

STRATEGY

FOR BULGARIAN NATIONAL BANK

DEVELOPMENT

BETWEEN 2004 AND 2009

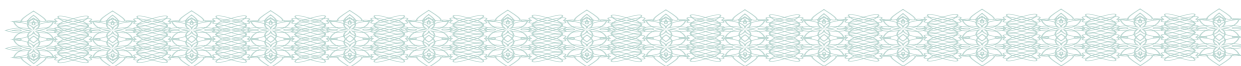




Strategy for Bulgarian National Bank Development between 2004 and 2009



Sofia, September 2004



**BULGARIAN NATIONAL BANK
MANAGEMENT**



**GOVERNING COUNCIL
OF THE
BULGARIAN NATIONAL BANK**

Ivan Iskrov
Governor

Tsvetan Manchev
Deputy Governor

Emilia Milanova
Deputy Governor

Bojidar Kabaktchiev
Deputy Governor

Nikolay Nenovsky

Garabed Minassian

Statty Stattev

Abbreviations

BIS	Bank for International Settlements, Basel, Switzerland
BISERA	Banking Integrated System for Electronic Transfers
BNB	Bulgarian National Bank
BORICA	Banking Organization for Payments Initiated by Cards
CPSS	Committee on Payment and Settlement Systems
EC	European Commission
ECB	European Central Bank
ESCB	European System of Central Banks
EU	European Union
EMU	Economic and Monetary Union
EMV standard	Europay–MasterCard–Visa standard
ERM II	Exchange Rate Mechanism II
IMF	International Monetary Fund
IOSCO	International Organization for Governmental Securities Commissions
IT	information technologies
NCBs	national central banks
RINGS	Real Time Gross Settlement System
SDDS	Special Data Dissemination Standard
TARGET	Trans-European Automated Real-time Gross Settlement Express Transfer



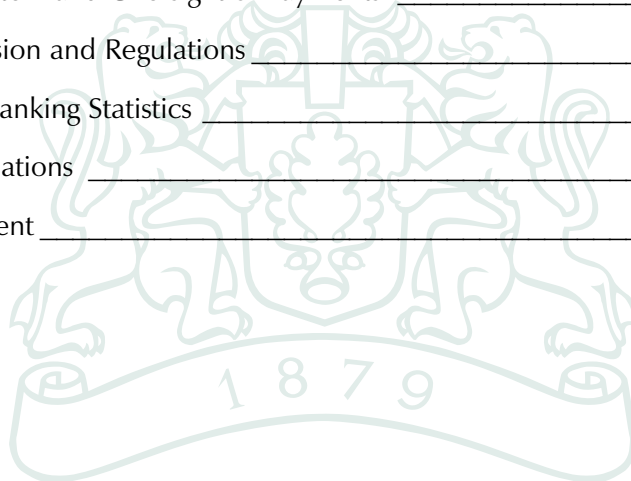
© Bulgarian National Bank, 2004

The contents may be quoted or reproduced without further permission. Due acknowledgment is requested.

Published by the Bulgarian National Bank
 1000 Sofia, 1, Alexander Battenberg Square, Bulgaria
 Telephone (+ 3592) 9145-1656, 1304
 Fax (+ 3592) 980 2425, 980 6493
 Website: www.bnb.bg

Contents

Bulgarian National Bank Management	2
Governing Council of the Bulgarian National Bank	3
I. OBJECTIVES AND TASKS	9
II. FULFILLMENT OF TASKS	12
II. 1. Monetary Policy under a Currency Board	12
II.2. International Reserves	13
II.3. Currency Circulation	14
II.3.1. Banknote and Coin Production	14
II.3.2. Issuing Activity	14
II.4. The Payment System and Oversight of Payments	15
II.5. Banking Supervision and Regulations	16
II. 6. Monetary and Banking Statistics	18
II. 7. International Relations	19
II. 8. Government Agent	20





Bulgaria is facing one of its greatest challenges: the full-fledged membership in the European Union (EU), the Economic and Monetary Union (EMU) and the euro area. The Bulgarian National Bank (BNB) is a public institution playing a key role in the integration process. It has to be successful in joining the European System of Central Banks (ESCB) and the Eurosystem. In response to this challenge, the BNB has proposed a strategy for Bulgarian National Bank development until becoming a member of the euro area. The Strategy presents BNB medium-term objectives and tasks as well as the measures to be initiated for their successful accomplishment.

