

### 3. KEY PRIORITIES PLANNED FOR 2018

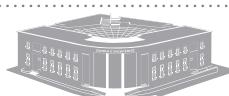
The priorities of Supervision Department for 2018 will focus on the assessment of main risks management to which the supervised entities are exposed; realisation of non-exhaustive supervisory actions; the continuous monitoring of the overall performance and individual risk profile for each of the supervised institutions. These priorities are further detailed in the following sections.

#### 3.1 CREDIT RISK FOCUSED ON NON-PERFORMING LOANS AND THE ADDRESSING OF BORROWERS IN FINANCIAL DIFFICULTIES

The reduction of non-performing loans ratio will continue to be on the focus of supervision in 2018. Notwithstanding the considerable fall in non-performing loans during 2017, the current level is still considered high affecting the long-term stability of banks and banking system. Maintaining a prudential approach on early addressing problems and the commitment of the Bank of Albania in the framework of the national program on addressing non-performing loans, has continued through the undertaking of an initiative for the regulation of cooperation among banks, for addressing common borrowers that are in financial difficulties to repay their liabilities. This initiative will be realised during 2018, through the compilation of a special regulatory framework on the possibility of resolving out-of-court the non-performing borrowers that are exposed to more than one bank. It will serve as a mechanism to bring banks into a common denominator to find a long-term stable solution for these borrowers. This initiative is based on the similar international experiences and is drafted in collaboration with FinSAC project of the World Bank and the IMF resident advisor at the Bank of Albania.

#### 3.2 APPROXIMATION OF REGULATORY FRAMEWORK WITH BASEL III

The global financial crisis highlighted the need to review the banking regulatory framework regarding the management of unfavourable situations. These changes were performed through Basel III. One of the important introduced elements is the establishment of the criteria on the quantitative management of banks liquidity through a new indicator named Liquidity Coverage Ratio (LCR). This indicator aims at the early preparing of banks to satisfy the needs for liquidity that may arise from unexpected events causing massive bank runs.



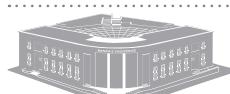
The Bank of Albania has planned the adoption of this regulatory framework and is carrying out all the needed preparations to draft it. This process, among others, considers also the preparation of banks on the new reporting elements of this framework and the adoption of their internal processes for the management of liquidity risk.

The revision of supervisory regulatory framework will aim at including Basel III elements, over 2018, related with the improvement of capital quality, after assessing the possibilities to adopt and establish adequate reserves of capital, to enhance the sustainability of banks in Albania.

### 3.3 REGULATION AND SUPERVISION OF BANK'S GOVERNANCE

Supervision has paid special attention to good governance in banks, as an important element for risk and management. Hence, the review of the internal regulations and manuals to assess banks is considered as necessary. The purpose of amendments is to approximate the supervisory requirements and methods with those of the European Union and to improve the internal criteria of assessment. Part of amendments have been released over 2017, while within 2018, other methodological changes will take place in collaboration with the European Bank for Reconstruction and Development (EBRD). This project consists in the structure and orientation for adequate assessment of banks' structures regarding the decision making, audit environment and the management process of important risks of banks.

The approval of the Guideline to the Internal Capital Adequacy Assessment Process (ICAAP) of banks, at the beginning of 2017, by considering a preparatory period for banks, has aimed at ensuring the realisation of an effective and comprehensive internal process of banks for the capital adequacy assessment. The process lays down the documentation and presentation, for the first time by banks till the end of April 2018, of capital adequacy self-assessment report. This report and the entire ICAAP will be subject of supervision assessment and review for the identification of possible deficiencies by supervisors and results will be informed to banks to make the necessary improvements in the next reporting. To conduct this assessment the internal guiding documents are reviewed and will be finalised to help in assessing each of ICAAP documents by all banks and the configuration of Internal Supervisory Review and Assessment Process. This process will take place throughout 2018. There will be continuous communication with banks, throughout this period, to discuss on the content and assessment conducted in the framework of this report.



