Pursuant to Article 17 paragraph 1 point 2) of the Law on the Central Bank of Montenegro OG RoM no. 52/00 and 47/01), and with regard to Article 54, paragraph 3 and Article 56, paragraph 3 of the Law on Banks (OG MNE no. 17/08), at its meeting held on 17 and 18 September 2008, the Council of the Central Bank of Montenegro passed the following

# DECISION
# on minimum standards for liquidity risk management in banks

## 1. General Provisions

### Subject of the Decision

### Article 1

This Decision shall establish in more details the minimum standards for liquidity risk management that the banks shall follow in their operations.

## 2. Liquidity risk management

### Elements of risk management

### Article 2

Liquidity risk management in banks shall include, in particular:

1) identification of existing sources of liquidity risk as well as liquidity risk that may arise from new business products or activities;
2) measurement and monitoring of concentration of deposits and other sources of funds by maturity and by clients;
3) measurement, assessment and monitoring of the degree of deposit variability;
4) monitoring of contingent liabilities recorder on bank's off-balance sheet;
5) monitoring of maturity structure of assets and assets sources in EUR and other currencies, including separate monitoring of the maturity structure of currencies having a significant impact on total liquidity, establishing and maintenance of adequate maturity match between assets and sources of assets;
6) projecting of inflow and outflow of monetary assets;
7) use of financial instruments for establishing a proper structure of assets and their sources;
8) stress testing;

9) establishing liquidity indicators and their use in the process of monitoring bank liquidity;
10) bank's actions in case of temporary or long-term liquidity disturbances.

**Deadlines for risk measurement and monitoring**

**Article 3**

Bank shall establish effective measurement and management of liquidity risk:

1) on daily, ten-day and quarterly basis, and
2) for periods longer than those under point 1 of this Article, as established by business policy acts, depending on the volume of cash flows, as well as volume and complexity of bank's business activities.

**Liquidity measurement**

**Article 4**

Bank is obliged, as the minimum requirement, to perform liquidity measurement based on the projection of cash flows and a set of indicators for liquidity measurement, calculated on the basis of the existing balance on the designated day.

The cash flow projection shall be established for time periods prescribed under Article 3 of this Decision and shall be based on the anticipated cash inflows and outflows and future financing requirements.

Anticipated cash inflows shall be based on the assessments of the following, as the minimum:

1) actual collectability of loans, whereby the estimated level of collectability may not be higher than the agreed inflow, reduced by the percentage of established loan loss reserves;
2) actual possibilities of converting assets without the established maturity date into cash;
3) availability of monetary assets arising from holding financial instruments kept until maturity;
4) real possibility of selling assets, whereby investments into other legal persons, non-performing loans and fixed assets shall be treated as the least liquid assets, and bank's assets given as security are excluded from the assessment;
5) expected deposit growth;
6) bank ability to acquire funds from additional sources and availability of market financing sources;
7) other cash inflows by analyzing the data on the level and trends of cash inflows in the previous period, taking into account seasonal effects, sensitivity of interest rates and macroeconomic factors.

Presumptions on cash outflows are based on the minimum analysis and assessment of the following:

1) maturing liabilities, including liabilities recorded on bank’s off-balance sheet that will cause assets outflow in the period for which the estimate of cash outflows has been made;
2) bank’s future lending activity;
3) a standard level of deposits and other liabilities established on the basis of usual variability of bank’s deposits and the knowledge of the deponents` behaviour and intentions;
4) real maturity of demand deposits and time deposits that may be withdrawn before maturity dates (earlier withdrawal option);
5) influence of the change in interest rates on deposits;
6) degree of deposit concentration and the influence of insufficient deposit concentration on lowering the level of deposits due to a change in relations between large depositors and bank and other circumstances;
7) contingent liabilities as per off-balance sheet items, including contingent liabilities as per financial derivatives that may cause outflow of assets in the reference period for assessment of cash outflows;
8) other cash outflows based on data about the level and trends of cash outflows in the previous period, taking into account seasonal effects, sensitivity of interest rates and macroeconomic factors.

Bank is obliged to periodically review the validity of presumptions used in the process of liquidity risk management.

**GAP analysis**

**Article 5**

For the purpose of bank inflows and outflows match, bank is obliged, as the minimum requirement, to establish the maturity scales (GAP analysis) for periods esatblished in its business policy, and at least for periods set out in Article 3 of this Decision.

Recording of cash inflows and outflows in the appropriate maturity scales will be performed by applying the following criteria:

1) cash inflows are recorded by assets maturity dates or by real frame converting assets into cash,
2) cash outflows are recorded by maturity dates or the earliest dates at which contingent liabilities may be paid.

Maturity mismatch of cash flows shall be disclosed for each maturity scale individually as well as at the aggregate level.

**Limits to maturity match**

**Article 6**

Bank is obliged to establish limits which will provide adequate maturity match between bank’s assets and assets sources, observing the following limitations:

1) short-term assets sources with maturity up to 30 days may be invested only in asset instruments with maturity up to 30 days;

2) short-term assets sources with maturity from 30 to 90 days may be invested only in asset instruments with maturity up to 90 days;
3) the maximum of 10% of short-term assets sources with maturity from 90 to 180 days may be invested only in asset instruments with maturity longer than 180 days;

The Central Bank of Montenegro (hereinafter: the Central Bank) may order a bank to establish stricter limits of maturity match other than those established by the bank, should it estimates that the originally established limits do not correspond to the bank's risk profile or that the bank does not manage liquidity risk in a proper manner.

