

Although survey¹ participants reported slightly worsened assessments of the current state of the financial sector, they were still satisfactory. Respondents believe that the state of the financial sector has deteriorated over the last six months. Expectations for the next six months are also mostly pessimistic – most respondents changed their views from positive to negative compared to the replies they provided in November 2019. Although the total risk level in the financial sector was believed to have increased slightly, it was not higher than some previous survey figures. The sector's resilience to high-impact negative events was little changed – it edged down slightly below the average figure. Financial institutions reported a decrease in their risk appetite.

In May 2020, respondents continued to cite corruption and the performance of the law enforcement authorities and the judicial system as the main source of risk. There was a sharp increase in risks of worsening economic activity and movements in global commodity prices – these risks were ranked among the top five risks. Since these surveys were launched, fraud and cyber threats have been ranked among the top five main sources of risk. Meanwhile, possible failures of and significant financial difficulties at financial institutions were ranked as the least important factor.

Respondents reported worsened assessments of the current state of the financial sector compared to the previous survey (November 2019). That said, the balance of responses² changed only slightly, and remained positive (7%). About a third of top managers are still optimistic about the current state of the financial sector.

Despite assessing the current state as positive, the majority of respondents (60%) said that the state of the financial sector had deteriorated over the past six months. The share of respondents who reported an improvement halved compared to the November 2019 survey.

There was a noticeable worsening in assessments of the financial sector outlook for the next six months. In November 2019, only 4% of respondents expected a deterioration, while now a deterioration is expected by 71% of respondents.

Assessments of the overall level of risk in the financial sector have remained negative for five reports running. The percentage of respondents who referred to the overall level of risk as high or very high was 37% in May 2020, up from 23%.

Despite the country entering an economic crisis, the assessment of the financial sector's resilience to high-impact negative events was little changed compared to the previous survey. A total of 67% of respondents described the financial sector's resilience as moderate, while 22% referred to it as low or very low (compared to 20% in November 2019).

For five reports running, respondents have cited corruption and the performance of the law enforcement authorities and the judicial system as the main source of risk. Some 86% of respondents believed this factor to be a source of high or very high risk. There was a sharp increase in risks of worsening economic activity and movements in global commodity prices. A total of 74% and 67% respondents respectively said in May 2020 that these risks were high, compared to 23% and 39% in November 2019. The top five main sources of risk also included fraud and cyber threats, and the political and social situation in Ukraine.

Risks that could arise from economic activity and changes in the inflow of foreign capital were said to have increased the most.

The risk arising from competition on the financial services market was reported to have decreased most of all. In addition, the factors of the quality of legislation and the tax system, and the state of protection of creditor and investor rights moved down four notches each compared to the previous survey. They were ranked as the top five main sources of risk in the previous survey. Despite the generally higher assessment of threats to the financial system, the risk of bankruptcy, according to respondents, is currently the least significant.

The risk appetite of financial institutions dropped dramatically, as the balance of responses turned from positive to negative. A total of 42% of top managers reported a decrease in risk appetite.

¹ See page 5 for information about the survey.

² Here and below, the balances of responses are aggregates, calculated as the sum of the numbers of each response weighted by weight coefficients ranging from -1 to 1. For example, 1 for "improved greatly," 0.5 for "improved," 0 for "no change" and so on. Balances of responses can lie between ±100. A positive balance of responses shows that respondents generally estimate that an indicator has improved or a risk has declined.

Figure 1. How respondents assess the current state of the Ukrainian financial sector

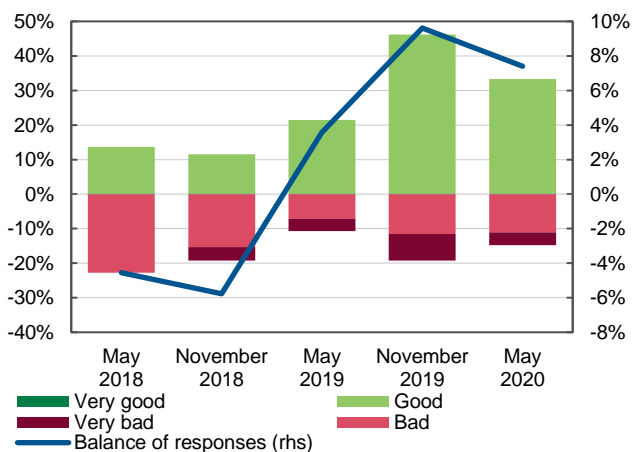


Figure 2. How respondents think the state of the Ukrainian financial sector has changed over the last six months

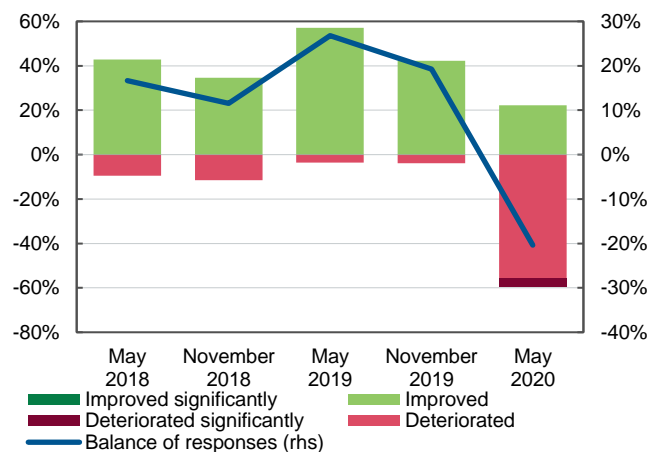


Figure 3. How respondents expect the state of the Ukrainian financial sector to change over the next six months

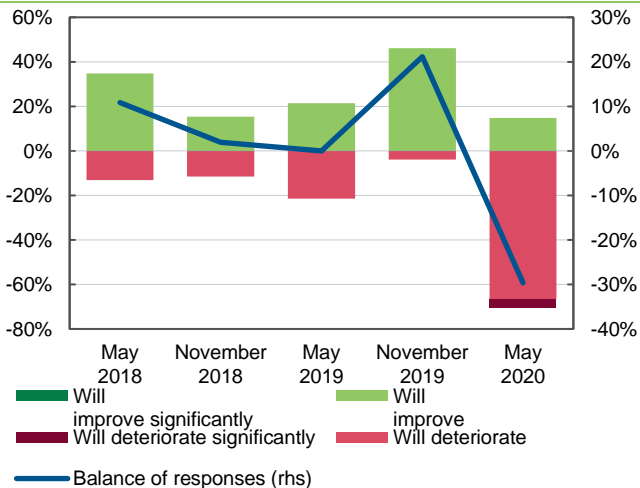


Figure 4. Perceptions of the total risk level in the Ukrainian financial sector

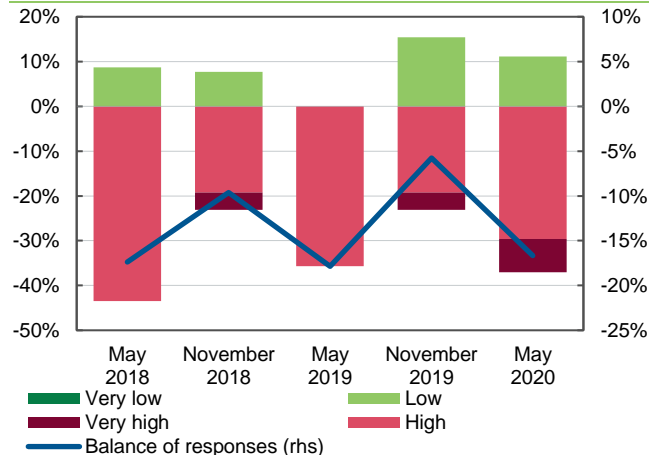


Figure 5. Perceptions of the resilience of the Ukrainian financial sector to high-impact negative events

