CENTRAL BANK OF MONTENEGRO

REPORT ON BANK LENDING SURVEY RESULTS THIRD QUARTER 2019

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INTRODUCTION

Since April 2018, the Central Bank of Montenegro has started conducting the bank lending survey, which is harmonised with the survey conducted in the Euro area central banks, but it is tailored to the Montenegrin market. Its main objective is to provide the Central Bank with an insight into key determinants of supply of and demand for the retail and wholesale loans.

The survey consists of twelve questions that refer to the approval of retail and wholesale loans. The respondents (banks) answered the questions on the change in their credit standards[1], as well as the impact of factors contributing to this change, change in terms and conditions[2] of the loan approval, the number of rejected loan applications, change in demand for loans and impact of factors contributing to such a change. The questions were divided into two sets, of which the first six questions referred to wholesale loans and/or their credit lines, while the remaining six questions referred to retail loans. With regard to the questions on wholesale loans and/or their credit lines, they are further divided based on the loan maturity (long-term and short-term loans) and the size of the enterprises (micro, small, medium and large). With regard to retail loans, the division is made on the basis of the purpose of the loan (housing, consumer and other loans).

This Report sums up the results of the survey that was conducted in the third quarter of 2019. The survey disclosed positions of banks on the changes in their credit policies during the third quarter and expected changes in the fourth quarter of 2019. With a view to providing statistical representation, the responses of individual banks are weighted by their market share[3], whereas the response of the bank with higher market share gains higher importance. The survey results are displayed as net percentages. For the responses to questions on the loan supply, i.e. credit standards and credit terms and conditions, the net percentage is defined as a difference between the sum of the percentages of banks responding "tightened considerably" and "tightened moderately" and the sum of the percentages of banks responding "eased considerably" and "eased moderately".

[1] *Credit standards* imply the criteria for the approval of loans and/or credit lines by banks that define the following: type of loan, recognised sectoral or geographical priorities, collateral acceptability, creditworthiness of the debtors, and the like, including internal guidelines, changes in loan approval policy and its application.

[2] *Credit terms and conditions* imply mandatory elements from the loan agreement and/or credit line agreement between the bank and the debtor (loan amount, interest rate, commission and fee expenses, collateral required or guarantees to be provided by the debtor, maturity, and the like). They are determined based on the creditworthiness of the debtor and they can be altered together with the credit standards or independently.

[3] The weight - share of bank's assets in total assets of the banking sector - is used for aggregating the responses of individual banks.

A positive net percentage indicates net tightening, whereas a negative net percentage indicates net easing of credit standards. The net percentages for the responses to questions related to the factors having an impact on change of credit standards are defined as the difference between the percentage of banks reporting that the given factor contributed to a tightening and the percentage of banks reporting that it contributed to an easing of credit standards.

In regards to the demand for loans, net percentage is defined as the difference between the sum of the percentages of banks responding "increased considerably" and the sum of the percentages of banks responding "decreased considerably". Therefore, a positive net percentage indicates net increasing, whereas a negative net percentage indicates net decreasing in demand.

SUMMARY

The survey results suggested that, according to the banks' responses, credit standards for wholesale and retail loans eased in the third quarter of 2019, which was in accordance with the previous quarter expectations. In the next quarter, the banks expect further easing of credit standards for wholesale loans, whereas a tightening of credit standards is expected for retail loans (especially for consumer and other loans).

Banks observe the easing of credit standards both for wholesale and retail loans recorded in the third quarter as a result of strengthened market competition. According to banks' expectations for the next quarter, lower costs of sources of funds should be a sign of further easing of credit standards for wholesale loans, while competition and higher required collateral will have impact on tightening the standards for granting retail loans. Also, when it comes to retail loans, the macro prudential measures concerning cash loans announced by the CBCG should be taken into account[4].

Banks assess that the prominent banking market competition has lead to the reduction of interest rate margins and commissions for wholesale and retail loans in the third quarter of 2019. In the conducted survey, banks expect to continue easing credit conditions in the next quarter as well, except in terms of required collateral and reduction of maturity in wholesale and retail lending. Banks also believe that increased mortgage lending requirements for retail loans could contribute to tightening of the terms and conditions.

Banks estimated that the demand for wholesale and retail loans increased during the third quarter of 2019. Demand for wholesale loans was driven by the requirement to fund capital investments, working capital and restructuring of the existing debts. However, in the households sector, the main factors contributing to the increase in demand for loans were requirements to refinance the existing debts and purchase immovable property, and consumer durable goods. Banks expect the uptrend in demand for loans to extend into the fourth quarter of 2019 as well.

[4] The CBCG Council, at its meeting held on 14 October, adopted the Decision on Macroprudential Measures, which defines that banks, as of 1 January 2020, when granting cash loans to individuals whose repayment period is longer than six and eight years respectively, must require that the loan be fully secured with quality collateral.

