CENTRAL BANK OF MONTENEGRO

REPORT ON BANK LENDING SURVEY RESULTS SECOND QUARTER 2019

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PUBLISHED BY: Central Bank of Montenegro
Bulevar Svetog Petra Cetinjskog 6
81000 Podgorica
Telephone: +382 20 665 331
Fax: +382 20 665 336

WEB SITE: http://www.cbcg.me

DESIGNED BY: Nikola Nikolić

TRANSLATED BY: Vladimir Radenović

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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 in key determinants of supply of and demand for the loans to enterprises and households.

The survey consists of twelve questions that refer to the approval of loans to enterprises and households. 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 the loans and/or credit lines to enterprises, while the remaining six questions referred to the loans approved to households. With regard to the questions on loans and/or credit lines to the enterprises, they are further divided based on the loan maturity (long-term and short-term loans) and the size of the enterprise (micro, small, and medium enterprises and large firms). With regard to the household 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 second quarter of 2019. The survey disclosed positions of banks on the changes in their credit policies during the second quarter and expected changes in the third 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

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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.

sum of the percentages of banks responding “eased considerably” and “eased moderately”. 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 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”. Thus, a positive net percentage indicates net increasing, whereas a negative net percentage indicates net decreasing of demand.

SUMMARY

The Survey results suggested that, according to the banks' responses, credit standards for loans to enterprises have eased in the second quarter of 2019, which was according to banks' expectations from the previous quarter while those for household loans remained unchanged, even though banks expected their easing. In the next quarter, the banks expect easing of credit standards for loans to enterprises and households, particularly for those to enterprises.

Banks regard the easing of credit standards both to enterprises and households recorded in the second quarter as a result of strengthened market competition, expecting the same for the next quarter. In addition to increased competition, the easing of credit standards for housing loans in the upcoming quarter will also be the result of general economic situation and economic outlook. On the other hand, banks have pointed to the possibility of increasing the required collateral for micro, small and medium-sized enterprises, and to lower risk appetite, which may affect the tightening of credit standards in the next quarter.

Banks assess that the prominent banking market competition has lead to the reduction of interest rate margins, commissions and fees in the second quarter of 2019. Banks expect that the credit conditions will be eased also in the following quarter, except the collateral requirements for the enterprises and households where they anticipate their mild tightening.

Banks estimated that the demand for enterprise and households loans increased during the second quarter of 2019. Demand for loans to enterprises was driven by the requirement to fund working capital and capital investments. In the households sector, the main factors contributing to the increase in demand for loans were requirements to refinance the existing debts and purchase of consumer durable goods. Banks expect the uptrend in demand for loans to extend into the third quarter of 2019.

Table 1 **Assessment of credit standards and demand for loans by banks, Q2 and Q3 2019**

	Demand		Supply	
	Credit standards			
	Q2 2019	Q3 2019 (expectations)	Q2 2019	Q3 2019 (expectations)
Loans to enterprises	↓	↓	↑	↑
Long-term loans	↗	↓	↑	↑
Short-term loans	-	↓	↑	↑
Micro, small and medium enterprises	-	↓	↑	↑
Large enterprises	↓	↓	↑	↑
Loans to households	-	↖	↑	↑
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%)

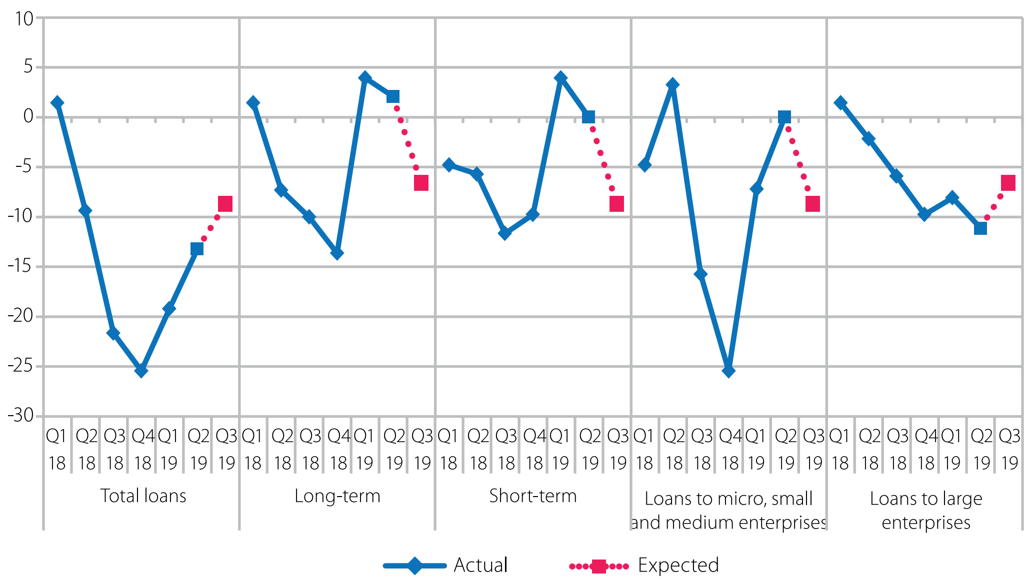
1. LOANS TO ENTERPRISES

1.1. Credit standards and credit terms and conditions for enterprises

The survey results reveal that the credit standards for loans to enterprises continued to ease in the second quarter of 2019. This was in accordance with the expectations of banks shown in the previous survey. The Survey shows that the easing of the credit standards was recorded in 13% of the banking sector. Credit standards were also eased for loans to large enterprises, while those for micro, small, medium enterprises remained unchanged compared to the previous quarter.