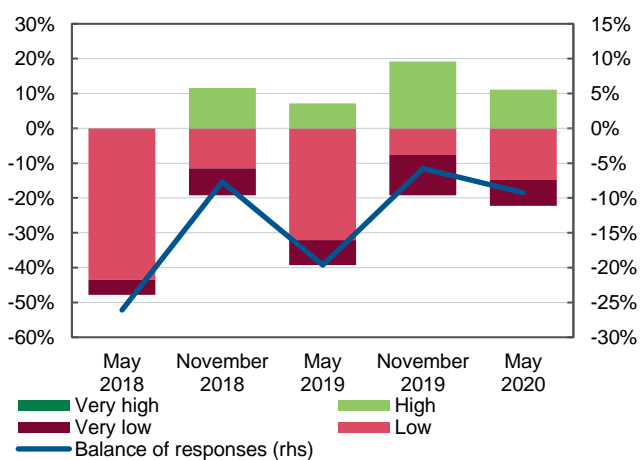


Figure 6. How respondents' risk appetite has changed over the last six months

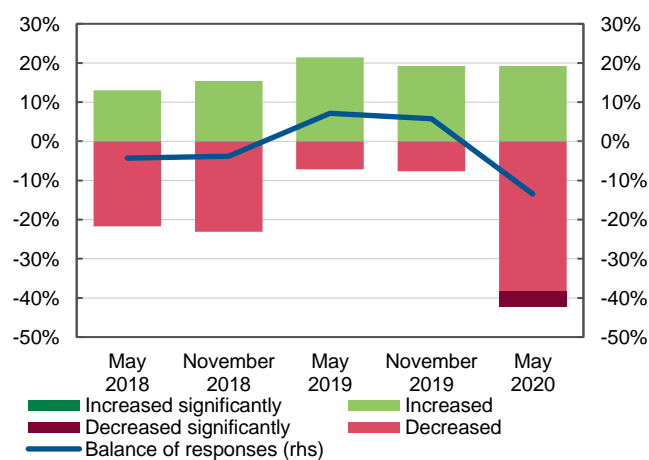
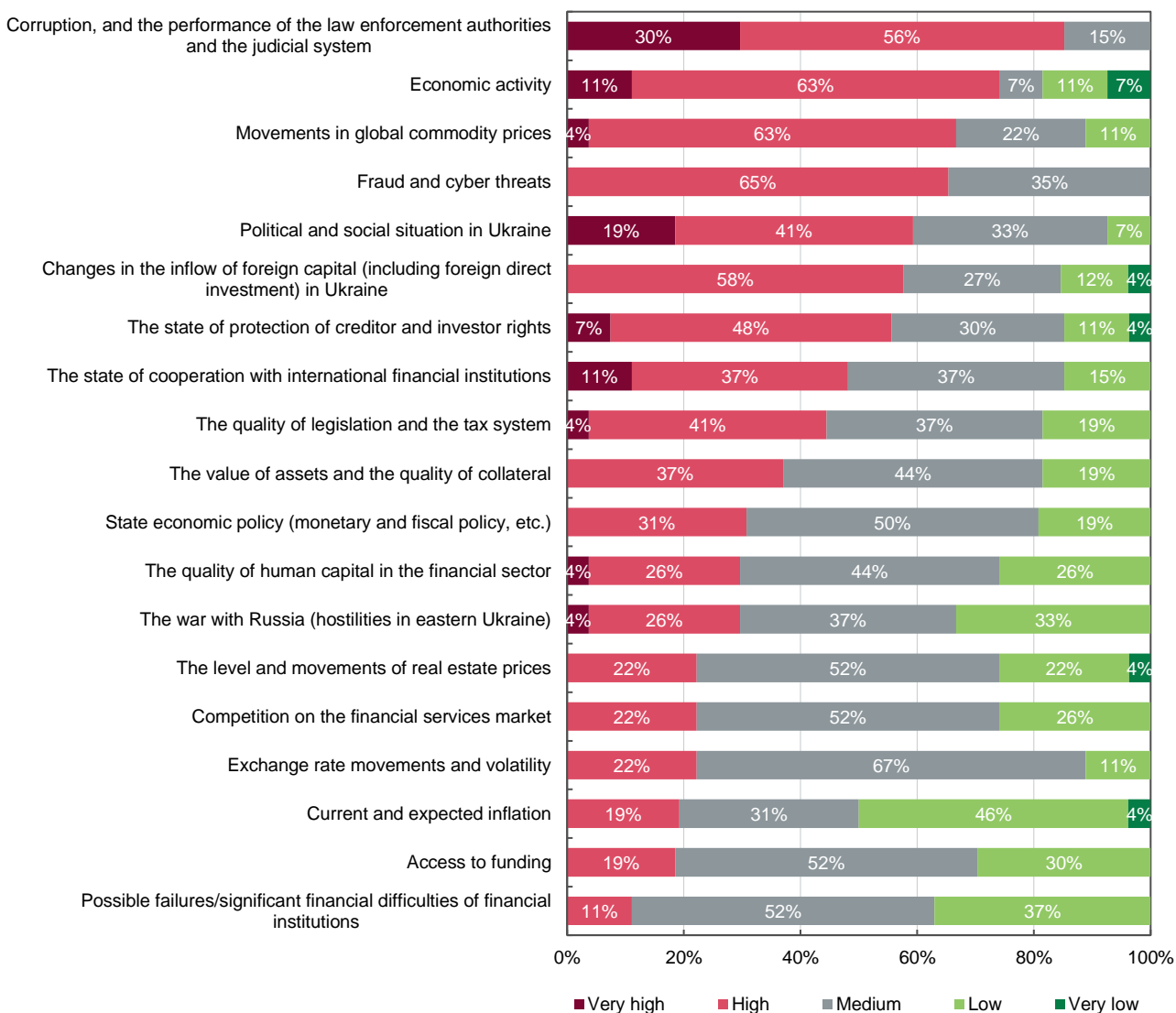