Bulgaria will become an EU full-fledged member as of 2007. The BNB declares its commitment to act within the current currency board framework until its full euro area and Eurosystem membership. The currency board in Bulgaria complies with the requirements of the European Commission (EC) and the European Central Bank (ECB) for participation in the intermediate stage – the Exchange Rate Mechanism II (ERM II). The BNB supports the view of Bulgaria's joining the ERM II immediately after EU accession, and commits to maintain unilaterally the currency board until euro area accession at the fixed exchange rate of 1.95583 leva per one euro. The BNB will conform to the framework set by the EC and the ECB, which precludes unilateral euroization of an acceding country.

The development and implementation of the Strategy are based on the full awareness of the BNB main strengths and weaknesses, as well as on the challenges related to the ESCB and Eurosystem membership. The Strategy may not detail all functions of the BNB. It should be regarded as an open document, a platform on which other tasks of the accession process would be built up.

The BNB integration into the ESCB is envisaged to take place in an organized and consistent manner. The current period is suitable for postulating and streamlining strategic concepts. It is necessary to identify and eliminate any hindrances for the BNB to participate in the ESCB, first as a member of the General Council, and then as a member of the Governing Council.

An important condition for the implementation of the Strategy is the enforcement of the legislative amendments envisaged in the negotiation process as regards:

- the institutional independence of the BNB;
- the personal independence of the Governing Council members;
- the ban on privileged access of the public sector to BNB financing.

It would be prudent and realistic to have the necessary legislative amendments in effect as early as possible.

The implementation of the Strategy presupposes a continuous dialogue with the public. The BNB regards the legislative amendments increasing its independence as a responsibility to pursue a transparent and consistent policy, and an obligation to report regularly its activities to the public. It is a guarantee that with its increased tasks and responsibilities in the process of Bulgaria's accession to the EU, the EMU, and the euro area, the BNB would be a factor of stability and predictability.

The Strategy envisages improvement of staff effectiveness and professionalism in fulfillment of individual tasks. The BNB membership in the Eurosystem requires an adequate capacity to participate in the euro area's monetary policy formulation and implementation. Until 2009 the BNB will make the most of any opportunity for dialogue and training offered by national central banks (NCBs), the ECB, and other international financial institutions. Bilateral agreements for exchange of researchers and experience with the central banks of the ESCB, as well as for doing joint research will be widely used. On the basis of its comparative advantages, the BNB will

seek the area of its future specialization within the Eurosystem .

The Strategy consists of two sections. The first section includes BNB objectives and tasks, and the second the approaches for fulfilling the objectives and tasks. The tasks related to the BNB supplementary and auxiliary functions are not dealt with, except for its function as an agent of the government (see II.8), because of their lesser importance for the public. The implementation of the Strategy will be reported regularly and, where necessary, additional adjustments and adaptations will be made.



I. OBJECTIVES AND TASKS

The primary objective of the BNB is to maintain price stability (see Chart 1). It is compliant with that of the ESCB. Prior to Bulgaria's membership in the EMU and the euro area, the BNB has to achieve its primary objective by maintaining the fixed exchange rate of the lev to the euro and the banking system stability. Following the introduction of the euro, the BNB primary objective will be achieved through Bank participation in euro area's monetary policy formulation and implementation. The maintenance of the banking system stability is the national central banks' main responsibility and intermediate objective with a view to the sustained role of the banking sector in the process of money supply.

The BNB is pursuing an active policy of communication with the public for elucidating its primary objective, thus ensuring high degree of public confidence. This will help strengthen both the reputation of the institution and the motivation of its staff.

The main BNB tasks include:

- 1) analysis of the financial system, monetary policy formulation and implementation under the existing currency board;
- 2) international reserves management;
- 3) currency circulation management;
- 4) maintenance of secure and efficient payment system and oversight of payments;
- 5) banking supervision and regulations;
- 6) monetary and banking statistics compilation;
- 7) development of international relations.