### 3.4 BANKING SYSTEM CONSOLIDATION

The consolidating trends of the banking system identified in the previous years, materialised in 2017, with the decision on the merger of Intesa SanPaolo Bank with Veneto Bank, mainly driven by the international developments and by the decision of the Bank of Italy and the European Central Bank in coordination with Intesa SanPaolo group in Italy, following the announcement on the bankruptcy of Vento Banking group. The merger by absorption of Veneto Bank is expected to end in 2018, while the Albanian banking system will have less banks as a result. The Bank of Albania deems that there is still scope for further consolidation, expected to be materialised and is carefully monitoring all developments in this regard. This assessment is based on the interest stated by some banks to expand and the shrinkage of some other banks due to the revision of plans for the presence in the Balkans by the parent banks.

### 3.5 SELF-ASSESSMENT OF THE EQUIVALENCE WITH EUROPEAN REGULATORY AND SUPERVISORY FRAMEWORK

In the framework of aligning the legislation and regulatory framework with the EU directives and the relevant standards, to assess the current situation and determine on future intervention, in 2017, work started on the self-assessment of the equivalence of the supervisory regulatory framework with European regulatory and supervisory framework (CRD and CRR)<sup>1</sup>, according to the filled in questions in the Questionnaire of the European Banking Authority (EBA)<sup>2</sup>. This process shall precede the identification of Supervision Department needs for drafting new regulatory acts and supervisory methodologies or the review of the existing ones, aiming at ensuring continuous alignment with Acquis Communautaire on the activity of credit institutions.

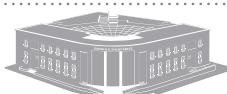
### 3.6 COLLABORATION WITH THE EUROPEAN CENTRAL BANK

With the creation of a Single Supervisory Mechanism (SSM) at the European Central Bank in November 2014 and considering the active presence in Albania of subsidiaries of large European banking groups, the Bank of Albania and the European Central Bank are in the process of drafting a comprehensive agreement that will regulate all the fields and aspects of this cooperation. The signing of the agreement by both institutions, within 2018, will finalise this collaboration.

During 2018, the Supervision Department aims to take part in some of the Supervisory Colleges for European banking groups present in Albania, as an

<sup>1</sup> Capital Requirement Directive and Regulation.

<sup>2</sup> EBA (European Banking Authority)



observer, through a specific agreement for this purpose. This is considered an important step not only in the framework of strengthening cooperation with EU supervision authorities and the alignment with the most advanced supervision practices, but also in the framework of a more comprehensive supervision assessment of EU-based banks that operate in Albania.

### 3.7 PREPARATION OF FINANCIAL REPORTING ACCORDING TO THE INTERNATIONAL ACCOUNTING STANDARDS

To adopt and apply the International Accounting Standards (IAS), the Bank of Albania is carrying out some theoretical and practical preparations. In addition, theoretical preparations through trainings, the possible effects arising from the application of standards in the financial statements and capital of banks are being assessed, with the assistance of the World Bank and Grant Thornton, an international auditor. During 2018, the Bank of Albania will carefully monitor the results from the application for the first time of the new standard - IFRS 9, at banks and, depending on the results, will determine a supervisory position with a prudential approach to ensure an adequate protection for banks.

*Table 2 Supervision priorities for 2017 - 2018 and foreseen activities*

Priorities 2017	Priorities 2018	Planned activities	Extension for a further period
Credit risk/ NPLs performance	Credit risk/ NPLs performance	- Assessment of banks' strategies and objectives for NPLs - Assessment of Recovery and Resolution Plans for large borrowers - Platform to address common borrowers of banks	✓
Capitalisation of business strategy	Consolidation of banking system	- Assessment of IAPCA documents and their consultation with banks - Monitoring the merger processes of banks and possible purchases	✓
Approximation of regulatory supervisory framework with European standards	Approximation of regulatory supervisory framework with European standards	- Liquidity risk - BASEL III - Capital reserves - Basel III - SREP (Supervisory Review and Evaluation Process) - BASEL II - Recovery and resolution in banks - Assessment of approximation of the regulatory framework with those of EBA	○
Regulation and supervision of banks' governance	Supervision of banks' governance	- Revision of assessment process of banks' corporate governance - Methodological developments - Staff training	○
Collaboration with ECB	Collaboration with domestic and foreign authorities	- Signature of collaboration agreement with ECB - Participation in Supervisory College of European banks - Collaboration with FSA for joint inspections, revision of Collaboration Agreement, information sharing	✓
	Risk-based supervision	- Assessment of banks' IAPCA - Assessment of Recovery Plans - Determination of assessing criteria on lending	○
	Implementation of International Accounting Standards	- Preparation of reporting framework on international accounting standards - Monitoring of IFRS 9	✓

