

REVIEW OF THE LEVEL OF THE STRUCTURAL SYSTEMIC RISK BUFFER RATE

Pursuant to Article 131 of the Credit Institutions Act (Official Gazette 159/2013) and Article 5 of the Decision on the application of the structural systemic risk buffer (Official Gazette 61/2014), the Croatian National Bank reviews the requirement to maintain the structural systemic risk buffer rate prescribed for all credit institutions with head offices in the Republic of Croatia at the level of 1.5% of the total risk exposure amount or 3% of the total amount of risk exposures if these are identified as systemically significant based on the market share criteria, beginning as of May 2014. In accordance with Article 382 of the Credit Institutions Act, the Decision on the application of the structural systemic risk buffer was based on the following systemic risk indicators:

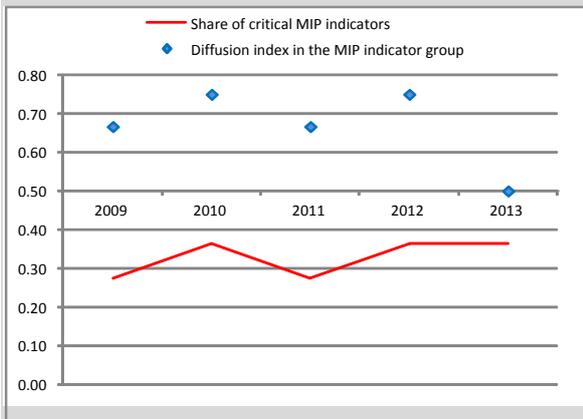
- 1) elevated structural macroeconomic imbalances that define the probability and intensity of a potential shock to the financial system;
- 2) a high level of market concentration that increases the vulnerability of the financial system;
- 3) a low liquidity of real-estate markets, complicating a fast and efficient exercise of collateral (at an adequate price);
- 4) the operations of systemically important financial institutions, with regard to the high complexity of their business activities, whose associated risks cannot currently be addressed by adequate instruments, due to the fact that the risk buffer for other systemically important credit institutions will be available to macroprudential policy makers from 2016 and that the structural systemic risk buffer rate is applied as a substitute in that period.

As shown by a recent analysis of structural financial stability issues and a comprehensive assessment of risks in the economy, regularly carried out by the CNB¹, identified systemic risks still exist, which means that maintaining this risk buffer rate at the previously determined levels (for two relevant groups of credit institutions) remains a requirement. Specifically, the vulnerabilities in the form of a high private sector indebtedness and disturbing public debt growth, coupled with weak export performances, the lack of economic growth and objectively lower potential for fast and efficient reforms, remain a constraint for economic development capacities (the indicators of the Macroeconomic Imbalances Procedure (MIP) suggest that the degree of imbalances has not changed significantly over the last year (Figure 1)). At the same time, the concentration in the financial sector has remained high, still exceeding the European average (Figure 2). Due to the depleted household financial resources and existing uncertainties, real-estate demand has remained subdued (Figure 3). Finally, the breakdown of institutions by size and the ratio of market shares between specific institutions have remained almost unaltered so that there is no

¹ Financial stability No. 14, Year 8, II, 2015, CNB (at: <http://www.hnb.hr/publikac/financijska%20stabilnost/h-fs-14-2015.pdf>).

need to change the calibrated level of the buffer rate for systemically important institutions in the transition period (Figure 4).

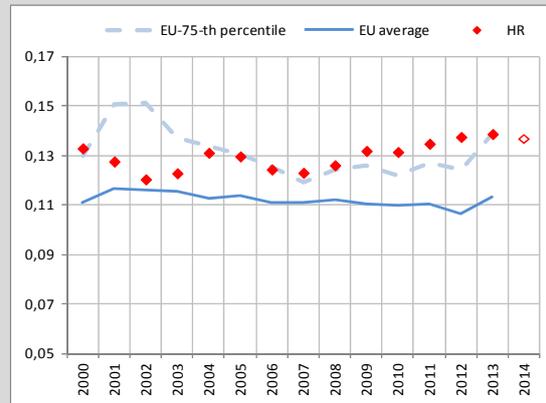
Figure 1 Structural macroeconomic imbalances remain



Source: European Commission.

Note: For a detailed analysis of the recent structure of MIP indicators see: *European Commission: Alert Mechanism Report 2015* (http://ec.europa.eu/europe2020/pdf/2015/amr2015_en.pdf)

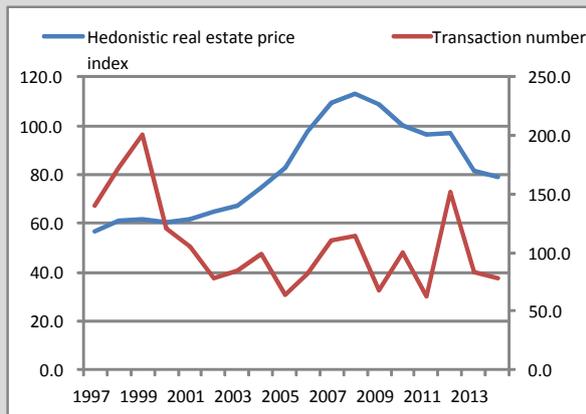
Figure 2 Level of market concentration remains high



Source: ECB, CNB.

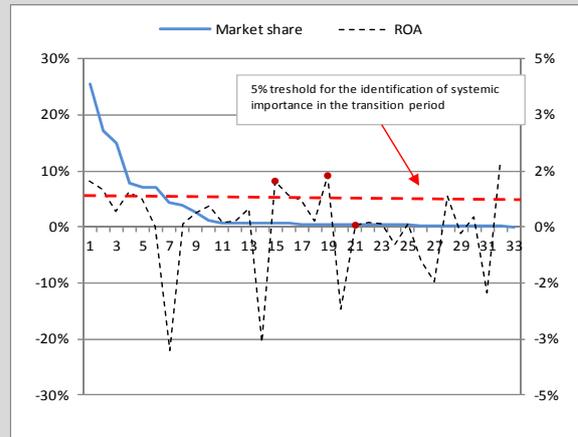
Note: The 2014 data for Croatia are based on unconsolidated interim reports of credit institutions.

Figure 3 Trends in real-estate prices give no indication of trend reversal (index 2010=100)



Source: CNB.

Figure 4 Breakdown of institutions by market share



Source: CNB.

Note:

- a) Red dots mark the performances of savings banks whose parent banks are identified in the group of systemically important institutions in the transition period.
- b) The figure excludes a minor institution with atypical values.

In view of the above said, the Croatian National Bank will not, at the moment, amend the Decision on the application of the structural systemic risk buffer of 19 May 2014. It will continue to regularly monitor the evolution of structural systemic risks and by the end of the year it will review the Decision in parallel with the introduction of the risk buffer for systemically important financial institutions under Article 137 of the Credit Institutions Act.