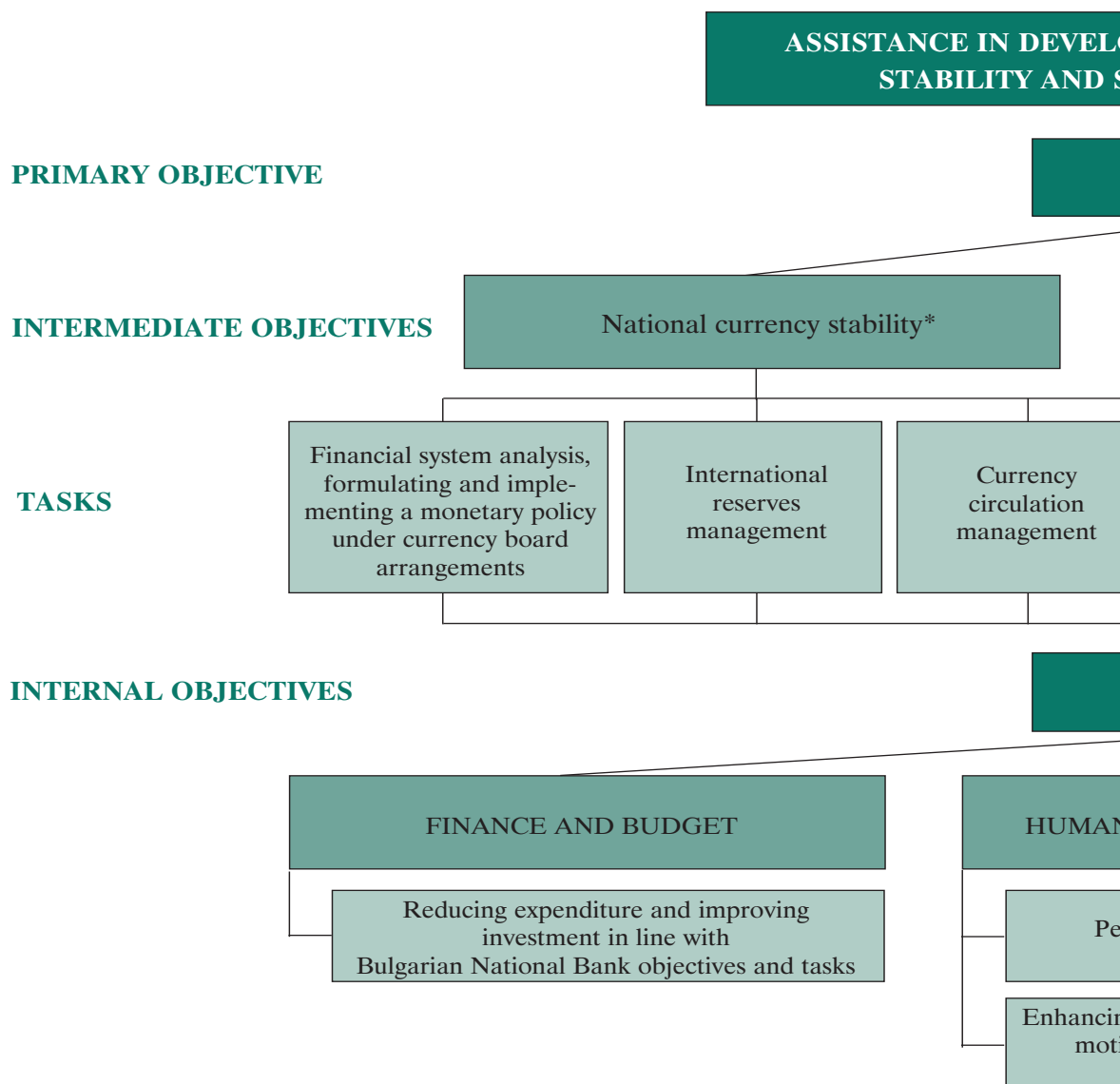
The BNB tasks are in line with the major functions of contemporary central banks. Their fulfillment requires a high degree of internal coordination and unremitting improvement of the Bank's organizational structure with a view to enhancing its effectiveness (see Chart 1).

The fulfillment of BNB primary tasks is of primary importance for achieving its primary objective. Maintaining the stability of the national currency in the period prior to Bulgaria's joining the euro area is its intermediate objective and a tool for achieving price stability given the currency board specificity. Attaining the primary objective, which is also an accession criterion, will guarantee Bulgaria's membership in the euro area. After joining the euro area and the Eurosystem, the focus of the BNB monetary policy will shift from the intermediate objective of national currency stability to price stability maintained by managing the ECB short-term interest rate.

Banking system stability prior to and after euro area membership will be maintained by improved banking regulations and payment system in accordance with the recommended international standards and practices, effective banking supervision and oversight of the payment system. Following the euro introduction, the interdependence between intermediate objectives will grow and the BNB will face the challenge of mastering the art of the 'new' monetary policy.

The good contacts and constructive relations between the BNB and the banking community are a prerequisite for effective supervision, proper payment system operation and monetary policy implementation. They may be developed by regular or extraordinary *ad-hoc* committees on a technical level and by a top management commit-

OBJECTIVES AND TASKS OF THE BULGARIAN NATIONAL BANK



* Until 2007 and in the course of ERM II



OF THE BULGARIAN NATIONAL BANK

DEVELOPING AND IMPLEMENTING A POLICY OF SUSTAINABLE ECONOMIC GROWTH

PRICE STABILITY

Banking system stability

Maintenance of a
secure and effective
payment
system

Banking
supervision and
regulations

Monetary and
banking statistics
compilation

Development of
international
relations

EFFECTIVENESS

PERSONNEL RESOURCES MANAGEMENT

Performance-based remuneration
of the staff

Increasing the degree of flexibility and training
motivation, professional development
based on team work

STRUCTURE AND ORGANIZATION

Reducing auxiliary and
supplementary activities

Introducing latest technologies and
methods of work organization

Maintaining a simplified hierarchical and
horizontal organizational structure

Providing modern IT infrastructure
of the Bulgarian National Bank

Chart 1

tee chaired by the BNB Governor. The BNB declares its willingness to work out consistent and transparent requirements to commercial banks. These interrelations are based on a stable and representative associative structure of commercial banks. The BNB actions are motivated not only by its position in the banking sector, but also by its responsibility in the broader context of integration into the EU.

The BNB attributes great importance to coordination in implementing its major tasks. The BNB internal objectives are related to the improvement of the effectiveness of its organizational structure, its staff, its own budget and the management of its tangible assets. The ability of establishing a market for particular activities, which has been considered only a central bank competence until recently, is being carefully considered, studied and analyzed by the BNB. The results from the analyses are being discussed on a work basis with the banking community and the interested agents in search of efficient and balanced solutions.

Improving the BNB effectiveness in offering services and achieving its main objectives goes through a process of simplifying and streamlining its organizational structure, introducing latest technologies and methods for work organization, and providing a modern IT and accounting infrastructure. This objective is of primary significance as regards allocation of costs. In the budgeting and finance area, the BNB makes efforts to achieve the recommended ESCB standards for reducing expenses and their distribution between core, auxiliary and supplementary activities.

The BNB involves itself in ensuring adequate staff qualification in compliance with its objectives and tasks. It will be achieved through:

- performance-based remuneration of the staff, and
- enhancing the degree of flexibility and training motivation, and professional development.

Eurosystem membership presupposes and requires an updated:

- institutional and hierarchical organization of the BNB;
- structure and qualities of the staff;
- technological platform of major systems: *inter alia*, information, accounting, statistical, communication.

Improvement of the institution's effectiveness is achieved through:

- change management;
- introducing project-management and teamwork;
- implementing a rule-based system for evaluation and remuneration of individuals' contribution;
- consistent staff training and carrier management;
- stimulating work environment and an adequate social climate for fulfillment of objectives and tasks.

II. FULFILLMENT OF TASKS

II. 1. Monetary Policy under a Currency Board

The political choice of maintaining a currency board until joining the euro area predetermines the solution of a number of strategic issues on the economic (including monetary) policy and the internal objectives of the BNB. Its clear rules do not exclude the need of institution's preparation to participate in monetary policy formulation and implementation after euro area membership. With that end in view, the BNB will ensure:

- adequately qualified staff to participate in the common monetary policy formulation and implementation;
- daily evaluation of banking system liquidity and of the factors for banking system liquidity management;
- training of employees for implementing the ESCB operational framework with regard to actions ensuring banking system liquidity;
- preparing information infrastructure and interface together with commercial banks to ensure interbank market transparency and implementation of market operations in an on-line mode, including the ones dealing with collateral.

The preparation of a medium-term plan and organizational structure to be used after joining the euro area is underway. This includes active cooperation with the NCBs members of the ESCB. After EU accession contacts with commercial banks aiming at joint practical measures will be intensified. Bilateral agreements with NCBs for training of experts, who will be prepared to become members of the ECB committees, will be concluded.

The result from the preparation is:

- establishment and adequate functioning of a BNB Monetary Policy Committee;
- a qualified team of economists serving the Monetary Policy Committee in making macroeconomic analyses and short- and long-term evaluations and forecasts for the effects of the ECB monetary policy on the Bulgarian and euro area economies.

The BNB strengthens its potential for analyses and forecasts of the processes and trends in the development of the national economy, for evaluation of the external environment and economic policy influence, including the EU general economic policy, focusing its research on the set of factors and measures which affect inflation processes. This will guarantee integration into the first pillar of the ESCB monetary policy. Research on the interrelation of monetary and lending processes, and price stability constitute the core of the BNB analytical and forecasting activities. Developing adequate estimations of the monetary policy transmission mechanism through the banking system will guarantee integration into the second pillar of the ESCB monetary policy.

