



Podgorica, 31 December 2021

Information on countercyclical capital buffer for Q1 2022

The Central Bank of Montenegro has set the countercyclical buffer rate for the first time under its Decision on the Countercyclical Capital Buffer Rate (OGM 134/21), in accordance with the Law on Credit Institutions (OGM 72/19, 82/20 and 8/21). The rate is set at 0% of the total amount of risk exposure and it will be applied in the first quarter of 2022.

The rate shall apply to the territory of Montenegro, that is, to exposures of all 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.

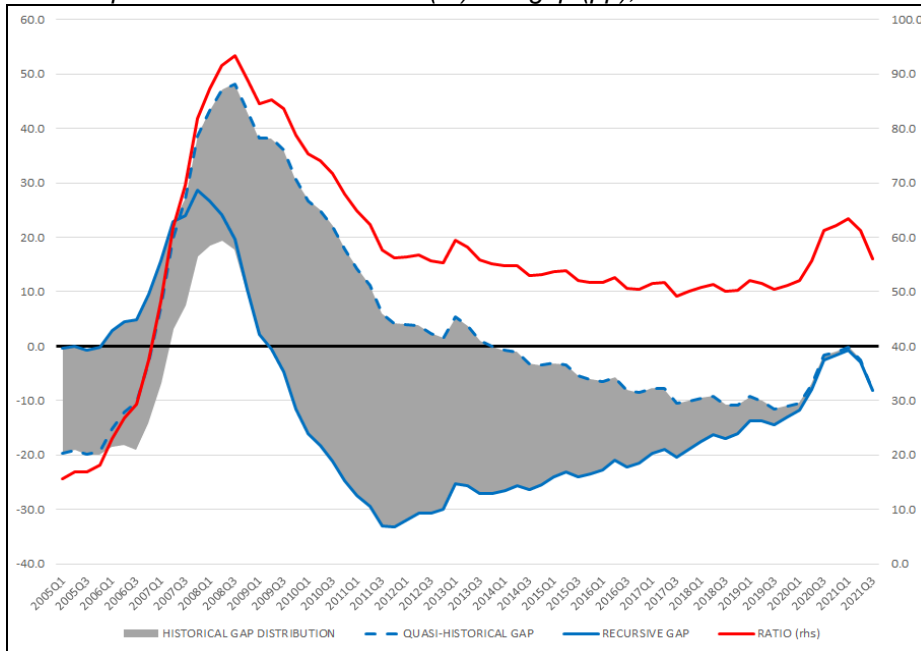
Article 144 of the aforesaid law specifies that the Central Bank is obliged to publish on its website the decision on application of the countercyclical buffer rate and the announcement thereof. The information to be contained in the announcement is specified under Articles 141 and 144 of the law. The key segments of the analytical basis used for passing the decision on countercyclical buffer rate are presented below.

The starting point is the calculation of a buffer guide, which is calculated using a standardised credit-to-GDP rate 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).

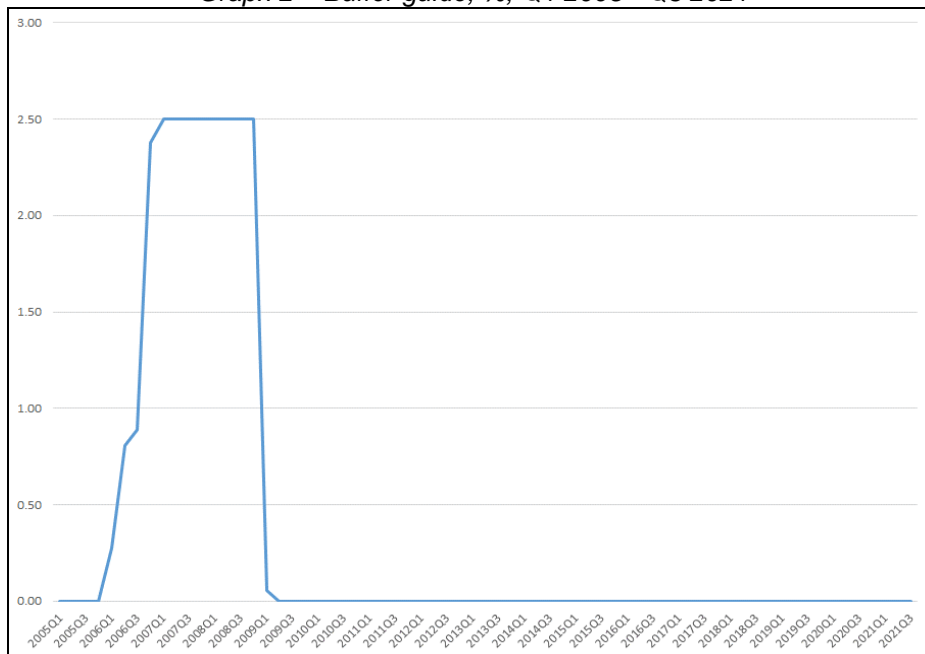
At end-Q3 2021, the credit-to-GDP ratio stood at 56%. Compared to its long-term trend, this is a deviation of -8.1 pp, which is below the lower threshold of 2 pp, i.e. the minimum value that would indicate the need to introduce a non-zero countercyclical buffer rate. Thus the value of the buffer guide was 0%.