Table 1 Assessment of credit standards and demand for loans by banks, Q3 and Q4 2019

	Demand		Supply	
	Credit standards			
	Q3 2019	Q4 2019 (expectations)	Q3 2019	Q4 2019 (expectations)
Wholesale loans	↓	↓	↑	↑
Long-term loans	↓	↓	↑	↑
Short-term loans	↓	↓	↑	↑
Micro, small and medium enterprises	↓	↓	↑	↑
Large enterprises	↓	↓	↑	↑
Retail loans	↖	↑	↑	↑
Housing loans	↖	↗	↑	↑
Consumer and other loans	↖	↑	↑	↑

Note: The table shows direction of change rather than its intensity.
↑ = credit standards/terms and conditions tightening (net percentage is higher than 5%)
↑ = increase in demand (net percentage is higher than 5%)
↗ = credit standards and credit terms and conditions tightening/increase in demand (net percentage up to 5%)
- = no change
↖ = credit standards and credit terms and conditions easing/decrease in demand (net percentage up to 5%)
↓ = credit standards and credit terms and conditions easing (net percentage higher than 5%)
↓ = decrease in demand (net percentage higher than 5%)

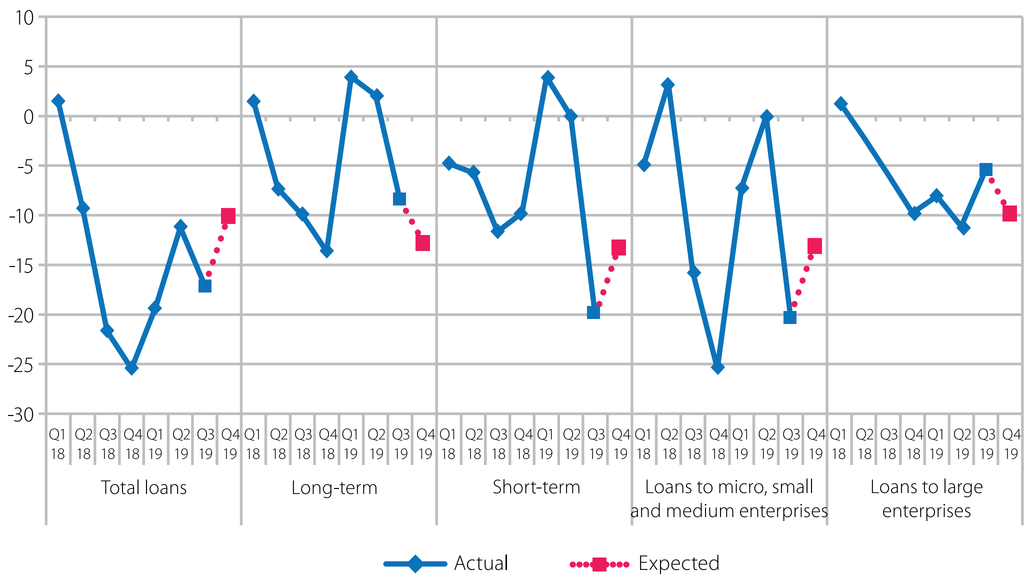
1. WHOLESALE LOANS

1.1. Credit standards and credit terms and conditions for wholesale loans

The survey results reveal that the credit standards for wholesale loans continued to ease in the third quarter of 2019. This was in accordance with the expectations of banks shown in the previous survey. Credit standards easing was recorded in 17% of the banking sector, which was above expectations from the previous quarter (6.61%). Credit standards were also eased for micro, small, medium, and large enterprises in the third quarter.

As expected by banks, the easing of the wholesale lending standards will continue throughout the next quarter.

Change in credit standards for wholesale loans (net percentage*) **Graph 1**



Source: CBCG

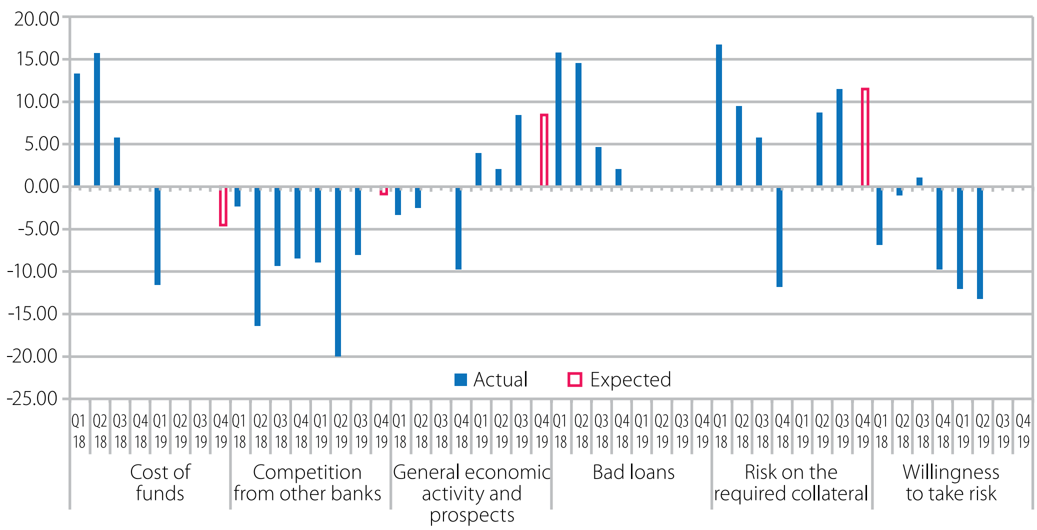
Note: A positive value indicates tightening of credit standards, whereas a negative value indicates easing of credit standards.

* The graph shows net percentage which indicates the direction of change rather than its intensity.

As in the previous survey, banks indicated that strengthened competition in the banking sector contributed to the easing of credit standards for new wholesale lending. On the other hand, higher risk of required collateral had an impact on tightening of credit standards for lending to all types of enterprises, regardless of their size and loan maturity. According to the testimony of a small part of the banking sector, the general economic situation triggered the tightening of the wholesale credit standards.

