected timing of future recoveries are regularly benchmarked against actual outcomes to ensure that they remain appropriate.

Impairment losses from assets carried at amortised cost are measured as the difference between the carrying amount of the financial asset and the present value of the estimated future cash flows discounted by the original effective interest rate of the asset. Impairment losses are recognised in profit or loss and reflected in an allowance account against loans and receivables. Interest on the impaired asset continues to be recognised through unwinding of the discount, but on the amortised cost. When a subsequent event reduces impairment loss, the reduction in the impairment loss is reversed through profit or loss.

Impairment losses on held-for-sale investment securities are recognised by transferring the cumulative loss that has been recognised in equity to profit or loss. The cumulative loss that is transferred from equity and recognised in profit or losses is the difference between the acquisition cost, net of any principal repayment and amortisation, and the current fair value, less any impairment loss previously recognised in profit or loss. If in a subsequent period the fair value of an impaired debt security available for sale increases and the increase can be objectively linked to an event that occurred after the impairment loss had been recognised in profit or losses, then the impairment loss is reversed and the reversed amount is recognised in profit or loss.

viii) Financial assets and liabilities held to collect contractual cash flows and for sale

Financial assets and liabilities held to collect contractual cash flows and for sale are recognised initially at fair value in the statement of financial position with transaction costs recognised in profit or loss. All changes in the fair value are recognised as net income from trading operations in profit or loss.

ix) Financial assets held within a business model whose objective is to hold financial assets to collect contractual cash flows

Financial assets held within a business model whose objective is to hold financial assets to collect contractual cash flows are initially recognised at acquisition cost and subsequently are carried at amortised cost which is the initial asset valuation adjusted for amortised premium or discount using the effective interest rate method. Premium or discount is amortised for each individual item and is recognised in the Bank's statement of comprehensive income. Interests is calculated or recognised on a daily basis in the Bank's statement of comprehensive income.

x) Investments held for sale

Available-for-sale investments are non-derivative assets that cannot be classified in any other category of financial assets. All other available-for-sale investments are carried at fair value. Differences in the fair value are recognised directly in equity until the investment is sold or fully impaired.

d) Gold and other precious metals

The BNB as a central bank maintains particular volumes of gold as part of Bulgaria's international reserves. In compliance with the requirements of the Law on the BNB, the Bank may take any necessary action in connection with the acquisition, possession and sale of gross international reserves, including monetary gold. Consequently, monetary gold as part of international reserves may be immediately used by the BNB without further constraints which determines it as a monetary asset. Pursuant to the requirements of the 'General Provisions for Defining the Valuation Basis in the Financial Statements' to the IFRS, as well as in the absence of specific IFRS to determine the treatment of such a transaction, the Bank defines the recognition and valuation of the monetary gold as an asset reported at fair value through profit or loss as the most reliable and appropriate base for a subsequent valuation of this financial asset. Gold and other precious metals are measured at market value based on the London Bullion Market fixing in euro at the reporting date.

Monetary gold

Gold in standard form (monetary gold) is initially recognised at acquisition cost. Monetary gold and other gold instruments are valued daily at the latest market value posted on the wholesale gold market in London, the UK. Unrealised gains and losses on the revaluation of the monetary gold and other gold instruments of the Bank are recognised in the income statement.

e) Equity investments

For the purposes of measuring the equity investments subsequent to initial recognition, they are classified as held-for-trading financial assets and measured at fair value.

Details of investments held by the Bank are set out in note 14.

f) Property, plant, equipment and intangible assets

The policy pursued by the Bank is to present land, buildings and other groups of fixed tangible assets in the statements of financial position at revalued amount as per the alternative approach allowed in IAS 16 'Property, Plant and Equipment'.

The Bank recognises an intangible asset if it meets the criteria for recognition under International Financial Reporting Standards. Intangible assets are presented in the statement of financial position at acquisition cost, including paid duties, non-recoverable taxes, as well as direct costs of preparing the asset for its intended use, less accumulated amortisation and impairment losses.

Land and buildings are measured at fair value which is regularly assessed by professionally qualified valuers. The revaluation of property is done asset by asset, and any accumulated depreciation at the revaluation date is derecognised against the gross carrying amount of the asset, and the net amount restated to the revalued amount of the asset. When the value of assets increases as a result of revaluation, the increase is reflected directly in other comprehensive income. When the value of assets decreases as a result of revaluation, the decrease is recognised by decreasing the revaluation reserve in equity, and in case of a shortage, the difference is recognised as an expense in profit or loss.

i) Subsequent costs

The separately accounted for costs incurred to replace a component of an item of property, plant and equipment are capitalised. All other subsequent costs are capitalised only when future economic benefits embodied in the item of property, plant and equipment will flow to the Bank. All other costs are recognised in 'profit or loss' as incurred.

ii) Depreciation and amortisation

The depreciation/amortisation shall be carried out from the day of initial asset recognition according to the straight-line method for the expected useful life. Land is not depreciated. The Governing Council of the BNB approves the annual depreciation rates presented below:

(per cent)

Buildings	2 – 4
Plant & equipment	3 – 15
Computers	30 – 33.3
Fixtures and fittings	15 – 20
Motor vehicles	8 – 25
Intangible fixed assets	20 – 25

Expenditures incurred for the acquisition of property, plant, equipment and intangible assets are not depreciated until they are brought into use.

iii) Recoverable amount of assets

The recoverable amount of the Bank's fixed assets is the higher of the net selling price and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using the Bank's incremental borrowing rate that reflects current market assessments of the time value of money and the risks specific to the asset. For an asset that does not generate largely independent cash inflows, the recoverable amount is determined for the cash-generating unit to which the asset belongs.

iv) Reversals of impairment

Impairment losses of tangible fixed assets are reversed when a change occurs in the estimates used to determine the recoverable amount and may be reversed only up to that carrying amount of the asset before recognising impairment losses.

v) Derecognition and sales

An item of property, plant or equipment is derecognised from the Bank's balance sheet at the time of its sale or when the asset is definitively disposed of and no other economic benefits are expected. Gains or losses arising from derecognition or disposal of tangible fixed assets are determined as the difference between the sale proceeds and the carrying amount of the asset and are recognised as income or expense in the statement of comprehensive income. Tangible fixed assets withdrawn from active use and held for sale are reported at their carrying amount at the date when the asset is retired from active use.

vi) Inventories

Inventories are assets held by the Bank that will be used in the core business, in the process of providing services. Inventories are reported in the Bank's balance sheet at a historical price that includes the sum of all purchase costs and costs associated with their delivery to their current location and condition. Purchase costs include a purchase price at invoice, import duties, non-refundable taxes and excise duties. Delivery costs include shipping and handling costs. Write-off of inventories is carried out using the weighted average method.

In the event of a fall in market prices, in the case of physical damage to inventories, when the products are aged, the value of inventories is adjusted, *i.e.* they are valued at the lower net realisable value.

In the end of the reporting period, the net realisable value of inventories is valued, and if it is lower than the supply, the difference is related to current expenses. For each subsequent reporting period, a new estimate of net realisable value is made. If during the relevant reporting period, there are conditions for an increase in the value of the inventory, its recovery is up to the amount that it had before the decrease. This reversal of the book value is accounted for as an increase in inventories and other current income.

g) Foreign exchange

Gains and losses arising in foreign currencies are translated to BGN at the official rates of exchange on the transaction date. Monetary assets and liabilities denominated in foreign currencies at the reporting date are translated at the official exchange rate of the Bank on that day. Foreign currency gains and losses resulting from the revaluation of monetary assets and liabilities are recognised in profit or loss. Non-monetary assets and liabilities denominated in foreign currency are retranslated to the functional currency at the exchange rate at the date that the fair value was determined.

Outstanding forward contracts in foreign currency are marked to market. Gains and losses on revaluation of outstanding forward contacts are recognised in profit or loss.

The exchange rates of the major foreign currencies as of 31 December 2019 and 31 December 2018 are as follows:

Currency	31 December 2019	31 December 2018
US dollar	1: BGN 1.74099	1: BGN 1.70815
Euro	1: BGN 1.95583	1: BGN 1.95583
Special drawing rights	1: BGN 2.40749	1: BGN 2.37568
Gold	1 troy ounce: BGN 2656.13	1 troy ounce: BGN 2190.59

h) Taxation

The Bank is not subject to income tax from its core activities. Income tax from subsidiaries for the period comprises current tax and deferred tax. Current tax comprises tax payable calculated on the basis of the expected taxable income for the period, using the effective tax rate or the current one at the reporting date. Deferred tax is derived using the balance sheet liability method on all temporary differences between the amounts used for taxation purposes and the carrying amounts of assets and liabilities.

The deferred tax is calculated using tax rates which are expected to be applied for the period of asset realisation or liability settlement. The effect on the deferred tax from changes in the tax rates is recorded in the statement of comprehensive income up to the amount already charged or reported directly as other comprehensive income.

A deferred tax asset is recognised to the extent that is probable that future taxable profits will be available against which the unused tax losses or tax credit can be utilised. The deferred tax assets are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

i) Provisions

Provisions related to ongoing legal cases or other obligations are reported when the Bank has assumed a legal or constructive obligation as a result of some past events, the repayment of which is likely to be associated with lost economic benefits. Provisions are charged only when the Bank is able to reliably determine the size of future outgoing cash flows.

j) Profit distribution policy of the Bank

The Bank's policy of distribution of profit from banking operations is defined in the Law on the BNB. Internal rules for preparation of financial statements and accounting policies were adopted upon a decision of the Governing Council effective from 1 January 2007, which are in compliance with Article 36, paragraphs 1 and 2 of the Law on the BNB. According to these rules, the Bank allocates to special reserves unrealised net gains and losses arising from revaluation of assets and liabilities denominated in foreign currency or gold. According to the requirements of Article 8, paragraph 2 of the Law on the BNB, the Bank sets aside 25 per cent of the excess of its annual revenue over its annual expenditure into a Reserve Fund. Under Article 8, paragraph 3 of the Law on the BNB, after the allocation to the Reserve Fund, the Bank may allocate reserves to cover market risk losses and other reserves upon a decision of the Governing Council. Subsequent to the allocation of reserves as required by the Law on the BNB, the Bank stipulates the remainder to be paid into the State Budget. The distribution of excess of revenue over expenditure is set out in note 23.

k) Cash and cash equivalents

For the purpose of the statement of cash flows, cash and cash equivalents consist of cash in hand, current accounts and time deposits with maturities of less than three months.

l) Employee benefits

The Bank has the obligation to pay certain amounts to each employee who retires in accordance with the requirements of Article 222, § 3 of the Labour Code in Bulgaria. According to these Labour Code requirements, on termination of the employment contract of an employee who has become entitled to retirement, the employer is obliged to pay him/her compensation amounting to twice his/her gross monthly salary. If, at the date of retirement, the employee has been employed by the Bank for ten or more years, the amount of the compensation is six gross monthly salaries. As at the date of the statement of financial position, the Bank's Management estimates the approximate amount of the potential expenditures for all employees based on an actuarial report using the projected unit credit method. The estimated amount of the obligation and the main assumptions, on the base of which the estimation of the obligation has been made, is disclosed to the Financial Statements in note 10.

Termination benefits

Termination benefits are recognised as an expense when the Bank is committed demonstrably, without realistic possibility of rejection, to a formal detailed plan to either terminate employment before the normal retirement date, or to provide termination benefits as a result of an offer made to encourage voluntary redundancy. Termination benefits for voluntary redundancies are recognised as an expense if the Bank has made an offer of voluntary redundancy. It is probable that the offer will be accepted and the number of acceptances can be estimated reliably. If benefits are payable more than 12 months after the reporting period, then they are discounted to their present value.

Short-term employee benefits

Short-term employee benefit obligations are measured on an undiscounted basis and are expensed as the related service is provided. A liability is recognised for the amount expected to be paid under a short-term cash bonus or profit-sharing plans if the Bank has a present constructive obligation to pay this amount as a result of past services provided by the employee, and the obligation can be estimated reliably. The Bank recognises as a liability the undiscounted amount of the estimated costs related to annual leave expected to be paid in exchange for the employee's service for the period completed.

m) Effect of applying IFRS 9 Financial Instruments

IFRS 9 introduces a new approach to the classification of financial assets based on contractual cash flow characteristics and the Bank's business model for managing them. All recognised financial assets within the IFRS 9 range must be subsequently carried at amortised cost or fair value, depending on the business model and the characteristics of their cash flows. Initially, the Bank recognised financial assets and liabilities at the acquisition price, which is the fair price paid at acquisition. The BNB uses the following business models for further evaluation of financial assets:

- financial assets held to collect contractual cash flows;
- financial assets held for the purposes of collecting contractual cash flows and for sale.

The business model is evaluated on the date of initial application of the standard. The evaluation whether cash flows of debt instruments consist only of the principal and interest is based on the facts and circumstances of the initial recognition of assets.

Accounting for financial liabilities remains substantially unchanged compared with that in IAS 39, except for the treatment of differences arising from changes in own credit risk for financial instruments designated to account for fair value in profit or loss. Under IFRS 9, these differences are recognised in other comprehensive income without subsequent reclassification in the statement of comprehensive income. As of the date of present statements, the Bank does not account financial liabilities in this category.

Regarding the Bulgarian National Bank, adoption of IFRS 9 requirements with respect to classification and subsequent reporting of its financial instruments did not result in significant changes and therefore had no material impact on the statement of financial position and/or capital.

Financial assets measured at fair value through profit or loss until the implementation of IFRS 9 up to 31 December 2017 continue to be reported in a similar manner. Debt instruments presented as available-for-sale under IAS 39 retain their fair value through other comprehensive income as the business model underlying them aims to provide ongoing liquidity by holding them to collect contractual cash flows and for sale, where necessary.

For equity instruments reported as available-for-sale, the Bank chose the fair value accounting option in other comprehensive income at the initial application of the standard as it intends to hold them in the near future. Equity instruments reported at acquisition cost under IAS 39 were measured at fair value upon initial application of IFRS 9.

Expected credit losses on financial instruments as a result of the application of IFRS 9 are calculated based on the methodology adopted by the BNB Governing Council. The Bank reports a credit loss on financial assets reported in the amortised cost category which as at 31 December 2019 amounted to BGN 5,961 thousand (31 December 2018 – BGN 8012 thousand). Information on expected credit losses is provided in notes 8 and 23.

n) Effect of applying IFRS 16 Leases

IFRS 16 Leases is effective from 1 January 2019. The Bank applies IFRS 16 for the first time. Adoption of IFRS 16 requirements had no material impact on the Bank's financial position or performance.

