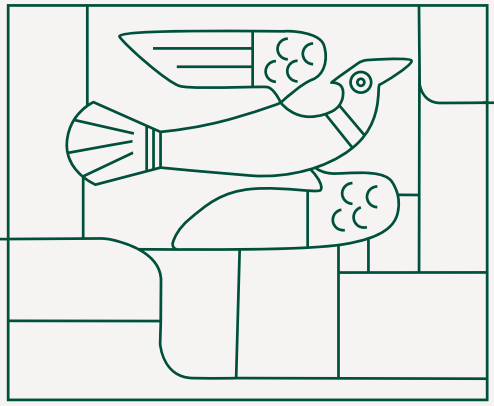
BULGARIAN NATIONAL BANK
EUROSYSTEM

Topical Research and Highlights

Analysis of the Initial Effects of the Monetary Regime Change in Bulgaria on the Banking Sector

Published as Part of ‘Economic Review’
Issue 1/2026



Analysis of the Initial Effects of the Monetary Regime Change in Bulgaria on the Banking Sector

With Bulgaria's accession to the euro area from the beginning of 2026, the currency board regime, in force from July 1997 to the end of 2025, was terminated. This topical research aims to analyse the initial effects on the banking sector in Bulgaria of the new monetary regime operating in Bulgaria after the BNB's accession to the Eurosystem in the beginning of 2026.

Key Features of the Currency Board Which Functioned until the End of 2025 and of the New Monetary Regime from the Beginning of 2026

Under the currency board in Bulgaria, the Bulgarian National Bank's primary objective of maintaining price stability was achieved through ensuring the stability of the national currency. The functioning of the currency board in Bulgaria was based on three fundamental principles: (1) a fixed exchange rate of the lev to the euro; (2) full coverage of the total amount of BNB monetary liabilities by high-liquid foreign reserves[1]; (3) the central bank's obligation to unconditionally and irrevocably sell and purchase levs against the reserve currency (euro) at the exchange rate fixed by the Law on the BNB. In accordance with these principles, the national currency was issued solely against providing reserve currency at the fixed exchange rate, as a result of which an automatic mechanism of balancing national currency demand and supply was guaranteed.[2]

Under the currency board arrangement, in force until the end of 2025, BNB's functions in relation to conducting monetary policy were limited. The BNB did not execute open market operations nor did it set the main policy rate.

Under this monetary regime, the BNB's main instrument for influencing the monetary conditions in Bulgaria was the regulation of minimum required reserves for commercial banks, with this instrument allowing the provision or withdrawal of liquidity from the banking system depending on the specific macroeconomic conditions. The second instrument the BNB could use in order to affect monetary conditions was the interest rate on excess reserves of commercial banks maintained at the central bank. The BNB could also indirectly influence monetary conditions in Bulgaria through the implementation of supervisory and macroprudential measures, but the primary objective of supervisory and macroprudential policy is building of buffers and improving the quality of banking system assets with a view to safeguarding financial stability rather than having a direct effect on monetary conditions.

With Bulgaria's accession to the euro area, the BNB's primary objective of maintaining price stability is preserved, and this objective is already achieved through the full involvement of the central bank in the formulation and implementation of the Eurosystem's monetary policy.[3] The principle of the Eurosystem functioning is limited to centralised decision-making on common monetary policy by the Governing Council of the European Central Bank (ECB) and decentralised implementation of this policy by the national central banks of euro area Member States.

The definition and implementation of the Eurosystem's monetary policy are provided for in its strategic and operational frameworks. The strategic framework defines the monetary policy objective–maintaining price stability in the euro area. According to the ECB's current monetary policy strategy, the quantitative definition of the price stability objective is to maintain inflation at 2 per cent in the medium term.[4] The operational framework includes the common rules for Eurosystem's monetary policy instruments and procedures, through which decisions of the ECB Governing Council concerning the monetary policy conduct in the euro area are implemented in

[1] Unlike the traditional currency board, which usually provides coverage only for banknotes and coins, the currency board in Bulgaria provided coverage for all BNB's monetary liabilities, including banknotes and coins in circulation, liabilities to banks, liabilities to the government and budget organisations, and liabilities to other depositors.

