The activities of the National Bank of Georgia in ensuring the long-term sustainable development of the banking system

Gelashvili Goga¹, Abutidze Gocha², Chelidze Medea³

¹ PhD Student, the Faculty of Business Technologies; Georgian Technical University; Republic of Georgia
² PhD in Business Administration, Assistant Professor, Assistant Professor at the Department of Financial and Banking Technologies; Georgian Technical University; Republic of Georgia
³ PhD in Economics, Professor, Professor at the Department of Financial and Banking Technologies; Georgian Technical University; Republic of Georgia

Abstract.
The article emphasizes that despite significant economic and financial challenges due to the coronavirus pandemic and Russia's military aggression against Ukraine, Georgia's banking system can be considered the most stable, resilient, and developed sector of the economy. This is primarily attributed to well-planned and prudently regulated policies. It is determined that the activities and regulations of the National Bank of Georgia in the financial sector align closely with the integration goals of our country in the European Union, demonstrating significant and sustained progress. This applies both to the comprehensive and stable functioning of the financial system and the challenges associated with this task. Within this context, there is a timely response to risks and precautions, resulting in the minimization of negative effects on the stable functioning of the financial system.

Keywords:
regulation
supervision
National Bank of Georgia
banking sector
financial sustainability
The issues related to the supervision and regulation of commercial banks in Georgia and the corresponding requirements are defined by the Organic Law of Georgia “On the National Bank of Georgia”, the Law of Georgia “On Commercial Bank Activities”, and other relevant legal acts. Additionally, the guidelines for the National Bank's supervision and regulation of the banking sector are established based on approved international practices, including those of the world's developed countries and the European Union's legal framework. The oversight and regulatory activities of the National Bank of Georgia (NBG) adhere to the standards and principles set by the Basel Committee on Banking Supervision and other relevant international standards (Banking supervision, 2023).

As of January 1, 2024, the banking sector of Georgia is represented by 17 banks (Table 1), of which 3 (JSC Pave Georgia, JSC Hash, JSC Paysera Bank Georgia) are digital banks. They intend to provide banking services to customers primarily through electronic channels. The banks aim to attract both traditional and modern technology-savvy customers to digital technologies.

The supervision of Georgia's banking sector by the NBG is based on principles established to address risks. It anticipates challenges when allocating more resources toward comparatively complex or high-risk institutions or transactions (Risk-Based Supervision Framework - General Risk Assessment Program (GRAPE), 2022).

<table>
<thead>
<tr>
<th>Bank Name</th>
<th>License Issuing Date</th>
</tr>
</thead>
<tbody>
<tr>
<td>2 JSC Hash</td>
<td>03.11.2023.</td>
</tr>
<tr>
<td>3 JSC Paysera Bank Georgia</td>
<td>17.11.2022.</td>
</tr>
<tr>
<td>4 JSC Credo Bank</td>
<td>20.03.2017.</td>
</tr>
<tr>
<td>5 JSC Isbank Georgia</td>
<td>30.07.2015.</td>
</tr>
<tr>
<td>6 JSC PASHA Bank Georgia</td>
<td>17.01.2013.</td>
</tr>
<tr>
<td>7 JSC Halyk Bank Georgia</td>
<td>29.01.2008.</td>
</tr>
</tbody>
</table>

1 Source. National Bank of Georgia, Licensed Commercial Banks, 2024.
The NGB, in assessing banks' performance, takes into account various indicators to identify and minimize deficiencies and mitigate various categories of risks. These actions are carried out systematically at each stage of the supervisory cycle. When taking supervisory measures, it is based on the principle and criteria of proportionality established by the Law of Georgia “On Commercial Bank Activities”. This approach allows the NGB to adapt its response to risks or deviations in a proportional and targeted manner. The NGB is prominent in providing continuous supervisory oversight in assessing risks, monitoring the implementation of risk management processes, and in obtaining new supervisory information related to new licenses and risk assessments. It represents an integral part of the entire supervisory process.

In Georgia, banks are subject to capital requirements defined by Basel III standards and the regulations of the European Parliament and Council dated June 26, 2013, No. 575/2013, and Directive 2013/36/EU. The minimum capital requirements are stipulated for the “Regulation on Capital Adequacy Requirements for Commercial Banks”. According to Pillar 1, the minimum capital requirements are determined as follows: Basic Primary Capital Ratio - 4.5%; Initial Capital Ratio - 6%; Supervisory Capital Ratio - 8% (Regulation on Capital Adequacy Requirements for Commercial Banks, Order No.100/04, 2013).

In addition to meeting these minimum requirements, a commercial bank should mandatorily ensure compliance with
additional capital buffer requirements for exposures not covered by Pillar 1.

Effective and sound corporate governance in banks is necessary to ensure the proper functioning and sustainability of the banking sector. Corporate governance issues for banks operating in Georgia are described in the “Corporate Governance Code of Commercial Banks”. This document is based on best practices and recognized global standards (On the Approval of the Corporate Governance Code for Commercial Banks, 2018).

For further development and full compliance with banking sector standards, the NBG actively cooperates with international organizations, various foreign central banks, and international groups responsible for banking supervision. This cooperation extends to the Group of Banking Supervisors from Central and Eastern Europe – BSCEE and Basel Consultative Group – BCG. The results of this cooperation in terms of employment, membership in supervisory groups, and agreements with various countries show that information sharing is facilitated and in line with international best practices.