IFRS 16 Leases

IFRS 16 Leases was issued on January 2016 and replaces IAS 17 Leases, IFRIC 4 Determining Whether an Arrangement Contains a Lease, SIC-15 Operating Leases – Incentives and SIC-27 Evaluating the Substance of Transactions Involving the Legal Form of a Lease. IFRS 16 sets out the principles for the recognition, measurement, presentation and disclosure of leases and requires lessees to report all leases under the same balance sheet model similar to accounting for financial leasing according to IAS 17.

The Bank has adopted IFRS 16 under the modified retrospective method of application with an effective date of 1 January 2019. According to this method, the standard is applied retrospectively, since the cumulative effect of its initial application is recognised at the date of initial application.

The Bank applies the short-term lease recognition exemption to its short-term leases of plant and equipment (leases that have a lease term up to 12 months from the start date and do not contain a purchase option). It also applies the lease of low-value assets recognition exemption to leases of office equipment, which is considered to be of low value. Lease payments for short-term leases and leases of low-value assets are recognised as expenses on a linear basis over the term of the lease.

o) New standards and clarifications issued but not yet effective and not early adopted

Already published standards which are not yet in effect or have not been previously applied by the Bank at the date of these financial statements are briefly presented below. It is disclosed how reasonably they are expected to impact disclosures, the financial position or performance when the Bank adopts these standards for the first time. It is expected to happen when they come into force.

IFRS 17: Insurance Contracts

The standard is effective for annual periods beginning on or after 1 January 2021 with earlier application permitted if both IFRS 15 Revenue from Contracts with Customers and IFRS 9 Financial Instruments have also been applied by the Bank. IFRS 17 Insurance Contracts establishes principles for the recognition, measurement, presentation and disclosure of insurance contracts issued. It also requires similar principles to be applied to reinsurance contracts held and investment contracts with discretionary participation features issued. The objective is to ensure that entities provide relevant information in a way that faithfully represents those contracts. This information gives a basis for users of financial statements to assess the effect that contracts within the scope of IFRS 17 have on the financial position, financial performance and cash flows of the Bank. The standard has not been yet endorsed by the EU. It is not applicable to the Bank.

IFRS 3 Business Combinations (Amendments): Definition of a Business

The amendments are effective for annual periods beginning on or after 1 January 2020 with earlier application permitted. The amendments clarify the minimum requirements for a business and narrow the definition of a business. The amendments also remove the assessment of whether market participants are capable of replacing any missing elements, add guidance to help entities assess whether an acquired process is substantive and introduce an optional fair value concentration test. These amendments have not yet been endorsed by the EU. It is not expected that these amendments would have a material impact on the financial position or performance of the Bank.

Amendments to IAS 1 Presentation of Financial Statements and IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors: Definition of 'Material'

The amendments were adopted by the EU on 29 November 2019 and entered into force for annual periods beginning on or after 1 January 2020 with earlier application permitted. The amendments clarify the definition of material and how it should be applied by including in the definition guidance that until now has featured elsewhere in IFRS Standards. The amendments also specify that materiality will depend on the nature or magnitude of information. The Bank will analyse and assess the impact of these amendments on its financial position or performance.

The Conceptual Framework for Financial Reporting

The International Accounting Standards Board (IASB) issued the revised Conceptual Framework for Financial Reporting on 29 March 2018, which is effective for annual periods beginning on or after 1 January 2020. The Conceptual Framework sets out a comprehensive set of concepts for financial reporting, standard setting, guidance for preparers in developing consistent accounting policies and assistance to others in their efforts to understand and interpret the standards. The main amendments introduced in the revised Conceptual Framework for financial reporting are related to measurement, including factors, which should be considered when choosing measurement basis, and to presentation and disclosure conception, including income and expenses which should be classified in other comprehensive income. The Conceptual Framework also provides of updated definitions of asset and liability and criteria for their recognition in the financial statements. The Conceptual Framework for financial reporting was adopted by the EU on 29 November 2019 and published in the Official Journal of the EU on 6 December 2019. The Bank will analyse and assess the impact of these amendments on its financial position or performance.

Interest Rate Benchmark Reform: Amendments to IFRS 9, IAS 39 and IFRS 7

The amendments are effective for annual reporting periods beginning on or after 1 January 2020 and retrospective application is required. Earlier application is permitted. In September 2019, the IASB issued Amendments to IFRS 9, IAS 39 and IFRS 7, thus completing phase 1 to address the effects of the interest rate benchmark reform on financial reporting. Phase 2 will focus on issues which might arise when the interest rate would be replaced by an alternative risk-free reference rate. These amendments solve problems that arise in the course of replacing the existing interest rate benchmark with an alternative interest rate. Effects on specific hedge accounting requirements in IFRS 9 Financial Instruments and IAS 39 Financial Instruments: Recognition and Measurement which require future-oriented analysis are taken into account. The amendments provide temporary exceptions from applying specific hedge accounting requirements directly affected by interest rate benchmark reform. The amendments allow hedge accounting to continue in the uncertainty period until the replacement of existing benchmarks with alternative risk-free rates. Changes have been made in IFRS 7 Financial Instruments: Disclosure according to which additional information about the uncertainties arising from the reform is required. The amendments have not yet been endorsed by the EU. The Bank will analyse and assess the impact of the amendments on its financial position or performance.

6. Financial Risk Management Policy Disclosure

a) Introduction and overview

Introduction to the financial risk management policy

The Bank is exposed to the following types of risk in relation to the financial instruments operations:

- credit risk;
- liquidity risk;
- market risk;
- operational risk.

This note provides information on the Bank's goals, exposures to each of the above types of risk and the policies and processes for risk measurement and management.

General provisions of risk management

In the process of management of the gross international reserves, the Bank aims to achieve high security and liquidity of the assets, first, and then to maximise returns in the situation of the current global financial markets. Its investment strategy depends mainly on the specific functions of the Bank operating under a currency board arrangement and in full compliance with the requirements of the Law on the BNB.

The major portion of BNB's international reserves is invested in assets of comparatively low credit risk, such as discount and coupon securities issued by highly rated issuers (governments, government agencies or supranational financial institutions), and short-term foreign currency or gold deposits placed with first-rate foreign banks. The remaining portion is held in SDRs on BNB accounts with the IMF and in monetary gold kept in the Bank's vaults.

A specialised international reserves risk management unit is responsible for preparing and submitting for approval a draft of strategic asset structuring, setting up benchmark for the international reserves and investment management limits. On a quarterly basis, an overall review is made of the changes in the market conditions, the amount and structure of international reserves, and if required, the investment limits and model portfolios (benchmarks) are updated. The monitoring of underlying limits, rules, and procedures is undertaken on a daily basis. Reports are regularly prepared for both the needs of international reserves operating management and providing updated information to the Bank's management.

All approved financial instruments and asset classes, in which the BNB may invest, are specified in internal documents. The documents define the main portfolios and the respective model portfolios (benchmarks), all limits for credit, interest rate, currency and operational risk, and give a list of the foreign financial institutions which are counterparties of the Bank.

The international reserves management is governed by a business procedure and rules of behaviour regulating the performance of the functions and tasks of the main structural units involved in the process.

b) Credit risk

The BNB is exposed to credit risk through its trading operations and investment activities and in cases where it acts as an intermediary on behalf of the government or other public institutions. The Bank assumes credit risk also in operations of purchases and sales of foreign currency with banks. In general, this credit risk is associated with the probability of insolvency of a BNB's counterparty or the insolvency of an issuer, in whose debt instruments the Bank has invested its own funds. The credit risk in managing BNB's gross international reserves is assessed in line with the requirements in Article 28, paragraph 3 of the Law on the BNB. According to these requirements, the BNB may invest international reserves in debt instruments issued by foreign governments, central banks, other foreign financial institutions or international financial organisations whose debts are rated with one of the top two grades by two internationally recognised credit rating agencies and are payable in freely convertible currency in line with an internally developed methodology as per the requirements of Article 28 of the LBNB.

According to these requirements, the approved types of financial instruments for investment of funds in managing the international reserves are as follows:

- investment programmes with central banks;
- automatic borrowings/lending of securities with the main depository;
- tri-party repo agreements with specially designated counterparties of the BNB carried out through the Bank's main depository as a third party;
- deposits in foreign currency (time deposits and funds on current accounts) with BNB counterparties, including central banks or supranational financial institutions;
- deposits in gold (time deposits and funds on current accounts) with BNB counterparties, including central banks or supranational financial institutions;
- commercial securities (of up to one year term to maturity), issued by governments or government guaranteed institutions, supranational financial institutions, specialised financial agencies, banks, and other financial institutions;
- bonds issued by governments or government guaranteed institutions, supranational financial institutions, specialised financial agencies, banks and other financial institutions – issuers of covered bonds. All bonds must be with a one-off payment of their face value on the maturity date and without any embedded option;
- purchases and sales of foreign currency with a value date of up to two business days.

Two basic types of limits are set which are calculated on the basis of the market value of foreign currency reserves: (i) a maximum or minimum limit on the weight of each asset class in the Issue Department balance sheet, and (ii) an individual maximum acceptable exposure of the BNB to a country, including an individual exposure to an issuer/counterparty (concentration limit).

c) **Liquidity risk**

Liquidity risk arises in the funding of the Bank's core activities and in the management of positions. It is primarily manifested in two aspects: the first aspect is risk for the Bank of being unable to meet its obligations when due and the second aspect comprises the risk of its being unable to sell an asset on international markets at a fair value within an appropriate time frame in compliance with the respective market conventions.

The BNB is striving to maintain a balance between the maturity of attracted funds and that of assets by means of investments in financial instruments of a different maturity structure. The instruments for attracting funds, which are provided to customers on the liability side, are primarily deposit/investment accounts and settlement accounts. The Bank maintains a minimum level of liquidity by type of currency on a daily basis to ensure all BNB payments in foreign currency. To better manage the risk arising from liquidation of positions in financial instruments, the latter are grouped by liquidity rank subject to the level of difficulty (*i.e.* discount from the fair value), at which they could be sold on the market in time of crisis. Limits are set for the different types of financial instruments based on the liquidity ranks.

As part of its overall liquidity risk management strategy, the Bank has defined requirements for the management of a portfolio of liquid assets denominated in euro and for maintaining assets denominated in other currencies for the purposes of meeting its cash inflows and outflows.

The Bank's financial assets and liabilities, analysed by residual term to maturity from the date of the statement of financial position to the date of any subsequent agreement or contractual maturity, are as follows:

(BGN'000)

	Up to 1 month	From 1 to 3 months	From 3 months to 1 year	From 1 to 5 years	Over five years	Undefined maturity	Total
As of 31 December 2019							
Financial assets							
Cash and deposits in foreign currency	14,551,307	-	-	-	-	(5,258)	14,546,049
incl. effect of applying IFRS 9	-	-	-	-	-	*(5,258)*	-
Gold, instruments in gold, and other precious metals	3,536,393	-	-	-	-	(703)	3,535,690
incl. effect of applying IFRS 9						*(703)*	
Financial assets at fair value through profit or loss	2,272,836	1,807,443	10,718,201	15,470,000	65,223	-	30,333,703
Financial assets at fair value in other comprehensive income	236,239	-	-	-	-	1,979,662	2,215,901
Other assets	38,428	15,564	128	-	-	-	54,120
Total financial assets	**20,635,203**	**1,823,007**	**10,718,329**	**15,470,000**	**65,223**	**1,973,701**	**50,685,463**
Financial liabilities							
Banknotes and coins in circulation	-	-	-	-	-	19,104,920	19,104,920
Liabilities to banks and other financial institutions	14,462,625	-	-	-	-	-	14,462,625
Liabilities to government institutions and other borrowings	8,853,715	-	-	-	-	-	8,853,715
Borrowings against Bulgaria's participation in international financial institutions	-	-	-	-	-	3,394,229	3,394,229
Total financial liabilities	**23,316,340**	-	-	-	-	**22,499,149**	**45,815,489**
Asset-liability maturity mismatch	**(2,681,137)**	**1,823,007**	**10,718,329**	**15,470,000**	**65,223**	**(20,525,448)**	**4,869,974**
As of 31 December 2018							
Financial assets							
Cash and deposits in foreign currency	18,445,863	807,613	586,677	-	-	(6,905)	19,833,248
incl. effect of applying IFRS 9	-	-	-	-	-	*(6,905)*	-
Gold, instruments in gold, and other precious metals	2,885,390	-	-	-	-	(1,107)	2,884,283
incl. effect of applying IFRS 9	-	-	-	-	-	*(1,107)*	-
Financial assets at fair value through profit or loss	1,818,476	2,189,323	7,598,911	14,476,775	36,680	-	26,120,165
Financial assets at fair value in other comprehensive income	233,117	-	-	-	-	1,949,491	2,182,608
Other assets	24,780	5,439	18,164	-	-	-	48,383
Total financial assets	**23,407,626**	**3,002,375**	**8,203,752**	**14,476,775**	**36,680**	**1,941,479**	**51,068,687**
Financial liabilities							
Banknotes and coins in circulation	-	-	-	-	-	17,325,475	17,325,475
Liabilities to banks and other financial institutions	15,267,214	-	-	-	-	-	15,267,214
Liabilities to government institutions and other borrowings	1,566,563	29,446	9,123,418	-	-	-	10,719,427
Borrowings against Bulgaria's participation in international financial institutions	-	-	-	-	-	3,349,973	3,349,973
Total financial liabilities	**16,833,777**	**29,446**	**9,123,418**	-	-	**20,675,448**	**46,662,089**
Asset-liability maturity mismatch	**6,573,849**	**2,972,929**	**(919,666)**	**14,476,775**	**36,680**	**(18,733,969)**	**4,406,598**

Notes: Initial application of IFRS 9 as of 1 January 2018. In accordance with the selected transition methods, comparative information has not been restated.

The outstanding contractual maturities of the Bank's financial liabilities are as follows:

(BGN'000)

	Book value	Gross nominal outgoing cash flow	Up to 1 month	From 1 to 3 months	From 3 months to 1 year	From 1 to 5 years	Over five years
As of 31 December 2019							
Banknotes and coins in circulation	19,104,920	19,104,920	-	-	-	-	19,104,920
Liabilities to banks and other financial institutions	14,462,625	14,462,625	14,462,625	-	-	-	-
Liabilities to government institutions and other borrowings	8,853,715	8,853,715	8,853,715	-	-	-	-
Borrowings against Bulgaria's participation in international financial institutions	3,394,229	3,394,229	-	-	-	-	3,394,229
	45,815,489	**45,815,489**	**23,316,340**	**-**	**-**	**-**	**22,499,149**
As of 31 December 2018							
Banknotes and coins in circulation	17,325,475	17,325,475	-	-	-	-	17,325,475
Liabilities to banks and other financial institutions	15,267,214	15,267,214	15,267,214	-	-	-	-
Liabilities to government institutions and other borrowings	10,719,427	10,706,393	1,566,530	29,430	9,110,433	-	-
Borrowings against Bulgaria's participation in international financial institutions	3,349,973	3,349,973	-	-	-	-	3,349,973
	46,662,089	**46,649,055**	**16,833,744**	**29,430**	**9,110,433**	**-**	**20,675,448**

d) Market risk

Market risk

All financial instruments are subject to market risk, *i.e.* the risk of impairment as a result of changes in the market conditions. The instruments are evaluated on a daily basis at fair market value which best reflects current financial market conditions for the respective type of financial instruments. The Bank manages its portfolios in response to changing market conditions and to changes in the liability structure of Issue Department balance sheet. Market risk exposure is managed in accordance with the risk limits specified in the document Investment Limits and Benchmarks for the Management of the Gross International Reserves.

The table below presents one important measure of market risk, *i.e.* Value at Risk (VaR). VaR is an indicator of the maximum loss over a certain period of time (holding period) and with a certain probability (called a confidence level or confidence interval). The VaR used in this report is based on a 95 per cent confidence level and a one-day holding period.

To calculate the total risk, currency risk and interest rate risk, the empiric distributions, derived from time series of 30 daily observations of total income, currency income and interest income of assets, respectively have been used. The correlation between the currency and interest rate risk is also presented. For each of the parameters, the value as of the last date for the period, the average value for the whole period and the minimum and maximum values have been calculated.

(BGN'000)

	As of 31 December 2019	Average	Maximum	Minimum
Currency risk	(23,316)	(24,083)	(39,695)	(6,305)
Interest rate risk	(5,564)	(4,214)	(11,728)	(1,032)
Correlation (per cent)	0.50	0.46	0.87	(0.13)
Overall risk	**(28,656)**	**(26,116)**	**(48,405)**	**(9,029)**

	As of 31 December 2018	Average	Maximum	Minimum
Currency risk	(9,207)	(17,391)	(32,028)	(7,268)
Interest rate risk	(3,822)	(3,930)	(11,335)	(1,552)
Correlation (per cent)	0.14	0.16	0.69	(0.45)
Overall risk	**(11,948)**	**(19,339)**	**(38,264)**	**(7,920)**

Interest rate risk

The Bank's operations are subject to the risk of interest rate fluctuations, which impact the prices of interest-earning assets (including investments) and interest-bearing liabilities. Modified duration is used as a key measurement for absolute interest rate risk. Modified duration measures the effect of the change in the market value of an asset (liability) in percentage points in response to a 1 basis point (1/100th of 1 per cent) change in the interest rate levels. In addition, portfolios' technical parameters such as protuberance (convexity), duration in a fixed point of the yield curve, *etc.* are monitored on a daily basis. For each portfolio held by the BNB, the interest rate risk is limited by a model portfolio (benchmark) and by the investment limits for a maximum deviation of the interest rate from that of the respective benchmark. The relative interest risk limit of investment portfolios has been set on the basis of the risk measure *i.e.* relative yield volatility measure.

Assets and liabilities with floating interest rates involve the risk of changes in the base which serves to determine the interest rates.

(BGN'000)

	Total	Floating rate instruments	Fixed rate instruments		
			Up to 1 month	From 1 to 3 months	Over 3 months
As of 31 December 2019					
Interest-earning assets					
Cash and deposits in foreign currency	12,490,270	2,267,045	10,223,225	-	-
Gold, instruments in gold, and other precious metals	2,094,291	-	2,094,291	-	-
Financial assets at fair value through profit or loss	30,502,301	392,770	2,289,696	1,813,407	26,006,428
Financial assets at fair value in other comprehensive income	236,238	-	236,238	-	-
Other interest-earning assets	54,120	38,428	-	15,564	128
Total	**45,377,220**	**2,698,243**	**14,843,450**	**1,828,971**	**26,006,556**
Interest-bearing liabilities					
Liabilities to banks and other financial institutions	14,462,625	-	14,462,625	-	-
Liabilities to government institutions and other borrowings	5,814,041	5,814,041	-	-	-
Borrowings against Bulgaria's participation in international financial institutions	1,470,677	1,470,677	-	-	-
Total	**21,747,343**	**7,284,718**	**14,462,625**	-	-
Interest-bearing asset/liability gap	**23,629,877**	**(4,586,475)**	**380,825**	**1,828,971**	**26,006,556**
As of 31 December 2018					
Interest-earning assets					
Cash and deposits in foreign currency	19,756,780	2,358,080	16,002,179	808,631	587,890
Gold, instruments in gold, and other precious metals	1,723,837	-	1,723,837	-	-
Financial assets at fair value through profit or loss	26,310,866	393,136	1,839,849	2,217,447	21,860,434
Financial assets at fair value in other comprehensive income	233,117	-	233,117	-	-
Other interest-earning assets	48,383	24,780	-	5,439	18,164
Total	**48,072,983**	**2,775,996**	**19,798,982**	**3,031,517**	**22,466,488**
Interest-bearing liabilities					
Liabilities to banks and other financial institutions	15,267,214	-	15,267,214	-	-
Liabilities to government institutions and other borrowings	9,436,112	-	277,893	29,513	9,128,706
Borrowings against Bulgaria's participation in international financial institutions	1,451,245	1,451,245	-	-	-
Total	**26,154,571**	**1,451,245**	**15,545,107**	**29,513**	**9,128,706**
Interest-bearing asset/liability gap	**21,918,412**	**1,324,751**	**4,253,875**	**3,002,004**	**13,337,782**

Notes: Initial application of IFRS 9 as of 1 January 2018. In accordance with the selected transition methods, comparative information has not been restated.

For managing interest rate risk and the band of interest rate changes, the sensitivity of financial assets and liabilities to various standard and non-standard interest rate movement scenarios are monitored.

The standard scenarios include the following changes in yield curves: (i) a 100 basis points instant and parallel increase; (ii) a 100 basis points instant parallel decrease; (iii) a 50 basis points parallel increase in the yield curves for a period of 12 months; and (iv) a 50 basis points parallel decrease in the yield curves also for a period of 12 months. The second two scenarios assume that the change in yields takes place at the beginning of the period, and over the one-year period the yield curve remains unchanged.

The analysis of the sensitivity of the Bank's assets (to first approximation) to changes in interest rates, assuming a constant spread of assets and liabilities and parallel shifts in the yield curves of the relevant assets, is as follows:

(BGN'000)

	100 b.p. intra-day instant parallel increase	100 b.p. intra-day instant parallel decrease	50 b.p. parallel increase in the beginning of the period	50 b.p. parallel decrease in the beginning of the period
As of 31 December 2019	(400,664)	400,664	(207,830)	(201,529)
As of 31 December 2018	(352,903)	352,903	(177,760)	(234,910)

Currency risk

For the Bank, a currency risk exists where there is a mismatch between the currency structure of assets and that of liabilities. The Bank is exposed to currency risk when entering into transactions in financial instruments denominated in foreign currencies other than the euro.

With the introduction of the currency board arrangement in Bulgaria and the fixing of the Bulgarian currency to the euro, the Bank's financial statements, prepared in Bulgarian levs, are affected by movements in the exchange rate of the lev against the currencies other than the euro.

To minimise currency risk, there is a limit to the mismatches between the currency structure of assets and that of liabilities. According to Article 31, paragraph 3 of the Law on the BNB, the total market value of assets in a foreign currency other than the euro, SDR and monetary gold, may not deviate by more than +/-2 per cent from the market value of the liabilities denominated in these currencies.

(BGN'000)

	31 December 2019	31 December 2018
Assets		
Bulgarian lev and euro	43,683,048	44,729,176
US dollar	79,635	75,110
Japanese yen	158	80
Pound sterling	294	236
SDR	3,660,357	3,610,906
Gold	3,457,041	2,848,174
Other	657	881
	50,881,190	**51,264,563**
Liabilities, capital and reserves		
Bulgarian lev and euro	47,245,649	47,682,094
US dollar	81,478	76,711
Japanese yen	1	1
Pound sterling	-	-
SDR	3,553,285	3,505,542
Other	777	215
	50,881,190	**51,264,563**

	31 December 2019	31 December 2018
Net position		
Bulgarian lev and euro	(3,562,601)	(2,952,918)
US dollar	(1,843)	(1,601)
Japanese yen	157	79
Pound sterling	294	236
SDR	107,072	105,364
Gold	3,457,041	2,848,174
Other	(120)	666

e) Using accounting judgements and assumptions

The Governing Council of the BNB discusses the development, selection and disclosure of critical accounting policies and assumptions, as well as their application.

These disclosures supplement the notes to the financial risk management.

Management's major priorities in the next few years will still be to maintain monetary and financial system stability in the country, keep the Bank's stable liquidity position and improve continuously Bank's valuation methods and techniques, international reserves management and control on international financial markets.

1) Determination of fair values

The determination of fair values of financial assets and liabilities for which there is no observable market price requires the use of valuation techniques described in the accounting policy. For financial instruments that trade infrequently and whose price is not transparent, the fair value is less objective and requires an expert's judgement depending on liquidity, concentration, market factors uncertainty, pricing assumptions, and other risks affecting the particular instrument.

2) Valuation of financial instruments

The Bank measures the fair value of financial instruments using the following hierarchy of methods:

- **Level 1**: Quoted market price or closing price for positions for which there is a reliable market;
- **Level 2**: Valuation techniques based on observable market information about the yield curve; This category of methods is used to measure debt securities for which there is no reliable market.
- **Level 3**: Valuation techniques, where inputs on financial assets and liabilities are not based on observable market data.

The fair values of financial assets and liabilities traded in international financial markets for which there is available market information are based on market quotations or closing market prices. The use of observable market prices and information reduces the need for management judgement and estimation and also reduces the uncertainty associated with determination of fair values. The availability of actual market prices and information varies depending on products and markets and changes because of specific events and the general conditions of financial markets. The Bank determines the fair values of all other financial instruments for which there are no current market quotes by using a valuation technique based on a net present value. The net present value is computed by means of market yield curves and credit spreads, where necessary, for the relevant instrument. The purpose of the valuation techniques is to determine a fair value which reflects the price of the financial instrument on the reporting date.

The Bank has established a control framework with respect to the measurement of fair values. The fair values of financial instruments controls are set by a specialised risk analysis and control unit. Specific controls include: checking the actual price information; regular reviews of current valuation models, and, if necessary, development, approval and introduction of new valuation models; follow-up verification by means of analysis and comparison of data from various information sources, *etc.*

The table below analyses financial instruments reported at fair value using valuation models. The data does not include equity instruments reported at acquisition cost (note 14).

(BGN'000)

	Level 1 Quoted market prices on active markets	Level 2 Valuation techniques (using market data)	Total
As of 31 December 2019			
Cash and deposits in foreign currency	14,546,049	-	14,546,049
incl. effect of applying IFRS 9	*(5,258)*	-	*(5,258)*
Gold, instruments in gold, and other precious metals	3,535,690	-	3,535,690
incl. effect of applying IFRS 9	*(703)*	-	*(703)*
Financial assets at fair value through profit or loss	28,407,813	1,925,890	30,333,703
Total	**46,489,552**	**1,925,890**	**48,415,442**
31 December 2018			
Cash and deposits in foreign currency	19,833,248	-	19,833,248
incl. effect of applying IFRS 9	*(6,905)*	-	*(6,905)*
Gold, instruments in gold, and other precious metals	2,884,283	-	2,884,283
incl. effect of applying IFRS 9	*(1,107)*	-	*(1,107)*
Financial assets at fair value through profit or loss	25,070,918	1,049,247	26,120,165
Total	**47,788,449**	**1,049,247**	**48,837,696**

Notes: Initial application of IFRS 9 as of 1 January 2018. In accordance with the selected transition methods, comparative information has not been restated.

Financial instruments not measured at fair value, but by applying a level of the fair value hierarchy where a fair value measurement is categorised, are analysed as follows:

(BGN'000)

	Level 1 Quoted market prices on active markets	Level 2 Observable inputs other than quoted prices	Total
31 December 2019			
Liabilities to banks and other financial institutions	-	14,462,625	14,462,625
Liabilities to government institutions and other borrowings	-	8,853,715	8,853,715
Borrowings against Bulgaria's participation in international financial institutions	-	3,394,229	3,394,229
Total	-	**26,710,569**	**26,710,569**
31 December 2018			
Liabilities to banks and other financial institutions	-	15,267,214	15,267,214
Liabilities to government institutions and other borrowings	-	10,719,427	10,719,427
Borrowings against Bulgaria's participation in international financial institutions	-	3,349,973	3,349,973
Total	-	**29,336,614**	**29,336,614**

The fair value of liabilities to banks and other financial institutions and of liabilities to government institutions is approximately equal to the reporting value as they are short-term.