[2] For more information on the principles of operation of the currency board, see the highlight entitled *The Principles of Operation of the Currency Board in Bulgaria*, Economic Review, Issue 1/2009.

[3] The Eurosystem comprises the European Central Bank and the national central banks of the Member States whose currency is the euro.

[4] The ECB Governing Council considers the 2 per cent inflation target in the medium term to be symmetric, meaning that deviations both above and below 2 per cent are regarded as equally undesirable.

a decentralised manner but under uniform conditions in all Member States. It aims to steer short-term money market interest rates so that they follow policy rates.

Eurosystem's monetary policy instruments can be divided into standard and non-standard. Standard instruments through which the ECB influences short-term money market rates and manages liquidity of the euro area banking system include open market operations, standing facilities and minimum reserve requirements. Open market operations are used to provide or absorb liquidity from the banking system of the euro area with the aim of steering short-term money market rates, managing liquidity and signalling the Eurosystem's monetary policy stance. These operations are classified into four categories: main refinancing operations (the most important monetary policy instrument for managing money markets), longer-term refinancing operations, fine-tuning operations and structural operations. Standing facilities (the deposit facility and the marginal lending facility) are used to provide or absorb overnight liquidity from the banking system, signal the monetary policy stance, and set the limits (a ceiling and a floor) for overnight interest rates. The minimum reserve requirement instrument requires credit institutions to hold a certain portion of their attracted funds with the central banks without being able to use them for other purposes, with the MRR rate standing at 1 per cent since 2012. Non-standard monetary policy instruments aim to help improve the monetary policy transmission and include instruments, such as asset purchase programmes, forward guidance, and targeted longer-term refinancing programmes for banks.

With Bulgaria's accession to the euro area, the BNB assumes the obligation to implement the common monetary policy of the Eurosystem. Hence, the BNB no longer has discretion to determine the reserve base for the MRR, the MRR rate and the interest rate on banks' excess reserves. Concurrently, the change in the monetary regime did not trigger a fundamental change in the method of determining monetary conditions in Bulgaria. Within the currency board framework where the lev was fixed to the euro, amid strong Bulgaria's financial and economic integration with euro area countries, the effects of euro area monetary policy spilled over to the Bulgarian economy. Major factors historically affecting the degree to which monetary conditions in the euro area were transmitted to monetary conditions in Bulgaria were related to the level of banking system liquidity, the assessment of borrower risk premium and of the country as a whole, as well as banks' risk appetite. Bulgaria's entry into the euro area is a prerequisite for the transmission of Eurosystem's monetary policy to Bulgaria's financial and economic conditions to become more direct and gradually strengthen, reflecting the direct implementation of the Eurosystem's monetary policy instruments in Bulgaria. The BNB, in turn, retains the possibility to use the set of macroprudential instruments, with their main objective remaining the maintenance of the banking system stability in Bulgaria.

Initial Effects of the Monetary Regime Change in Bulgaria on the Banking Sector

Minimum Reserves of Commercial Banks at the BNB

The MRR amount to be held by commercial banks at the central bank is determined based on the reserve base and the MRR rate. Under the currency board regime in Bulgaria, the BNB used the MRR mainly as a tool for maintaining precautionary liquidity buffers in the banking system due to its limited role as a lender of last resort. At the same time, the BNB made several changes to the scope of the reserve base and the minimum reserve rate in order to pursue counter-cyclical monetary policy and manage liquidity in the banking system.

Just before Bulgaria's accession to the euro area, the MRR rate was 12 per cent, applied to funds attracted by banks from residents and non-residents (excluding funds attracted from central and local government budgets), with 50 per cent of banks' cash balances being accepted also as minimum reserves. No distinction was made for funds attracted by banks across term and initial maturity. By end-2025, the effective minimum reserve rate was 11.77 per cent and banks' minimum required reserves amounted to EUR 10.1 billion (BGN 19.7 billion), which were remunerated by the BNB at 0 per cent. Strong growth of private sector deposits amid rising labour income and limited low-risk investment alternatives contributed to the high amount of banks' minimum required reserves at the BNB in the years prior to Bulgaria's accession to the euro area.

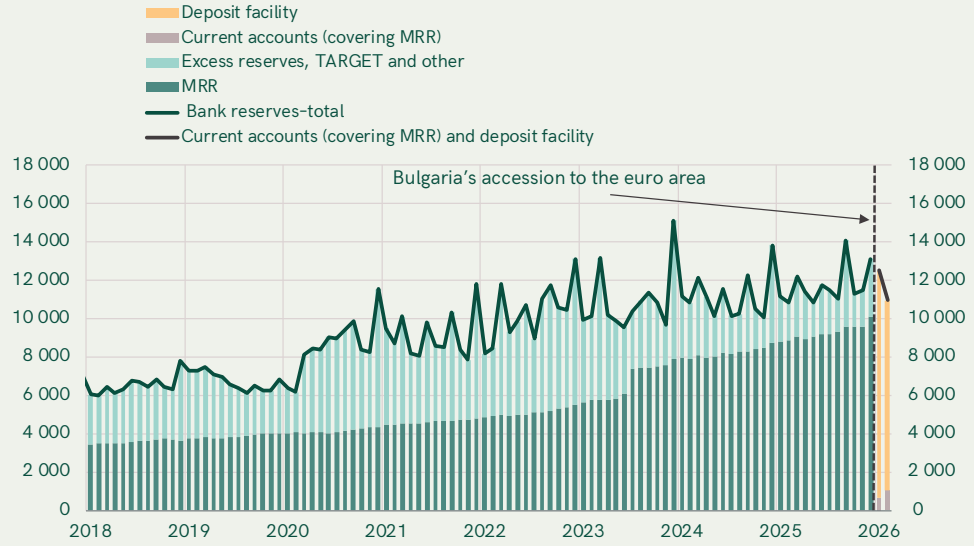
With the accession to the common monetary union, Bulgaria became subject to the common rules in the euro area, involving a change in the applicable MRR rate, maintenance periods and the reserve base scope. As required by Regulation (EU) 2021/378 of the ECB of 22 January 2021,[5] the reserve base includes deposits and debt securities issued. A zero per cent rate is applied to deposits with an agreed maturity of over two years, deposits redeemable at notice of over two years, repos and debt securities with an agreed maturity of over two years. In addition, liabilities to euro area credit institutions subject to minimum reserve requirements are excluded from the reserve base. A 1 per cent rate is applied to all other liabilities included in the reserve base.

The decrease in the reserve base and the significant cut in the applicable MRR rate led to a substantial decline in commercial banks' minimum reserve requirements (Chart 1). For the first maintenance period (from 1 January 2026 to 10 February 2026), the required amount of minimum reserves was EUR 798 million, down by EUR 9.3 billion from the end of 2025. Banks' minimum reserves at the BNB continue to be remunerated at 0 per cent after the change in the monetary regime in line with the current operational framework of the Eurosystem.

CHART 1

Impact of the MRR Rate Reduction on Banks' Funds Held at the BNB

(EUR million)



Note: Current accounts (covering minimum required reserves) include banks' funds for covering minimum reserves and those exceeding minimum reserve requirements. To ensure comparability with data for the period prior to the beginning of 2026, data are presented as of the end of the relevant month and do not coincide with the MRR maintenance periods.

Source: BNB.

Banks' possibilities for using the significant liquidity released as a result of the reduction in the MRR rate include investments in Bulgarian government securities, an increase in foreign assets, growth in lending to the private sector or maintenance of the released funds on the deposit facility at a current rate of 2 per cent. According to the new BNB balance sheet data, the main portion of banks' minimum reserves were transferred to the deposit facility, thus ensuring return on maintained funds at close to zero risk. Within the first two months of 2026, there was some decrease in these funds. Statistical balance sheet data on other monetary financial institutions (other MFIs)[6] for January 2026 show a stronger decline in the amount of repo agreements and banks' deposits and a corresponding stronger increase in the amount of their holdings of debt securities. Part of banks' deposit facility funds are probably invested in alternative assets providing higher yields, such as Bulgarian government bonds and securities of other euro area residents.

[5] https://op.europa.eu/en/publication-detail/-/publication/3f003aed-7bec-11eb-9ac9-01aa75ed71a1.

[6] The analysis employs BNB's monetary statistics data.

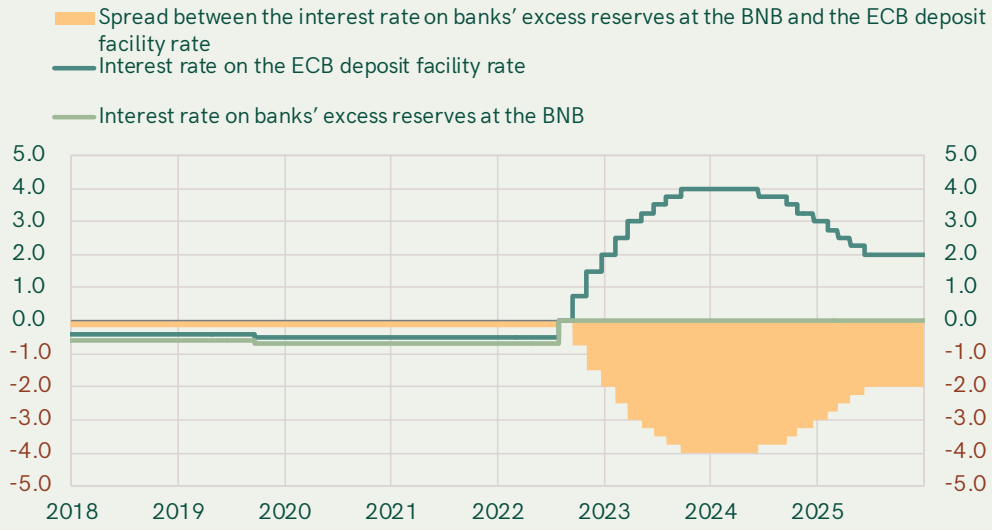
Interbank Money Market Trade

A major function of the interbank money market is raising and providing liquidity among commercial banks in Bulgaria, with unsecured overnight deposits being the most commonly used instrument in the market until the end of 2025. In the 2023-2025 period, interbank money market activity in Bulgaria was relatively high, with the average daily volume of concluded transactions amounting to EUR 416 million (BGN 814 million) as of December 2025.

CHART 2

Deposit Facility Rate of the ECB and the Interest Rate on Banks' Excess Reserves at the BNB

(per cent, percentage points)



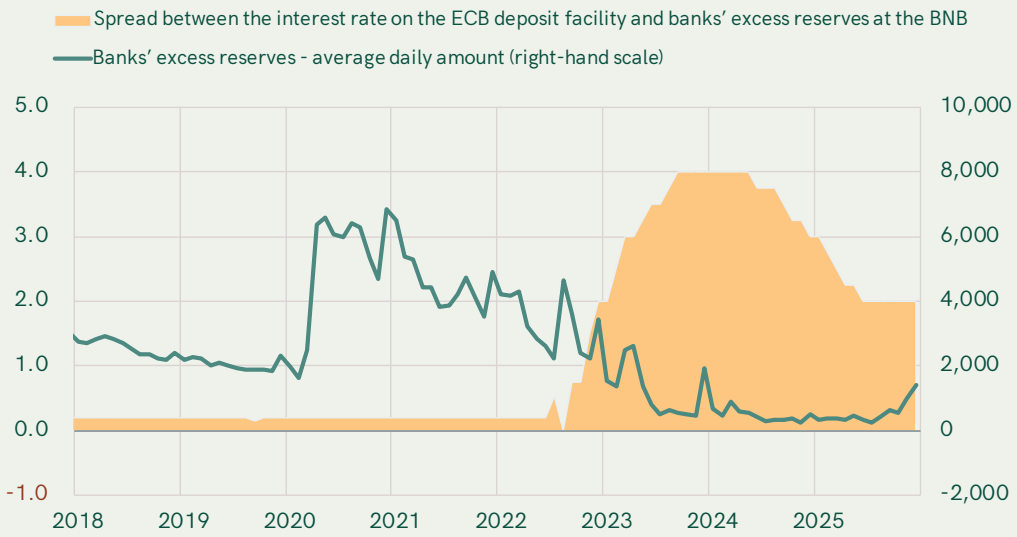
Source: BNB.