For regulators in the financial sector, encouraging meaningful innovation and facilitating its implementation are critical tasks. Accordingly, the NBG encourages the development of financial innovation and supports its implementation for successful business operations. This approach involves both improving the supervisory framework and creating a successful foundation for financial technology infrastructure. Operational activities cover two main areas: the development of financial infrastructure and the promotion of supervisory standards.

In pursuit of regulatory objectives, the NBG faces the challenge of finding an optimal balance between fostering innovation and managing risks associated with it. It is noteworthy that a risk-oriented approach to the utilization of innovative solutions contributes to maintaining high stability and integrity within the Georgian banking sector (On determining the main directions of supervision and regulation of the financial sector, 2022).

The NBG has successfully taken comprehensive steps guided by the goal of fostering innovation and development of the
FinTech ecosystem. These initiatives include standardizing open banking, facilitating most electronic payments, working to obtain digital currencies, and efforts to reduce fixed costs for FinTech companies, particularly the costs associated with setting up a digital bank.

The activities of the NGB are related to several key priorities related to climate change. An important aspect is the examination and analysis of climate change and its impact on the economy, and the financial sector. The focus is on risk assessment of important changes in climate scenarios and climate-related stress testing. The objective is to contribute to the financial stability and financial sustainability of institutions by addressing climate change. These business activities include climate scenario analysis and stress testing as critical components for understanding and managing climate risk.

To ensure the resilience of the financial sector to climate-related risks, the most important issue is to focus on and address environmental, social and governance (ESG) factors, as climate change, as a major environmental factor, is essential to support stable and sustainable economic development (Gelitashvili, Burdiashvili, & Chelidze, 2023).

To achieve stability, sustainability, transparency and competitiveness in the financial market, the NGB has initiated measures, starting from the beginning of 2023, aimed at determining the systemic importance of banks and updating their buffers. This strategic document is crafted following the best international practices, focusing on bolstering the resilience of the banking system through revised measures addressing systemic importance. The assigned scores for banks' systemic importance, coupled with their respective weights, have been defined. Notably, the threshold for the systemic importance score is established at 8%, and a buffer range for systemic resilience is set at 0.5%.

Using the mentioned methodology, there are three systemic commercial banks in Georgia. They have determined the following buffer rates: JSC TBC Bank – 2.5%; JSC Bank of Georgia – 2.5%; JSC Liberty Bank – 1%.

The upper threshold of the systemic buffer, which is currently 2.5%, will be adjusted in case the concentration of
FINANCE AND CREDIT

Deposits of each bank exceeds 40% in the banking sector. In such a scenario, the upper threshold for the systemic buffer set for the bank will increase to 3%. To meet the return requirement, the bank must reduce its share of deposits based on the specific methodology by at least 2.5%.

The NGB has developed a document - Supervisory Strategy for more effective regulatory planning, increased predictability of future events in the industry, and ensuring access to information on supervisory priorities and plans for various stakeholders.

The first document of Supervisory Strategy, prepared by the NGB, was released in 2020. It outlined strategic priorities for the years 2020-2022 and the corresponding operational activities aimed at achieving these goals. The identified strategic priorities included strengthening leadership and initiatives for a renewed corporate culture, enhancing collaboration with interested parties, ensuring the effective functioning of the financial sector, aligning with international standards, and integrating emerging financial technologies into the ecosystem (Supervisory strategy 2020-2022, 2020).

In August 2023, the NGB released the final Supervisory Strategy document for the years 2023-2025. During its development process, active involvement and collaboration were ensured with key stakeholders, including the financial sector, private and public sectors, and other interested parties. The document serves the purpose of fulfilling the systemic mandate, providing insights into the vision and objectives, outlining strategic priorities, and planning the implementation of corresponding activities for achieving the goals set in the document.

The five key supervisory priorities of the 2023-2025 Supervisory Strategy were identified, taking into account in-depth analysis of international practice and trends, input from various stakeholders, recommendations from foreign partners, commitments by the NGB to the stream, and needs identified within the supervisory mandate. The supervisory priorities include: improving the financial sector risk management framework and responding proactively to outcomes; promoting competition in the financial sector; encouraging...
financial innovation and the development of supervisory technologies; converging to international standards; strengthening the supervisory function of the NGB and increasing transparency (Supervisory strategy 2023-2025, 2023).

The supervisory strategy document is updated annually, as it has become an important reference document for representatives of the financial sector.

The goal of the NGB is to represent the current status and readiness of Georgia's financial system and to plan for the future. Accordingly, the structure developed by it aligns with the priorities and planned activities set by it to achieve these goals.

To achieve the set priorities and goals, the NGB relies on its strengths and advantages, among which it is based on: employees and values; in-depth supervisory vision and awareness; evaluating the sector from a systemic perspective; strong regulatory powers.

Implementation Risks of the Supervisory Strategy. There are risks and external factors that, like operational environment issues, can impact the effectiveness of the supervisory strategy/certain parts of it. These include: a change in priorities caused by force majeure circumstances, unforeseen elements in the supervisory strategy, or other external factors unexpected for the NGB; risks related to the recruitment and retention of the necessary personnel required for implementing the strategy; Defects/damage or the absence of infrastructure hindering the normal operation of the NGB and other entities.

Both the analysis of implemented measures and planned activities clearly demonstrate that the National Bank of Georgia actively contributes to the stable and effective functioning of the financial system, the creation of a competitive environment, the control of systemic risk, and the reduction of risks. The existing prudential supervision regime is oriented towards the sustainable functioning and stable development of the entire financial system.

References:


