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Security of the Financial System of Ukraine under Martial Law

Bezpieczeństwo systemu finansowego Ukrainy w stanie wojennym

• Abstract •

The purpose of the article is to present the financial situation in Ukraine and the activities of the National Bank of Ukraine (NBU) for the stability of the financial system during the ongoing war with Russia. The impact of the war on the financial stability of the banking sector is undeniable. The main goal was to analyze and assess the causes of the deteriorating financial situation of the country, the increase in the level of credit risk, the causes of the deterioration of the quality of the loan portfolio, and the increase in the level of non-performing assets in Ukrainian banks. The development of the ratio of assets and liabilities in foreign currencies in Ukrainian banks in the years 2018–2022 was considered. Statistical data published in the reports of the National Bank of Ukraine and the State Statistical Service of Ukraine were used for the analyses and assessments carried out.

Keywords: National Bank of Ukraine; financial system; economy; credit risk; non-performing loan assets (NPL); loan portfolio

• Abstrakt •

Celem niniejszego artykułu jest przedstawienie sytuacji finansowej w Ukrainie oraz działań Narodowego Banku Ukrainy (NBU) na rzecz stabilności systemu finansowego w czasie toczącej się wojny z Rosją. Oddziaływanie wojny na stabilność finansową sektora bankowego jest niezaprzeczalne. Głównym celem było zanalizowanie i ocena przyczyn pogarszającej się sytuacji finansowej kraju, wzrostu poziomu ryzyka kredytowego, przyczyn pogorszenia jakości portfela kredytowego oraz wzrostu poziomu aktywów zagrożonych w ukraińskich bankach. Rozważono kształtowanie się relacji aktywów i pasywów w walutach obcych w bankach Ukrainy w latach 2018–2022. Do przeprowadzonych analiz i ewaluacji wykorzystano dane statystyczne publikowane w raportach Narodowego Banku Ukrainy i Państwowej Służby Statystycznej Ukrainy.

Słowa kluczowe: Narodowy Bank Ukrainy; system finansowy; gospodarka; ryzyko kredytowe; aktywa zagrożone (NPL); portfel kredytowy

Introduction

Throughout 2022, the ongoing Russian-Ukrainian war had a negative impact on the Ukrainian economy. However, thanks to exceptional monetary, fiscal, regulatory and supervisory measures, as well as sound capital and liquidity positions, the banking sector has played a key role in the overall response to the situation. Banks supported Ukraine's real economy by providing loans and satisfying the liquidity needs of households and non-financial enterprises. In the last months of 2022 and in the first months of 2023, the overall risk structure has changed significantly. In particular, there was a high level of risk and uncertainty, which complicated the functioning of the financial sector, but macrofinancial stability was and continues to be supported by significant international financial assistance. Under the circumstances of martial law and acting in accordance with its mandate, the NBU identified, assessed and monitored existing and new types of risk and sources of vulnerability in the financial sector. The NBU tried to adjust and prioritize its supervisory activities in order to ensure, if necessary, an operative change of resources in accordance with the existing risk.

The NBU, in close cooperation with the competent national authorities, recorded and assessed the greatest challenges expected to affect the supervised institutions. In its assessment, the NBU indicated the main risks from the point of view of the banking sector and its susceptibility to threats and adverse phenomena.

The Russia-Ukraine war constitutes the main factor of risk, threats and adverse phenomena, having led to an unprecedented decline in economic activity in Ukraine in 2022. The Ukrainian economy shrank by over 30% in 2022, with the annual inflation rate amounting to 26.6% (Bilous, 2022). Economic activity in 2023 is projected to remain below the level of the previous year, and the pace of the recovery will be uneven. In 2023, the Ukrainian economy may grow by about 0.3%, and the inflation rate is projected to fall to 18.7% (*Inflation Report...*, 2023). Continuation of the war increases uncertainty about the economic outlook and leads to the inhibition of long-term economic growth and development, at least until the peace is secured. The extent to which projected levels of economic activity and inflation are at risk depends very much on how the war unfolds, and in particular on its impact on energy markets.