ECB's monetary policy tightening cycle, which started in July 2022, contributed to the formation of a negative spread between the interest rate on banks' excess reserves at the BNB (0 per cent) and the ECB deposit facility rate (Chart 2). As a result, banks started to gradually reduce their excess reserves at the BNB and raise more liquidity from the domestic interbank money market (Chart 3 and Chart 4). Following the reversal of the euro area interest rate cycle from mid-2024, the spread between the interest rate on banks' excess reserves at the BNB and the ECB deposit facility rate remained negative, which continued to contribute to a comparatively high interbank money market activity. An additional factor for the active trading in this market was the positive spread between the ECB deposit facility rate and the average interbank money market rate in Bulgaria, which created an opportunity for an interest rate arbitrage related to the generation of additional income by domestic commercial banks owned by euro area credit institutions (Chart 4).

CHART 3

Spread Between the ECB Deposit Facility Rate and the Interest Rate on Banks' Excess Reserves at the BNB, and the Amount of Excess Reserves

(per cent, percentage points) (EUR million)

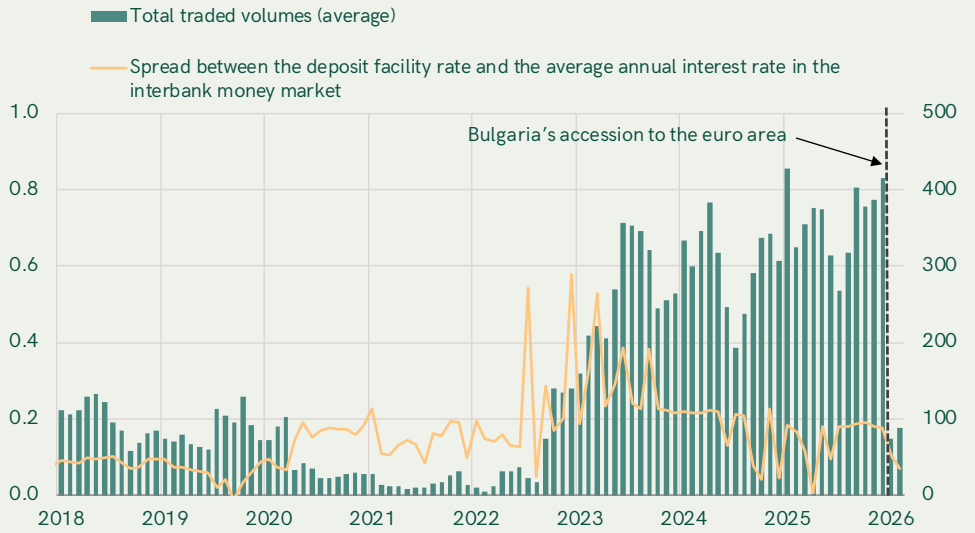


Source: BNB.

CHART 4

Spread between the ECB Deposit Facility Rate and the Interbank Money Market Rate, and Traded Volumes in the Interbank Money Market

(per cent, percentage points) (EUR million)



Source: BNB.

The release of significant additional liquidity in the banking system following Bulgaria's entry into the euro area led to a strong reduction in banks' incentives to trade in the interbank money market. As a result, the activity in this market has declined significantly since the beginning of 2026, with the average daily volume of concluded transactions reaching EUR 73 million in January (down 82 per cent from traded volumes in December 2025) and in February this volume came to EUR 88 million (down 79 per cent from December 2025). In addition,

trading data for the interbank money market for the first two months of 2026 show a significant decline in the share of deposit transactions and an increase in the share of repurchase agreements in total transactions. This change was mainly due to the significant decrease in the volumes of deposit transactions concluded since the beginning of 2026 compared to the average monthly volumes in 2025, with the average monthly volumes of concluded repurchase agreements remaining relatively unchanged. Concurrently, since the beginning of 2026, a slight increase has been recorded in both the overnight deposit rate and the average interest rate on all concluded transactions in the interbank money market in Bulgaria. The upward dynamics recorded in the two rates in the first two months of the year resulted in a narrowing of spreads with euro area money market rates.