The banks expect that lower costs of sources of funds will trigger further easing of credit standards in the upcoming quarter. A minor part of the banking sector finds that weaker economic situation might fuel the mild tightening of wholesale credit standards, and that an increased risk of required collateral in lending to micro, small, and medium sized enterprises might be expected, which could result in tightening the standards. It is expected that uncollectability of receivables, and risk appetite would not contribute to the credit standards in the upcoming quarter.

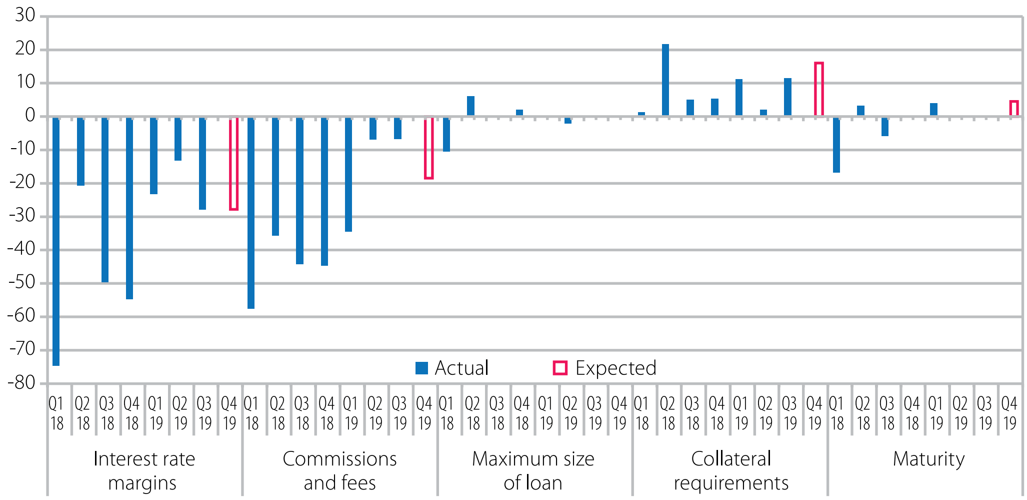
Graph 2 **Impact of factors on the change in credit standards (net percentage)**



Source: CBCG
Note: A positive value indicates the contribution of a specific factor to the tightening of credit standards, whereas a negative value indicates the contribution of a specific factor to the credit standards easing.
* The graph shows net percentage which indicates the direction of change rather than its intensity.

The survey results showed that the easing of interest rate margins, and commissions and fees on wholesale loans continued in the third quarter of 2019 as well. Some 30% of the banking sector showed a decrease in interest margins, which is similar to expectations from the previous quarter (26%) but also significantly higher than in the second quarter when it amounted to 13%. On the other hand, in the third quarter of 2019, one part of the banking sector increased its collateral requirements, which could have affected the flexibility of terms and conditions when granting loans.

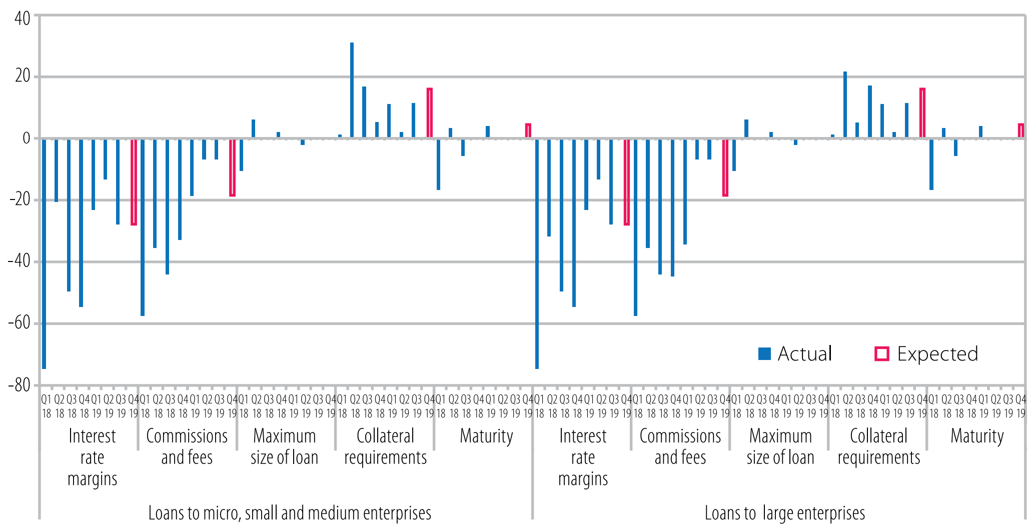
Change in terms and conditions for wholesale loans (net percentage) **Graph 3**



Source: CBCG
Note: The graph shows net percentage which indicates the direction of change rather than its intensity.

During the next quarter, banks expect further easing of interest rate margins, commissions and fees, which would contribute to the easing of terms and conditions for granting wholesale loans. A part of the banking sector saw tightening of credit conditions only in terms of reducing maturity and higher collateral requirements in micro, small, medium and large enterprises.