## Liquidity indicator

### Article 7

Bank's liquidity level is shown by its liquidity indicator.

The liquidity indicator is the ratio of a sum of liquid assets from Article 8, paragraph 1 of this Decision to a sum of due liabilities from Article 8, paragraph 2 of the Decision.

## Liquid assets and due liabilities

### Article 8

Within the meaning of this Decision, liquid assets shall be considered the following:

1) cash;
2) funds on the settlement account at the Central Bank;
3) cheques and other cash receivables;
4) funds on accounts at domestic banks (demand deposits);
5) funds at payment system agents;
6) funds on accounts at foreign banks (demand deposits);
7) a part reserve requirement funds which may be used for maintaining bank's daily liquidity, as regulated by a special regulation of the Central Bank.

Within the meaning of this Decision, due liabilities shall be considered the following:

1) loan payables;
2) interest and fee payables;
3) due time deposits;
4) 30% of demand deposits;
5) 10% of liabilities for granted but not-performed irrevocable loan liabilities (credit lines);
6) Other due liabilities.

## Minimum liquidity indicator

### Article 9

Bank shall maintain the liquidity level so that the minimum value of liquidity shall amount to:

1) 0.9 – when calculated for one working day;
2) 1.0 – when calculated as an average of liquidity indicators for all working days in a ten-day period.

## Information system

### Article 10

Bank's information system must provide data for timely and ongoing liquidity risk management, and the minimum for:

1) the measurement and monitoring of bank's liquidity on a daily basis and over other established periods;
2) the measurement and monitoring of liquidity for each foreign currency having a substantial effect on total bank's liquidity;
3) monitoring the compliance of operations with the established limits for liquidity risk management;
4) determining liquidity indicators;
5) analysis of deposit trends and assessment of deposit stability;
6) conducting stress tests of bank's liquidity;
7) creation of reports and information for bank management and other persons included in the liquidity risk management process.

## Stress testing

### Article 11

Bank is obliged to perform tests of liquidity in different situations using several types of stress test scenarios in order to estimate the impact of these situations on bank's cash flows or liquidity.

Stress scenario, within the meaning of this decision, shall include presumptions about extreme changes in internal and external factors that affect bank's liquidity.

Bank is obliged to enact procedures for various stress scenarios and to make annual schedule of bank's liquidity testing using the stress scenarios, at least on quarterly basis.

During liquidity stress testing procedure, bank is obliged, as the minimum, to:

1) identify the key internal and external factors which changes affect bank's liquidity;
2) present quantitative changes of internal and external factors that are the subjects of stress scenario;
3) estimate the effects of internal and external factors from the established stress scenarios on bank's liquidity;
4) report to bank management on results of stress testing.

Bank shall periodically review and, if necessary, revise presumptions for performing stress testing.

## Contingency plan

## Article 12

Bank is obliged to adopt the contingency plan for liquidity risk management in emergency situation.

The plan under paragraph 1 above should at least contain:

1) defined condition in which the plan is to be applied;
2) clear distribution of tasks, powers and responsibilities in the bank regarding the plan implementation;
3) early warning indicators which point to the possibility of a crisis situation emergence (abrupt decrease of deposits, higher financing costs compared to other banks, difficulties in collecting assets on money markets, deterioration of asset quality and profitability, and the like);
4) planned forms of communication with main depositors, business partners, other customers and the public;
5) identification, size and reliability of all financing sources with the indicated order of use in various situations varying from normal circumstances to serious bank crises;
6) access to additional sources of funds that are not used in bank`s ordinary course of business;
7) procedures of acquiring missing liquidity and the time frame for undertaking certain activities (e.g. sale of property, establishing new lines of financing, etc.);
8) procedures of timely reporting to bank management in order to make timely decisions in crisis situations.

Bank is obliged to periodically review and, if necessary, revise the plan under paragraph 1 of this Article.

## Informing the public

## Article 13

Bank is obliged to establish a mechanism to provide proper public dissemination of information regarding the organization and financial position of the bank, especially in situations when negative information about the bank appear in the public.

## Reporting to the Central Bank

## Article 14

In case of shortfall in liquidity, banks are obliged to immediately inform the Central Bank about the amount of lacking liquid assets, the reasons for liquidity shortfall and planned activities for overcoming the liquidity shortage problem.

## 3. Transitional and Final provisions

### Article 15

With the coming into force of this Decision, the Decision on the minimal standards for liquidity risk management in banks (OG RoM No. 58/05) shall cease to be valid.

### Article 16

This Decision shall come into force on the eighth day of its publication in the "Official Gazette of Montenegro".

**THE COUNCIL OF THE CENTRAL BANK OF MONTENEGRO**

**PRE SIDENT OF THE COUNCIL**

**Ljubiša Krgović**

Decision No. 0101-323/11-8
Podgorica, 18 September 2008