Banks expect that the easing of credit standards for enterprises will continue in the next quarter, albeit to a lesser extent in relation to the previous quarter.

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



Source: CBCG

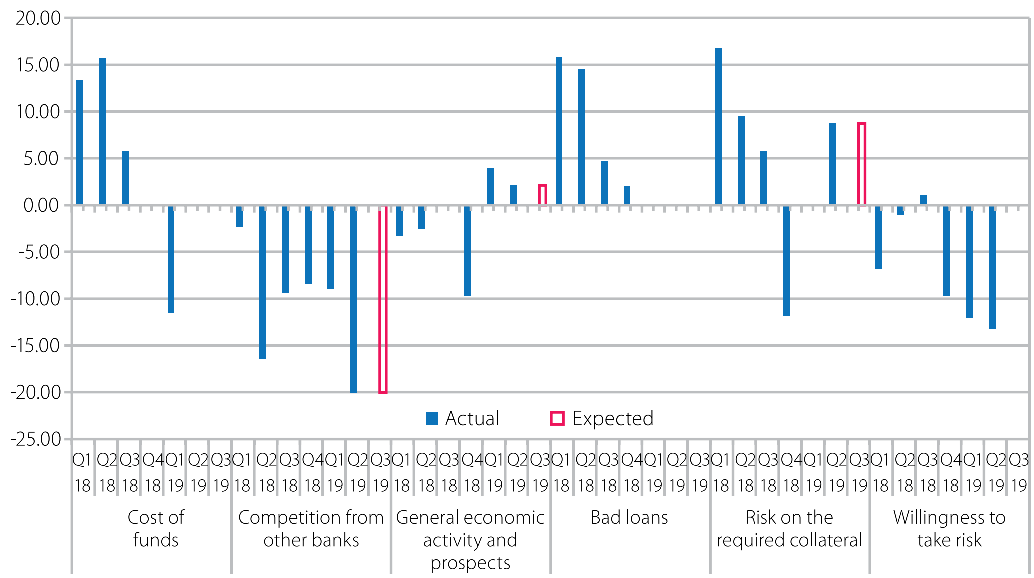
Note: A positive value indicates tightening of credit standards, whereas a negative value indicates easing of credit standards.

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

Banks indicated that strengthened competition in the banking sector, in addition to higher risk appetite, contributed to the easing of credit standards for new lending to enterprises. On the other hand, the higher risk of required collateral required tightening of credit standards for lending to micro, medium and small enterprises. A minor part of the banking sector stated that the general economic situation resulted in mild tightening of credit standards, while the costs of costs of sources of funds and non-collectability of claims did not affect credit standards in the second quarter.

Banks expected that increased banking market competition would contribute to the further easing of standards in the upcoming quarter. A minor portion of the banking sector finds that weaker economic situation might fuel the mild tightening of credit standards, and that an increased risk of required collateral in lending to micro, small, and medium sized companies might be expected, which could result in tightening the standards. It is expected that costs of sources of funds, non-collectability of claims, and risk appetite would not contribute to the credit standards in the upcoming quarter.

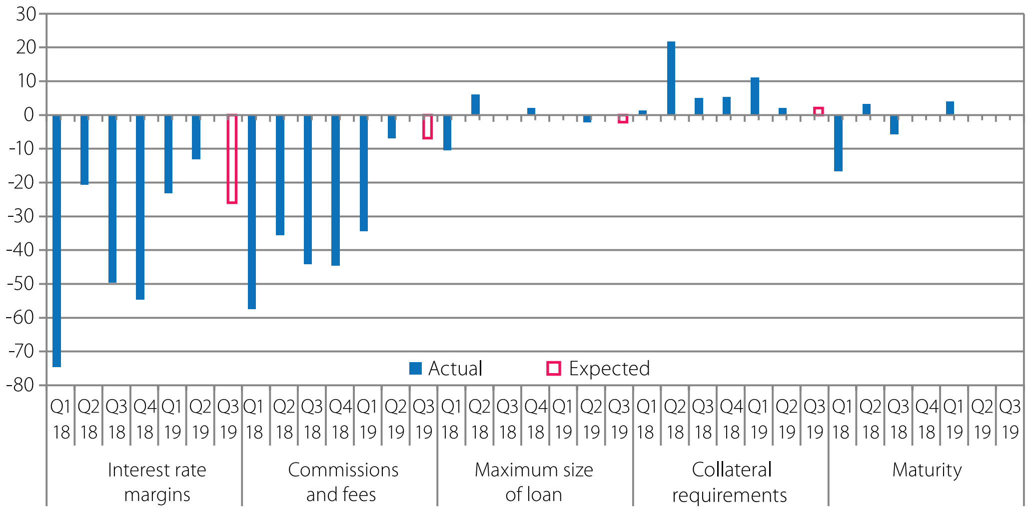
Graph 2 Impact of factors on the change in credit standards (net percentage)



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 loans to enterprises continued in the second quarter of 2019 as well. On the other hand, a minor part of the banking sector increased collateral requirements resulting in credit standards' tightening, still without higher effect to reducing the flexibility of terms and conditions for approving loans to enterprises.

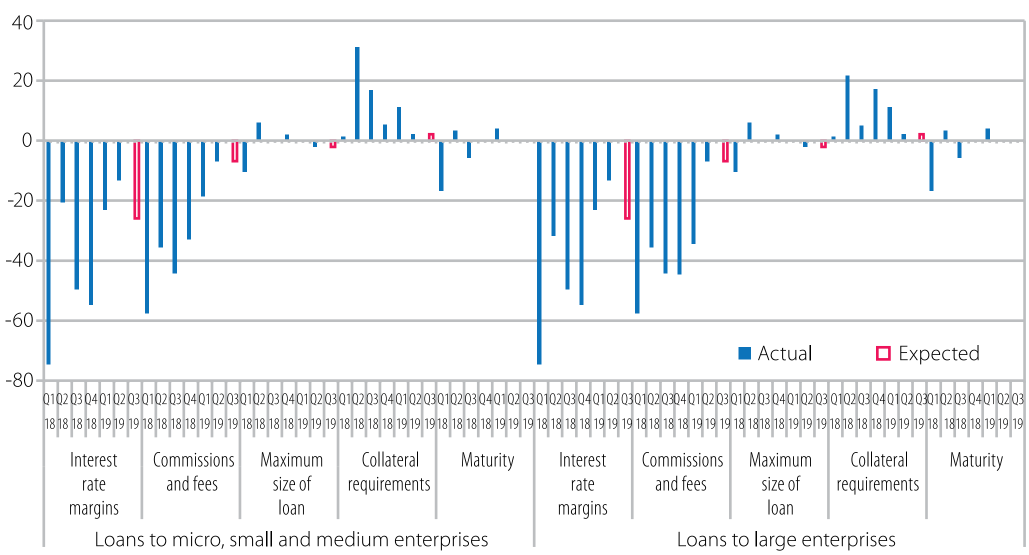
Change in terms and conditions for loans to enterprises (net percentage) **Graph 3**



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, and increasing maximum amounts in granting loans, which would contribute to the easing of conditions for granting loans to enterprises. A small portion of the banking sector saw thightening of credit conditions only in terms of higher demands for collaterals in micro, small, medium and large enterprises.

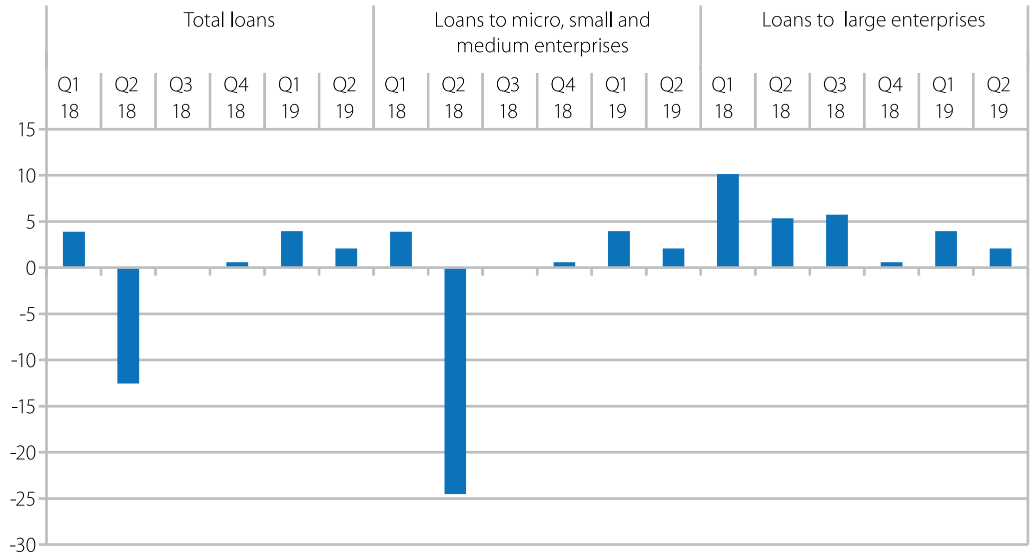
Change in terms and conditions for loans to enterprises by the size (net percentage) **Graph 3a**



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

The results show that the share of rejected loan applications to micro, small, medium and large enterprises recorded mild quarterly increase in the second quarter of 2019 (change in some 2% of the banking market).