II.2. International Reserves

International reserves management will continue to be a main task of the BNB, even after the accession to the euro area. The Bulgarian National Bank will be also responsible for the operational management of that portion of its international reserves which is deposited with the ECB. It is important to maintain and increase the analytical potential of the units responsible for reserve strategic assets allocation and operational management. In many national central banks, members of the Eurosystem, own reserves and those deposited with the ECB are managed by the same team and under the same rules. The BNB will follow this principle.

The creation of an adequate capacity of international reserves management is also partly a matter of knowing practices and developments in the international financial markets. This suggests concluding agreements for exchange of portfolio managers under mutually beneficial conditions with the national central banks and international financial institutions, and in case of interest, with some experienced transnational commercial banks. The volume of BNB international reserves as of 2004 and the expectations for their dynamics in the coming years until the acces-

sion to the ESCB do not involve hiring of private financial institutions as external managers. By 2007, the BNB will establish a backup center as part of the security system of its activities and limitation of risks.

Transparency of international reserves management deserves special attention. The ESCB rules of international reserves management rule out a high level of transparency in view of preserving the efficiency in operation on international markets, whose participants are not so transparent as central banks themselves. The operational efficiency of the monetary policy requires reasonable limitation of transparency of operations but not in terms of accountability.

In seeking and finding the right balance, the BNB will further improve internal rules and procedures for international reserves management, and will disclose publicly that portion of them which is in compliance with the effective legal provisions regarding confidentiality of professional, banking, and commercial secret. The BNB regularly informs the public about the employed models of strategic allocation of international reserves and the maximum risk it undertakes in the process of operational management. The expected result involves guaranteeing security, liquidity and profitability in minimizing risks, as well as limiting political speculations.

II.3. Currency Circulation

II.3.1. Banknote and Coin Production

Until the accession to the euro area, the BNB is the only issuing institution on the territory of the Republic of Bulgaria. The Bank organizes, controls and reports banknote and coin production. Upon acceding the Eurosystem, the national central banks have the right to:

- independently produce their own *quota* of euro banknotes and coins;
- supply their *quota* by means of a purchase from other licensed printing works and mints.

In the event of placing the production of euro banknotes on a competitive instead of on a quota principle, the BNB will seek opportunities for realizing the competitive advantages of its enterprises. The high technological level and capacity of the BNB Printing Works EAD and the recognized name of the Mint EOOD on the European market are important prerequisites for their licensing by the ECB. The BNB makes efforts to strengthen the enterprise management. This will guarantee maintaining a high technological level by means of long-term planning and prudent investments with a view to adapting the production and security to ECB requirements without breaching the EU directives for state aids. Euro banknote and coin production requires enhancing the capacity of the Bank and its subsidiaries, especially in studying and analyzing the trends in EU banknote and coin production: *inter alia* technology and equipment, inputs, design, security features, costs. Extended partnership between the BNB enterprises and banknote and coin producing companies of good reputation on the European market will be sought.

II.3.2. Issuing Activity

The BNB objective in currency circulation management is ensuring purity, security and efficiency of cash operations aligned with regulations and decisions of the ECB. Comparative analyses of these indicators in Bulgaria and the euro area and the trends until 2009 show that significant investment is required from the BNB and the Bulgarian banking system in order to achieve the minimum requirements. Building a modern cash center of the BNB is both the first important step and the best solution from a technological point of view.

Reaching an agreement with commercial banks and their active participation in the reorganization of currency distribution is the second required step. The ECB has developed and the national central banks apply a standard of minimum free services offered by them. The BNB complies with this standard which requires withdrawal from some niches which are serviced by it presently.

The bulk of cash distribution starting from 2007 will be organized on a market principle. Distribution, processing, keeping and destruction of banknotes and coins jointly with commercial banks will minimize overall investment and guarantee smooth changeover consistent with the ECB standards. This organization of the currency circulation gives comparative advantages to Bulgaria after accession of the other Balkan countries to the euro area.

II.4. The Payment System and Oversight of Payments

The BNB key objective in developing the national payment system is mitigating systemic risk and preparing the integration into the payment system of the euro area. This objective will be achieved primarily through:

- maintaining a stable, secure, reliable and effective national payment system;
- maintaining a clearly defined legal framework;
- effective oversight of payment systems;
- ensuring full compliance with the basic principles of the systemically important payment systems and recommendations of the Bank for International Settlements (BIS), Basel, and the ECB;
- maintaining close coordination and cooperation with the national and international institutions involved in the payment process.

The BNB ensures secure, reliable, and effective national payment system based on a permanent dialogue with the participants and regular contacts with the ECB and BIS, Basel. The operation of the Payment System Committee at the BNB, a coordination and consultation body governing the payment system development, has a special importance for the payment system operation. A backup center of operation in case of emergency will be built in order to ensure system security.

The BNB is responsible not only for operating RINGS, but also for all other elements of Bulgaria's payment system. The Bank ensures permanent training and qualification of the staff as a binding condition for maintaining and developing high technological and dynamic activities.

A clearly defined legal framework is ensured by the Law on money transfers, electronic payment instruments and payment systems. This Law helps harmonize the legal framework of operation and oversight of the national payment system with the EU directives. The Law provides for:

- the payments on the territory of the Republic of Bulgaria;
- cross-border transfers;
- issuance and use of electronic payment instruments;
- establishment and operation of payment systems;
- the oversight of the payment systems and operations;
- payment systems-related dispute settlement.

Oversight of payment systems is a new activity for central banks. It suggests creating and improving methodology, as well as maintaining database for all-time monitoring of the systems included in the national payment system. BNB analytical units evaluate compatibility of the national payment system with the principles and standards of the ECB and BIS, Basel. On this basis recommendations for improving

the operation of the national payment system are prepared.

Full compliance with the principles of the payment systems and recommendations of BIS, Basel, and the ECB is achieved by:

- maintaining regular contacts with the respective international organizations;
- strengthening and further developing the payment system oversight and periodic improvement of the payment system parameters, and updating the regulatory framework.

The BNB is preparing the national payment system for its integration into the payment system of the euro area. The BNB provides staffing, technical and infrastructure support to the national payment system. Depending on the views about the development of TARGET, the ECB payment system, ways are explored for joining a common platform, as this option is seen as the most efficient for Bulgaria.

As regards the individual elements included in the national payment system, the following policy is pursued by the BNB:

- promoting the development and improving all systems: RINGS, BISERA, BORICA, the Central Depository, the system of servicing payments on government securities transactions;
- finalizing the privatization procedure of BORICA EOOD;
- continuing work related to development of the Electronic Budget Payments System (SEBRA) with a view to making it fully compliant with the new structure and organization of the EU payment system.

In 2005 the card payments will ensure the implementation of the EMV standard, which will enhance the security of card payments. For this purpose a National Committee has been established.

II.5. Banking Supervision and Regulations

Banking supervision is another significant function of the BNB which exerts direct influence for achieving the primary and intermediate objectives. The BNB preserves its supervisory function with a view to guaranteeing financial stability. The Bank ensures concurrently a high degree of independence, as well as staffing and resource provision of the banking supervision. In the financial system of the Republic of Bulgaria dominated by the banking sector, the link of the supervisory function with the other BNB functions is much stronger than with other regulators. Banking supervision position is predetermined by the ECB recommendation for keeping the tie between the supervisory function of the banking sector, on the one hand, and the quality and efficiency of the monetary policy and control over implementation of the decisions in this area, on the other hand.

The BNB performs its supervisory function directing its efforts mainly to:

- 1) preparing and enforcing the European banking legislation;
- 2) maintaining a high degree of stability of the banking system adequate to strengthening bank intermediation and free competition with the EU monetary financial institutions.

Efforts in these directions involve achieving short-term, medium-term and long-term objectives.

Full harmonization of the Bulgarian banking legislation with the EU banking directives is an intermediate objective of the EU integration in the supervision area. An updated Law on Banks is underway along with the relevant supervision regulations. For this purpose the BNB:

- collaborates actively with the National Assembly and the Government, and in the area of its competence implements the major portion of expert work;

- maintains operational cooperation with the national central banks and supervisory bodies from the EU countries in relation to the treatment and enactment of the European directives;

- trains experts for contacts with the EC and ECB banking committees.

An important objective in the pre-accession period which needs to be basically attained in 2004 in keeping with the official commitments of Bulgaria in the negotiation process is the implementation of the EU directives on the market risk.

The BNB will:

- continue training bank supervision experts in the content and manners of implementing EU directives on market risks;

- complete the work on a supervision regulation and the supporting reporting;

- set up a specialized unit for market risk evaluation.

Prior to the introduction of the regulation on the capital treatment of market risks, the BNB intends to hold discussions with commercial banks' representatives on its implementation. To this end, the central bank also plans to arrange training for bank experts about the manner and forms of market risk reporting.

In terms of harmonizing the Bulgarian banking legislation with the EU legislation, the implementation of the future directive whereby the EU will adopt the New Capital Accord of the Basel Committee is a BNB medium-term objective.