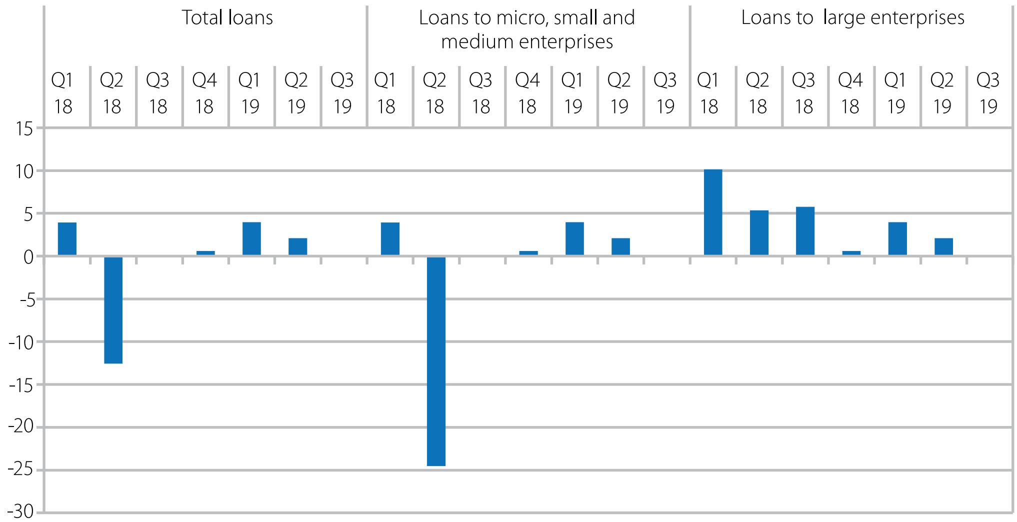
Change in terms and conditions for loans by the size of enterprise (net percentage) **Graph 3a**



Source: CBCG
Note: The graph shows net percentage which indicates the direction of change rather than its intensity.

The survey results show that in the third quarter compared to the second quarter of 2019, there were no changes in the share of rejected loan applications to micro, small, medium and large enterprises.

Graph 4 Share of rejected wholesale loan applications

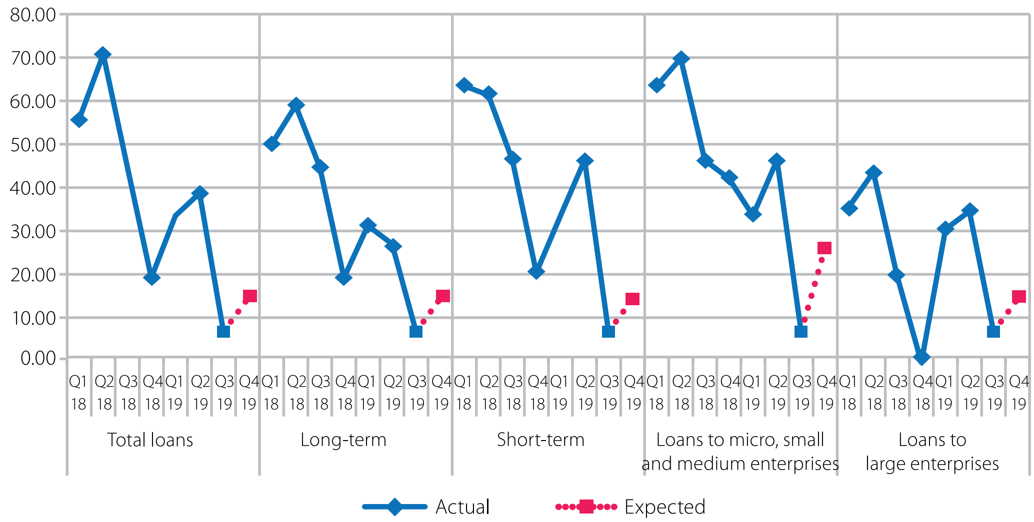


Source: CBCG
Note: A positive value indicates the increase of rejected wholesale loan applications, whereas a negative value indicates the decrease of the rejected loan applications.
* The graph shows net percentage which indicates the direction of change rather than its intensity.

1.2. Demand for wholesale loans

In the third quarter, banks recorded a rise in demand for loans to micro, small and medium enterprises, which was in accordance with banks' expectations from the previous quarter. However, the growth in demand was significantly lower than in the second quarter of 2019. For example, the growth in demand for total loans and/or credit lines was 6% in the third quarter and 38% in the second quarter. The survey showed that the contributing factor to the increase in demand was the financing of enterprises i.e. the requirement to finance capital investments, working capital and debt restructuring of the enterprises.

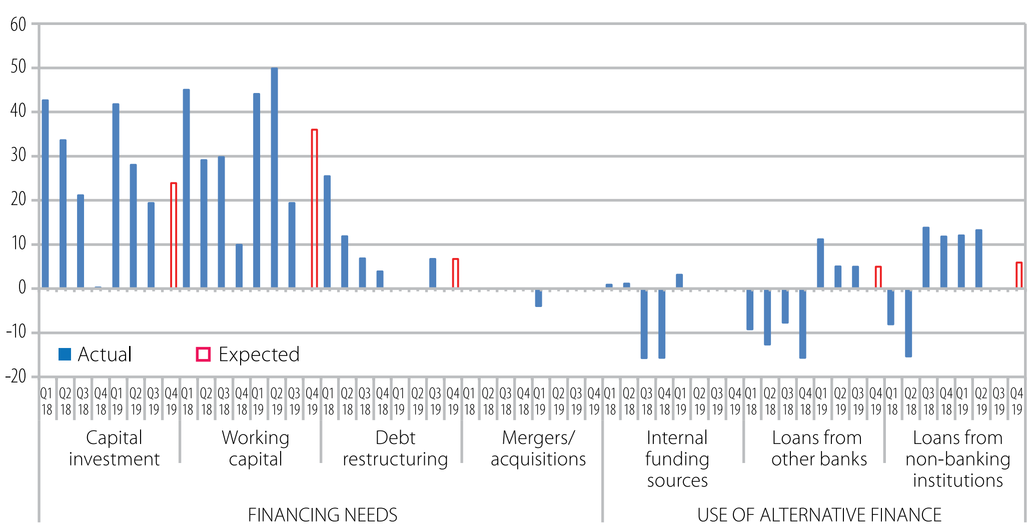
Factors contributing to the change in demand for wholesale loans (net percentage) **Graph 5**