Graph 4 Share of rejected applications for loans to enterprises

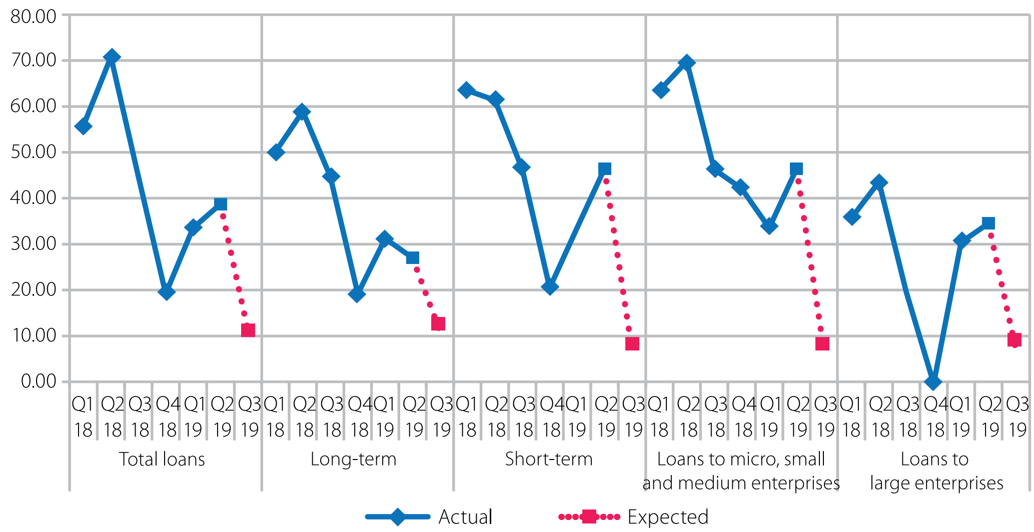


Source: CBCG
Note: A positive value indicates the increase of rejected loan applications, whereas a negative value indicates the decrease of rejected applications for loans to enterprises.
* The graph shows net percentage which indicates the direction of change rather than its intensity.

1.2. Demand for loans to enterprises

In the second quarter, banks recorded a rise in demand for loans to micro, small and medium enterprises, which was according to banks' expectations from the previous survey. The Survey cited the requirements for financing of enterprises i.e. the requirements for capital investments and working capital, while the debt restructuring of enterprises were not a contributing factor to the increase in demand in the second quarter.

Change in demand for loans to enterprises (net percentage) **Graph 5**



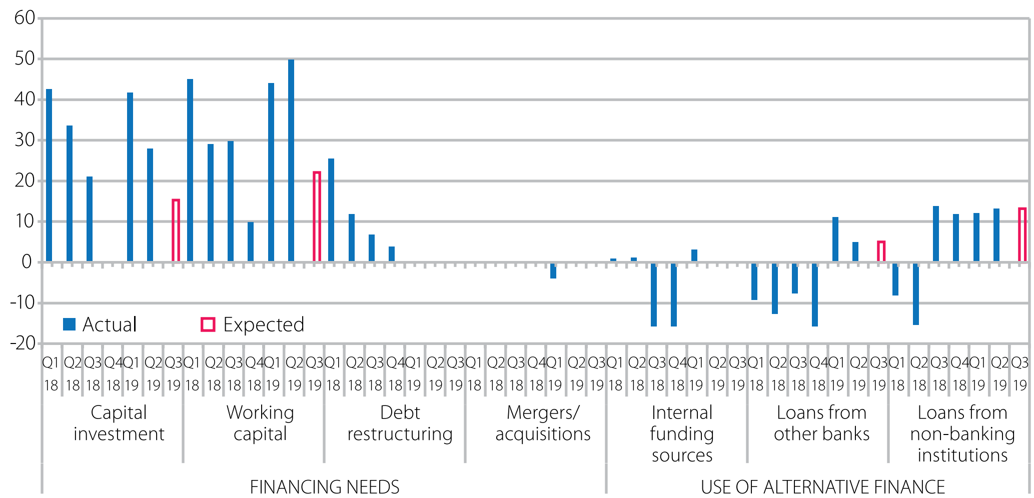
Source: CBCG

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 next quarter, banks expect a rise in demand for all enterprises, regardless of their size, still lower than in the previous quarter. The needs for capital investments and working capital will drive the increase in demand, except for the needs for restructuring of debt that would not affect the demand for loans to enterprises.

Factors contributing to the change in demand for loans to enterprises (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.

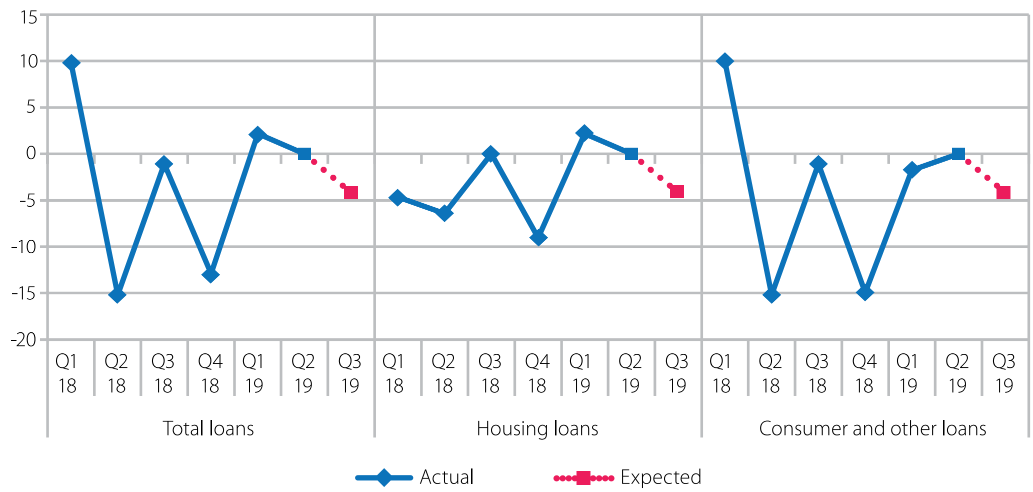
* The graph shows net percentage which indicates the direction of change rather than its intensity.

2. HOUSING LOANS

2.1. Credit standards and credit terms and conditions for households

According to the Survey for the second quarter of 2019, credit standards for households remained unchanged relative to the previous quarter, even though banks' expectations from the previous quarter showed easing of credit standards. Expectations of a minor part of the banking sector for the next quarter showed the easing of standards in loans to households.

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

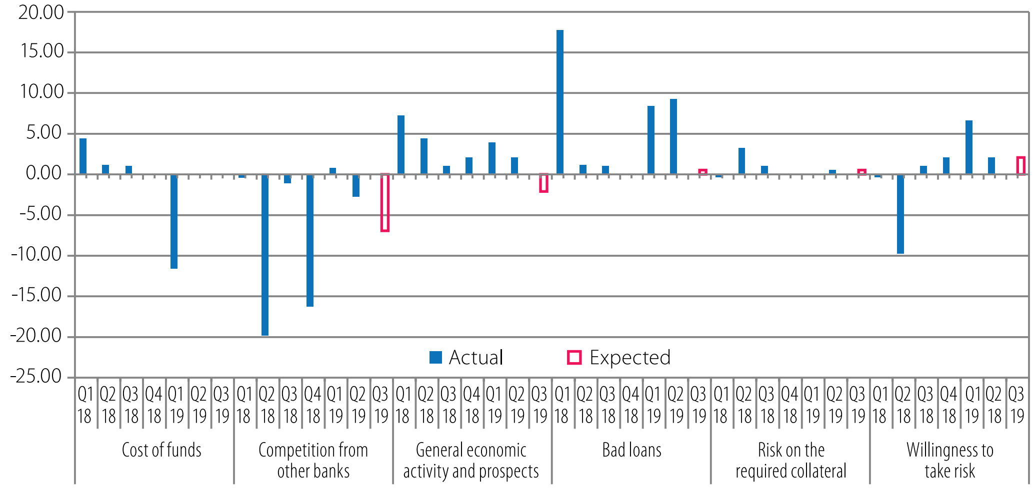


Source: CBCG
Note: A positive value indicates tightening of credit standards, whereas a negative value indicates easing of credit standards.
* The graph shows net percentage which indicates the direction of change rather than its intensity.

In the second quarter, increased competition contributed to the easing of lending standards in minor portion of the banking sector while, in opposite, increased non-collectability of claims resulted in standards' tightening. However, such developments did not affect the aggregate level in terms of the change in credit standards compared to the previous quarter.

Banks expected that, in addition to increased competition, easing of standards would be a result of better economic situation, with expected slightly lower risk appetite. Inability to collect claims and risks of required collateral might act towards mild tightening of standards for approving household loans, still in a very small portion of the banking sector.

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



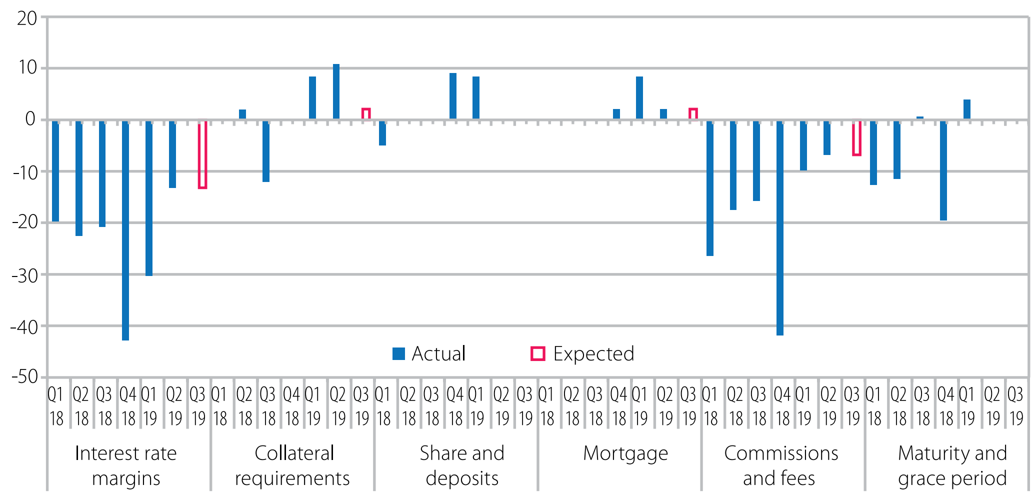
Source: CBCG

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 second quarter of 2019 credit terms and conditions for approving household loans eased in reference to interest rate margins, commissions and fees. Increased demands in terms of collaterals and mortgage value resulted in tightening of conditions for all categories of household loans relative to Q1 2019. Banks had similar expectations for the upcoming quarter.

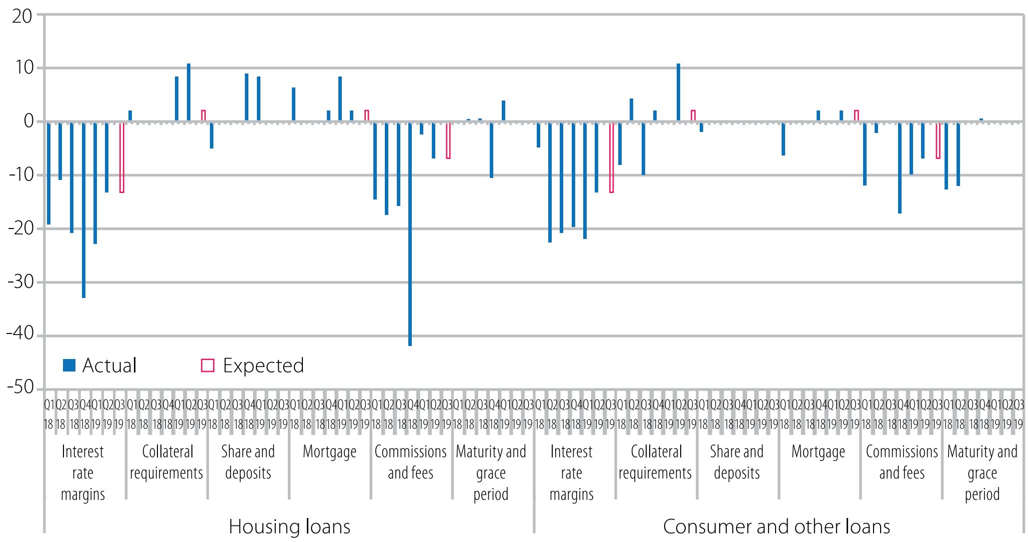
Change in terms and conditions for loans to households (net percentage) **Graph 9**



Source: CBCG

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

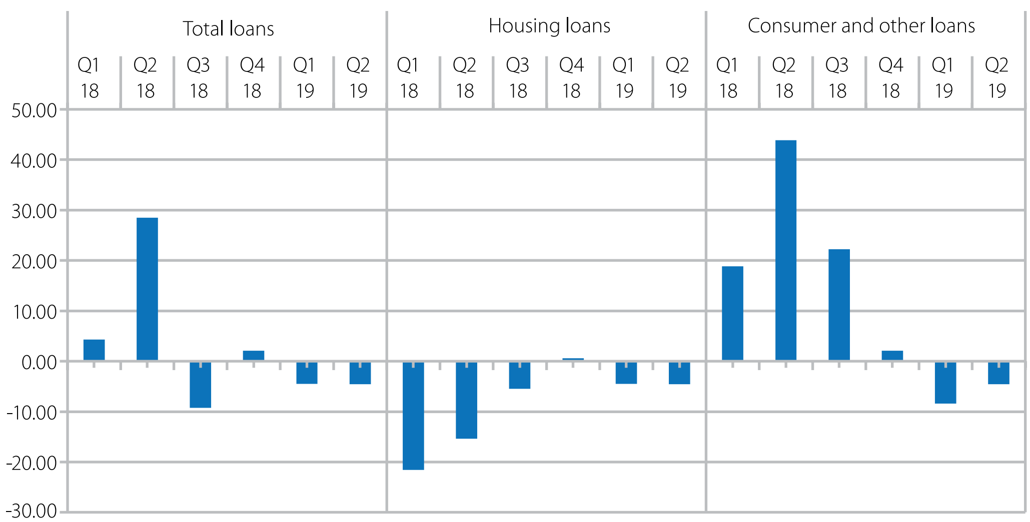
Graph 9a **Change in terms and conditions for housing loans and consumer and other loans (net percentage)**



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 loans to households decreased in the second quarter of 2019 in all categories of loans compared to the previous quarter (by 4.5%).

