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Abstract

This paper uses interviews with commercial bank officials to investigate how well the banking system assesses risk and allocates credit, monitors borrowers, facilitates risk diversification, and pools savings while the credit boom in Bulgaria is unfolding. Bank credit to enterprises more than tripled in only five years despite significant institutional problems in the country. The interviews show that the banking system adapts to the local conditions and performs its theoretical functions reasonably well. The area that is most severely influenced by weak institutions seems to be monitoring and exerting control over borrowers.