Source: CBCG
Note: A positive value shows an increase in demand, whereas a negative value indicates a decrease in demand.
*The graph shows net percentage which indicates the direction of change rather than its intensity.

In the coming quarter, banks expect loans demand to grow, with more substantial growth in demand for micro, small and medium enterprises. Financing of capital investments and working capital along with the needs for refinancing enterprise debt will be the main bearers of the increase in demand.

Factors contributing to the change in demand for wholesale loans (net percentage) **Graph 6**



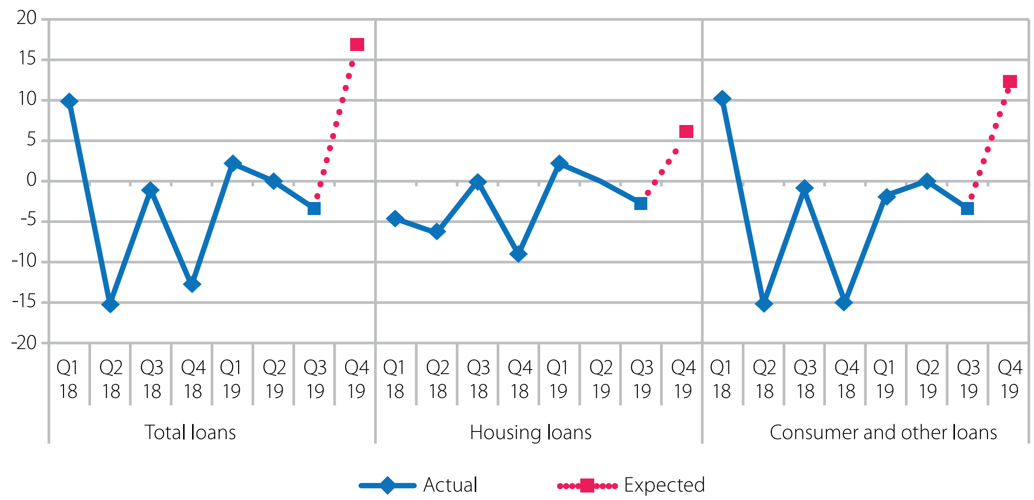
Source: CBCG
Note: A positive value indicates contribution of a specific factor to the increase in demand, while a negative value indicates contribution of a specific factor to the decrease in demand.
* The graph shows net percentage which indicates the direction of change rather than its intensity.

2. RETAIL LOANS

2.1. Credit standards and credit terms and conditions for retail loans

According to banks' assessment in the third quarter of 2019, credit standards for retail loans have slightly eased compared to the previous quarter, which is in line with the expectations of banks in the previous survey. As expected, banks will tighten their standards for granting retail loans, especially consumer and other loans, in the coming quarter.

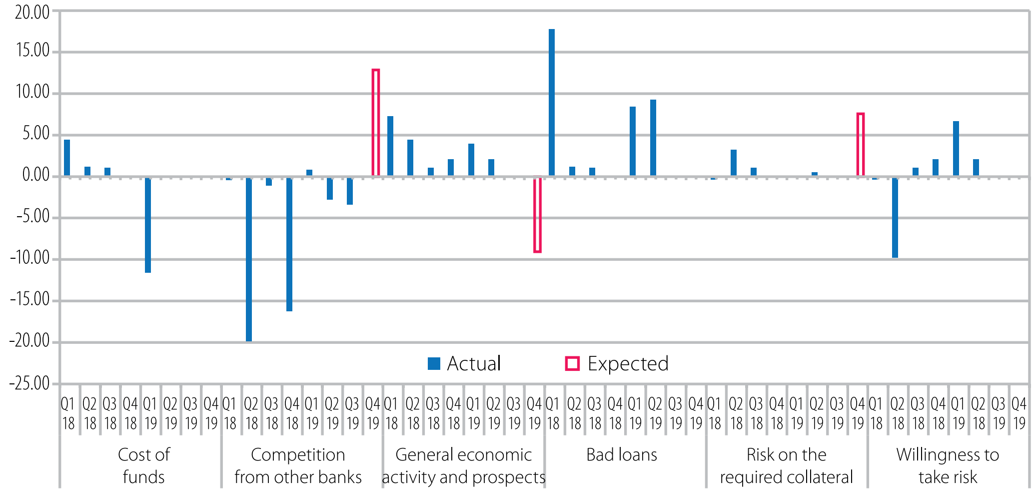
Graph 7 **Change in credit standards for retail loans (net percentage)**



Source: CBCG
Note: A positive value indicates tightening of credit standards, whereas a negative value indicates easing of credit standards.
* The graph shows net percentage which indicates the direction of change rather than its intensity.