An important factor weakening the pace of recovery is the increase in geopolitical tensions related to the sanctions imposed on Russia and Belarus by the EU, the USA, and other countries. The renewed intensification of trade conflicts has a negative impact. Also important is the increase in tensions of the financial markets, the growth in commodity prices and uncertainty in the economy, which is manifested

by a slowdown in economic growth and rising inflation. Geopolitical tensions exert a negative impact on the growth outlook and will therefore pose a threat to key macroeconomic and financial indicators.

Stability of the Ukrainian financial system during the war

The stability of the financial system is understood as a state in which the financial system performs its functions in a continuous and effective manner, even in the event of unexpected and unfavorable disturbances on a significant scale. Ukraine's financial system has survived the hardest challenges of the first year of aggression, performing its functions and effectively coping with the challenges posed by the Russian-Ukrainian war.

The National Bank of Ukraine is jointly responsible for the stability and development of the Ukrainian financial system. The NBU was granted such a mandate in 2015 (*The Law of Ukraine...*, 1999), when the function of promoting financial stability was established (as the second priority after maintaining price stability). The NBU actively participates in the construction of the financial safety net in Ukraine and in the work of the Financial Stability Committee for macroprudential supervision and crisis management. The President of the NBU is a member of the Financial Stability Committee, alongside the Minister of Finance, the president of the National Securities and Exchange Commission, and the president of the Management Board of the Bank Guarantee Fund. The Financial Stability Committee acts as a macroprudential authority and is responsible for crisis management in the financial system.

The NBU takes measures to maintain the stability of the financial system and to minimize the impact of the war. This involves, on the one hand, applying solutions aimed at the financial institutions themselves, and on the other hand, taking measures to facilitate the situation of Ukrainian banks' customers and prevent panic, which would be extremely dangerous, even in calmer periods than during the war. The first thing, the NBU performs qualitative analyses and informs about identified threats. The dissemination of this type of knowledge is intended to help maintain financial stability and identify the level and scope of risk in the financial system.

The restrictive monetary policy measures applied by the NBU contributed to the stability of the financial system during the first year of the war. The most important activities of the NBU in this direction were, in particular, setting interest rates at a constant level of 25 percent, fixing the exchange rate of the hryvnia, and introducing restrictions on the functioning of the banking system and the currency

market. Foreign aid played a key role in maintaining the stability of Ukraine's financial system in the face of the economic collapse caused by the war.

The NBU Report for 2022 presents the results of the financial situation of the banking sector and the sector of non-bank financial institutions, which deteriorated in the analyzed period. Basing a synthetic assessment of the stability of the domestic financial system on NBU research, it should be noted that the outlook for the system's stability in 2023 will deteriorate.

Among the risk factors affecting the stability of the financial system, macro-economic risk and financing risk should be distinguished. The interdependence between the deterioration of the financial conditions and the weakening of economic activity, which increases the risk of these processes taking place, would adversely affect the stability of the financial system in Ukraine. This situation has led to higher funding risks and increased costs of credit risk in the banking sector. In addition, turmoil in the global financial markets has a negative impact on Ukraine's GDP, which will lead to a deterioration in the quality of loans. Moreover, the economic slowdown will affect credit losses in the portfolio of unsecured loans, as the share of loans with a high ratio of loan-to-value of collateral is significant in the Ukrainian banking system.

The increase in uncertainty as to the scope and scale of durability of disruptions in the functioning of the world economy caused by Russia's armed aggression against Ukraine is the main external factor affecting the conditions of operation of the Ukrainian financial system.

The economic situation of Ukraine

The Ukrainian economy entered 2022 with a high pace of economic development, having ended 2021 with an all-time high GDP of \$195 billion, an increase in consumer spending and a progressive rebuilding of inventories. The economy was gaining momentum, which was also manifested in a not excessively high unemployment rate of 10.3% and an increase in wages by 37.6% compared to 2020. In 2022, inflation was one of the biggest economic challenges. After a period of relatively low level (in 2020 – 5%, in 2021 – 10%), at the end of 2022 it approached 26.6% (Pavlysh, 2023). In this period, measures were also taken in the field of monetary and fiscal policy aimed at reducing the pace of further growth in the prices of consumer goods and services. These efforts must continue in 2023.