The fair value of the liabilities for participation in international financial institutions is approximately equal to their reporting value as they are interest-free and of undefined maturity.

f) Maturity structure of assets and liabilities

The Bank's assets and liabilities, analysed by residual term to maturity from the date of the statement of financial position to the date of any subsequent agreement or contractual maturity, are as follows:

(BGN'000)

	Up to 1 month	From 1 to 3 months	From 3 months to 1 year	From 1 to 5 years	Over 5 years	Undefined maturity	Total
As of 31 December 2019							
Financial assets							
Cash and deposits in foreign currency	14,551,307	-	-	-	-	(5,258)	14,546,049
incl. effect of applying IFRS 9	-	-	-	-	-	*(5,258)*	-
Gold, instruments in gold, and other precious metals	3,536,393	-	-	-	-	(703)	3,535,690
incl. effect of applying IFRS 9	-	-	-	-	-	*(703)*	-
Financial assets at fair value through profit or loss	2,272,836	1,807,443	10,718,201	15,470,000	65,223	-	30,333,703
Financial assets at fair value in other comprehensive income	236,239	-	-	-	-	1,979,662	2,215,901
Tangible assets	-	-	-	-	-	150,771	150,771
Intangible assets	-	-	-	-	-	6,229	6,229
Other assets	38,428	15,564	128	-	-	38,727	92,847
Total financial assets	**20,635,203**	**1,823,007**	**10,718,329**	**15,470,000**	**65,223**	**2,169,428**	**50,881,190**
Financial liabilities							
Banknotes and coins in circulation	-	-	-	-	-	19,104,920	19,104,920
Liabilities to banks and other financial institutions	14,462,625	-	-	-	-	-	14,462,625
Liabilities to government institutions and other borrowings	8,853,715	-	-	-	-	-	8,853,715
Borrowings against Bulgaria's participation in international financial institutions	-	-	-	-	-	3,394,229	3,394,229
Other liabilities	-	-	-	-	-	265,627	265,627
Total financial liabilities	**23,316,340**	**-**	**-**	**-**	**-**	**22,764,776**	**46,081,116**
Asset-liability maturity mismatch	**(2,681,137)**	**1,823,007,**	**10,718,329,**	**15,470,000,**	**65,223,**	**(20,595,348)**	**4,800,074,**
As of 31 December 2018							
Financial assets							
Cash and deposits in foreign currency	18,445,863	807,613	586,677	-	-	(6,905)	19,833,248
incl. effect of applying IFRS 9	-	-	-	-	-	*(6,905)*	-
Gold, instruments in gold, and other precious metals	2,885,390	-	-	-	-	(1,107)	2,884,283
incl. effect of applying IFRS 9	-	-	-	-	-	*(1,107)*	-
Financial assets at fair value through profit and loss	1,818,476	2,189,323	7,598,911	14,476,775	36,680	-	26,120,165
Financial assets at fair value in other comprehensive income	233,117	-	-	-	-	1,949,491	2,182,608
Tangible assets	-	-	-	-	-	154,065	154,065
Intangible assets	-	-	-	-	-	5,323	5,323
Other assets	24,780	5,439	18,164	-	-	36,488	84,871
Total financial assets	**23,407,626**	**3,002,375**	**8,203,752**	**14,476,775**	**36,680**	**2,137,355**	**51,264,563**
Financial liabilities							
Banknotes and coins in circulation	-	-	-	-	-	17,325,475	17,325,475
Liabilities to banks and other financial institutions	15,267,214	-	-	-	-	-	15,267,214
Liabilities to government institutions and other borrowings	1,566,563	29,446	9,123,418	-	-	-	10,719,427
Borrowings against Bulgaria's participation in international financial institutions	-	-	-	-	-	3,349,973	3,349,973
Other liabilities	-	-	-	-	-	294,432	294,432
Total financial liabilities	**16,833,777**	**29,446**	**9,123,418**	**-**	**-**	**20,969,880**	**46,956,521**
Asset-liability maturity mismatch	**6,573,849**	**2,972,929**	**(919,666)**	**14,476,775**	**36,680**	**(18,832,525)**	**4,308,042**

Notes: Initial application of IFRS 9 as of 1 January 2018. In accordance with the selected transition methods, comparative information has not been restated.

7. Interest Income and Expense

(BGN'000)

	31 December 2019	31 December 2018
Interest income		
– securities	194,599	203,172
– deposits	65,002	61,732
– other	36	4
	259,637	**264,908**
Interest expense		
– deposits	74,527	71,167
– other	-	-
	74,527	**71,167**

As of 31 December 2019 interest expenses paid on government deposits in foreign currency amounted to BGN 1833 thousand (compared to BGN 1276 thousand as of 31 December 2018).

As of 31 December 2019, as well as of 31 December 2018, there are no interests paid on deposits of other organizations in foreign currency.

Interest expenses paid on deposits include interest paid of BGN 54,284 thousand on deposits and current accounts with foreign correspondent banks as a result of using negative reference interest rates (31 December 2018: BGN 36,974 thousand).

In addition BGN 3657 thousand interest paid on the technical account of the national system component TARGET2-BNB at the ECB are included (31 December 2018: BGN 1602 thousand).

Over the review period the interest rate on the Eurosystem's deposit facility set by the ECB Governing Council remained negative. In September 2019 the interest rate on the Eurosystem's deposit facility was lowered by 10 basis points and at the end of the reporting period it was fixed at -0.50 per cent (as of 31 December 2018 the interest rate on the deposit facility was -0.40 per cent).

8. Net Gains/(Losses) from Financial Assets and Liabilities at Fair Value through Profit or Loss

(BGN'000)

	31 December 2019	31 December 2018
Net (losses) from operations in securities	(256,402)	(248,854)
Net gains from operations in foreign currency	2,042	471
Net revaluation (losses) on futures	(154)	(108)
Net revaluation (losses) on securities	(13,192)	(23,254)
Net revaluation gains on foreign currency assets and liabilities	1,037	1,722
Net revaluation gains on gold	647,198	96,223
Provisions for expected credit losses*	-	(8,012)
	380,529	**(181,812)**

* Initial application of IFRS 9 as of 1 January 2018. In accordance with the selected transition methods, comparative information has not been restated.

Net gains/(losses) from financial assets and liabilities carried at fair value through profit or loss as at 31 December 2019 are largely attributable to revaluation of gold of BGN 647,198 thousand due to an increase in the market price of gold from BGN 2190.59 per troy ounce as of 31 December 2018 to BGN 2656.13 as of 31 December 2019.

Net losses from operations in securities amounted to BGN 256,402 thousand. The main factor for that is the lower market yields on securities from their coupon yield which led to be traded at premium above their nominal value.

During the reporting period the market yield on the securities is characterised by mixed movements across issuers, maturity sectors and quarters. The market yield increased between 15 and 17 basis points on the short-term securities in which the BNB primarily invested, while market yields decreased between 1 and 9 basis points on the bulk of securities of other issuers.

9. Other Operating Income

(BGN'000)

	31 December 2019	31 December 2018
Income from subsidiaries	36,401	25,353
Income from associates	4,063	2,896
Income from sale of coins	1,194	1,992
Dividend income	4,701	4,573
Other income, net	2,592	1,740
	48,951	**36,554**

Dividend income includes dividends from BNB's participation in the Bank for International Settlements (BIS) amounting to BGN 4701 thousand.

In 2019 BNB's dividends from its participation in Bulgarian Mint EAD and Printing Works AD were BGN 232 thousand and BGN 2282 thousand, respectively, which were eliminated for the purposes of consolidated financial statements.

The other net income includes financial income from subsidiaries of BGN 295 thousand and income from reallocated remuneration from the ECB in relation to TARGET2 of BGN 915 thousand.

10. General Administrative Expenses

(BGN'000)

	31 December 2019	31 December 2018
Staff expenditure	42,227	39,077
Administrative expenses	66,644	53,334
Depreciation	13,970	13,677
Other expenses	5,191	4,632
	128,032	**110,720**

The number of employees of the Bank and its subsidiaries is 1160 as of 31 December 2019 (31 December 2018: 1160), including the BNB staff of 895 (31 December 2018: 886).

Staff expenditure include salaries, social and health insurance costs charged under the local legislation provisions as of 31 December 2019, and social activities costs, respectively for the BNB: BGN 34,506 thousand (31 December 2018: BGN 31,554 thousand), for the BNB Printing Works AD: BGN 5090 thousand (31 December 2018: BGN 4613 thousand), and for the Bulgarian Mint EAD: BGN 2631 thousand (31 December 2018: BGN 2910 thousand).

Staff expenditure includes expenses for remunerations paid to the BNB Governing Council members of BGN 1256 thousand as of 31 December 2019 (31 December 2018: BGN 1175 thousand), presented, as follows:

(BGN'000)

	31 December 2019	31 December 2018
Total gross remuneration expenses*	1,256	1,175
including bonuses up to established thresholds in accordance with Article 23, paragraph 3 of the LBNB by BNB Governing Council's resolution of 30 July 2015**	384	350
Expenses on BNB Governing Council members' retirement/termination benefits	136	-,
Total gross remuneration paid to the BNB Governing Council members	**1,392**	**1,175**

* Remunerations are before tax.

** http://www.bnb.bg/PressOffice/POPressReleases/POPRDate/PR_20150730_1_EN

With the adoption of the BNB budget for 2019, the amount of monthly remunerations of the Governing Council members is defined, as follows: Governor: BGN 16,849; Deputy Governors: BGN 14,442; other Governing Council members: BGN 4814.

Staff retirement liabilities calculated based on actuarial valuation and pursuant to IAS 19 Employee Benefits are given below:

(BGN'000)

	31 December 2019	31 December 2018
Defined benefit liabilities as of 1 January	**3,311**	**2,810**
Plan benefits paid	(350)	(172)
Current service costs	437	365
Interest costs	20	24
Re-measurements	(2)	-
Actuarial (gain)/loss arising from experience adjustment	104	264
Actuarial (gain) arising from change in demographic assumptions	-	(1)
Actuarial loss arising from change in financial assumptions	164	19
Actuarial loss recognised in expenses	-	2
Defined benefit liabilities as at 31 December	**3,684**	**3,311**

Costs recognised in profit or loss

(BGN'000)

	31 December 2019	31 December 2018
Current service costs	437	365
Interest costs	20	24
Actuarial loss	-	2
Re-measurements	-	-
Total	**457**	**391**

Actuarial assumptions

The key actuarial assumptions as at the Financial Statements date are the following (weighted average):

(per cent)

	31 December 2019	31 December 2018
Discount interest rate as at 31 December	0.19	0.53
Future salary growth	5.00	4.50

(BGN'000)

Distribution of BNB staff liabilities (subsidiaries excluded) by residual term	31 December 2019	31 December 2018
Up to 1 year	494	539
From 1 to 3 years	466	394
From 3 to 5 years	321	221
From 5 to 10 years	549	474
Over ten years	1,034	789
Total	**2,864**	**2,417**

Administrative expenses include the BNB's currency circulation expenses of BGN 30,779 thousand as of 31 December 2019 (31 December 2018: BGN 24,825 thousand) as well as expenses on conducting an international audit at BGN 104 thousand (31 December 2018: BGN 115 thousand).

11. Cash and Deposits in Foreign Currency

(BGN'000)

	31 December 2019	31 December 2018
Cash in foreign currency	2,077,206	96,926
Current accounts in other banks	2,267,233	6,775,887
incl. effect of applying IFRS 9	*(34)*	*(805)*
Deposits in foreign currency	10,201,610	12,960,435
incl. effect of applying IFRS 9	*(5,224)*	*(6,100)*
	14,546,049	**19,833,248**

Cash and deposits in foreign currency with correspondents are disclosed as follows:

(BGN'000)

	31 December 2019	31 December 2018
Euro area residents		
In EUR	7,095,125	12,872,516
incl. effect of applying IFRS 9	*(3,390)*	*(4,516)*
In other currencies	-	71,836
incl. effect of applying IFRS 9	-	*(46)*
	7,095,125	**12,944,352**
Non-euro area residents		
In EUR	5,891,877	5,426,761
incl. effect of applying IFRS 9	*(1,838)*	*(2,343)*
In other currencies	1,559,047	1,462,135
incl. effect of applying IFRS 9	*(30)*	-
	7,450,924	**6,888,896**
	14,546,049	**19,833,248**

Deposits in foreign currency with correspondents with counterparty's credit rating graded by at least two of the six internationally recognised credit rating agencies – Standard&Poor's, Fitch Ratings, Moody's, DBRS, R&I and JCRA – are disclosed as follows:

(BGN'000)

	Counterparty short-term credit rating	31 December 2019	31 December 2018
Investment graded deposits by the counterparty's credit rating	*A-1+*	1,172,338	1,953,864
	incl. effect of applying IFRS 9	*(252)*	*(318)*
	A-1	9,028,464	11,005,131
	incl. effect of applying IFRS 9	*(4,972)*	*(5,782)*
		10,200,802	**12,958,995**

The disclosure by credit rating does not include demand deposits with external managers.

The BNB maximum exposure to credit risk is equivalent to the book value of cash on current accounts and deposits.

12. Gold, Instruments in Gold, and Other Precious Metals

	31 December 2019		31 December 2018	
	'000 troy ounces	BGN'000	'000 troy ounces	BGN'000
Gold bullion in standard form	513	1,362,709	513	1,123,867
Gold deposits in standard form	788	2,093,588	787	1,723,201
incl. effect of applying IFRS 9		*(703)*		*(1,107)*
Gold in other form	16	41,959	16	34,552
Other precious metals		37,434		2,663
		3,535,690		**2,884,283**

Gold in standard form includes gold held for safekeeping with a depository and deposits. Deposits in gold are held with banks whose liabilities are rated with one of the two highest ratings given by two internationally recognised rating agencies and bear interest between 0.01 per cent and 0.22 per cent annually.

Gold in other form includes commemorative gold coins of BGN 35,296 thousand.

Other precious metals include silver commemorative coins of BGN 122 thousand, platinum commemorative coins of BGN 2523 thousand and scrub silver coins revaluation at market price of BGN 34,459 thousand.

13. Financial Assets at Fair Value through Profit and Loss

(BGN'000)

Securities at fair value through profit or loss	31 December 2019	31 December 2018
Foreign treasury bills, notes and bonds	30,333,703	26,120,165
	30,333,703	**26,120,165**

Securities comprise of both coupon and discount securities denominated in euro. The maximum coupon interest of the EUR-denominated securities was 0.74 per cent as of 31 December 2019 (31 December 2018: 0.79 per cent).

As of 31 December 2019, similarly to 31 December 2018, there were no securities pledged as collateral on futures transactions.