Banks expect that in the coming quarter, competition in the banking sector and the risk of collateral required could trigger tightening of the standards for granting retail loans. On the other hand, the easing of the standard may be influenced by a better economic situation.

Factors contributing to the change in credit standards for retail loans (net percentage) **Graph 8**



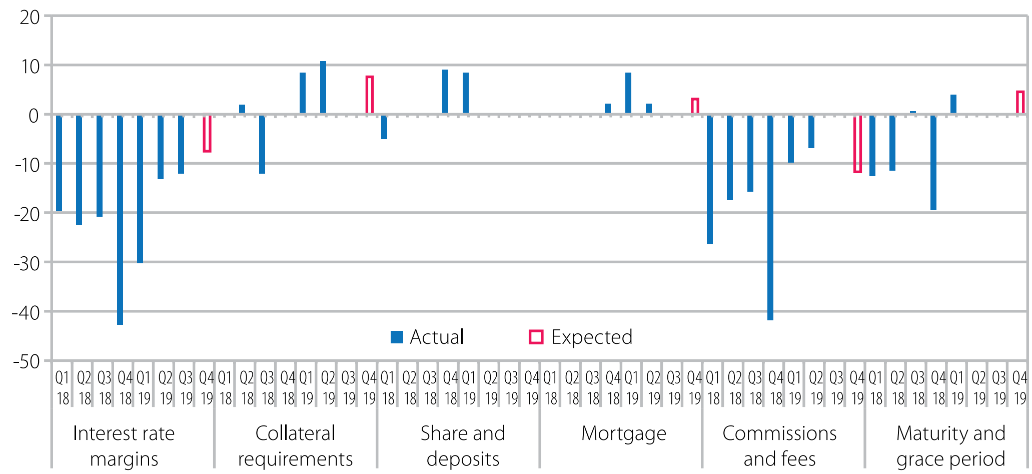
Source: CBCG

Note: A positive value indicates tightening of credit standards, whereas a negative value indicates easing of credit standards.

* The graph shows net percentage which indicates the direction of change rather than its intensity.

Banks find that in the third quarter of 2019 terms and conditions for approving retail loans eased in terms of the interest rate margins. In the next quarter, banks expect to continue easing their pricing conditions, interest margins, commissions, and fees. However, increased collateral requirements, mortgage value and decrease in maturity may result in tightening of terms and conditions for all categories of retail loans.

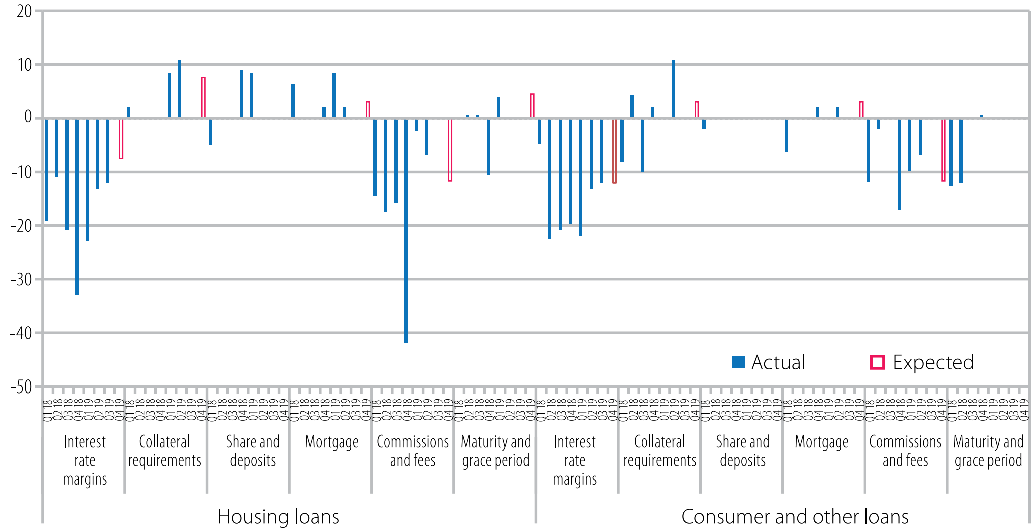
Change in terms and conditions for retail loans (net percentage) **Graph 9**



Source: CBCG

Note: The graph shows net percentage which indicates the direction of change rather than its intensity.

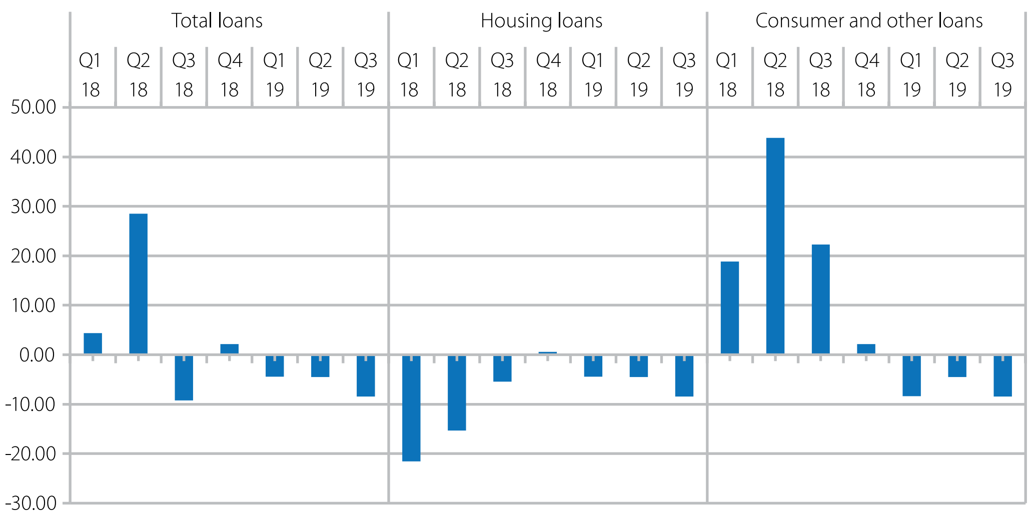
Graph 9a **Change in terms and conditions for housing loans and consumer and other loans (net percentage)**