Before the war broke out, solid long-term growth was forecasted for the Ukrainian economy. However, as soon as Ukraine's economy had started its recovery from

the pandemic, the Russian invasion brought new challenges. Forecasts of economic decline in Ukraine in 2022 were inflated. However, the projected decline in GDP dynamics because of the economic slowdown and the ongoing war was much smaller (30.4%) than the historically assumed level of over 35% (*Ukraine's Economy...*, 2023). Also, the NBU macroeconomic projections formulated in December 2022 point out to economic growth being expected in 2023 compared to a decline in 2022, even though public debt and budget deficit in relation to GDP remain at a high level. Large-scale shelling of energy infrastructure has also worsened the macroeconomic outlook. This had an impact on the stability of the financial system in Ukraine and will certainly affect the profitability of financial institutions; moreover, there is still significant uncertainty about the nature of the economic situation, especially in countries that are Ukraine's trading partners.

For this reason, the deterioration of the economic growth outlook and the persisting debt crisis in Ukraine indicate that the risk of materialization of a threat to the stability of the financial system has increased. There is no doubt that the current war in Ukraine constitutes a serious challenge for the entire economy and economic policy. Even when the war is over, Ukraine may be perceived for a certain period as an unstable and high-risk country, even if this perception is not reflected in reality. The destruction caused by the war will also encourage a permanent increase in the number of people leaving Ukraine. These extraordinary circumstances make it extremely difficult to assess Ukraine's macroeconomic situation in the coming months. Current economic development may be distorted much more strongly.

The war and the resulting changes in economic conditions (sanctions, changes in exchange rates, demand for necessities) make this challenge much more difficult. Regardless of the introduced solutions, inflation can be expected to increase further and stabilize at a high level throughout 2023. This will pose a challenge not only for the entire economy, but also for banks operating in Ukraine. The decline in the interest in investment activity in the conditions of war will constitute a barrier to lending activity in most economic areas. Controlling inflation will become the most important problem from the perspective of creating conditions for further economic development of the country.

According to the latest System Stability Report – the financial report published periodically by the National Bank of Ukraine – the increase in uncertainty related to the scope, scale and duration of disturbances in the functioning of the global economy caused by Russia's armed aggression against Ukraine, constitutes the main external factor affecting the situation of the Ukrainian financial system (*Report on Financial Stability*, 2022).

The outlook for the situation of the Ukrainian economy has changed significantly, as the Russian invasion dealt an unprecedented blow. This will have an impact on the functioning of the Ukrainian financial system. It should be noted, however, that in 2023 the growth rate of the Ukrainian economy may slow down more than forecasts in 2023, as the ongoing war has worsened the prospects for a post-pandemic recovery both in the country and across Europe.

The Ukrainian economy proved able to quickly adapt to difficult war conditions. However, the challenges of reconstruction will be enormous, from building physical infrastructure, mainly energy, to the functioning of institutions in the face of a potentially significant inflow of aid funds. An important driving factor for the country's economic reconstruction after the war will be foreign investments, as well as the mechanism of Ukraine's integration with the EU single market.

Banking system under martial law

The indicators measuring the condition of the Ukrainian banking sector, analyzed at the end of 2022, pointed out to a good condition of banks. Equity in capital, the rate of growth of lending (especially at the end of the year) and the positive financial result serve as a basis for the statements that the situation of the Ukrainian banking sector is stable.

Banks continued to renew their outlets in the liberated regions and to regain customer confidence. A significant part of the banks in Ukraine recorded an increase in funds from customers, especially in the form of household's term deposits. The growth rate of foreign currency deposits is also increasing. The loan portfolio shrank as a result of both falling demand and rising credit risk losses. The share of non-performing loans increased (*Overview of the Banking Sector, 2023*, pp. 1–4). Despite significant write-downs, the banking sector posted an annual profit.