Figure 7. The risk level in the financial sector, as determined by specific factors, May 2020*



* The order in which the factors appears in this figure has been determined on the basis of “very high” and “high” responses.

Table 1. Ranks of risk factors (determined on the basis of “very high” and “high” responses)

| Risk factors | Rank, May 2020 | Rank, November 2019 | Difference, +/- |
|--|----------------|---------------------|-----------------|
| Corruption, and the performance of the law enforcement authorities and the judicial system | 1 | 1 | 0 |
| Economic activity | 2 | 13 | 11 |
| Movements in global commodity prices | 3 | 7 | 4 |
| Fraud and cyber threats | 4 | 2 | -2 |
| Fraud and cyber threats | 5 | 4 | -1 |
| Changes in the inflow of foreign capital (including foreign direct investment) in Ukraine | 6 | 11 | 5 |
| The state of protection of creditor and investor rights | 7 | 3 | -4 |
| The state of cooperation with international financial institutions | 8 | 5 | -3 |
| The quality of legislation and the tax system | 9 | 5 | -4 |
| The value of assets and the quality of collateral | 10 | 8 | -2 |
| State economic policy (monetary and fiscal policy, etc.) | 11 | 13 | 2 |
| The war with Russia (hostilities in eastern Ukraine) | 12 | 8 | -4 |
| The quality of human capital in the financial sector | 12 | 11 | -1 |
| Exchange rate movements and volatility | 14 | 15 | 1 |
| Competition on the financial services market | 14 | 8 | -6 |
| The level and movements of real estate prices | 14 | 18 | 4 |
| Current and expected inflation | 17 | 19 | 2 |
| Access to funding | 18 | 15 | -3 |
| Possible failures/significant financial difficulties of financial institutions | 19 | 17 | -2 |