Source: CBCG
Note: The graph shows net percentage which indicates the direction of change rather than its intensity.

The survey results indicate that the share of rejected applications for retail loans decreased in the third quarter of 2019 in all categories of loans compared to the previous quarter (by 8.4%).

Graph 10 **Share of rejected retail loans applications**



Source: CBCG
Note: A positive value indicates the increase of rejected loan applications, whereas a negative value indicates the decrease of rejected retail loans applications.
* The graph shows net percentage which indicates the direction of change rather than its intensity.

2.2. Demand for retail loans

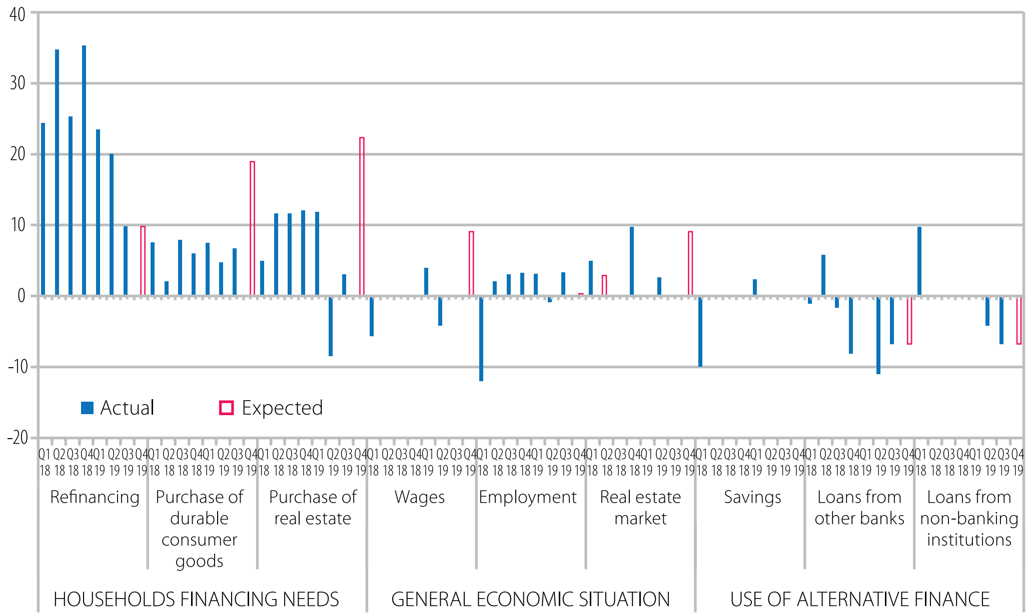
The survey results reveal a rise in the demand for retail loans in the third quarter of 2019. Banks find that the increase in demand in the last quarter was fuelled more by the financial needs of households than by the improved economic situation in the country. The banks marked refinancing requirements and purchase of immovable property as well as the purchase of consumer durables (cars, furniture, and the like) as factors contributing to the increase in demand for retail loans.

Change in demand for retail loans (net percentage) Graph 11

Source: CBCG
Note: A positive value shows an increase in demand, whereas a negative value indicates a decrease in demand.
* The graph shows net percentage which indicates the direction of change rather than its intensity.

Looking ahead to the fourth quarter of 2019, banks expect further increase in demand for retail loans, both consumer and other loans. The increase in demand in the upcoming quarter will be driven by the financial needs of the households for refinancing, and purchase of consumable durables, alongside positive macroeconomic outlooks (increase in wages and salaries and employment and improved situation in the real estate market).

Graph 12 **Factors contributing to the change in demand for retail loans (net percentage)**



Source: CBCG
Note: A positive value indicates contribution of a specific factor to the increase in demand, while a negative value indicates contribution of a specific factor to the decrease in demand.
* The graph shows net percentage which indicates the direction of change rather than its intensity.