Access of Commercial Banks in Bulgaria to Eurosystem Monetary Policy Instruments

With Bulgaria joining the euro area, commercial banks were granted direct access to the Eurosystem's monetary policy instruments. In order to provide access to and participate in these instruments, commercial banks had to be approved by the central bank in advance as eligible monetary policy counterparties. The process of regulating the relations between the BNB and commercial banks was formalised in a special ordinance of the BNB (Ordinance No 45) and completed in the period prior to euro area accession.

Banks' ability to generate income at a very low risk determined the active use from early 2026 of one of the Eurosystem's standard monetary policy instruments, such as the standing deposit facility. At the same time, despite the possibility of using open market operations, data from the BNB's new statistical balance sheet show that banks have not made active use of this possibility since the beginning of the year. There were single and of minimum quantity participations of certain counterparties in the main refinancing operations, as well as in the marginal lending facility, which are of a test nature and are aimed at verifying banks' operational readiness to use the Eurosystem's monetary policy instruments. The lack of incentives to use these instruments can be explained by the current very high liquidity in the banking system.

Interest Rates on Deposits and Loans

Interest rates on loans to natural persons and legal entities may be variable or fixed for the whole or part of the duration of the credit agreement. In the case of the variable interest rates prevailing in the Bulgarian market, the interest rate is composed of two components. The first component is a reference interest rate set by a specific commercial bank to which banks apply a case-by-case approach and, for most of the cases, is based on a selected deposit rate (interest rates on outstanding amounts of deposits with different maturities of the BNB interest rate statistics are most commonly used). The second component is a risk margin, which largely depends on the borrower's specific characteristics, such as creditworthiness and credit history, income level and income stability (for individuals), respectively, the level and stability of revenue of non-financial corporations, indebtedness, loan collateral, as well as the macroeconomic environment and market conditions.

With Bulgaria's accession to the euro area, deposits and loans of natural persons and legal entities in national currency were automatically converted into euro. As a result, the BNB suspended the calculation and publication of interest rates in levs. This has created a need for commercial banks applying variable lending rates, the reference component of which is based on deposit interest rates denominated in levs, to update their interest rate methodologies. A review of commercial banks' interest rate bulletins and methodological documents in early 2026 shows that with regards to consumer and housing loans, the majority of banks retained their approach from the end of 2025, replacing the interest rates on deposits in levs used so far with similar indicators in euro. For a minority of banks, reference interest rates are linked to EURIBOR indices with different maturities. At the same time, with regards to loans to non-financial corporations, a more balanced distribution is observed as benchmarks based on deposit rates and based on EURIBOR are used roughly to the same extent.

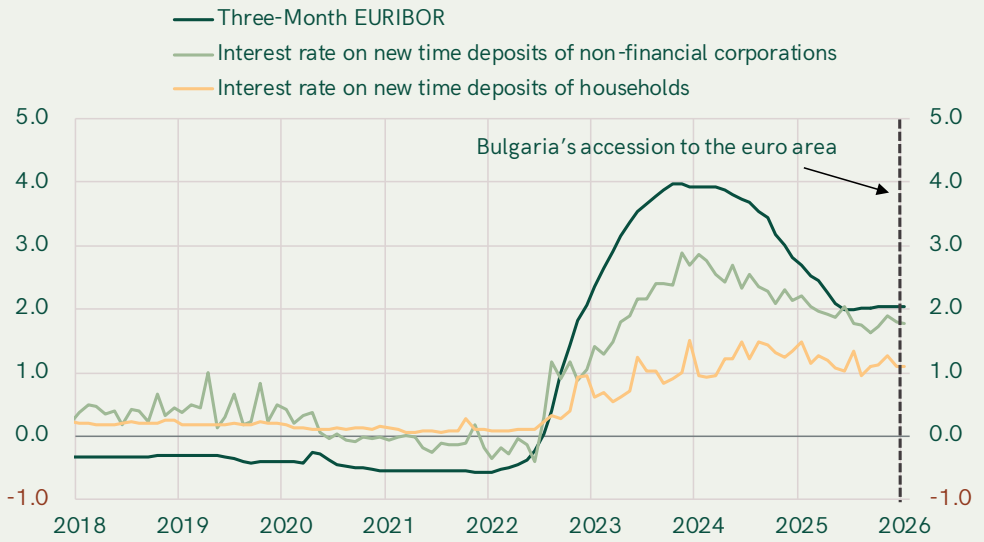
BNB interest rate statistics data for January 2026 show limited changes in interest rates on deposits of households and non-financial corporations compared to the levels at the end of the previous year. In the household sector, the average weighted interest rate on newly attracted deposits increased by 2 basis points, while for non-financial corporations it decreased by 3 basis points. At the end of January 2026, there were no significant changes in the average weighted interest rates on new loans compared to the end of 2025. Consumer loans recorded a slight

