

# NPL Reduction Strategy – the FSAP findings and recommendations



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# Summary



This session will discuss the FSAP recommendations for  
Non-Performing Loans

- Background: the FSAP key elements
- The NPL context
- NPL – reduction strategy

# Background: The FSAP



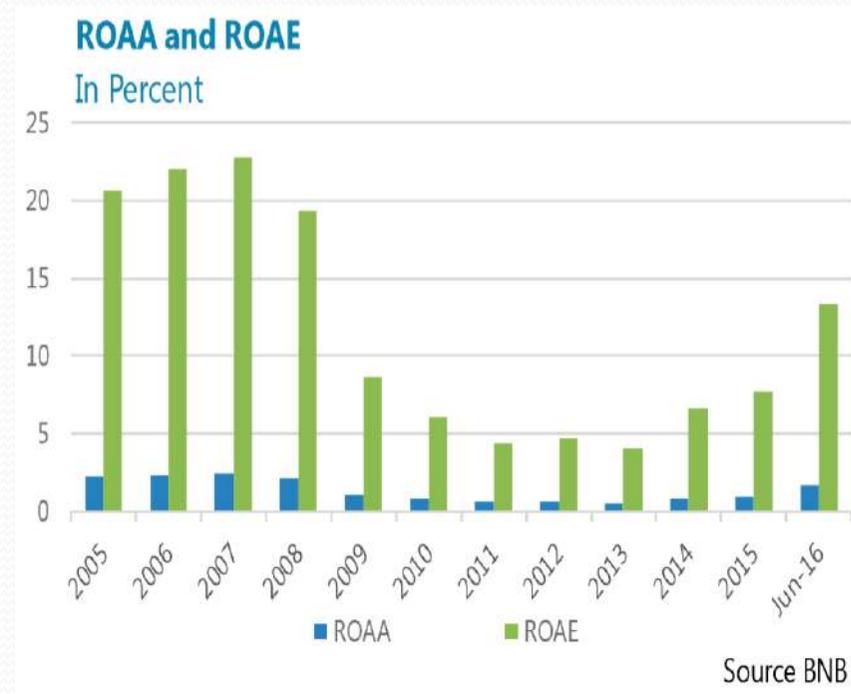
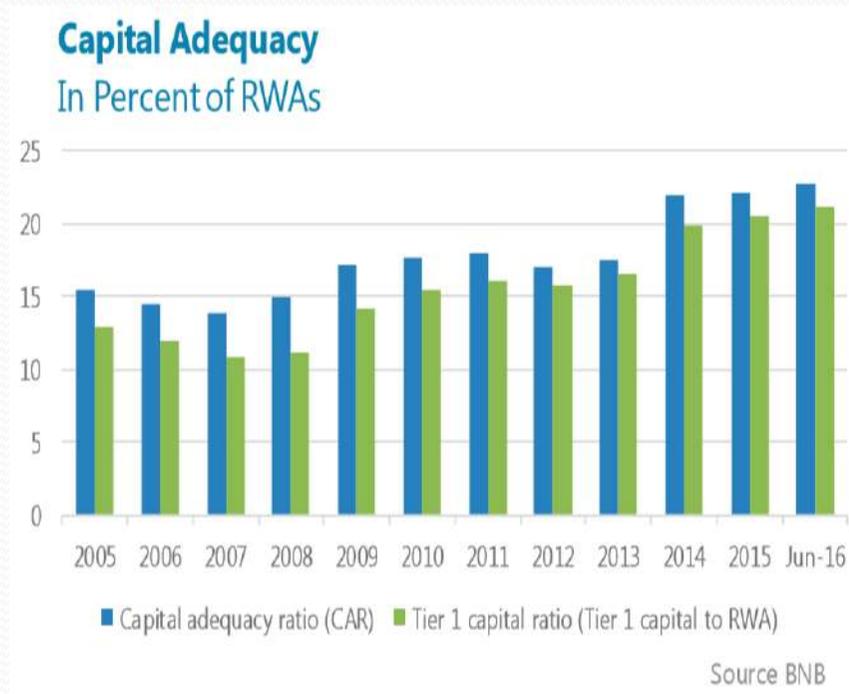
- The FSAP is a diagnostic tool of the IMF and WB
  - The FSAP follows the invitation of the Ministry and BNB
  - Excellent engagement with the authorities
  - Takes place in proximity to upheaval – global financial crisis and domestically the failure of Corporate Commercial Bank
- Components:
  - Main report summarizes findings
  - Technical notes on 4 key risk areas: (i) risk assessment and stress test; (ii) safety net; (iii) stock take on banking supervision; and (iv) **strategy for NPL reduction\***