The securities issued by foreign governments and other issuers or relevant issuers with credit rating graded by at least two of the six internationally recognised credit rating agencies – Standard&Poor's, Fitch Ratings, Moody's, DBRS, R&I and JCRA are disclosed as follows:

(BGN'000)

	Issue/issuer credit rating	31 December 2019	31 December 2018
Investment graded securities by the issue/issuer credit rating	AAA	28,013,765	24,624,997
	AA+	224,223	160,096
	AA	2,033,570	1,335,072
	AA-	4,091	-
	A+	54,499	-
	A	3,555	-
		30,333,703	**26,120,165**

14. Financial Assets at Fair Value in Other Comprehensive Income

(BGN'000)

	31 December 2019	31 December 2018
Republic of Bulgaria's quota in the IMF	2,157,833	2,129,322
Equity investments in international financial institutions	30,868	30,613
Investments in associates	27,200	22,673
	2,215,901	**2,182,608**

The Republic of Bulgaria's quota in the IMF is SDR 896,300 thousand (31 December 2018: SDR 896,300 thousand). The amount of BGN 236,238 thousand of the Republic of Bulgaria's quota in the IMF represents the reserve tranche held with the IMF (31 December 2018: BGN 233,117 thousand). The IMF pays remuneration (interest) to those members who have a remunerated reserve tranche position, at an average rate of 0.99 per cent (31 December 2018: 0.93 per cent).

Equity investments in international financial institutions include the equity investment in the Bank for International Settlements (BIS), and 25 per cent of the equity investment in BIS Basel is paid up. As of 31 December 2019 the current value of SDR 10,000 thousand shares amounts to BGN 24,075 thousand while as of 31 December 2018 it was BGN 23,757 thousand (ref. note 28). The capital subscribed, but not paid-in has an option to be paid in within three months upon a decision of the BIS Board of Governors.

Equity investments in international financial institutions do not exceed 10 per cent of the subscribed share capital of the respective institution.

Investments in international financial institutions also include BNB's participation in the ECB. As of 1 January 2007 (when the Republic of Bulgaria joined the EU), the Bulgarian National Bank has a share in the ECB capital. As of 31 December 2019 the amount of the BNB paid-up share in the ECB capital is EUR 3455 thousand or BGN 6757 thousand.

Pursuant to Article 28 of the Statute of the ESCB and the ECB, only ESCB NCBs are entitled to participate in the ECB capital. Capital subscription follows the requirements and the key set forth in Article 29 of the Statute of the ESCB and ECB; *i.e.* the share of each NCB in the ECB capital is determined in percentage and corresponds to the share of the respective Member State in the EU's total population and GDP (in equal proportions). The percentage is adjusted every five years (the last adjustment in force from 1 January 2019) and whenever a new Member State joins the EU. As of 31 December 2019, the BNB's capital share in the ECB subscribed capital is 0.8511 per cent, which corresponds to EUR 92,131.6 thousand.

As a non-euro area NCB, the BNB is required to pay up the minimum percentage of its subscribed capital in the ECB, which is pursuant to Article 47 of the Statute of the ESCB and of the ECB (as set out by the ECB General Council) and represents the BNB contribution to the ECB operational costs. As of 29 December 2010 this percentage amounts to 3.75 per cent. Unlike euro area NCBs, the BNB is not entitled to the ECB's distributable profit, nor is it required to fund any loss of the ECB. Upon joining the euro area, the BNB will be required to pay up the remaining 96.25 per cent of its capital subscription to the ECB, which is EUR 88,676.6 thousand.

The Bank exercises significant influence on the financial and operational policies of the associated companies listed below, and its investments in domestic companies are analysed as follows:

Associates	Share holding, per cent	Principal activity
BORICA AD	36.11	Interbank card payments
Cash Services Company AD	25.00	Handling of sealed parcels of Bulgarian coins and banknotes transferred from the BNB and the banks

BNB's shareholding in Cash Services Company AD through 2019 increased from 20 per cent to 25 per cent after the withdrawal of Raiffesien Bank (Bulgaria) EAD from the company.

15. Tangible Assets

The fair value of land and buildings is categorised as Level 3 fair value based on the input data for the given assessment technique.

For the remaining asset classes Plant and Machinery, Equipment, Vehicles, Fixtures and Fittings, the fair value is considered to be their present value on the Bank's balance sheet as most of them were bought in the last four years and their book value is close to their fair value.

When revaluating tangible fixed assets the Bank derecognises the accrued depreciation at the expense of the gross book value of the assets and their net value is recalculated against the revalued amount.

(BGN'000)

	Land and buildings	Plant and equipment	IT equipment	Office equipment	Other equipment (including motor vehicles)	Assets under construction	Total
As of 1 January 2019	**184,096**	**92,828**	**49,982**	**10,047**	**8,754**	**2,591**	**348,298**
Additions	42	1,329	20	17	6	6,996	8,410
Disposals	-	(1,424)	(993)	(205)	(38)	-	(2,660)
Transfers	73	396	1,815	75	637	(3,027)	(31)
Revaluation	-	-	-	-	-	-	-
As of 31 December 2019	184,211	93,129	50,824	9,934	9,359	6,560	354,017
Depreciation and impairment loss							
As of 1 January 2019	(61,537)	(71,030)	(45,982)	(8,892)	(6,792)	-	(194,233)
Charge for the period	(5,223)	(3,170)	(2,614)	(162)	(503)	-	(11,672)
On disposals	-	1,424	993	205	37	-	2,659
Revaluation	-	-	-	-	-	-	-
As of 31 December 2019	(66,760)	(72,776)	(47,603)	(8,849)	(7,258)	-	(203,246)
Net book value as of 31 December 2019	117,451	20,353	3,221	1,085	2,101	6,560	150,771
Net book value as of 31 December 2018	122,559	21,798	4,000	1,155	1,962	2,591	154,065
As of 1 January 2018	184,096,,	91,053,,	48,237,,	9,984,,	8,233,,	2,142,,	343,745,,
Additions	-	4,055	22	24	16	5,475	9,592
Disposals	-	(4,752)	(120)	(54)	(298)	-,	(5,224)
Transfers	-	2,269	1,843	93	803	(5,026)	(18)
Revaluation	-	203	-	-	-	-	203
As of 31 December 2018	184,096	92,828	49,982	10,047	8,754	2,591	348,298
Depreciation and impairment loss							
As of 1 January 2018	(56,320)	(73,244)	(42,728)	(8,721)	(6,711)	-	(187,724)
Charge for the period	(5,217)	(2,505)	(3,373)	(224)	(379)	-	(11,698)
On disposals	-	1,073	119	53	298	-	1,543
Revaluation	-	3,646	-	-	-	-	3,646
As of 31 December 2018	(61,537)	(71,030)	(45,982)	(8,892)	(6,792)	-	(194,233)
Net book value as of 31 December 2018	122,559	21,798	4,000	1,155	1,962	2,591	154,065
Net book value as of 31 December 2017	127,776	17,809	5,509	1,263	1,522	2,142	156,021

In applying IAS 16 Property, Plant and Equipment and BNB's Internal Rules for Financial Statements and Accounting Policy, as of December 2013 a review was made of the book value of tangible fixed assets stated in the Bank's statement of financial position. The fair value of land and buildings was determined by an external, independent and licensed assessor of recognised professional qualification and experience in assessing property of location and category similar to the assessed ones. As at 31 December 2019, the fair value of land and buildings did not differ materially from their book value as at the same date; therefore, it is considered that the present book value of land and buildings on the Bank's balance sheet fairly reflects their market value. The fair value of fully amortized tangible fixed assets as of 31 December 2019 was BGN 86,189 thousand (31 December 2018: BGN 80,102 thousand).

16. Intangible Assets

(BGN'000)

	Software	Other intangible assets	Development costs	Total
As of 1 January 2019	**54,732**	**174**	**272**	**55,178**
Additions	1,037	6	2,161	3,204
Disposals	(746)	-	-	(746)
Transfers	1,952	-	(1,952)	-
As of 31 December 2019	**56,975**	**180**	**481**	**57,636**
Depreciation and impairment loss				
As of 1 January 2019	**(49,691)**	**(164)**	**-**	**(49,855)**
Charge for the period	(2,294)	(4)	-	(2,298)
On disposals	746	-	-	746
As of 31 December 2019	**(51,239)**	**(168)**	**-**	**(51,407)**
Net book value as of 31 December 2019	**5,736**	**12**	**481**	**6,229**
Net book value as of 31 December 2018	**5,041**	**10**	**272**	**5,323**

As of 31 December 2019 software includes licenses purchased by the BNB to the total amount of BGN 1027 thousand (31 December 2018: BGN 1303 thousand) and software products to the amount of BGN 925 thousand (31 December 2018: BGN 1365 thousand).

(BGN'000)

	Software	Other intangible assets	Development costs	Total
As of 1 January 2018	**52,064**	**174**	**63**	**52,301**
Additions	-	-	2,877	2,877
Disposals	-	-	-	-
Transfers	2,668	-	(2,668)	-
As of 31 December 2018	**54,732**	**174**	**272**	**55,178**
Depreciation and impairment loss				
As of 1 January 2018	**(47,714)**	**(161)**	**-**	**(47,875)**
Charge for the period	(1,977)	(3)	-	(1,980)
On disposals	-	-	-	-
As of 31 December 2018	**(49,691)**	**(164)**	**-**	**(49,855)**
Net book value as of 31 December 2018	**5,041**	**10**	**272**	**5,323**
Net book value as of 31 December 2017	**4,350**	**13**	**63**	**4,426**

As of 31 December 2018 software includes, licenses purchased by the BNB to the total amount of BGN 1303 thousand (31 December 2017: BGN 486 thousand), and software products to the amount of BGN 1365 thousand (31 December 2017: BGN 1170 thousand).

17. Other Assets

(BGN'000)

	31 December 2019	31 December 2018
Cash held by subsidiaries with local banks	54,140	48,413
Investments of subsidiary undertakings in joint ventures and associates	11,077	8,791
Commemorative coins for sale	388	414
Inventories	23,127	19,215
Accounts receivable	1,553	5,113
Deferred charges	1,135	1,446
Other receivables	1,427	1,479
	92,847	**84,871**

Cash held by subsidiaries with local banks comprise BGN 48,502 thousand of Printing Works of the BNB AD and BGN 5638 thousand of Bulgarian Mint EAD.

Investments of subsidiary undertakings in joint ventures and associates include a non-monetary contribution in the form of banknote production equipment to the capital of François-Charles Oberthur Group with which BNB Printing Works AD has established a joint venture for banknote production.

18. Banknotes and Coins in Circulation

(BGN'000)

	31 December 2019	31 December 2018
Banknotes in circulation	18,637,279	16,000,000
Coins in circulation	467,641	1,325,475
	19,104,920	**17,325,475**

19. Liabilities to Banks and Other Financial Institutions

(BGN'000)

	31 December 2019	31 December 2018
Demand deposits from banks and other financial institutions		
– in BGN	13,434,604	12,147,527
– in foreign currency	1,028,021	3,119,687
	14,462,625	**15,267,214**

Demand deposits include BGN 7,816,332 thousand representing the required reserves, which all local banks are required to maintain on accounts with the BNB (31 December 2018: BGN 7,148,799 thousand).

On 26 November 2015 the Governing Council of the Bulgarian National Bank adopted a new Ordinance No 21 on Minimum Required Reserves Maintained with the Bulgarian National Bank by Banks which came into force as of 4 January 2016. The new BNB Ordinance No 21 removed the recognition of banks' funds in the TARGET2-BNB national system component as a component of reserve assets.

Pursuant to Article 42 of BNB Ordinance No 3 this position includes also the banks' participation in the Guarantee Mechanism for Settlement of Payments of the participants in the system operated by BORICA and processing card related payments, amounting to BGN 166,848 thousand as of 31 December 2019 (31 December 2018: BGN 108,288 thousand).

20. Liabilities to Government Institutions and Other Borrowings

(BGN'000)

	31 December 2019	31 December 2018
Current accounts		
– in BGN	6,451,412	1,134,858
– in foreign currency	2,402,303	148,456
Time deposit accounts		
– in BGN	-	5,816,000
– in foreign currency	-	3,620,113
	8,853,715	**10,719,427**

Government's deposits and current accounts with the Bank comprise funds held on behalf of the state budget and other government organisations. The Bank applies interest rates in line with the General Terms and Conditions of the Bulgarian National Bank on accepting cash deposits and servicing accounts of banks, budget organisations and other customers adopted by a resolution of the BNB Governing Council of 26 November 2015 and amended by a resolution of the BNB Governing Council of 14 November 2019. As from

18 November 2019, the Bank does not open and service time deposit accounts of the government and other government organisations in accordance with the General Terms and Conditions of the Bulgarian National Bank on servicing accounts of banks, budget organisations and other customers.

21. Borrowings against Bulgaria's Participation in International Financial Institutions

Borrowings against Bulgaria's participation in the IMF as of 31 December 2019 amount to BGN 1,916,201 thousand, or SDR 795,933 thousand (31 December 2018: BGN 1,890,882 thousand or SDR 795,933 thousand).

Borrowings from the IMF are denominated in SDRs. Borrowings related to Bulgaria's quota in the IMF are non-interest bearing with no stated maturity. This note includes account No 1 and account No 2 of the IMF in levs amounting to BGN 5440 thousand (31 December 2018: BGN 5243 thousand).

The Bank's borrowings from the IMF of the general and special allocation of SDRs amount to SDR 474,586,534 and SDR 136,829,102, respectively. Repayment will take place on IMF's demand. Under Article XX of IMF Statute, the Bank receives interest on the existing SDRs and pays a fee on its borrowings from the general and special allocation at the same interest rate.

22. Other Liabilities

(BGN'000)

	31 December 2019	31 December 2018
Funds of EU institutions and bodies	2,656	3,479
Salaries and social security payable	5,199	4,751
Deferred income	1,330	1,329
Other liabilities	256,442	284,873
	265,627	**294,432**

Funds of EU institutions and bodies' include European Commission's funds and European Investment Bank's funds. Pursuant to Article 9 of Council Regulation No 1150 of 2000 and Bulgaria's participation in the funding of the EU budget, the Bank opened accounts of the European Commission. As at 31 December 2019 the funds on these accounts were BGN 2656 thousand (31 December 2018: BGN 3479 thousand).

23. Capital and Reserves

The capital of the Bank is determined by the Law on the BNB and amounts to BGN 20,000 thousand.

Non-monetary asset revaluation reserves comprise the net change in fair value of property, equity investments and other non-monetary assets.

Pursuant to Article 36 of the Law on the Bulgarian National Bank, unrealised gains/losses arising from the revaluation of assets and liabilities denominated in foreign currencies or gold are transferred to a special reserve account and form special reserves.

Other reserves include 25 per cent of the annual excess of revenue over expenditure after the allocation to special reserves and reserves established in accordance with a resolution of the BNB Governing Council.