The BNB will:

- continue training bank supervision experts in the content of the Accord;

- carry out current analyses on the results of implementing the new capital standards and will participate in the quantitative research of the Basel Committee, the EU and other organizations;

- prepare legal and regulatory texts which will create the legal framework for the implementation of the New Capital Accord;

- adjust supervisory reporting systems;

- require from commercial banks to design programs for staff, technical and procedural support.

Maintaining a high degree of banking system stability adequate to the increasing bank intermediation and free competition with EU credit institutions is the second direction of strategic importance for banking supervision. The efforts are concentrated in accomplishing several major tasks. Effective supervision over commercial bank lending activities is a BNB priority objective. To this end, efforts will be made to set up new examination teams in order to streamline supervisory examination procedures, to improve the methodology and techniques of the Early Warning System. In order to sustain the control over the quality of bank lending, the BNB will revise the rules on credit risk evaluation.

Maintaining high transparency of shareholders' capital as a prerequisite for banking system stability is BNB all-time supervisory objective. In order to achieve it the BNB will continue to strengthen the publicity requirements for banks' shareholders, will study and analyze in detail all information received with regard to any bank shareholder of scale and will remove, where needed, the unsuitable investors of unproven qualities and suspicious origin of funds.

To keep up with market developments the BNB is building a capacity for on-site supervisory examinations in foreign bank branches and subsidiaries of local banks abroad. This will acquire increasing significance with the expansion of credit institutions abroad. BNB efforts are aimed at developing and adopting procedures for foreign examinations, at setting up a specialized team and starting regular examinations.

Supervisory cooperation, particularly in the form of bilateral agreements with

foreign supervisory bodies, plays an important role in ensuring effective banking supervision and maintaining stability of a banking system dominated by foreign banks. Expansion of supervisory cooperation will remain a BNB objective until Bulgaria's membership in the EU. By 2004 the BNB has ten bilateral agreements concluded. New agreements in the future will be signed with countries whose banks are represented on the Bulgarian market or where local banks operate.

Another all-time BNB objective concerning overall stability, involves intensive collaboration with local administrative bodies related to supervisory activity. The BNB will strive to improve the information exchange and coordination with the Financial Supervision Commission, the Financial Intelligence Agency and the Bank Deposit Insurance Fund. Being aware of the importance of timely response, the BNB, based on the supervisory analyses, participates actively in the work of the Financial Stability Council.

II. 6. Monetary and Banking Statistics

An important objective until end-2006 is to have the monetary and banking statistics, the balance of payments and external debt statistics developed and disseminated by the BNB fully compliant with EU standards, thus contributing to fulfillment of the central bank's commitment under Negotiation Chapter 12 Statistics. After EU accession, any further development and improvement of statistics at the BNB will be aimed at facilitating more speedy accession to the euro area. This will be BNB contribution to the uniform statistical activities of the ECB and Eurostat.

Another important objective of statistics is to ensure the preparation and support of the necessary database and metadata for Bulgaria's participation in the Special Data Dissemination Standard (SDDS) developed by the IMF. Realization of this objective requires adequately qualified statisticians to meet the forthcoming significant changes in approaches and methodology.

In the area of monetary and banking statistics, the BNB continues to implement consistently the requirements of the ECB and IMF. The implementation of a new input system of indicators for compiling monetary statistics, which replaced the so-called trial balance sheets in the BNB and commercial banks, has been finished. The new system complies with ECB requirements for processed data in terms of breakdown by institutional sector, financial instrument, maturity and currency. The implementation of the new system also reflects the changeover by banks to individual chart of accounts associated with the adoption of the international accounting standards. The introduction of the new input system is also intended to further improve the system of output indicators.

In addition to the existing monetary statistics reflecting the state of individual indicators at a particular moment in time, statistics of flows will also be developed and implemented. Seasonal adjustments of some monetary and banking statistical indicators will be also initiated and the monetary survey will be supplemented by short analyses. Further development of interest rate statistics will be intended to fully comply with ECB requirements. The interest rate statistics will be further supplemented by interest rate data on balances, new types of interest rates and instruments. Within the step-by-step introduction of the European System of Accounts (1995 revision), the scope of currently compiled monetary statistics needs to be extended by including statistics on nonbank financial institutions, some of which are currently included in the Financial Corporations institutional sector.

Monetary statistics plays a decisive role in preparing annual and quarterly sectoral financial accounts, which in turn, constitute a part of statistical macroeconomic infor-

mation prepared by the ECB for euro area countries.