Graph 10 **Share of rejected applications for loans to households**

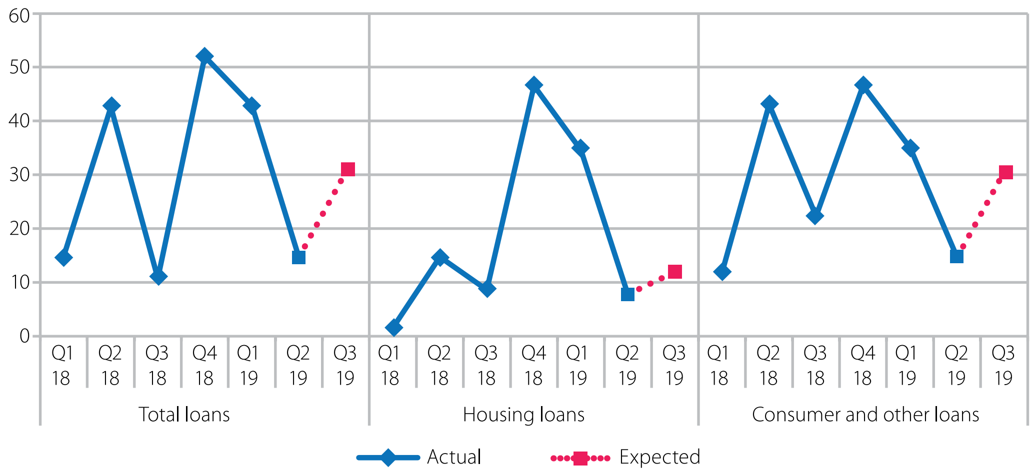


Source: CBCG
Note: A positive value indicates the increase of rejected loan applications, whereas a negative value indicates the decrease of rejected applications for loans to households.
* The graph shows net percentage which indicates the direction of change rather than its intensity.

2.2. Demand for loans to households

The Survey results reveal a rise in the demand for loans to households over the second 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. To wit, the banks marked refinancing requirements and purchase of consumer durables (cars, furniture, and the like) as factors contributing to the increase in demand for loans to households.

Change in demand for loans to households (net percentage) **Graph 11**



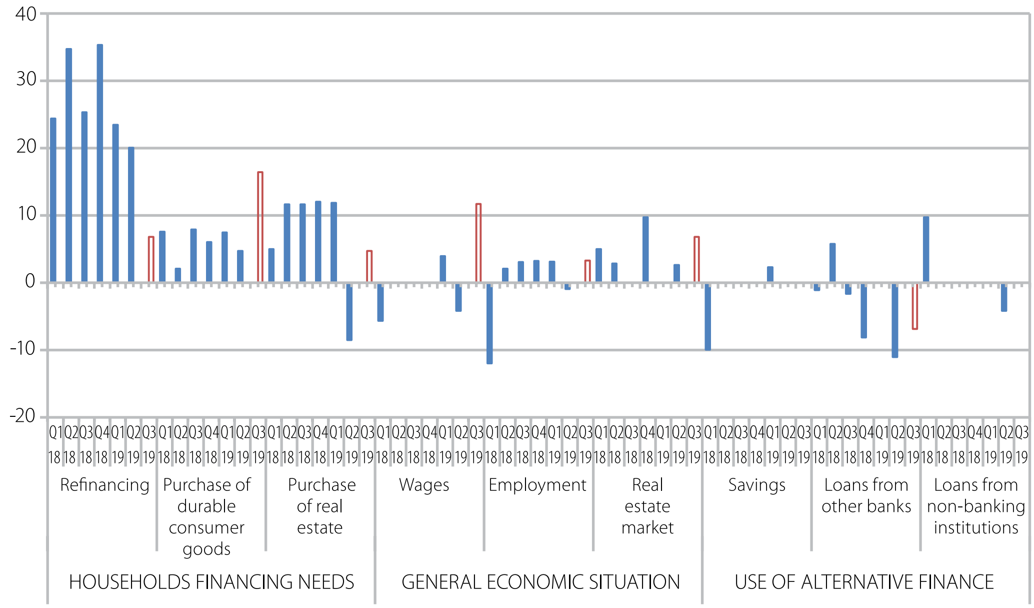
Source: CBCG

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 third quarter of 2019, banks expect further increase in demand for loans to households, 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 (slight increase in the employment and improved situation at the real estate market).