As of 31 December 2019 profit distribution in accordance with the profit distribution policy disclosed in note 5 (j) is as follows:

(BGN'000)

	31 December 2019	31 December 2018
Profit/(loss) for the period	**490,115**	**(58,863)**
Allocation to special reserve under Article 36 of the LBNB:		
Unrealised (profit)/loss from gold revaluation	(647,198)	(96,223)
Unrealised (profit)/loss from revaluation of financial assets at fair value through profit or loss	13,192	23,254
Unrealised (profit)/loss from foreign currency valuation	(1,037)	(1,722)
Other unrealised (profit)/loss	795	656
Result after allocation to special reserve including:	**(144,133)**	**(132,898)**
Allocation (from)/to Reserve Fund under Article 8 of the LBNB	*(153,203)*	*(130,863)*
Result from consolidation and non-controlling interest	*9,070*	*(2,035)*
Allocation to a special-purpose fund under Article 8 of the LBNB	-	-
Planned contribution to the state budget	-	-

As of 31 December 2019 the amount of accrued provisions for expected credit losses was BGN 5961 thousand (as of 31 December 2018: BGN 8012 thousand) as it is included in the amount of BGN 153,203 thousand (as of 31 December 2018: BGN 130,863 thousand), reported under the Allocation (from)/to Reserve Fund position pursuant to Article 8 of the LBNB.

24. Non-controlling Interest

The BNB Printing Works AD is a joint-stock company with two shareholders: the BNB and the government represented by the Ministry of Finance. The BNB holds 95.6 per cent of the company's capital and the government holds the remaining 4.4 per cent of the company's capital.

25. Monetary Liabilities and Gross International Reserves

(BGN'000)

	31 December 2019	31 December 2018
Gross international reserves		
Cash and foreign currency denominated deposits	14,546,049	19,833,248
Monetary gold and other instruments in gold	3,456,338	2,847,067
Security investments	30,333,703	26,120,165
Equity investments and quota in the IMF	236,238	233,117
	48,572,328	**49,033,597**
Monetary liabilities		
Banknotes and coins in circulation	19,104,920	17,325,475
Liabilities to banks and other financial institutions	13,372,652	15,264,723
Liabilities to government institutions	8,101,121	8,608,047
Other liabilities	1,845,223	2,117,350
	42,423,916	**43,315,595**
Surplus of gross international reserves over monetary liabilities	6,148,412	5,718,002

Interest receivable and interest payable are carried to the relevant assets and liabilities.

Monetary gold and other instruments in gold are revalued on a daily basis based on the euro fixing of the London Bullion Market closing price.

26. Related Party Transactions

Bulgarian Government

International Monetary Fund

As of 31 December 2019 the Republic of Bulgaria has not received funds under IMF agreements.

The Republic of Bulgaria's quota in the IMF is secured by promissory notes jointly signed by the Bank and the government (ref. note 21).

Government bank accounts

Government budget organisations have bank accounts with the Bank (ref. note 20).

Fiduciary activities

In accordance with the Law on the BNB and under the terms agreed upon with the Minister of Finance, the BNB acts as an agent in government or government-guaranteed debts. With regard to this role, the BNB performs depository and agent services related to the administration and management of government securities issued by the Ministry of Finance. The Bank receives commission for providing these services. These government securities are not assets or liabilities of the Bank and are not recognised in its consolidated statement of financial position. The Bank is not exposed to any credit risk relating to government securities as it does not guarantee them. As of 31 December 2019 the par value of the government securities held in custody was BGN 5479 million (31 December 2018: BGN 5454 million).

27. Subsidiaries Included in Consolidated Financial Statements

(per cent)

Ownership interest	31 December 2019	31 December 2018
Bulgarian Mint EAD	100	100
BNB Printing Works AD (ref. note 24)	95.6	95.6

The net income from subsidiaries for the period comprises net profit of BGN 77 thousand from the Bulgarian Mint EAD (31 December 2018: BGN 232 thousand) and BGN 7444 thousand from the BNB Printing Works AD (31 December 2018: BGN 2650 thousand).

28. Commitments and Contingencies

1) Participation in the Bank for international Settlements

The Bank holds 8000 shares of the capital of the BIS, Basel, each amounting to SDR 5000. Twenty-five per cent of the equity investment in the BIS, Basel is paid up. The capital subscribed but not paid in is with an option to be paid in within three months following a decision of the BIS Board of Governors. As of 31 December 2019 the contingent amount is BGN 72,225 thousand (31 December 2018: BGN 71,270 thousand).

2) IMF quota

The IMF quota is secured by promissory notes jointly signed by the Bank and the Government of the Republic of Bulgaria amounting to BGN 1,922,999 thousand.

3) Capital commitments

As of 31 December 2019 the Bank has committed to BGN 13,274 thousand to purchase non-current assets (31 December 2018: BGN 3224 thousand).

4) Other commitments and liabilities

There are no other outstanding guarantees, letters of credit or commitments to purchase or sell either gold, other precious metals or foreign currency.

5) Other contingent liabilities

The BNB is being sued in relation to alleged compensation for delayed payment of deposits above the guaranteed amount or for challenging money transfers by customers of Corporate Commercial Bank AD (in bankruptcy) to a total amount of around BGN 108 million (31 December 2018: BGN 61 million). Currently, in Bulgaria there is no settled case-law on similar issues. Court proceedings are at an early stage and most of them have been stayed pending until Bulgarian courts hear and determine questions referred for a preliminary ruling.

Two court proceedings have been instituted against the BNB before a Federal Court of the State of New York in relation to alleged compensation of USD 400 million for actions of Corporate Commercial Bank AD (in bankruptcy) conservators appointed in 2014. Both cases are at an early stage, and the question of the federal court's jurisdiction is still pending.

Therefore and based on available information on both cases, the Bank's management considers that no reliable assessment of the likely outcome of legal proceedings could be made and, consequently, no provisions for these contingent liabilities should be made.

29. Events Occurred after the Reporting Date

In March 2020 the World Health Organisation declared the spread of the COVID-19 virus a global pandemic. The pandemic poses serious challenges to both human health and the global economy, including international financial markets.

The Bank's management assesses the effect of events related to COVID-19 as non-adjusting event as regards the consolidated financial statements for 2019.

As of the date of approving the report: 1) there are no events related to COVID-19; 2) there are no direct short-terms effects to the Bank's financial statements due to timely measures taken by the BNB to curb market (interest rate) risk and to further mitigate credit risk associated with managing gross international reserves and maintaining continuously an extremely high liquidity of foreign currency reserves; and 3) no changes to the BNB budget for 2020 are initiated on COVID-19 related events and measures. At this stage it is impossible to determine the medium-term and long-term financial consequences from the pandemic. If in the course of 2020 there is a need to adjust the planned funds on indicators of the 2020 Bank's budget, they will be changed in compliance with the budgetary procedure.

There are no events after the reporting date that require additional disclosure or adjustments to the Bank's Financial Statements.

Information under Article 17, Paragraph 5 of the LBNB Concerning Resolutions Adopted by the BNB Governing Council in 2019

Reporting and Budget

RESOLUTION No 121 of 28 March

The Report on BNB Budget Implementation for 2018 was approved.

RESOLUTION No 130 of 4 April

The BNB Annual Report for 2018 was approved on first reading.

RESOLUTION No 145 of 24 April

The BNB Annual Report for 2018 was approved.

RESOLUTION No 326 of 3 October

The Report on BNB Budget Implementation as of 30 June 2019 was approved.

RESOLUTION No 360 of 31 October

The BNB Report for January–June 2019 was approved on first reading.

RESOLUTION No 361 of 31 October

The BNB Budget for 2020 was approved on first reading.

RESOLUTION No 380 of 14 November

The BNB adopted amendments to the General Terms and Conditions of the Bulgarian National Bank on Servicing Accounts of Banks, Budget Organisations and Other Customers, effective from 18 November 2019.

RESOLUTION No 391 of 29 November

The BNB Report for January–June 2019 was approved.

RESOLUTION No 392 of 29 November

The BNB draft budget for 2020 was adopted.

RESOLUTION No 426 of 12 December

The Governing Council approved amendments to the Tariff of Fees Charged by the BNB for Servicing Accounts and Providing Payment Services.

Gross International Reserves

RESOLUTION No 9 of 24 January

The BNB Governing Council took note of the selected benchmark for dynamic asset allocation in the first quarter of 2019.

RESOLUTION No 75 of 7 March

The BNB Governing Council took note of the International Reserve Management Report for 2018.

RESOLUTION No 153 of 24 April

The BNB Governing Council took note of the selected benchmark for dynamic asset allocation in the second quarter of 2019.

RESOLUTION No 195 of 30 May

The BNB Governing Council took note of the International Reserve Management Report for the first quarter of 2019.

RESOLUTION No 251 of 25 July

The BNB Governing Council took note of the selected benchmark for dynamic asset allocation in the third quarter of 2019.

RESOLUTION No 330 of 3 October

The BNB Governing Council took note of the International Reserve Management Report for the second quarter of 2019.

RESOLUTION No 340 of 15 October

The BNB Governing Council took note of the selected benchmark for dynamic asset allocation in the fourth quarter of 2019.

RESOLUTION No 395 of 29 November

The BNB Governing Council took note of the International Reserve Management Report for the third quarter of 2019.

RESOLUTION No 443 of 20 December

BNB risk tolerance for 2020 was set with regard to gross international reserve management.

Payment Systems and Payment Oversight

RESOLUTION No 14 of 24 January

The licence granted by Resolution No 11 of 23 February 2012 of the BNB Governing Council to the Euromoney Transfer OOD to conduct activities as a payment institution providing payment services under Article 4, item 6 of the Law on Payment Services and Payment Systems (LPSPS) is deemed cancelled with effect from 1 February 2019.

RESOLUTION No 36 of 7 February

The BNB Governing Council approved the launch of preparations of the BNB and TARGET2-BNB participants to join the consolidated platform of TARGET services by 21 November 2021.

RESOLUTION No 37 of 7 February

The BNB refused to issue a licence to Varchev Transfers EOOD for conducting activities as a payment institution.

RESOLUTION No 59 of 28 February

The Governing Council of the BNB adopted amendments to Ordinance No 16 of 29 March 2018 on Granting Licenses and Approvals, Entry into the Register under

Article 19 of the Law on Payment Services and Payment Systems, and Requirements to the Activity of Operators of Payment Systems with Settlement Finality.

RESOLUTION No 60 of 28 February

The Governing Council suggests that the BNB starts implementing by the end of the first half of 2019 the guidelines on the conditions to benefit from an exemption from the contingency mechanism under Article 33(6) of Regulation (EU) 2018/389 (RTS on SCA & CSC) (EBA/GL/2018/07 of 4 December 2018) issued by the European Banking Authority and published on its official website.

RESOLUTION No 63 of 28 February

The Governing Council took note of the calculated average amount of fees charged by banks on current account services under Appendix 1 to Article 34 of Ordinance No 3 of the BNB as of 31 December 2018 in relation to Article 120, paragraph 6 of the Law on Payment Services and Payment Systems and Article 35, paragraph 2 of Ordinance No 3 of the BNB.

RESOLUTION No 76 of 7 March

The Governing Council of the BNB decided to supplement the payment institution license of Transcart Financial Services AD issued by Resolution No 61 of 3 June 2010 of the BNB Governing Council with the payment services under Article 4, item 3 (c) and item 4 (c) of the LPSPS.

RESOLUTION No 209 of 13 June

The Governing Council of the BNB adopted amendments to Ordinance No 3 of 18 April 2018 on the Terms and Procedure for Opening Payment Accounts, Executing Payment Transactions and Using Payment Instruments.

RESOLUTION No 214 of 25 June

The Governing Council of the BNB approved amendments to Ordinance No 9 of 26 July 2017 on the information and documents which prove fulfilment of the requirements to temporary administrators or special managers of a bank.

RESOLUTION No 229 of 4 July

The BNB decided to supplement the licence granted to Diners Club Bulgaria AD to provide payment services under Article 4, item 4, letter b and item 5 of the LPSPS with the payment services under Article 4, item 3, letter c of the LPSPS.

RESOLUTION No 263 of 26 July

The BNB Governing Council approved the draft Law Amending the Law on Payment Services and Payment Systems.

RESOLUTION No 264 of 26 July

The BNB Governing Council approved the entry of Shell Bulgaria EAD into the Register under Article 19 of the LPSPS as a service provider under Article 2, paragraph 3 of the LPSPS.

RESOLUTION No 315 of 17 September

The BNB decided to supplement the licence granted to BORICA AD to provide payment services under Article 4, second alternative of item 5 of the LPSPS with the payment services under Article 4, items 7 and 8 of the LPSPS.

RESOLUTION No 316 of 17 September

The BNB Governing Council granted a payment institution licence to Iris Solutions OOD to provide payment services under Article 4, items 7 and 8 of the LPSPS.

RESOLUTION No 317 of 17 September

The BNB Governing Council approved the entry of Bulgarian Telecommunications Company EAD into the BNB Register under Article 19 of the LPSPS as a service provider under Article 2, paragraph 4 of the LPSPS.

RESOLUTION No 318 of 17 September

The BNB Governing Council approved the entry of Telenor Bulgaria EAD into the BNB Register under Article 19 of the LPSPS as a service provider under Article 2, paragraph 4 of the LPSPS.

RESOLUTION No 319 of 17 September

The BNB Governing Council approved the entry of A1 Bulgaria EAD into the Register under Article 19 of the LPSPS as a service provider under Article 2, paragraph 4 of the LPSPS.

RESOLUTION No 347 of 15 October

The BNB Governing Council approved the entry of Eco Bulgaria EAD into the Register under Article 19 of the LPSPS as a service provider under Article 2, paragraph 3 of the LPSPS.

RESOLUTION No 348 of 15 October

The BNB Governing Council approved the entry of Motobul EAD into the Register under Article 19 of the LPSPS as a service provider under Article 2, paragraph 3 of the LPSPS.

RESOLUTION No 349 of 15 October

The BNB Governing Council approved the entry of Rompetrol Bulgaria EAD into the Register under Article 19 of the LPSPS as a service provider under Article 2, paragraph 3 of the LPSPS.

RESOLUTION No 350 of 15 October

The BNB Governing Council approved the entry of ZARA-E OOD into the Register under Article 19 of the LPSPS as a service provider under Article 2, paragraph 3 of the LPSPS.