\*NPL Strategy Note prepared by Jerry Edwards and Karlis Bauze  
(<https://www.imf.org/en/Publications/CR/Issues/2017/07/11/Bulgaria-Financial-Sector-Assessment-Program-Technical-Note-NonPerforming-Loans-Reduction-45059>)

# Soundness Indicators



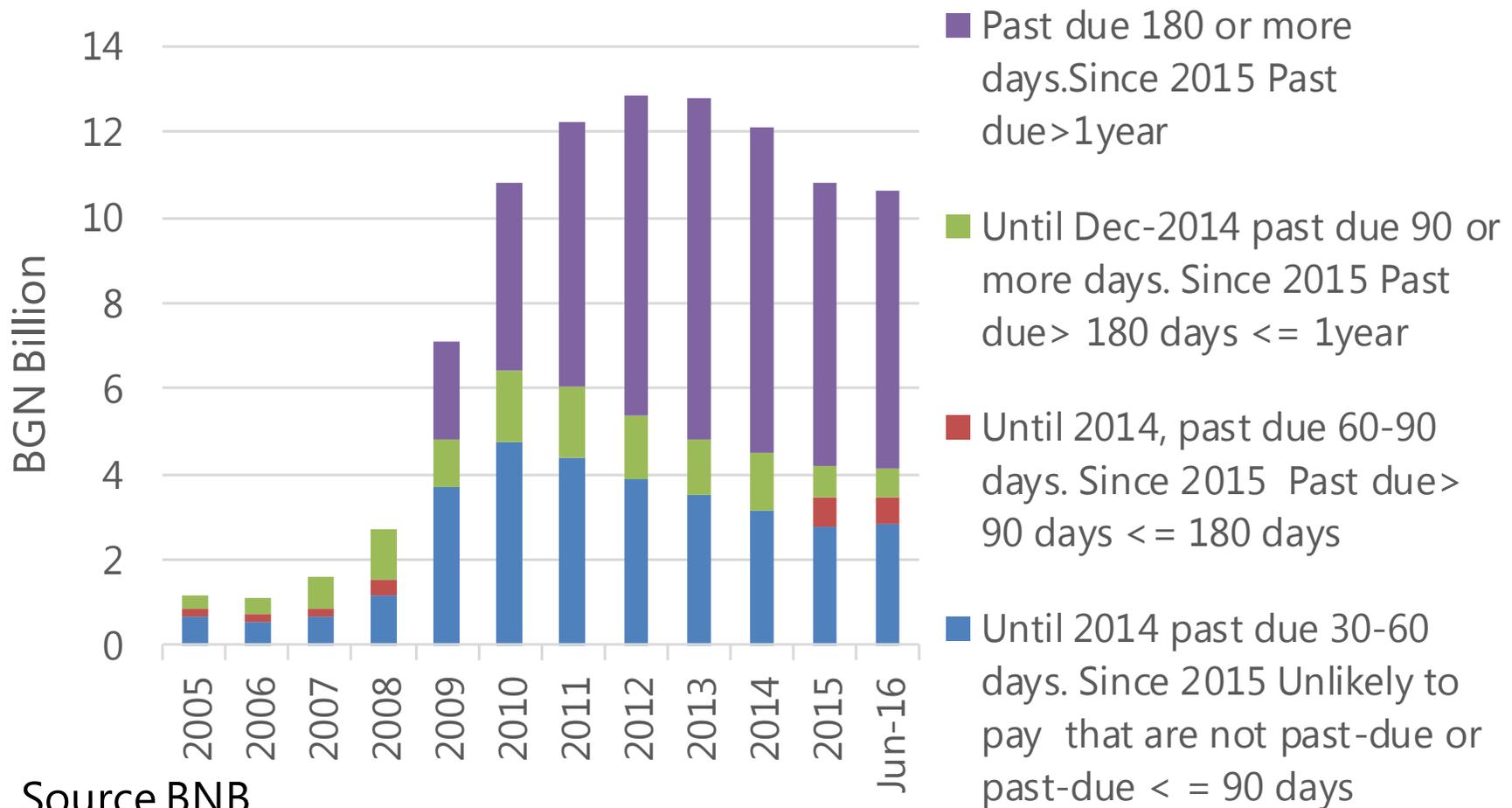
Banks show high capital adequacy and improving profitability