Graph 12 Factors contributing to the change in demand for loans to households (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 second quarter 2019

1. Credit standards for loans to enterprises

	Past three months	Next three months
A) Total loans and/or credit line	-13.22	-8.70
Long-term (over 1 year)	2.09	-6.61
Short-term (up to 1 year)	0.00	-8.70
B) Loans and/or credit lines to micro, small and medium enterprises	0.00	-8.70
C) Loans and/or credit lines to large firms	-11.12	-6.61

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

	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	0.00	0.00	0.00
B) Competition of other banks	-20.03	-20.03	-11.33	-20.03	-20.03	-11.33
C) Risk perception	8.70	8.70	0.00	8.70	8.70	0.00
- General economic situation and outlooks	2.09	2.09	2.09	2.09	2.09	2.09
- Bad debt	0.00	0.00	0.00	0.00	0.00	0.00
- Risk related to required collateral	8.70	8.70	0.00	8.70	8.70	0.00
D) Risk appetite	-13.22	-13.22	-13.22	0.00	0.00	0.00

3. Credit terms and conditions for loans to enterprises

	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*	-13.22	-13.22	-13.22	-25.94	-25.94	-25.94
B) Commissions and fees *	-6.83	-6.83	-6.83	-6.83	-6.83	-6.83
C) Maximum amount of loans and/or credit lines**	-2.09	-2.09	-2.09	-2.09	-2.09	-2.09
D) Collateral requirements*	2.09	2.09	2.09	2.09	2.09	2.09
E) Maturity**	0.00	0.00	0.00	0.00	0.00	0.00

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	2.09	2.09	2.09

5. Demand for loans to enterprises

	Past three months	Next three months
A) Demand for total loans and/or credit lines	38.71	11.01
Long-term (over 1 year)	27.01	11.01
Short-term (up to 1 year)	46.39	6.83
B) Demand of micro, small and medium enterprises	46.39	6.83
C) Demand of large firms	34.52	6.83

6. Factors contributing to the demand of enterprises for loans

	Past three months	Next three months
A) FINANCIAL NEEDS OF ENTERPRISES	46.55	22.13
- for capital investments	28.03	15.31
- for working capital	49.83	22.13
- for debt restructuring	0.00	0.00
- for mergers/acquisitions	0.00	0.00
B) USE OF ALTERNATIVE SOURCES OF FINANCING	6.39	6.39
- internal sources of financing	0.00	0.00
- loans from other banks	5.04	5.04
- loans from non-banks	13.22	13.22
C) OTHER FACTORS (it should be specified)		

7. Credit standards for loans to households

	Past three months	Next three months
Total loans	0.00	-4.18
- housing loans	0.00	-4.18
- consumer and other loans	0.00	-4.18

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

	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	-2.75	-2.75	-2.75	-6.93	-7.47	-7.47
C) Risk perception	0.00	0.00	0.00	0.00	0.00	0.00
- General economic situation and outlooks	2.09	2.09	2.09	-2.09	-2.09	-2.09
- Bad debt	9.23	9.23	9.23	0.53	0.53	0.53
- Risk related to required collateral	0.53	0.53	0.53	0.53	0.53	0.53
D) Risk appetite	2.09	2.09	2.09	2.09	2.09	2.09
E) Other factors, if exist (it should be specified)	0.00	0.00	0.00	0.00	0.00	0.00

9. Terms and conditions for loans to households

	Past three months			Next three months		
	Total	Housing loans	Consumer and other loans	Total	Housing loans	Consumer and other loans
A) Interest rate margin*	-13.22	-13.22	-13.22	-13.22	-13.22	-13.22
B) Collateral requirements*	10.79	10.79	10.79	2.09	2.09	2.09
C) Share and deposits*	0.00	0.00	0.00	0.00	0.00	0.00
D) Mortgage value*	2.09	2.09	2.09	2.09	2.09	2.09
E) Commissions and fees*	-6.83	-6.83	-6.83	-6.83	-6.83	-6.83
F) Maturity and grace period*	0.00	0.00	0.00	0.00	0.00	0.00
G) Other factors, if exist (it should be specified)interest	0.00	8.99	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	-4.52	-4.52	-4.52

11. Demand for loans to households

	Past three months	Next three months
Total loans	14.63	30.50
- housing loans	7.80	11.98
- consumer and other loans	14.63	30.50

12. Factors contributing to the demand for loans to households

	Past three months	Next three months
A) FINANCIAL NEEDS OF HOUSEHOLDS	6.83	18.52
- for refinancing	20.04	6.83
- for purchase of consumables (cars, furniture, etc.)	4.73	16.43
- for immovable property purchase	-8.48	4.73
B) GENERAL ECONOMIC SITUATION	5.93	21.80
- wages and salaries	-4.18	11.69
- employment	-0.90	3.28
- real estate market situation	2.64	6.83
C) USE OF ALTERNATIVE SOURCES OF FINANCING	-11.01	-6.83
- household savings	0.00	0.00
- loans to households from other banks	-11.01	-6.83
- loan from non-banks	-4.18	0.00
C) OTHER FACTORS (it should be specified)	0.00	0.00