increase of 1 basis point, compared to December 2025, while housing loans recorded a decrease by 1 basis point. In the non-financial corporations' sector, the average weighted interest rate on new loans decreased by 10 basis points for the same period.

CHART 5

Interest Rates on New Deposits and Three-Month EURIBOR

(per cent)

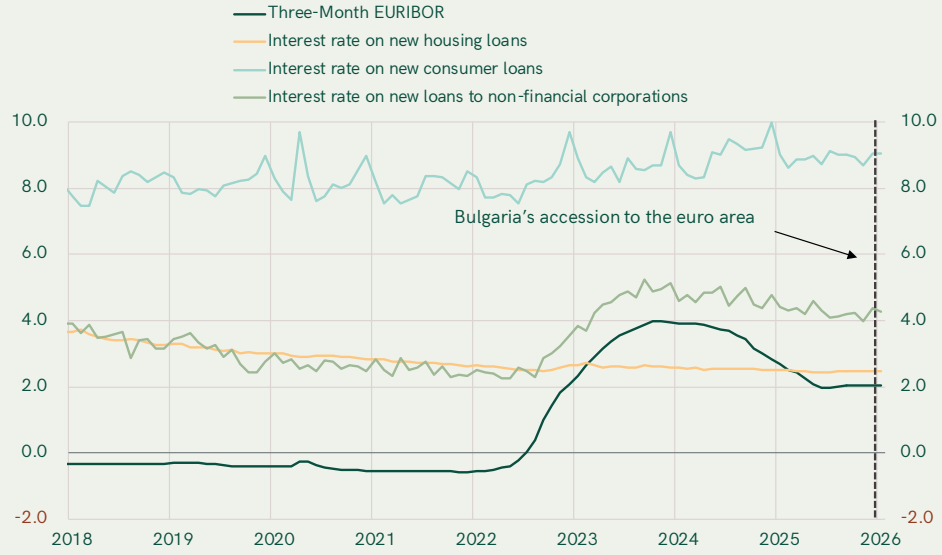


Source: BNB.

CHART 6

Interest Rates on New Loans and Three-Month EURIBOR

(per cent)

