

Pursuant to Article 17 paragraph 1 point 2 of the Central Bank of Montenegro Law (OGRM 52/00, 47/01), and Article 66, paragraph 3 of the Banking Law (OGM 17/08), the Council of the Central Bank of Montenegro, at the meeting held on 17 and 18 September 2008, passed the following

DECISION
on Methodology for Country Risk Measurement in Banks

1. General Provisions

Subject of the Decision

Article 1

This Decision shall prescribe the methodology that banks shall apply in country risk measurement, including the manner of calculating required capital for country risk.

2. Country risk measurement

Risk measurement obligation

Article 2

Bank shall measure the exposure to country risk for all countries where head office and/or residence of bank's debtors is located (hereinafter: the debtor country).

Exposure to country risk

Article 3

Total bank exposure to a single debtor country shall represent a sum of net exposures to all persons whose head office and/or residence is in that country.

Notwithstanding paragraph 1 above:

- 1) for receivables guaranteed by a person from a third country other than the debtor country, the country in which the guarantor has a head office and/or residence may be considered the debtor country;
- 2) for receivables which the bank may collect in full from funds on accounts in countries other than the debtor country, the country in which these funds are located may be considered the debtor country.

Calculation of exposure

Article 4

The calculation of total exposure to a single debtor country shall include loans, shares, debt securities, equity investments, funds at correspondent bank accounts, financial derivatives, guarantees and other unconditional off-balance sheet liabilities.

By way of derogation from paragraph 1 above, the calculation of the exposure to a single country shall not include:

- 1) shares and debt securities issued in the debtor country which meet the following criteria:
 - these securities are recorded in the bank's trading books,
 - if these securities are regularly traded on an organised securities market and price quotation may be obtained from reliable sources that adequately reflect country risk of the country in which the issuer has its head office,
 - if the bank regularly reconciles book value and market value of securities;
- 2) receivables from units of foreign companies with head office in Montenegro registered in accordance with the law governing the legal status of companies;
- 3) receivables from organisational units of the bank with the head office in another country, which are funded from sources originating from country of head office of that organisational unit, regardless of the currency in which the source of funds and/or the receivable is disclosed;
- 4) off-balance sheet liabilities that can be cancelled at any time;
- 5) the amount of receivables for which risk hedging has been performed.

Classification of debtor country

Article 5

Bank shall classify all debtor countries into one of the following risk categories:

- 1) safe countries;
- 2) low-risk countries;
- 3) medium-risk countries;
- 4) high-risk countries.

Bank shall classify debtor country to which there is no country risk as a safe country.

Bank shall classify debtor country to which there is country risk, but there is no current danger of uncollectibility of receivables as a low-risk or a medium-risk country, depending on the country risk rating.

Bank shall classify debtor country to which there is current danger of uncollectibility of receivables or actual problems in the collection of receivables as a high-risk country, depending on the country risk rating.

Bank shall use the classification of debtor countries for establishing required capital for country risk and for establishing limits of bank exposure to individual debtor countries, groups of countries, or regions.

Basis for classification

Article 6

Bank shall use the following for the classification of countries into appropriate categories under Article 5 herein:

- 1) long-term credit rating of debtor country, as assigned by an internationally recognised rating agency;
- 2) information available at national or international level such as information prepared by the International Monetary Fund, the Organization for Economic Cooperation and Development and the Bank for International Settlements;
- 3) available information on the amount, nature and maturity of debtor country's external debt, inflation rate and historical data about the country's servicing of external debt;
- 4) available information on current situation in debtor country, especially regarding the economic and political situation, including the estimates of social and political stability.

Classification schedule

Article 7

The classification of debtor countries shall be performed at least semi-annually.

By way of derogation from paragraph 1 above, in case of changes or events in debtor country that may cause the country to be classified as a high-risk country, a bank shall immediately classify the country as a high-risk country.

3. Capital requirement

Calculation of capital requirement

Article 8

Capital requirement for country risk shall be calculated by weighting total net exposure to debtors from certain country using the appropriate risk weight from the following table:

Risk categories	Risk weight
Safe countries	0%
Low-risk countries	50% - 100%
Medium-risk countries	150% - 250%
High-risk countries	minimum 300%

Net exposure to a single debtor country shall be total exposure to debtors from that country calculated in line with Article 4 herein and reduced by the established loan loss provisions as per these exposures.

The total sum of weighted net exposures under paragraph 1 above for all debtor countries divided by 10 shall represent the capital requirement for country risk.

Provisions

Article 9

By way of derogation from Article 8 herein, a bank may, instead of calculating capital requirement for country risk, calculate and allocate certain provisions based on the estimate of expected losses as per exposure to country risk.

The calculation of provisions under paragraph 1 above shall be performed by deducting provisions established for bank exposure to credit risk from the total amount of exposure and applying to the obtained amount the established percentage of provisions for country risk.

Bank shall provide documents explaining the established percentage of country risk provisions.

Stricter classification and provisioning

Article 10

The Central Bank may require a bank to establish stricter classification or allocate higher percentage of country risk provisions if it determines that the bank has not performed adequate classification of debtor countries and/or it has not established appropriate country risk provisions, or if the bank's country risk management does not correspond to the bank's risk profile.

4. Final provision

Article 11

This Decision shall enter into force on the eighth day following that of its publication in the Official Gazette of Montenegro.

THE COUNCIL OF THE CENTRAL BANK OF MONTENEGRO

PRESIDENT OF THE COUNCIL

Ljubiša Krgović

Decision No. 0101-323/11-4
Podgorica, 18 September 2008