According to the information provided by the NBU (*Report on the Condition...*, 2022), despite the increase in allocations for provisions, the banking system generated UAH 24.7 billion in profit, i.e., more than three times less than in 2021, including UAH 17.3 billion – in Q4. Of course, there are banks that have suffered losses and banks, which record profits. Over 20 banks suffered losses, including 2 state-owned banks of Ukraine (Ukreximbank – losses of UAH 6.88 billion, and Ukrigasbank – losses of UAH 2.76 billion). In turn, in the private sector with foreign capital, Sense Bank (until July 2022 JSC “Alfa-Bank”) with Russian capital suffered the greatest losses. PrivatBank, Ukraine's largest state-owned bank, recorded a profit

of over 30 billion, and UKRSIBBANK with foreign capital – 3.53 billion UAH (*Overview of the Banking Sector*, 2023, pp. 1–4).

In 2022, banks put more emphasis on the increase in fee and commission income, as attacks on energy infrastructure had a moderate impact on the dynamics of commission income. Revenues from foreign exchange operations supported the growth in operating revenues. The banking system survived and quickly adapted to work in the conditions of war, becoming operationally stable, liquid and profitable (*Overview of the Banking Sector*, 2023, pp. 9–11).

As for profitability, after the decline that occurred in 2022, in 2023, banks expect moderate growth, although not a very strong one. However, these forecasts are burdened with the risk related to the further course of the war and its adverse economic consequences. This situation fuels pressure on banks to eliminate existing vulnerabilities and adapt business models to the conditions and challenges of war.

The stability of the banking system was preserved thanks to the reforms carried out in previous years, the efforts of the banks themselves, timely actions, and the support of the National Bank of Ukraine.

Although the war in Ukraine is not able to shake the foundations of the Ukrainian banking sector, it may amplify existing tensions or weaknesses in the banking system. First of all, the greatest threat to the stability of the banking sector is the occurrence of many shocks over the last year, leading to losses in the banking system and negatively affecting the long-term ability of banks to generate profits.

Working conditions for financial institutions remain difficult: the war drags on and Russia continues to use terror tactics and destroy civilian infrastructure. Despite this, the financial sector operates efficiently: payments are made on time and customers have free access to their own funds. However, the consequences of large-scale shelling reduce the growth rate of demand for banking services and cause additional credit losses and operational losses for banks. Public confidence in banks is stable and remains at a relatively stable level.

Changes in the structure of the bank balance sheet

When assessing the lending policy of commercial banks, it is worth noting that the growth rate of consumer loans and car loans at the end of December 2022 was negative (over -30%), and that the amounts of these loans were successively decreasing. This trend was noticeable from the beginning of the war. The reason for the reduction of the loan portfolio is the awareness of credit risk and the small number of new loans that do not compensate for the amount of currently repaid

ones. The volume of unsecured consumer loans is falling sharply, primarily as a result of the tightening of banks' lending policies resulting from a significant deterioration in the quality of loans granted under a lenient lending policy and (which is related to) high impairment losses. Commercial banks also decided to change the currency structure of newly granted loans, increasing the share of hryvnia loans, although foreign currency loans still have a significant share in their portfolio, which poses a danger of a credit risk arising from the depreciation of the Ukrainian currency (*Report on Financial Stability*, 2022).

According to the currency structure of the banking sector's balance sheet in 2018–2022 in Ukraine (Table 1), it follows that in 2018 and 2022 an increase in the value of both foreign currency liabilities and assets was recorded. Foreign currency assets in 2022 amounted to UAH 819 billion and accounted for 30.2% of total assets compared to 28.8% at the end of 2021. Foreign currency liabilities amounted to UAH 657 billion, i.e., 35.1% of total liabilities compared to 32.9% at the end of 2021.

A significant increase in the value of both assets (by 15.7%) and foreign currency liabilities (by 21.3%) in 2022 resulted primarily from the weakening of the hryvnia. The phenomenon of high value of foreign currency loans granted to households is associated with the risk taken by banks and increases the risk in the financial system. It should be underlined that only a small part of households that receive income in foreign currencies is hedged against currency risk.

The challenges for banks arising from the war are primarily related to the need to create additional reserves. What is equally important, the war also affects the ability of banks to generate revenues, which further weakens the already low level of revenues and profitability. Undoubtedly, interest income will remain under constant pressure. This is partly mitigated by the high volume of loans; however, the potential tightening of credit standards and the expiration of government guarantees entail downside risk for the future. At the same time, revenues from fees and commissions are decreasing due to strong competition. All these factors combined with a parallel strong increase in the level of provisioning resulted in a decline in the rate of return on equity. Further development of the situation depends on how the hostilities will proceed.

Table 1. Currency Structure of the Banking Sector Balance Sheet in 2018–2022 (Billion UAH)

Year	2018	2019	2020	2021	2022
Assets					
Total assets	1 911	1 982	2 206	2 358	2 717
<i>of which in foreign currency</i>	779	718	746	679	819
Net assets	1 360	1 493	1 823	2 053	2 354
<i>of which in foreign currency</i>	495	492	585	583	731
Gross loans to business entities	919	822	749	796	801
<i>of which in foreign currency</i>	460	381	332	292	281
Net loans to business entities	472	415	432	540	529
Gross loans to natural persons	197	207	200	243	210
<i>of which in foreign currency</i>	61	38	31	21	13
Net loans to natural persons	114	143	149	200	134
Liabilities					
Funds of business (<i>deposits</i>)	430	525	681	800	943
<i>of which in foreign currency</i>	150	191	233	233	317
Funds of individuals (<i>deposits</i>)	508	552	682	727	934
<i>of which in foreign currency</i>	241	238	285	270	340
Change (y/y, %)					
Total assets	3.8%	3.7%	11.3%	6.9%	15.2%
Net assets	1.9%	9.8%	22.1%	12.6%	14.6%
Gross loans to business entities	6.3%	-10.6%	-8.8%	6.2%	0.7%
Gross loans to individuals	15.3%	5.0%	-3.5%	21.6%	-13.5%
Funds of business entities (<i>deposits</i>)	0.8%	22.1%	29.7%	17.4%	17.9%
Funds of individuals (<i>deposits</i>)	6.3%	8.6%	23.5%	6.6%	28.4%

Source: *Overview of the Banking Sector* (2023).

Credit risk is a challenge for Ukrainian banks

The increase in the value of credit risk and its effective management in Ukrainian banking sector is determined by the deterioration in both the economic and financial situation of a significant number of borrowers and the quality of credit portfolios. The increased importance of credit risk in banks is also related to the heightened exposure to such risks as: market risk of the borrower's activity or operational risk of credit transaction execution. Supervisory prudential standards constitute an important instrument for credit risk management. They define the requirements for capital adequacy, credit concentration, specific provisions as well as for limiting operational risk. In addition to supervisory prudential standards, banks rely, in the process of credit risk management, on internal regulations based on the recommendations of the NBU, e.g., internal concentration limits and monitoring rules. In addition to concentration limits and quantitative and qualitative diversification, syndicated loans, relevant provisions in the loan agreement, the assessment of creditworthiness is also of great importance. In the procedures for assessing this capacity, Ukrainian banks use Western European solutions.

In Ukraine, as in other countries of Central and Eastern Europe, there have been significant changes in banking in recent years. Before the crisis in 2008, the largest increase in assets concerned housing loans, while in the years 2018–2021 an increase in non-purpose cash loans was noticeable. Credit risk entails the risk of loss due to the default of a debtor. Due to the fact that banks have insufficient equity in relation to the value of assets, if a certain part of total loans becomes unpaid, the bank may find itself on the brink of bankruptcy. As scientific research shows, credit risk is by far the most important of all risk exposures in commercial banks. Over 90% of bank failures in the world result from exposure to credit risk.