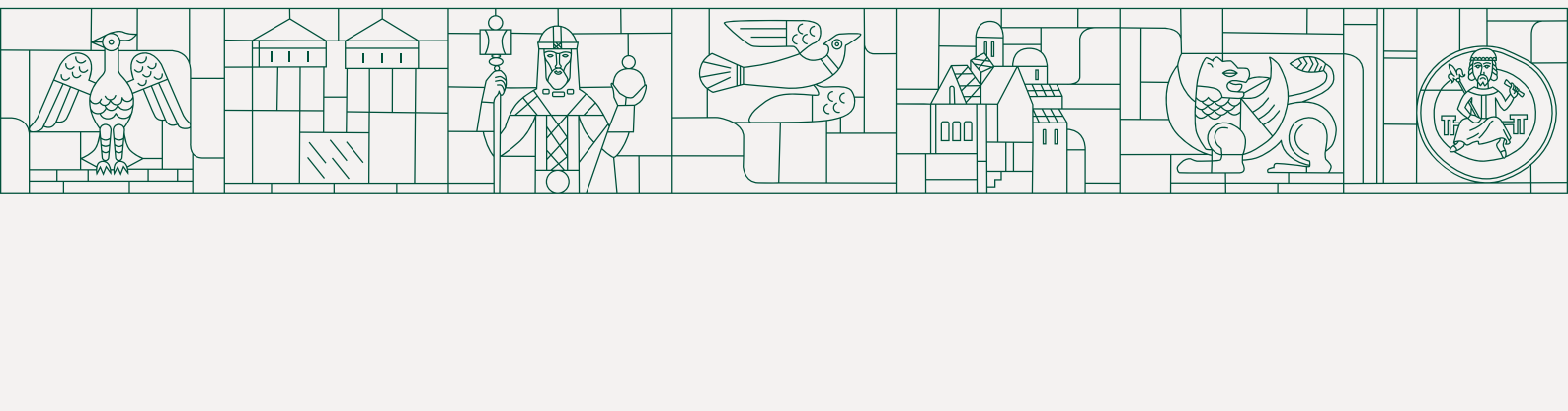


Note: Interest rates on new loans to non-financial corporations do not include overdrafts.

Source: BNB.

The initial limited effects of the change in the monetary regime on deposit and lending rates in Bulgaria can be explained by several main factors:

- A short period since the introduction of the new monetary regime: the period since Bulgaria's accession to the euro area has been rather short and therefore no effects are observed at this stage related to a potential strengthening of the transmission of Eurosystem's monetary policy to Bulgaria's monetary conditions. Ample liquidity in Bulgaria's banking system and the unchanged key euro area interest rates from mid-2025 to date do not constitute a precondition for changes in the interest rates on deposits and loans in Bulgaria.
- Specificities of the Bulgarian banking system: the interbank money market, where the transmission of the ECB's monetary policy is fastest, has more of a supporting role in the liquidity management of commercial banks. To finance their lending activities, banks in Bulgaria rely heavily on resident deposits, which accounted for around 73 per cent of the banking system liabilities at the end of 2025. In addition, the banking sector is characterised by high levels of liquidity well above minimum regulatory requirements, mainly as a result of the continuing upward trend in deposits and, above all, preserved households' preferences to keep their free funds mainly in the form of deposits in the banking system. Ample liquidity limits banks' incentives to raise deposit rates, which serve as the basis for the formation of lending rates and, to a significant extent, determine their dynamics.
- Maintaining the methodologies used to determine reference lending rates: after Bulgaria's accession to the euro area, the majority of commercial banks have retained their approach in determining reference lending rates and continued to base them on outstanding deposit rates. These rates are generally characterised by more limited and slower dynamics than interbank interest rates, which also contribute to the current slight changes in lending rates. The current low interest rates on outstanding amounts of deposits are also supported by the high share of overnight deposits in total deposits of non-financial corporations and households in the banking system.

Conclusion

This topical research provides an analysis of the initial effects on the banking sector of the new monetary regime that has been operating in Bulgaria since its accession to the euro area from the beginning of 2026. The available data so far show that, as expected, the bulk of commercial banks' liquidity released as a result of the significantly lower amount of minimum reserve requirements has been transferred to the deposit facility. Further developments in deposit facility funds maintained by banks will depend on the specific macroeconomic conditions and banks' individual decisions to invest the released liquidity, taking into account the profitability and risk associated with potential alternative assets to which this liquidity could be directed. Ample banking system liquidity is currently reflected in a strong decline in trading volumes in the interbank market, with a narrowing also being observed in the spread between the interest rate in the interbank market in Bulgaria and the interest rates in the interbank money market in the euro area. To date, ample liquidity in the banking system limits the use of main refinancing operations and the marginal lending facility by banks. In the current environment, there are no factors for significant changes in deposit and lending rates in Bulgaria. At the same time, Bulgaria's accession to the euro area is a precondition for the transmission of the Eurosystem's monetary policy to the country's financial and economic conditions to become more direct and to gradually strengthen over time.