



Podgorica, 1 October 2024

## **Information on the countercyclical capital buffer rate for Montenegro in Q4 2024**

In its Decision on the Countercyclical Capital Buffer Rate in Q4 2024 and in accordance with the Law on Credit Institutions (OGM 72/19, 82/20, 8/21), the Central Bank of Montenegro has set the countercyclical capital buffer rate for the fourth quarter of 2024. The rate shall be 0% of the total amount of risk exposure.

The 0% rate shall apply to the territory of Montenegro, that is, to relevant exposures of credit institutions in Montenegro. Pursuant to Article 147 of the Law on Credit Institutions, every credit institution is obliged to calculate the specific countercyclical buffer rate as the weighted average of the countercyclical buffer rates that apply in Montenegro and other countries where the relevant credit exposures of the credit institution are located.

Article 144 of the Law on Credit Institutions specifies that the Central Bank is obliged to publish the decision on the countercyclical buffer rate and the announcement thereof on its website. The information to be contained in the announcement is specified under Articles 141 and 144 of the law.

The key findings of the analytical base used for the countercyclical buffer decision are presented below.

The starting point was the calculation of the buffer guide. The buffer guide was calculated using the so-called standardised credit-to-GDP gap in line with the Law on Credit Institutions and the Recommendation of the European Systemic Risk Board on guidance for setting countercyclical buffer rates (ESRB/2014/1).

At end-Q2 2024, the credit-to-GDP ratio stood at 47.9%. Compared to its long-term trend, this is a deviation of -10,2 pp, which is below the lower threshold of 2 pp, i.e. the minimum value that would indicate the need to introduce a non-zero countercyclical buffer rate, so the value of the buffer guide was 0%. Over the past two years, the credit-to-GDP ratio was particularly pronounced, showing negative deviations from the longstanding trend as a result of a stronger growth of GDP over credits.



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In addition to the buffer guide, the analysis covers numerous other selected indicators that the CBCG uses to monitor cyclical systemic risks in Montenegro.

When it comes to the real estate market, according to the latest survey (July/August 2024), the value of the hedonic real estate price index (data produced by the CBCG) points to a further increase in real estate prices. On the other hand, the prices of dwellings in new residential buildings (data produced by MONSTAT) in Podgorica remained almost the same, while observing at the national level, they reached a new growth in the second quarter of 2024, mainly due to the prices increase in the coastal region (mainly as a result of foreign demand). Thus the prices of dwellings in new residential buildings reached their new record highs. However, the increase in the real prices of dwellings in new residential buildings (deflated by the consumer price index) as well as the growth of the prices of dwellings in new residential buildings in relation to nominal earnings have eased slightly over the past few quarters.

The assessment shows that there is a certain accumulation of cyclical systemic risks connected to the real estate market. Real estate prices are important for the assessment of cyclical systemic risks because real estate is one of the most significant forms of collateral used to secure both housing and mortgage loans as unrealistically high real estate prices can reinforce the upward phase of the financial cycle, thus spurring credits above the justified levels, so in the phase of a possible sudden drop in real estate prices they could negatively affect both borrowers and banks' balance sheets.

The leading factor spurring the growth of real estate prices was foreign direct investments in real estate, which amounted to 911.6 million euros in the period 2022-2023 or 7% of nominal GDP per year on average, which is significantly more than over several years before that period. In the first seven months of 2024, the inflow of foreign direct investments in real estate remained significant, albeit somewhat lower than in the comparative period. In addition, the real estate prices were affected by a growth in housing loans. In June this year, housing loans recorded the annual growth rate of 26.6%, reaching a cumulative growth of nearly 50% in relation to the end of 2020. A similar dynamics was seen with new housing loans.

In this regard, a certain accumulation of cyclical risks is noticeable regarding the growth of retail loans, with housing loans being the key driver of credit growth, as well as cash (all-purpose) loans. The annual growth rate of retail loans reached 12.3% in June this year, while retail cash loans rose 12% (mainly due to improved creditworthiness of private individuals due to an increase in nominal income). Also, the twelve-month cumulative amount of newly approved retail cash loans has significantly exceeded the pre-pandemic level and remains on the upward trajectory. Therefore, those credit segments will remain in the spotlight of attention in the coming period as well.



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What is relevant for the assessment of cyclical systemic risk are geopolitical circumstances, primarily the conflicts in Ukraine and the Middle East, which point to the continued uncertainty and/or intensification of such risk factors in recent period.

The banking business parameters are generally stable. Due to the aforementioned intensification of credit growth in the first half of 2024, the structure of assets additionally changed in favour of loans, considering that the share of net loans increased to 64.8%, which is almost 10 pp compared to end-2022. In the previous year, the asset structure also recorded a large growth in securities. Consequently, the share of liquid assets in total assets dropped to 20.3% at end-June this year, but this is still a relatively high share. Since lending activity was very intensive, the ratio of loans to deposits additionally increased and amounted to 83.3% (gross) and 80.8% (net).

In the first six months of 2024, banks' profit was almost one third higher than in the comparative period last year, reaching the amount of 87.2 million euros. The capital adequacy ratio stood at 19.5% and it was slightly lower than at the end of the first quarter this year. Non-performing loans further declined and this downward trend has been present since early 2022. At the end of the second quarter of 2024, their share in total loans amounted to 4.3%.

The growth of the weighted average lending interest rate for the entire loan portfolio of banks (outstanding principal/debt) was halted and the rate amounted to 6.61% at the end of the second quarter of this year. The interest rate on new loans fell during the second quarter, amounting to 6.87% at end-June, same as the twelve-month weighted average rate.

In view of the above, primarily the circumstances surrounding the real estate market, the conditions have been met for increasing the countercyclical capital buffer rate to 0.5%. However, bearing in mind that the application date of any increase of the countercyclical buffer rate must be determined within 12 months following the date of the buffer rate publication and that, currently, it cannot be assessed whether any extraordinary circumstances exist due to which the application date of the higher buffer rate should be determined within a period shorter than 12 months, the Central Bank has set the countercyclical capital buffer rate at 0% for the fourth quarter of 2024. All credit institutions are obliged to apply this rate when calculating their individual countercyclical capital buffer rates. On the other hand, the increase in the buffer rate to 0.5% was previously implemented under the Decision on increasing the countercyclical capital buffer rate (OGM 27/24), which will apply as of 1 April 2025.

In accordance with its powers, the CBCG will continue to regularly monitor the development of potential imbalances in financing the needs of the non-financial sector and households, and publish the countercyclical capital buffer rate on



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quarterly level, in line with the provisions of Article 144 paragraph 1 of the Law on Credit Institutions.