Therefore, one of the main challenges for the banking sector and the NBU is credit risk. The potential negative impact on banks is further magnified by a clear vulnerability to external threats. In sectors – especially those hit hardest by the war – non-financial companies saw their profits fall sharply because of the war, and thus the risk of insolvency increased. At the same time, the labor market situation is likely to deteriorate in case of households related to these sectors, which in turn will be reflected in their ability to pay. These developments are accompanied by a growing risk of a correction in real estate markets. In Ukraine, residential real estate markets have suffered greatly, mortgage lending has almost disappeared, the mortgage market will remain inactive until the end of the war due to high risk, while activity in the commercial real estate sector is already slowly stabilizing.

Credit risk is identified as the risk of an individual borrower and the risk of the entire loan portfolio. Banks try to limit the credit risk based on the probability that the customer will not meet their obligations until the end of the loan agreement by assessing the borrower's creditworthiness and determining the credit rating. In Ukraine, the process of assessing the borrower's creditworthiness is very complex because of high share of the shadow economy in the national economy. It is estimated that in 2021 the above-mentioned share amounted to 31% of GDP (Schwartz, 2022). At the same time, it should be noted that in certain individual cases the financial statements of companies do not constitute reliable sources of information. In addition to the credit rating, the collateral itself is also very important. The situation with the recovery of collateral in Ukraine is not good, especially during the ongoing war, and the periods of forced debt collection are very long. In relation to the loan portfolio, banks apply various tools and methods for their measurement, assessment, and credit risk management. Portfolio diversification serves as one of the most important tools used by individual banks – banks try to diversify their loans to different clients to ensure low interdependence of settlement problems, since diversity reduces the likelihood that more debtors will have problems at the same time.

The economic downturn caused by the war will cause a deterioration in asset quality. It is necessary to pay attention to the financial difficulties experienced by non-financial enterprises and households due to the war rather than to the more permanent economic effects resulting from the deterioration of the macroeconomic environment due to the impact of both supply and demand factors. Difficulties with logistics, an increase in the prices of production raw materials, restrictions in trade relations and sanctions have a negative impact on the aggregate supply. On the demand side, rising energy and commodity prices as well as the cost of financing have a negative impact on the real income of households and enterprises. Increased uncertainty caused by the ongoing war is hampering investment and lowering consumer confidence. This lowers the credit ratings of companies and weakens the ability of households to service their debts. In addition, the risk of deterioration of the state's fiscal position as a result of the economic slowdown caused by the war decreases space for intervention in the area of the real economy. Hence, an increase in credit risk and a tightening of lending policy in banks can be expected.

Non-performing loans assets (NPL) are a threat to Ukrainian banks

The Ukrainian banking system in recent years has been characterized by a relatively high interest rate on non-performing loans (NPL) and a slow recovery of collateral. For a number of reasons, the total value of NPL has been declining since 2018 and was one of the reasons for the improvement in the macroeconomic situation, as reflected in GDP growth and increased purchasing power. In recent years, banks have made a significant change in terms of concentration, consisting in the transition from simply granting loans to the construction of appropriate debt recovery centers. Added to this is the strengthening of the market for the purchase and sale of non-performing loans.

Russia's invasion of Ukraine reversed the trend of a gradual reduction in the share of non-performing loans (NPL) in Ukrainian banks, which had been ongoing since 2018. During this time, the amount of NPL decreased by almost UAH 300 billion, and their share in the loan portfolio decreased from 55% to 27% on March 1, 2022. The consequences of the war, i.e., destruction of assets and collateral, loss of income and deterioration of borrowers' solvency, reduce the ability of banks to service loans, deteriorate the quality of their loan portfolios and lead to an increase in write-downs on provisions. Banks have already recorded significant credit losses – since the beginning of the war, the amount of write-downs for provisions for loans has exceeded UAH 100 billion and constitutes over 12% of the loan portfolio that banks had at the end of February 2022. Potential losses of the loan portfolio due to the war, economic crisis and energy terror by the aggressor may be as high as 30%. At the end of 2022, the NPL coverage ratio (the ratio of all loan loss provisions to NPLs) amounted to 95%.