RESOLUTION No 367 of 31 October

The BNB Governing Council approved the entry of NIS Petrol EOOD into the Register under Article 19 of the LPSPS as a service provider under Article 2, paragraph 3 of the LPSPS.

RESOLUTION No 368 of 31 October

The BNB Governing Council approved the entry of Lukoil-Bulgaria EOOD into the Register under Article 19 of the LPSPS as a service provider under Article 2, paragraph 3 of the LPSPS.

***

In 2019 the Governing Council of the BNB took a resolution to refuse issuance of a payment institution licence and six resolutions on imposition of supervisory measures, performed supervisory inspections and other approvals, authorisations and administrative procedure actions.

Circulation of Banknotes and Coins

RESOLUTION No 10 of 24 January

The list of selling prices of Bulgarian coins, issues 1951-2019, was approved.

The list of selling prices of Bulgarian banknotes, issues 1950–2006, was approved.

RESOLUTION No 11 of 24 January

Pursuant to the Law on the BNB Article 26, the BNB Governing Council decided to withdraw from circulation the commemorative coins issued in 2013, which ceased to be legal tender on 8 February 2019.

Commemorative coins issued in 2013 will be exchangeable at BNB tills at nominal value with no limits to amounts and free of charge until 31 December 2020.

RESOLUTION No 53 of 28 February

The BNB Governing Council took note of the availability and developments in the BNB Strategic Stock of Banknotes for 2018.

RESOLUTION No 54 of 28 February

The Governing Council of the BNB decided to put into circulation on 3 June 2019 a silver commemorative coin 'Evlogi and Hristo Georgiev' of the Bulgarian National Revival series.

RESOLUTION No 117 of 28 March

The Governing Council of the BNB adopted Ordinance No 39 on the Nominal Value, Coverage, Form and Design of Banknotes and Coins in Circulation.

RESOLUTION No 136 of 4 April

The silver commemorative coin 'Evlogi and Hristo Georgiev', issue 2019, will be sold at BNB tills at BGN 78.

RESOLUTION No 206 of 13 June

The BNB Governing Council decided to put into circulation on 16 September 2019 a silver commemorative coin '150 Years Bulgarian Academy of Sciences'.

RESOLUTION No 222 of 25 June

The BNB Governing Council adopted the Commemorative Coin and Banknote Production Programme for 2020.

The BNB Governing Council approved a Preliminary Commemorative Coin and Banknote Production Programme for 2021–2022 as a basis for preparing annual programmes.

RESOLUTION No 253 of 25 July

The silver commemorative coin '150 Years Bulgarian Academy of Sciences', issue 2019, will be sold at BNB tills at BGN 78.

RESOLUTION No 254 of 25 July

On 28 October 2019 the BNB put into circulation a silver commemorative coin ‘Dryanovo Monastery’ of the ‘Bulgarian Churches and Monasteries’ series.

RESOLUTION No 255 of 25 July

A list of selling prices of banknotes and coins sold by the BNB at prices other than their nominal value was approved.

RESOLUTION No 256 of 25 July

On 1 November 2019 the BNB put into circulation as legal tender a banknote of BGN 50 nominal value, issue 2019.

RESOLUTION No 307 of 17 September

The silver commemorative coin ‘Dryanovo Monastery’ of the ‘Bulgarian Churches and Monasteries’ series, issue 2019, will be sold at BNB tills at BGN 78.

RESOLUTION No 331 of 3 October

The BNB Governing Council adopted Ordinance No 18 on the Control over Quality of Banknotes and Coins in Cash Circulation.

The BNB Governing Council adopted General Terms and Conditions of the BNB for Providing Test Sets and Samples of Banknotes and Circulation Coins and for Testing of Sorting Machines and Customer Operated Machines, and the Tariff of Rates of the Bulgarian National Bank for Providing Test Sets and Samples of New Issues of Banknotes/Circulation Coins and for Testing of Sorting Machines and Customer Operated Machines.

RESOLUTION No 332 of 3 October

The BNB Governing Council set the final ranking in the anonymous competition for a silver commemorative coin ‘Kukeri’ of the ‘Bulgarian Customs and Traditions’ series and chose the design by Vanya Dimitrova-Hadzhigaeva. It also determined coin specifications.

RESOLUTION No 333 of 3 October

The BNB Governing Council set the final ranking in the anonymous competition for a copper commemorative coin ‘125 Years since the Birth of Geo Milev’ of the Bulgarian Artists series and chose the design by Evgenia Tsankova and Orlin Ivanov. It also determined coin specifications.

RESOLUTION No 382 of 14 November

The BNB Governing Council set the final ranking in the anonymous competition for a gold commemorative coin ‘The Nativity’ of the ‘Bulgarian Iconography’ series and chose the design by Plamen Chernev and Preslav Chernev. It also determined coin specifications.

RESOLUTION No 383 of 14 November

The BNB Governing Council set the final ranking in the anonymous competition for a silver commemorative coin ‘100 Years University of National and World Economy’ and chose the second ranked design by Plamen Chernev. It also determined coin specifications.

RESOLUTION No 396 of 29 November

The BNB Governing Council decided to put into circulation on 6 January 2020 a copper commemorative coin '125 Years since the Birth of Geo Milev' of the Bulgarian Artists series.

RESOLUTION No 422 of 12 December

The copper commemorative coin '125 Years since the Birth of Geo Milev' of the Bulgarian Artists series, issue 2020, will be sold at BNB tills at BGN 24.

RESOLUTION No 444 of 20 December

The BNB Governing Council decided to put into circulation on 20 March 2020 as legal tender a banknote of BGN 20 nominal value, issue 2020.

RESOLUTION No 445 of 20 December

The BNB Governing Council decided to put into circulation on 17 February 2020 a silver commemorative coin 'Kukeri' of the 'Bulgarian Customs and Traditions' series.

Maintaining Banking System Stability and Protecting Depositor Interests

RESOLUTION No 1 of 8 January

The BNB Governing Council decided to sign with the European Central Bank a multilateral agreement on the practical modalities and the terms of information in compliance with Directive (EU) 2015/849 on the prevention of the use of the financial system for the purposes of money laundering or terrorist financing amending Regulation (EU) No 648/2012 of the European Parliament and of the Council, and repealing Directive 2005/60/EC of the European Parliament and of the Council and Commission Directive 2006/70/EC, as amended by Directive (EU) 2018/843 of the European Parliament and of the Council of 30 May 2018 amending Directive (EU) 2015/849 on the prevention of the use of the financial system for the purposes of money laundering or terrorist financing, and amending Directives 2009/138/EC and 2013/36/EU.

RESOLUTION No 12 of 24 January

The Governing Council approved the Draft Joint Decision of the Bulgarian National Bank, the National Bank of Hungary, the National Bank of Romania, the National Bank of Croatia and the National Bank of Slovakia on an assessment of the group recovery plan of the OTP Bank Group.

RESOLUTION No 23 of 7 February

The Governing Council suggests that the BNB starts implementing from 1 January 2019 Guidelines on stress testing of institutions under Articles 108 and 109 of Directive 2013/36/EU (EBA/GL/2018/04) issued by the European Banking Authority and published on its official website.

RESOLUTION No 24 of 7 February

The Governing Council suggests that the BNB starts implementing from 30 June 2019 Guidelines on the management of interest rate risk arising from non-trading book activities (EBA/GL/2018/02) issued by the European Banking Authority and published on its official website.

RESOLUTION No 25 of 7 February

The Governing Council suggests that the BNB starts implementing until the end of the first quarter of 2019 Guidelines on the revised common procedures and methodologies for the supervisory review and evaluation process (SREP) and supervisory stress testing amending EBA/GL/2014/13 of 19 December 2014 issued by the European Banking Authority and published on its official website.

RESOLUTION No 26 of 7 February

The Governing Council approved the Joint Decision of the Bulgarian National Bank and the European Central Bank on determining the adequacy of liquidity and the adequacy of own funds, and the required own funds to be maintained by Eurobank Ergasias S.A.

RESOLUTION No 27 of 7 February

The Governing Council approved the Joint Decision of the Bulgarian National Bank and the European Central Bank on determining the adequacy of liquidity and the adequacy of own funds, and the required own funds to be maintained by Raiffeisen Bank International AG.

RESOLUTION No 28 of 7 February

The Governing Council approved the Joint Decision of the Bulgarian National Bank, the National Bank of Hungary, the National Bank of Romania, the National Bank of Croatia and the National Bank of Slovakia on determining the adequacy of liquidity of OTP Group.

The Governing Council approved the Joint Decision of the Bulgarian National Bank, the National Bank of Hungary, the National Bank of Romania, the National Bank of Croatia and the National Bank of Slovakia on determining the adequacy of own funds and the required own funds to be maintained by OTP Group.

RESOLUTION No 29 of 7 February

The Governing Council approved the Joint Decision of the Bulgarian National Bank, the European Central Bank, the National Bank of the Czech Republic and the National Bank of Hungary on determining of prudential requirements of KBC Group NV.

RESOLUTION No 30 of 7 February

The Governing Council approved the Joint Decision of the Bulgarian National Bank and the European Central Bank on determining the adequacy of liquidity and the adequacy of own funds, and the required own funds to be maintained by UniCredit S.p.A.

RESOLUTION No 31 of 7 February

The Governing Council approved the Joint Decision of the Bulgarian National Bank and the European Central Bank on determining the adequacy of liquidity and the adequacy of own funds, and the required own funds to be maintained by Piraeus Bank S.A.

RESOLUTION No 32 of 7 February

The Governing Council approved the Joint Decision of the Bulgarian National Bank and the European Central Bank on an assessment of the group recovery plan of Piraeus Bank S.A. (as at 30 September 2018).

RESOLUTION No 103 of 28 March

The BNB Governing Council took note of the Report on the State of the Banking System (fourth quarter of 2018).

The BNB Governing Council took note of the publication of Banks in Bulgaria (October–December 2018).

RESOLUTION No 104 of 28 March

The countercyclical capital buffer rate applicable to credit risk exposures in the Republic of Bulgaria was set at 1 per cent, effective as of 1 April 2020.

RESOLUTION No 105 of 28 March

The BNB Governing Council took note of the Supervisory Review of Banks Report as of 31 December 2018.

RESOLUTION No 106 of 28 March

The Governing Council approved the direct acquisition by EUROBANK BULGARIA AD of 99.9819 per cent of PIRAEUS BANK BULGARIA AD paid up equity.

The Governing Council approved the indirect acquisition by EUROBANK ERGASIAS SA of 99.9819 per cent of PIRAEUS BANK BULGARIA AD paid up equity.

RESOLUTION No 108 of 28 March

The Governing Council approved the Joint Decision of the Bulgarian National Bank and the European Central Bank on an assessment of the group recovery plan of Piraeus Bank S.A. (as of 30 September 2018).

RESOLUTION No 109 of 28 March

The Governing Council approved the Joint Decision of the Bulgarian National Bank and the European Central Bank on an assessment of the group recovery plan of Eurobank Ergasias S.A. submitted in September 2018.

RESOLUTION No 110 of 28 March

The Governing Council approved the Draft Joint Decision of the Bulgarian National Bank and the European Central Bank on an assessment of Raiffeisen Bank International group recovery plan.

RESOLUTION No 111 of 28 March

The Governing Council approved the Draft Joint Decision of the Bulgarian National Bank and the German Federal Financial Supervisory Authority (BaFin) on the liquidity adequacy and special liquidity requirements related to liquidity supervision of the ProCredit Group.

RESOLUTION No 112 of 28 March

The Governing Council approved the Draft Joint Decision of the Bulgarian National Bank, the European Central Bank, the Czech National Bank and the National Bank of Hungary on an assessment of KBC Group NV recovery plan (as of 30 September 2018).

RESOLUTION No 113 of 28 March

The BNB Governing Council approved a proposal on amending the Law on Credit Institutions.

RESOLUTION No 132 of 4 April

The Governing Council approved the Draft Joint Decision of the Bulgarian National Bank and the European Central Bank on an assessment of the group recovery plan of UniCredit Group.

RESOLUTION No 148 of 24 April

The Governing Council adopted Ordinance No 20 on the Issuance of Approvals to the Members of the Management Board (Board of Directors) and Supervisory Board of a Credit Institution and Requirements for Performing their Duties.

RESOLUTION No 149 of 24 April

The Governing Council adopted Ordinance No 10 on the Organisation, Governance and Internal Control of Banks.

RESOLUTION No 150 of 24 April

The Governing Council approved Ordinance on Amendment to Ordinance No 4 of the BNB of 21 December 2010 on the Requirements for Remunerations in Banks.

RESOLUTION No 151 of 24 April

The Governing Council adopted Ordinance on Amendment to Ordinance No 7 of the BNB of 24 April 2014 on the Organisation and Risk Management in Banks.

RESOLUTION No 171 of 16 May

The Governing Council suggests that the BNB starts implementing from 1 July 2019 Guidelines on specification of types of exposures to be associated with high risk (EBA/GL/2019/01) issued by the European Banking Authority.

RESOLUTION No 172 of 16 May

The Governing Council suggests that the BNB starts implementing from 20 May 2019 Guidelines on the STS criteria for non-ABCP securitisation (EBA/GL/2018/09) issued in conjunction with Articles 20, 21 and 22 of Regulation (EU) 2017/2402 and published by the European Banking Authority.

RESOLUTION No 173 of 16 May

The Governing Council suggests that the BNB starts implementing from 20 May 2019 Guidelines on the STS criteria for ABCP securitisation (EBA/GL/2018/08) issued in conjunction with Articles 24 and 25 of Regulation (EU) 2017/2402 and published by the European Banking Authority.

RESOLUTION No 193 of 30 May

The Governing Council suggests that the BNB starts implementing from 31 December 2019 Guidelines on disclosure of non-performing and forborne exposures (EBA/GL/2018/10) issued by the European Banking Authority.

RESOLUTION No 194 of 30 May

The Governing Council suggests that the BNB starts implementing from 30 June 2019 Guidelines on management of non-performing and forborne exposures (EBA/GL/2018/06) issued in conjunction with Article 74 of Directive 2013/36/EU by the European Banking Authority.

RESOLUTION No 216 of 25 June

The Governing Council set the countercyclical capital buffer rate applicable to credit risk exposures in the Republic of Bulgaria at 1 per cent for the third quarter of 2020.

RESOLUTION No 217 of 25 June

The BNB Governing Council took note of the Report on the State of the Banking System (first quarter of 2019).

