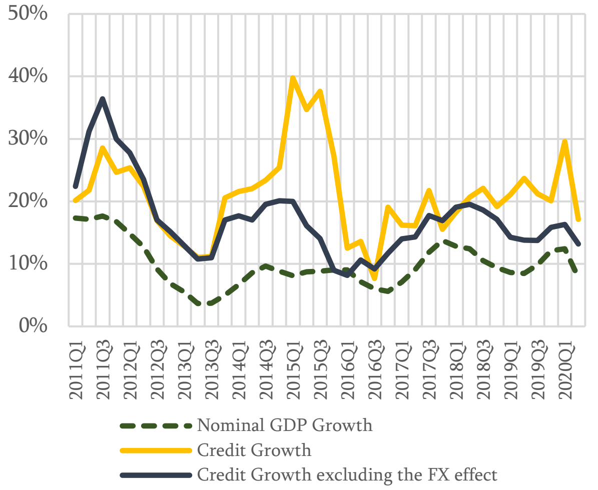
Financial Stability Committee's Decision

November 25, 2020

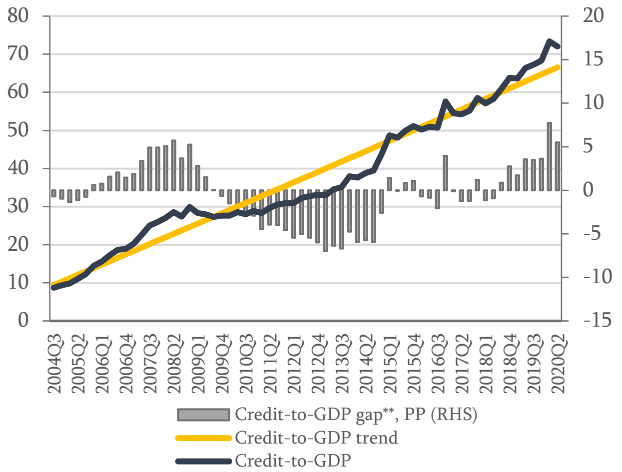
As a result of the financial stability policy measures implemented by the National Bank of Georgia financial system maintains stability and continues lending to the economy without any difficulties. Additional capital requirements imposed by the NBG and profits gained by banks in previous periods enabled them to build up sufficient capital buffers to handle such stress. Asset quality also maintains resilience, which was supported by the responsible lending regulation and macroprudential measures implemented to reduce loan dollarization. In addition, Liquidity Coverage (LCR) and Net Stable Funding (NSFR) ratios imposed during the previous years promoted stability of bank's funding and contributed to built up of solid liquidity buffer. Besides, to further support lending to the real economy, the NBG expanded GEL liquidity instruments in 2020, while a temporary supervisory plan released portion of bank's capital buffers and gave them flexibility in managing liquidity. Due to the pandemic, the share of non-performing loans is expected to increase. However, commercial banks have made loan loss provisions in advance. Consequently, the banking system is healthy and has enough resources to continue providing loans to the economy without any difficulties.

Under the baseline scenario, in 2021 the NBG will announce the recovery plan and the dates to increase capital buffer requirements, which were released in March, 2020, after that reasonable time will be given to the banking sector to accumulate capital buffers. The annual growth rate of credit portfolio in October 2020, excluding the exchange rate effect, amounted to 11.5%. It should be noted that Credit-to-GDP ratio exceeds its long run trend, which reflects the high credit growth and exchange rate effects in previous periods. Increased gap indicates the raised debt burden and vulnerability, especially, in the corporate sector. After the spread of the Coronavirus, initially credit activity slowed down significantly, but it has increased again in the recent months, and if this tendency continues, the growth of loan portfolio will be around 10%. As stated in the Financial Stability Committee's previous decision the NBG will not increase the countercyclical buffer requirement in 2020. Under the baseline scenario the recovery plan of released capital buffers will be announced in 2021, and banks will be given reasonable time to accumulate capital buffers gradually, without facing significant hardship.

Annual Growth of Nominal GDP and Credit*



Credit*-to-GDP Ratio (%)



Source: NBG; Geostat

* Nominal GDP growth reflects the YoY GDP growth of the last 4 quarters.

** Credit includes loans directly issued by commercial banks and microfinance institutions as well as bonds issued domestically by the non-financial sector.

*** Credit-to-GDP gap is the deviation of Credit-to-GDP ratio from its long-run trend. The trend is estimated using HP filter in line with the Basel recommendations.

Despite the significant decline, dollarization remains one of the main challenges for the financial sector. On the one hand, foreign currency denominated loans are exposed to exchange rate risk. On the other hand, they are accompanied by interest rate risk, which, given historically low interest rates on US dollar and Euro in global markets, is especially noteworthy now due to its potential impact in the medium term. In the pre-crisis period the NBG implemented a set of macroprudential measures to reduce loan dollarization, which contributed to the significant decline of current vulnerabilities. However, due to the high share of FX loans and the increased exchange rate volatility, dollarization remains the main risk for unhedged borrowers and for the whole financial system resilience.

It should be noted that from the current perspective, when the magnitude of the pandemic can be better assessed, the potential impact of the shock on the financial sector is already largely realized. However, significant uncertainty remains, including how long the pandemic will last. The National Bank of Georgia continues monitoring the country's financial stability and assessing domestic and foreign risks. If necessary, it will use all available instruments to minimize the possible risks.

The Financial Stability Committee's next meeting will be held on February 24, 2021.