# Bulgaria: - NPLs



## Non Performing Loans

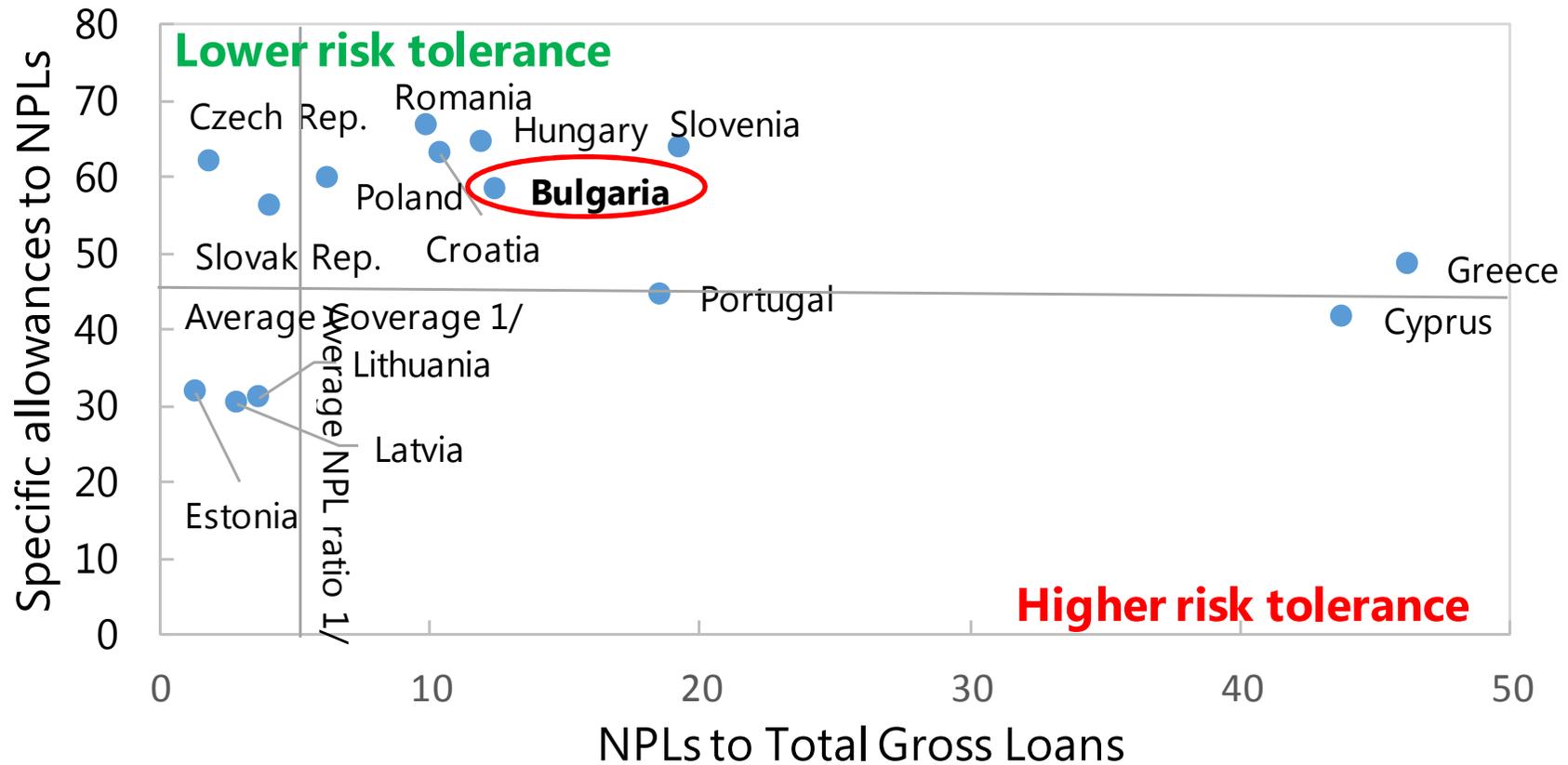


Source BNB

# Recent EU Experience - NPLs



**NPL ratio and Coverage, March 2017**  
In Percent



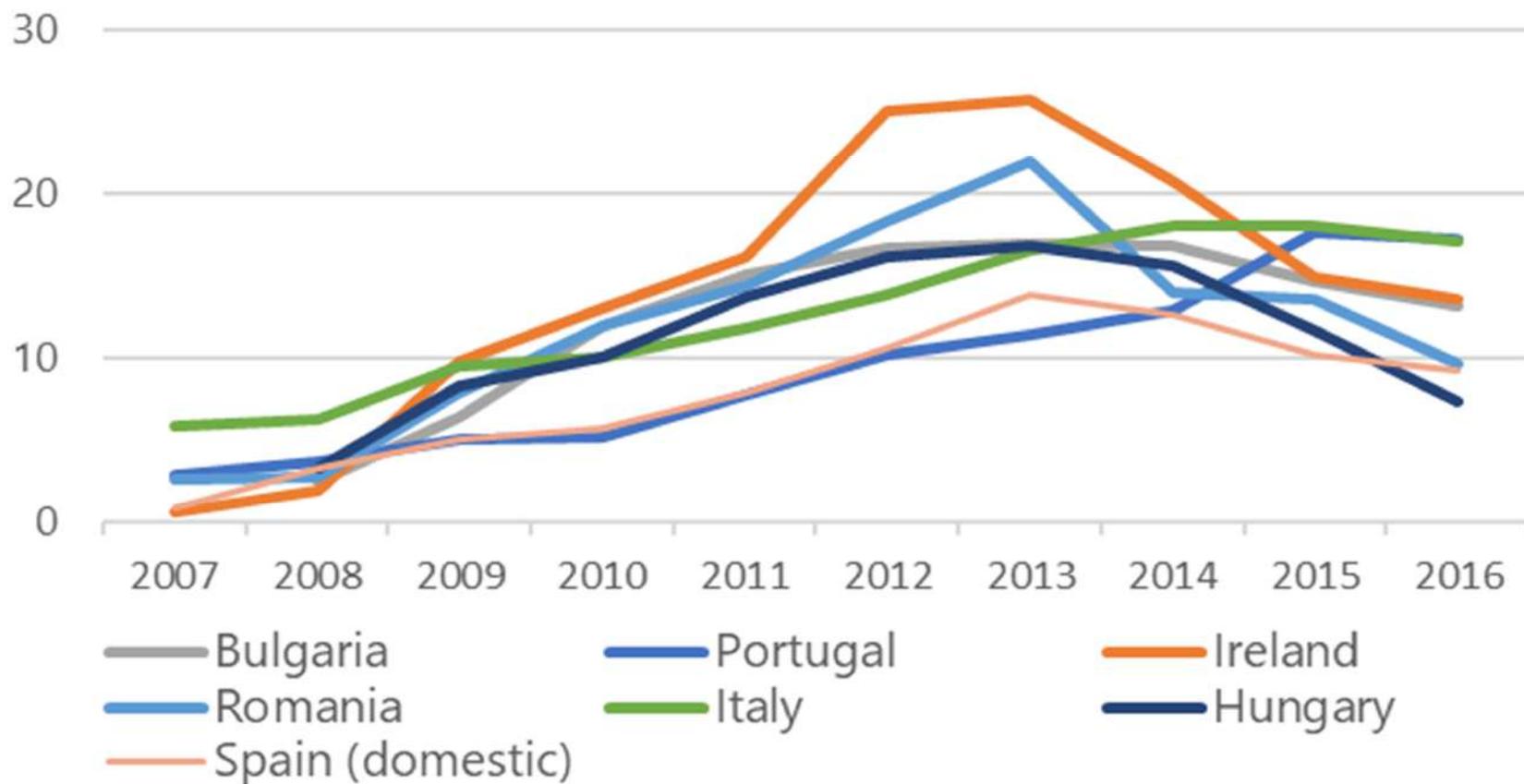
1/. EU weighted average

Source: EBA Risk Dashboard

# Select EU Experience - NPLs



## Non Performing Loans to Total Loans In Percent



Source: IMF FSI

# NPL reduction and link to capital



- BNB prudential policies have pushed banks to retain earnings towards achieving generally high capital ratios.
- Important objective yes, but capital is not a buffer for NPLs. Loan losses can only be taken against the loan loss allowance, which first must be fortified through provision expense.
- High NPLs with more than half of system level past due more than a year.
- This has led to an overstated loan loss that reflects inconsistent and unguided practices that are not robust.
- IFRS - the accounting standard – gives wide latitude to banks to determine provisioning and still comply with the standard.

# NPL reduction strategy



- Strategy to achieve a substantive reduction in NPL levels over three- to five-years.

## The strategy:

- (i) is in line with BNB macroprudential objective to limit buildup of risks that threaten financial system stability;
- (ii) focuses on intensive prudential “supervisory review” against metrics designed to achieve:
  - Higher provisioning to build a robust loan loss allowance;
  - Loan write-offs to achieve NPL reduction use allowance;
  - and
  - Stricter collateral valuation.
- (iii) is to be complemented by enhanced supervisory reporting and risk disclosure.

# NPL reduction strategy (cont)



- Macroprudential motivation for the strategy
  - Introduction is counter-cyclical given improving macro.
  - Banks have capital to absorb higher provision expense, while still meeting regulatory requirements.
  - One-time sharper decline, as the future will see earlier loss recognition/write off that will dampen peak levels.
- Compatible within banks' application of IFRS.
  - Stricter expectations of provisions, write-offs, and collateral valuation would still be intended to fit within what is allowable under IAS 39 and IFRS 9.
- Loan write-offs to achieve NPL reductions
  - More aggressive treatment of highly delinquent loans.



# Thank You

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