The volume of loans and the share of non-performing assets (*Provisions on the Determination by Banks...*, 2016) in the banking sector as of January 1, 2023, amounted to 38% compared to January 1, 2022. The volume of non-performing loans increased during the year by UAH 87 million to UAH 432 billion (Table 2).

The assessment of assets will continue, so the volume of NPLs will continue to grow. The NBU expects banks to take a balanced approach to credit risk assessment, especially in relation to borrowers who lost their income as a result of the war and are unable to repay their debt. Banks should conduct flexible restructuring in case of borrowers with the prospect of business recovery, as well as appropriately assess the value of collateral, recognizing loss of access to property, its damage or destruction in a timely manner. The NBU plans to carry out an asset quality assessment in 2023 in order to confirm the correctness of the presented quality of the loan portfolio, the adequacy of creating provisions and to assess the actual amount of regulatory capital.

Table 2. Loan Volume and Share of NPL (Million UAH)

Assets	Jan 1, 2018	Jan 1, 2019	Jan 1, 2020	Jan 1, 2021	Jan 1, 2022	Jan 1, 2023
Credits:						
Corporate loans	892 900	959 601	847 259	795 405	835 658	847 586
<i>NPL</i>	500 263	535 770	456 074	371 157	301 665	363 321
<i>NPL share, %</i>	56.03	55.83	53.83	46.66	36.10	42.87
Household loans (including SEA* loans)	174 448	202 202	214 252	208 383	256 291	224 260
<i>NPL</i>	93 353	93 086	73 077	58 230	43 210	68 272
<i>NPL share, %</i>	53.51	46.04	34.11	27.94	16.86	30.44
Household loans (including SEA loans)	22 046	28 888	31 368	34 057	30 581	36 917
<i>NPL</i>	1 372	1 073	946	984	256	4
<i>c, %</i>	6.22	3.71	3.02	2.89	0.84	0.01
Credit to the authority of the government	1 519	2 867	4 717	1 519	2 867	24 800
<i>NPL</i>	10	838	683	10	838	507
<i>NPL share, %</i>	0.69	29.22	14.48	0.69	29.22	2.04
Total loans	1 090 914	1 193 558	1 097 595	1 049 579	1 149 567	1 133 563
<i>NPL</i>	594 999	630 767	530 780	430 371	345 131	432 105
<i>NPL share, %</i>	54.54	52.85	48.36	41.00	30.02	38.12

* Subject of Entrepreneurial Activity,

Source: *Overview of the Banking Sector* (2023).

Based on the results of the assessment, a transitional period for capital increases to the minimum regulatory values will be determined. Most banks will be able to recapitalize with future profits, but many banks will likely need shareholder support.

Summary

An efficiently operating central bank and banking system is the basis for the stability of the state's financial system. During the war, the NBU and the banking sector play an important role in maintaining balance in the financial markets, e.g., by taking quick radical decisions and implementing the rules of operation and execution of transactions, risk management, or maintaining liquidity. The analysis of the

impact of the NBU and commercial banks on the stability of the financial system in Ukraine, with an indication of activities and threats to this stability, which is the purpose of this article, leads to the conclusion that despite the good condition of the Ukrainian banking sector, the lending and deposit policy of banks should be conducted with particular caution. This is mainly due to the economic slowdown and the related increase in non-performing loans in banks' portfolios. The not very optimistic prospects for economic growth and the ongoing war pose a risk of materializing a threat to the stability of the financial system in Ukraine. Based on the assessment of the main risks and vulnerabilities in the banking sector, the NBU set supervisory priorities for 2023 in assessing asset quality, adequacy of provisioning and assessing the actual size of regulatory capital. Priority areas for the NBU for 2023 should include: credit risk and liquidity risk management; capital; maintaining business models and internal management, including ensuring the continuity of operation of bank branches under martial law.

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