Annex: Survey findings

| | Balance of responses, % | | | | | Answer options, May 2020, % | | | | | N |
|--|-------------------------|-------|-------|-------|-------|--------------------------------|------------------|-----------------|--------------|----------------------------|----|
| | 05'18 | 11'18 | 05'19 | 11'19 | 05'20 | | | | | | |
| 1. What is your perception of state of the Ukrainian financial sector today? | | | | | | Very bad | Bad | Satisfactory | Good | Very good | |
| | -5% | -6% | 4% | 10% | 7% | 4% | 11% | 52% | 33% | 0% | 27 |
| 2. How do you think the state of the Ukrainian financial sector has changed over the last six months? | | | | | | Deteriorated significantly | Deteriorated | Has not changed | Improved | Improved significantly | |
| | 17% | 12% | 27% | 19% | -20% | 4% | 56% | 19% | 22% | 0% | 27 |
| 3. How do you think the state of the financial sector will change over the next six months? | | | | | | Will deteriorate significantly | Will deteriorate | Will not change | Will improve | Will improve significantly | |
| | 11% | 2% | 0% | 21% | -30% | 4% | 67% | 15% | 15% | 0% | 27 |
| 4. What is your perception of the total risk level in the financial sector? | | | | | | Very high | High | Medium | Low | Very low | |
| | -17% | -10% | -18% | -6% | -17% | 7% | 30% | 52% | 11% | 0% | 27 |
| 5. What is your assessment of the financial sector's resilience to high-impact negative events? | | | | | | Very low | Low | Medium | High | Very high | |
| | -26% | -8% | -20% | -6% | -9% | 7% | 15% | 67% | 11% | 0% | 27 |
| 6. What are your perceptions of the financial sector's risks stemming from the following factors | | | | | | Very high | High | Medium | Low | Very low | |
| 6.1. Political and social situation in Ukraine | -46% | -37% | -57% | -29% | -35% | 19% | 41% | 33% | 7% | 0% | 27 |
| 6.2. The war with Russia (hostilities in eastern Ukraine) | -15% | -17% | -18% | -12% | 0% | 4% | 26% | 37% | 33% | 0% | 27 |
| 6.3. Corruption, and the performance of the law enforcement authorities and the judicial system | -54% | -52% | -57% | -58% | -57% | 30% | 56% | 15% | 0% | 0% | 27 |
| 6.4. The quality of legislation and the tax system | -20% | -29% | -14% | -23% | -15% | 4% | 41% | 37% | 19% | 0% | 27 |
| 6.5. The state of protection of creditor and investor rights | -33% | -42% | -36% | -31% | -22% | 7% | 48% | 30% | 11% | 4% | 27 |
| 6.6. Economic activity | 7% | -8% | 7% | 4% | -30% | 11% | 63% | 7% | 11% | 7% | 27 |
| 6.7. Current and expected inflation | -4% | -4% | 16% | 31% | 17% | 0% | 19% | 31% | 46% | 4% | 26 |
| 6.8. State economic policy (monetary and fiscal policy, etc.) | 2% | -6% | 0% | 2% | -6% | 0% | 31% | 50% | 19% | 0% | 26 |
| 6.9. Exchange rate movements and volatility | -20% | -20% | -9% | 6% | -6% | 0% | 22% | 67% | 11% | 0% | 27 |
| 6.10. Changes in the inflow of foreign capital (including foreign direct investment) in Ukraine | 4% | 2% | -10% | 2% | -19% | 0% | 58% | 27% | 12% | 4% | 26 |
| 6.11. Movements in global commodity prices | -15% | -27% | -24% | -13% | -30% | 4% | 63% | 22% | 11% | 0% | 27 |
| 6.12. The state of cooperation with international financial institutions | -35% | -44% | -54% | -21% | -22% | 11% | 37% | 37% | 15% | 0% | 27 |
| 6.13. Possible failures/significant financial difficulties of financial institutions | 11% | 25% | 18% | 20% | 13% | 0% | 11% | 52% | 37% | 0% | 27 |
| 6.14. Competition on the financial services market | 13% | -10% | 5% | -4% | 2% | 0% | 22% | 52% | 26% | 0% | 27 |
| 6.15. Access to funding | 9% | -21% | -18% | 10% | 6% | 0% | 19% | 52% | 30% | 0% | 27 |
| 6.16. The quality of human capital in the financial sector | -4% | -10% | -13% | -2% | -4% | 4% | 26% | 44% | 26% | 0% | 27 |
| 6.17. The value of assets and the quality of collateral | -13% | 0% | -7% | -12% | -9% | 0% | 37% | 44% | 19% | 0% | 27 |
| 6.18. The level and movements of real estate prices | 17% | 17% | 18% | 15% | 4% | 0% | 22% | 52% | 22% | 4% | 27 |
| 6.19. Fraud and cyber threats | -37% | -37% | -25% | -35% | -33% | 0% | 65% | 35% | 0% | 0% | 26 |
| 7. How has the risk appetite of your institution changed over the last six months? | | | | | | Decreased significantly | Decreased | Has not changed | Increased | Increased significantly | |
| | -4% | -4% | 7% | 6% | -13% | 4% | 38% | 38% | 19% | 0% | 26 |

Information about the survey

In May 2018, the NBU introduced a survey of the financial sector's systemic risks. Twice a year, top managers from the largest Ukrainian banks and non-bank financial institutions respond to the questions of this survey of financial sector risks. Central banks use such surveys to monitor perception of such risks by market participants, and to respond to them in a timely manner.

This report shows how top managers of financial institutions assessed the state of the financial sector over the past six months, and what they expect for the following six months. This survey was carried out from 12 May through 25 May 2020. Executives from 18 banks, 6 insurance companies, and 3 investment firms took part in this survey. The survey did not cover financial institutions under sanctions. Final results were calculated by giving equal weight to each survey response, regardless of the size of the bank/company, or its market share.

The results are based on the respondents' opinions and do not necessarily reflect the NBU's views.

The next report will be published in November 2020.