After the credit-to-GDP gap had approached the zero value at end-Q1 due to a sharp drop in GDP induced by the coronavirus pandemic, it moved back deeper into the negative zone in Q2 and Q3.

Graph 1 – Credit-to-GDP ratio (%) and gap (pp), Q1 2005 - Q3 2021



Graph 2 – Buffer guide, %, Q1 2005 - Q3 2021



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



Credit growth of banks, observed through the definition of credit used to calculate the buffer guide, slowed down significantly during the pandemic, only to end on a slightly positive level at the end of the third quarter. New bank loans declined significantly in 2020, followed by a strong recovery in the first three quarters of 2021 which, however, was not sufficient to lead to any notable increase in the balance of loans in banks' balance sheets.

Observed by sectors and purpose of new loans, the aforementioned dynamics was guided by the dynamics of new retail loans, specifically cash (all-purpose) loans. Risks associated with retail cash loans eased during the pandemic as those loans decreased, as did their share in retail loans. However, the maturity structure of these loans is still relatively unfavourably shifted towards long-term loans.

Interest rates on new loans have remained broadly stable during the pandemic, while interest rates on credit stock have fell slightly further.

The balance sheets of banks were primarily characterized by growing deposits during the current year, reaching their all-time high at the end of the third quarter. It was the deposit growth that conditioned the growth of banks' assets, with banks redirecting the received funds more into liquid assets and less into loans. At end-Q3, liquid assets accounted for 27.5% of total assets, compared to 24.3% a year ago. At the same time, the loan-to-deposit ratio fell to 87.7% gross and 84.2% net.

In 2021, banks made significantly higher profits than in 2020, yet lower than in 2019. The solvency ratio, which banks maintain significantly above the regulatory minimum of 10%, amounted to 18.5% at end-Q3. The share of non-performing loans increased during the pandemic albeit not significantly, sitting at 5.6% at the end of the third quarter.

When it comes to the real estate market, the value of the hedonic real estate price index (data produced by the CBCG) indicates that real estate prices were generally stagnant. On the other hand, the prices of new apartments (data produced by MONSTAT) have been on a notable uptrend and the interesting fact is that this has been driven by rising prices of solidarity housing construction. However, the prices of newly built apartments are not above the maximum values recorded in the past 10 years and they are also much lower than during the 2006-2008 boom period.

Newly approved housing loans were on a notable decline during most of the pandemic period but they recovered considerably in the third quarter of 2021. Interest rates on these loans remained generally stable during the pandemic and they are at their all-time low. Construction activity is currently lower than



CENTRALNA BANKA
CRNE GORE

before the pandemic, but it is slowly stabilising and even recording growth in effective working hours.

Activity on the capital market is still quite weak, with both turnover and index values being multiple times lower compared to the time of the strong expansion in 2007.

In view of the above, the CBCG introduced the countercyclical capital buffer rate of 0%. In accordance with its macroprudential powers, the CBCG will continue to regularly monitor the development of potential imbalances in financing the needs of the non-financial sector and the population, and publish quarterly countercyclical capital buffer rates.

Methodological notes on the calculation of the buffer guide:

The calculation of the credit-to-GDP ratio and gaps was conducted on a sample from Q1 2002. The quasi-historical gap is calculated for the entire sample, while the recursive gap is calculated using the right-hand shifting sample (of available data in each quarter), with the latest observations always being the same for both gap indicators. The historical distribution of the calculated gap represents the area between the smallest and the largest value of the gap calculated by moving the sample to the right. The historical series of the buffer guide is presented as a function of the recursive gap, with the upper limit of the standard statutory maximum of 2.5% (exceptionally, the countercyclical buffer rate exceed 2.5%).

Data sources:

1. **MONSTAT, nominal GDP.** GDP data are recalculated as annual cumulatives, i.e. as the sum of the values of GDP in a given quarter and the three previous quarters. Data on GDP before 2006 were obtained by applying the average share of quarterly GDP values in the annual GDP value for the period 2006Q1 – 2020Q4.

2. **CBCG, gross loans and other credit receivables.** Data on loans refer to the sum of loans in banks, microcredit financial institutions, and leasing companies at end-quarter, which these institutions approved to the non-financial sector and households, excluding non-residents. These loans do not include those that the non-financial sector and households received from foreign entities due to the inadequate length, frequency, and reliability of those data series.