3. ANNEX - Aggregate results of Bank Lending Survey in the third quarter 2019

1. Credit standards for wholesale loans

	Past three months	Next three months
A) Total loans and/or credit lines	-17.08	-9.91
Long-term (over 1 year)	-8.44	-12.96
Short-term (up to 1 year)	-20.13	-12.96
B) Loans and/or credit lines to micro, small and medium enterprises	-20.13	-12.96
C) Loans and/or credit lines to large enterprises	-5.38	-9.91

2. Factors contributing to the change in credit standards for wholesale loans

	Past three months			Next three months		
	Total	Loans to small, micro and medium enterprises	Loans to large enterprises	Total	Loans to small, micro and medium enterprises	Loans to large enterprises
A) Costs of sources of funds	0.00	0.00	0.00	-4.52	-4.52	-4.52
B) Competition of other banks	-8.03	-8.03	-8.03	-0.85	-0.85	-0.85
C) Risk perception	8.44	8.44	8.44	8.44	8.44	8.44
- General economic situation and outlooks	8.44	8.44	8.44	8.44	8.44	8.44
- Bad debt	0.00	0.00	0.00	0.00	0.00	0.00
- Risk related to required collateral	11.49	11.49	11.49	11.49	11.49	11.49
D) Risk appetite	0.00	0.00	0.00	0.00	0.00	0.00

3. Credit terms and conditions for wholesale loans

	Past three months			Next three months		
	Total	Loans to small, micro and medium enterprises	Loans to large enterprises	Total	Loans to small, micro and medium enterprises	Loans to large enterprises
A) Interest rate margin*	-27.84	-27.84	-27.84	-27.84	-27.84	-27.84
B) Commissions and fees*	-6.74	-6.74	-6.74	-18.44	-18.44	-18.44
C) Maximum amount of loans and/or credit lines**	0.00	0.00	0.00	0.00	0.00	0.00
D) Collateral requirements*	11.49	11.49	11.49	16.01	16.01	16.01
E) Maturity**	0.00	0.00	0.00	4.52	4.52	4.52

4. Share of the rejected loan applications

	Past three months		
	Total	Loans to small, micro and medium enterprises	Loans to large enterprises
Share of rejected applications	0.00	0.00	0.00

5. Demand for wholesale loans

	Past three months	Next three months
A) Demand for total loans and/or credit lines	6.74	14.32
Long-term (over 1 year)	6.74	14.32
Short-term (up to 1 year)	6.74	14.32
B) Demand of micro, small and medium enterprises	6.74	26.02
C) Demand of large enterprises	6.74	14.32

6. Factors contributing to the demand for wholesale loans

	Past three months	Next three months
A) FINANCIAL NEEDS OF COMPANIES	19.40	23.92
- For capital investments	19.40	23.92
- For working capital	19.40	36.02
- For debt restructuring	6.74	6.74
- For mergers/acquisitions	0.00	0.00
B) USE OF ALTERNATIVE SOURCES OF FINANCING	12.66	12.66
- Internal sources of financing	0.00	0.00
- Loans from other banks	4.96	4.96
- Loans from non-banks	5.92	5.92
C) OTHER FACTORS (should be specified)		

7. Credit standards for retail loans

	Past three months	Next three months
Total loans	-3.36	15.91
- Housing loans	-2.74	4.83
- Consumer and other loans	-3.36	11.39

8. Factors contributing to the change in credit standards for retail loans

	Past three months			Next three months		
	Total	Housing loans	Consumer and other loans	Total	Housing loans	Consumer and other loans
A) Costs of sources of funds	0.00	0.00	0.00	0.00	0.00	0.00
B) Competition of other banks	-3.36	-3.36	-3.36	12.86	12.86	12.86
C) Risk perception	0.00	0.00	0.00	3.05	3.05	3.05
- General economic situation and outlooks	0.00	0.00	0.00	-9.05	-9.05	-9.05
- Bad debt	0.00	0.00	0.00	0.00	0.00	0.00
- Risk related to required collateral	0.00	0.00	0.00	7.57	7.57	3.05
D) Risk appetite	0.00	0.00	0.00	0.00	0.00	0.00
E) Other factors, if exist (should be specified)	0.00	0.00	0.00	0.00	0.00	0.00

9. Terms and conditions for retail loans

	Past three months			Next three months		
	Total	Housing loans	Consumer and other loans	Total	Housing loans	Consumer and other loans
A) Interest rate margin*	-12.04	-12.04	-12.04	-7.52	-7.52	-12.04
B) Collateral requirements*	0.00	0.00	0.00	7.57	7.57	3.05
C) Share and deposits*	0.00	0.00	0.00	0.00	0.00	0.00
D) Mortgage value*	0.00	0.00	0.00	3.05	3.05	3.05
E) Commissions and fees*	0.00	0.00	0.00	-11.70	-11.70	-11.70
F) Maturity and grace period*	0.00	0.00	0.00	4.52	4.52	0.00
G) Other factors, if exist (should be specified) interest	0.00	0.00	0.00	0.00	0.00	0.00

10. Share of the rejected loan applications

	Past three months		
	Total	Housing loans	Consumer and other loans
Share of rejected applications	-8.44	-8.44	-8.44

11. Demand for retail loans

	Past three months	Next three months
Total loans	18.54	50.48
- Housing loans	24.45	31.08
- Consumer and other loans	5.88	55.00

12. Factors contributing to the demand for retail loans

	Past three months	Next three months
A) FINANCIAL NEEDS OF HOUSEHOLDS	9.79	29.57
- For refinancing	9.79	9.79
- For purchase of consumables (cars, furniture, etc.)	6.74	18.94
- For immovable property purchase	3.05	22.33
B) GENERAL ECONOMIC SITUATION	3.36	12.41
- Wages and salaries	0.00	9.05
- Employment	3.36	0.31
- Real estate market situation	0.00	9.05
C) USE OF ALTERNATIVE SOURCES OF FINANCING	-6.74	-6.74
- Household savings	0.00	0.00
- Retail loans from other banks	-6.74	-6.74
- Loan from non-banks	-6.74	-6.74
C) OTHER FACTORS (should be specified)	0.00	0.00