In the process of Bulgaria's accession into the EU, the BNB will continue to improve the information exchange with the ECB in the area of monetary and interest rate statistics, and after the EU accession, the central bank will participate in the uniform statistical activities under ECB guidance.

In the area of external sector statistics, the BNB continues the harmonization with the requirements of Eurostat, the ECB, and the IMF. Developments in this area are based on the latest amendments to the Foreign Exchange Law, which significantly improve the legal framework for the compilation of the balance of payments statistics. In the 2004–2006 period, the balance of payments compilation system will be gradually adjusted aiming at full compliance with all European standards by the time of Bulgaria's accession to the EU. The main areas of improvement of the balance of payments compilation methodology include services (2004), direct investments (2005) and portfolio investments (2006).

There are two main approaches to be implemented in parallel. The first includes the development of a BNB system for reporting individual bank transactions with the rest of the world. It will help considerably improve the quality and the scope of the balance of payments statistics. The second approach involves the use of direct methods for collecting the balance of payments data from the real sector. The legal basis for its application is provided for by the amendments to the Foreign Exchange Law. Direct methods are to be applied primarily in reporting direct and portfolio investments and to complement the system of electronic data processing system by individual transaction. The compilation of the balance of payments will expand with the seasonal adjustment of time series, and the analysis of external sector dynamics. In the process of Bulgaria's accession to the EU, the BNB will continue to take part in and improve the information exchange with the ECB and Eurostat in the area of the balance of payments statistics, and after the EU accession, it will participate in the uniform statistical activities under the guidance of the ECB and Eurostat.

BNB experts will continue to participate in the work on compiling the financial account. The financial and external sector statistics, which is being developed at the BNB, is the information basis for compiling the financial account and facilitate its consistency within the whole system of national accounts.

II. 7. International Relations

European integration and international cooperation pervade almost every area of BNB activities and determine to a great extent both its primary objective and intermediate objectives, and tasks. In line with the Strategy the BNB will approve an action plan on European integration, which will contain the activities with their description and timing that will be necessary for the successful integration of the BNB into the ESCB, and of the Bulgarian banking and financial system into the EU. It will be implemented through consistent and coordinated contacts with the ECB itself, and bilateral agreements with individual national central banks of EU member states. Strategic objectives in the area of eurointegration involve:

- ensuring compliance of the structure and functions of individual BNB units with those in place in the ECB committees and the euro area;
- establishing and training a coordination unit to prepare BNB participation in various ECB committees and the euro area. In addition to the standing coordination unit, if required, all BNB representatives in ESCB committees will gather periodically, so that the top management is acquainted in a timely manner about any key

issues.

- getting acquainted with the approaches and methods of operation at the ECB and ESCB;
- ensuring effective internal information exchange in the preparation and participation in the ECB committees and consistency in the positions taken according to the rules of the Eurosystem .

Starting the operation of the coordination unit organizing relations with the ECB (and with other EU institutions) will require investment in:

- selecting and training highly qualified staff to assume the future responsibilities in ESCB committees;
- equipment and technologies.

II. 8. Government Agent

The BNB performs agency functions for the government, and acts as a government securities depository and government debt agent. The successful performance of these functions entails development and improvement of all information systems. The terms and conditions for rendering such services are determined after negotiations and in coordination with the Ministry of Finance. In accordance with the Government Debt Management Strategy, the central bank and the Ministry of Finance have agreed upon developing domestic debt registration and servicing systems at the BNB in the short run through:

- improving communications with government securities market participants in accordance with the international procedures and standards, including implementation of SWIFT and other alternative technical means of communication;
- modernizing the Computerized Book-Entry System for Registration of and Trade in Government Securities, which will allow to streamline the auction process and implement straight-through processing of government securities transactions. This will ensure a more efficient regulation and control over the secondary government securities market operation and enhancing its liquidity.

With the improvement of the infrastructure servicing the government securities market, and in relation to Bulgaria's accession to the EU in the period until 2007, the recommendations and standards applicable to the systems for registration and settlement of government securities transactions developed and adopted by CPSS and IOSCO will be phased in. The EU directives on settlement finality and on the agreements for financial collateral will be implemented in parallel.

This will ensure better efficiency and transparency of the government securities market, more comprehensive protection of investors' interests and minimization of risks in the government securities settlement system.

The changes in the government debt servicing infrastructure will be done by gradually redistributing the functions agreed between the Ministry of Finance and the BNB, in coordination with government securities market participants and after consultations with EU representatives.

Adopted by the Governing Council of the Bulgarian National Bank by Resolution No.103 of 9 September 2004.