1. OVERVIEW OF THE MAIN RISKS TO FINANCIAL STABILITY

1.1 FINANCIAL STABILITY MAP

As at end of 2019 H2, data in the Financial Stability Map show, overall, an unchanged level of risks in the overall macroeconomic environment and in real economy agents, and evidences various developments in risks related to banking sector activity. In more concrete terms:

A. Overall economic environment:

I. Risk from the “domestic economy” is rated as “average” and unchanged over a one-year period, mainly driven by the narrowing of output gap due to the decline in the size of the external debt stock to GDP and in the needs for external financing.

II. Risk from “external environment” remains at “average” rate, but downward during the year, mainly driven by the fall of oil prices in international markets. The economic performance of our trading partners and the fall in unemployment in countries with the highest share of remittances contributed at a lower degree in the mitigation of this risk.

B. Developments in the main real economy sectors show that:

I. Risk from “enterprises” is assessed as “average”, maintaining the level of the previous year. Notwithstanding the improvement in the credit portfolio quality to enterprises and in the sub-indicator “financial position”, private sector’s expectations appear deteriorated regarding employment.

II. Risk from “households” is assessed as “average” and downward from the previous year. The rate of this category was affected by the upward pace of remittances, the improvement in credit portfolio quality to households and the developments in housing market.

III. Risk from “Government” continues to be assessed as “low” and unchanged over the last year. Nevertheless, the further expansion of deficit budget suggests for an increased attention on this sector.
C. The banking sector activity at the end of the period:

I. Risk from “capitalisation and profitability” continues to be assessed as “average”, albeit it showed an upward trend over the last year, mainly driven by the fall in the interest income of the banking activity.

II. Risk from “funding and liquidity” fell from “moderate” in December 2018 to “average”, reflecting a lower support on the external funding sources.

III. The risk associated with the “banking sector structure” is assessed as “average” but slightly upward from a year earlier, mainly as a result of the increase of concentration in the banking sector.

1.2 SYSTEMIC RISK

1.2.1 INDICATORS RELATED TO THE MATERIALIZATION AND ACCUMULATION OF SYSTEMIC RISK

Exposure of banking system to systemic risk is assessed based on the indicators related to the materialisation and accumulation of systemic risk and of financial stress. Also, the perception of the banking industry regarding these risks is included in this assessment.

The materialisation and accumulation of systemic risk and financial stress indices reflect positive developments during the period. The improvement of credit quality, the fall of unemployment rate and the stability of foreign exchange rate contributed in the decline of risk materialisation. Also, financial stress index appears downward, by mainly reflecting the improvement from the expansion of deposits base.

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4 Systemic risk is defined as “the possibility for the materialisation of shocks that impair the functioning of a financial system to the point where economic growth and welfare suffer materially”.

5 Banking sector perception related to main systemic risks in Albania is attained through an ad hoc survey.
Systemic risk accumulation did not show strong movements during the year. Its increase is affected by the increase in the share of loans with variable interest rate, increase of house prices and the increase of loans to enterprises; while its fall is affected by the decrease in both public debt and external debt, in relative terms.

1.2.2 PERCEPTION OF BANKING SECTOR ON SYSTEMIC RISK

Banking sector continues to identify “domestic political risk” and “the deterioration of domestic economy”, as the two main systemic risks in the country. Nevertheless, the banks assessment on these risks has decreased from “high” in H1 2019 to “average” level in H2 2019.

On the other side, banks concern on “credit risk from all categories of clients” and on risk associated with the process of “execution of collaterals” has increased reflecting the overall uncertainty in the aftermath of the November 2019 earthquake, due to the major material and psychological damages caused.

Although “domestic political risk” and “deterioration of domestic economy” remain the two most important systemic risks, the earthquake of November 2019 increased the uncertainty about the performance of a part of credit portfolio of banks.
Chart 4 Bank’s assessment on the main systemic risks in Albania

- Public risk in the country
- Deterioration of domestic economy
- Difficulties in collateral execution
- Credit risk from all entities
- Exchange rate instability

Risk level:
- Very high
- High
- Average
- Low
- Very low

Source: Bank of Albania