The BNB Governing Council approved the publication of Banks in Bulgaria (January–March 2019).

RESOLUTION No 218 of 25 June

The Governing Council approved the Draft Joint Decision of the Bulgarian National Bank, the National Bank of Hungary and the National Bank of Slovakia supervising OTP Group Plc and its subsidiaries on significant changes to the Advanced Measurement Approach applied at a group level for measuring operational risk.

RESOLUTION No 219 of 25 June

The Governing Council approved the Joint Decision of the Bulgarian National Bank and Bundesanstalt für Finanzdienstleistungsaufsicht, Germany (BaFin) on determining the adequacy of own funds and required own funds to be maintained by ProCredit Holding Group.

RESOLUTION No 260 of 25 July

The Governing Council suggests that the BNB starts implementing from 1 January 2021 Guidelines for the estimation of LGD appropriate for an economic downturn (‘downturn LGD estimation’)(EBA/GL/2019/03) issued by the European Banking Authority and published on its official website.

RESOLUTION No 261

The BNB Governing Council approved the Joint Decision of the Bulgarian National Bank, the European Central Bank, Banca Națională a României, Česká národní banka and Magyar Nemzeti Bank on significant changes in internal validation rules related to the Internal Ratings Based Approach used to calculate capital requirements for credit risk at an individual and group level.

RESOLUTION No 262 of 26 July

The Governing Council suggests that the BNB starts implementing from 30 September 2019 Guidelines on Outsourcing (EBA/GL/2019/02 of 25 February 2019) issued by the European Banking Authority and published on its official website.

RESOLUTION No 311 of 17 September

The Governing Council set the countercyclical capital buffer rate applicable to credit risk exposures in the Republic of Bulgaria at 1 per cent for the fourth quarter of 2020.

RESOLUTION No 312 of 17 September

The BNB Governing Council took note of the Report on the State of the Banking System (second quarter of 2019).

The BNB Governing Council took note of the publication of Banks in Bulgaria (April–June 2019).

RESOLUTION No 342 of 15 October

The systemic risk buffer rate was set at 3 per cent of risk exposures incurred by banks in Bulgaria. Thus established systemic risk buffer is cumulative with the other systemically important institution (O-SII) buffer.

RESOLUTION No 343 of 15 October

The BNB Governing Council designated eight banks as systematically important institutions.

RESOLUTION No 346 of 15 October

The Governing Council approved the transformation of Piraeus Bank Bulgaria AD by its merging into Eurobank Bulgaria AD pursuant to Article 262 of the Law on Commerce.

RESOLUTION No 364 of 31 October

The BNB Governing Council took note of the Supervisory Review of Banks as of 31 March 2019.

RESOLUTION No 398 of 29 November

The Governing Council approved the Joint Decision of the Bulgarian National Bank, the European Central Bank, the National Bank of Italy, the National Bank of Croatia, the Czech National Bank, the National Bank of Hungary, and the National Bank of Romania on determining the adequacy of liquidity, the adequacy of own funds and required own funds to be maintained by UniCredit S.p.A and its subsidiaries.

RESOLUTION No 419 of 12 December

The BNB Governing Council approved the Joint Decision of the Bulgarian National Bank, the European Central Bank, the Czech National Bank and the National Bank of Hungary on determining the adequacy of liquidity, the adequacy of own funds, and required own funds to be maintained by KBC Bank NV and its subsidiaries.

RESOLUTION No 420 of 12 December

The Governing Council approved the Joint Decision of the Bulgarian National Bank, the European Central Bank, the National Bank of Croatia, the National Bank of Hungary, and the National Bank of Romania on determining the adequacy of liquidity, the adequacy of own funds, and required own funds to be maintained by Raiffeisen Bank International AG and its subsidiaries.

RESOLUTION No 438 of 20 December

The countercyclical capital buffer rate applicable to credit risk exposures in the Republic of Bulgaria was set at 1.5 per cent for the first quarter of 2021.

RESOLUTION No 439 of 20 December

The BNB Governing Council took note of the Report on the State of the Banking System (third quarter of 2019).

The BNB Governing Council took note of the publication of Banks in Bulgaria (July–September 2019).

RESOLUTION No 441 of 20 December

The BNB Governing Council approved implementation of Recommendation amending EBA/Rec/2015/01 on the equivalence of confidentiality regimes (EBA/

REC/2015/01) as amended by EBA/REC/2015/02 and EBA/REC/2017/01 issued by the European Banking Authority and published in the national languages of the EU on its official website on 7 August 2018.

RESOLUTION No 442 of 20 December

The Governing Council approved the Joint Decision of the Bulgarian National Bank and the European Central Bank on determining the adequacy of liquidity, the adequacy of own funds and required own funds to be maintained by Eurobank Ergasias S.A. and its subsidiaries.

***

In 2019 the BNB Governing Council adopted:

- 38 resolutions pursuant to Article 11, paragraphs 1 and 3 of the Law on Credit Institutions on approvals for holding a position of a member of a management body of a credit institution;
- 29 resolutions related to supervisory reviews pursuant to Article 79c of the Law on Credit Institutions;
- 20 resolutions pursuant to Article 76, paragraph 4 of the Law on Credit Institutions on coordinating the choice of an auditor of a credit institution;
- 34 resolutions related to the imposition of supervisory measures, performed supervisory inspections and other approvals, authorisations and actions on administrative procedures;
- eight resolutions pursuant to Article 26(2), in conjunction with Article 26(1)(c) of Regulation (EU) No 575/2013 concerning inclusion of credit institution's net profit in Common Equity Tier 1 capital;
- six resolutions under Article 71, paragraph 3 in connection with paragraph 1, item 6 of the Law on Credit Institutions on an approval of amendments to the Articles of Association of a credit institution.

BNB Activities on Resolution of Credit Institutions

RESOLUTION No 7 of 24 January

The Bulgarian National Bank as a resolution authority shall adhere to the following guidelines of the European Banking Authority: Final guidelines concerning the interrelationship between the sequence of write-down and conversion under Directive 2014/59/EU and the Capital Requirements Regulation/Capital Requirements Directive (EBA/GL/2017/02); Final guidelines on the rate of conversion of debt to equity in bail-in (EBA/GL/2017/03); and Final guidelines on the treatment of shareholders in bail-in or the write-down and conversion of capital instruments (EBA/GL/2017/04).

RESOLUTION No 74 of 7 March

The Governing Council of the BNB set the annual banking system contribution to the Bank Resolution Fund for 2019 at BGN 137,257,821.

RESOLUTION No 116 of 28 March

The Governing Council of the BNB adopted a methodology setting out the minimum requirement for own funds and eligible liabilities of credit institutions for which the Bulgarian National Bank is a resolution authority.

RESOLUTION No 135 of 4 April

The Governing Council of the BNB does not object for the National Bank of Serbia as a third-country resolution authority to be invited by the Single Resolution Mechanism to participate as an observer in the resolution college of UniCredit Group.

RESOLUTION No 154 of 24 April

The BNB Governing Council took note of the information provided by the Bulgarian Deposit Insurance Fund on the annual accounts of the Bank Resolution Fund for the year ending 31 December 2018.

RESOLUTION No 155 of 24 April

The BNB set the individual annual contributions of credit institutions and branches of third country credit institutions to the Bank Resolution Fund for 2019.

RESOLUTION No 204 of 13 June

The BNB Governing Council adopted the results of implementation of the methodology setting out critical functions of credit institutions and branches for which the BNB is the group level resolution authority in 2019.

RESOLUTION No 231 of 4 July

The BNB Governing Council took note of the implementation of the methodology setting out the minimum requirement for own funds and eligible liabilities of credit institutions for which the Bulgarian National Bank is a resolution authority with regard to credit institutions which are subsidiary undertakings of EU parent companies within active resolution colleges at an individual level for 2018.

RESOLUTION No 232 of 4 July

The BNB Governing Council does not object with regard to the National Bank of Serbia and the National Bank of Albania in their capacity as third-country resolution authorities to be invited by the Single Resolution Board to participate as observers in the resolution college of Raiffeisen Bank International.

RESOLUTION No 233 of 4 July

The BNB Governing Council took note of the summarised information on resolution colleges and the stage of developing group resolution plans for 2018.

RESOLUTION No 249 of 25 July

The BNB Governing Council took note of the summarised information and analysis on the final draft resolution plan of OTP Group and on the work of resolution colleges of OTP Group in the process of resolution planning in 2018.

The BNB Governing Council adopted a joint decision on a resolution plan and an assessment of resolvability of OTP in 2018.

The BNB Governing Council adopted a joint decision on setting a minimum requirement for own funds and eligible liabilities on a consolidated basis for OTP Group in 2018.

RESOLUTION No 294 of 6 August

The BNB Governing Council approved the results of implementation of the methodology for considering actions on resolution and liquidation under insolvency proceedings of credit institutions for which the BNB is a resolution authority for 2019.

RESOLUTION No 295 of 6 August

The BNB Governing Council took note of the results of implementation of the methodology setting out the minimum requirement for own funds and eligible liabilities of credit institutions for which the Bulgarian National Bank is a resolution authority at an individual level for 2019.

RESOLUTION No 329 of 3 October

The BNB as a resolution authority of credit institutions adheres to the Final Guidelines on the minimum criteria to be fulfilled by a business reorganisation plan (EBA/GL/2015/21).

RESOLUTION No 339 of 15 October

The BNB Governing Council took note of the summarised information and analysis on the final draft resolution plan of Eurobank Ergasias and on the work of the resolution college of Eurobank Ergasias Group in the process of planning the resolution in 2018.

The BNB Governing Council adopted a joint decision on a resolution plan and an assessment of the resolvability of the Eurobank Ergasias Group for 2018.

The BNB Governing Council adopted a joint decision on setting a minimum requirement for own funds and eligible liabilities on a consolidated basis of the Eurobank Ergasias Group and of the Eurobank Cyprus subsidiary on an individual basis for 2018.

RESOLUTION No 365 of 31 October

The BNB Governing Council does nor apply simplified requirements in preparing resolution plans with regard to credit institutions for which the BNB is the resolution authority.

RESOLUTION No 378 of 14 November

The BNB Governing Council took note of the summarised information and analysis on the final draft resolution plan of the KBC Group and on the work of resolution colleges of the KBC Group in the process of planning the resolution in 2018.

The BNB Governing Council adopted a joint decision on a resolution plan and an assessment of resolvability of KBC Group for 2018.

The BNB Governing Council adopted a joint decision on setting a minimum requirement for own funds and eligible liabilities on a consolidated basis for KBC Group NV and on an individual basis in 2018.

RESOLUTION No 379 of 14 November

The BNB Governing Council took note of the summarised information and analysis on the final draft resolution plan of UniCredit Group and on the work of the resolution college of UniCredit Group in the process of planning the resolution in 2018.

The BNB Governing Council adopted a joint decision on a resolution plan and an assessment of the resolvability of UniCredit Group in 2018.

The BNB Governing Council approved a joint decision on setting minimum requirements for own funds and eligible liabilities on a consolidated basis for UniCredit S.p.A and on an individual basis for its subsidiaries in 2018.

The Central Credit Register and the Register of Bank Accounts and Safe Deposit Boxes

RESOLUTION No 13 of 24 January

The Governing Council of the BNB took note of draft amendments to Articles 56 and 56a of the Law on Credit Institutions.

RESOLUTION No 176 of 16 May

The Governing Council of the BNB adopted Ordinance on Amendment to Ordinance No 22 of 16 July 2009 on the Central Credit Register with the notes made thereto.

RESOLUTION No 177 of 16 May

The Governing Council of the BNB adopted Ordinance on Amendment to Ordinance No 12 of 29 September 2016 on the Register of Bank Accounts with the notes made thereto.

RESOLUTION No 424 of 12 December

The BNB Governing Council adopted Ordinance on Amendment to Ordinance No 12 of 29 September 2016 on the Register of Bank Accounts and Safe Deposit Boxes.

RESOLUTION No 425 of 12 December

The BNB Governing Council adopted Ordinance on Amendment to Ordinance No 22 of 16 July 2009 on the Central Credit Register.

Research

RESOLUTION No 34 of 7 February

The BNB Governing Council took note of the assessments of developments in major macroeconomic indicators in the first and second quarters of 2019 along with BNB forecasts of major macroeconomic indicators for 2018–2020 (based on data as of 18 December 2018) to be published in the Economic Review quarterly (issue 4 of 2018).

RESOLUTION No 35 of 7 February

The BNB awarded no master's degree scholarships in 2019.

The BNB awarded two doctor's degree scholarships in 2019.

RESOLUTION No 118 of 28 March

The Governing Council of the BNB took note of the Report on the BNB Research Plan (2017–2018) and the BNB Research Plan (2019–2020).

RESOLUTION No 157 of 24 April

The BNB Governing Council took note of the assessments of developments in major macroeconomic indicators in the second and third quarters of 2019 to be published in the Economic Review quarterly (issue 1 of 2019).

RESOLUTION No 252 of 25 July

The BNB Governing Council took note of the assessments of developments in major macroeconomic indicators in the third and fourth quarters of 2019 along with BNB forecasts of major macroeconomic indicators for 2019–2021 (based on data as of 24 June 2019) to be published in the Economic Review quarterly (issue 2 of 2019).

RESOLUTION No 366 of 31 October

The BNB Governing Council took note of the assessments of developments in major macroeconomic indicators in the fourth quarter of 2019 and first quarter of 2020 to be published in the Economic Review quarterly (issue 3 of 2019).

BNB Internal Audit

RESOLUTION No 224 of 25 June

The Governing Council of the BNB took note of the Chief Auditor's Report on the Activity of the BNB Internal Audit Directorate for 2018.

RESOLUTION No 371 of 31 October

The BNB Governing Council adopted the Annual Plan of the BNB Internal Audit for 2020 and the updated strategy on the activity of the BNB Internal Audit for the period until 2022.

***

In 2019 the BNB Governing Council adopted decisions on internal bank rules of the Bank (nine decisions), representation in general meetings of companies in which the BNB holds participation (nine decisions), public procurements and contracts* (21 decisions) and organisation of bank activities (120 decisions).

---

* Detailed information on procurement procedures is available on the BNB website, About BNB, Public Procurement: http://www.bnb.bg/AboutUs/.

ISSN 2367-492X
ELEMENTS OF THE 2 LEV BANKNOTE, ISSUES 1999 AND 2005, ARE USED IN COVER DESIGN.