



Pursuant to the decision of the Board of Directors of the Banco de Portugal, taken on 22 June 2021, the updated list of third countries to which the Portuguese banking system is exposed for the purposes of recognising and setting the countercyclical capital buffer (CCyB) rates for third countries, valid until the second quarter of 2022, includes the Republic of Mozambique and Macao Special Administrative Region of the People's Republic of China

According to Recommendation ESRB/2015/1 of the European Systemic Risk Board (ESRB), the Banco de Portugal should identify, on an annual basis, the third countries to which the Portuguese banking system is materially and directly exposed for the purposes of recognising and setting the CCyB rates for exposures to those countries and monitor the risks stemming from excessive credit growth in those countries (Recommendation B).¹ The CCyB is a macroprudential instrument designed with the aim of increasing resilience of the banking sector against system-wide cyclical risks from excessive credit growth. This note summarises the main results of the 2021 identification exercise, based on supervisory data with reference date of 31 December 2020, and presents the updated list of material third countries.

In line with Decision ESRB/2015/3, the identification methodology adopted by the Banco de Portugal focuses on (i) the evolution of three indicators – risk-weighted exposures, original exposures and defaulted exposures as a percentage of the respective total exposure amount and (ii) the criteria that guide the revision of the list of material third countries.²

The aforementioned indicators include only direct (risk-weighted, original and defaulted) exposures of the Portuguese banking system to the private non-financial sector in third countries, such as exposures to corporates and retail or mortgages secured by immovable property, thus excluding direct exposures to public sector entities or financial institutions. Moreover, exposures of the Portuguese banking system via credit granted to non-financial corporations located in Portugal but whose activity is, to some extent, dependent on third countries were also excluded from this analysis.

As for the criteria on the identification of material third countries, a third country is identified as material if at least one of the three indicators is equal to or higher than 1% in each of the last two quarters and, on average, in the eight quarters preceding the reference date. On the other hand, a third country is dropped from the list if all the three indicators are lower than 1% in each of the last two quarters and, on average, in the twelve quarters preceding the reference date. A sustained decrease in exposures' materiality (less than 1% of total exposures) for a long period of time (three years) for all metrics considered is needed in order to exclude a country from the list.

¹ A third country is any jurisdiction outside the European Economic Area. The European Economic Area includes the European Union Member States, Iceland, Liechtenstein and Norway.

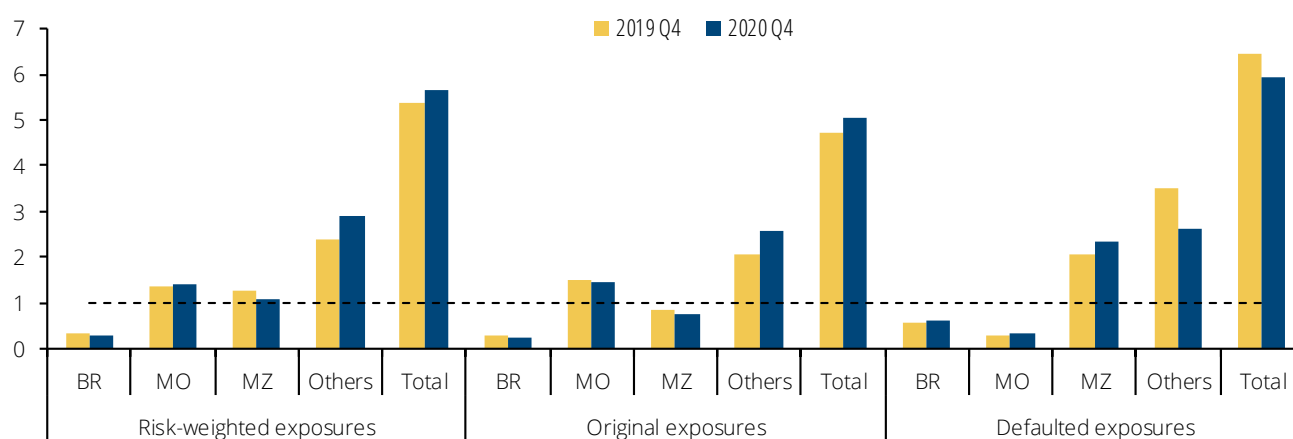
² The identification of material third countries follows the methodology described in https://www.bportugal.pt/sites/default/files/anexos/documentos-relacionados/institution_specific_countercyclical_capital_buffer.pdf

Following an assessment based on the methodology briefly described, the list of material third countries for the Portuguese banking system has been changed in 2021, vis-à-vis 2020, now comprising only Macao and Mozambique, and will be in force until the second quarter of 2022. In comparison with last year, Brazil was removed from the list of material third countries for the purpose of recognising and setting the CCyB rates for exposures to third countries since all exit criteria are met.

In the last quarter of 2020, there was a departure from the trend previously observed on the relative exposures of the Portuguese banking system to third countries. When compared with the same period in the previous year, both relative risk-weighted and original exposures increased slightly from 5.39% to 5.67% and from 4.70% to 5.05%, respectively (Chart 1). However, this change is mostly related to increases in the relative exposures to other third countries, rather than to countries included in the current and last year's list of material third countries. Defaulted exposures have fallen from 6.47% to 5.94% over the same period, reflecting an increase in the relative exposures to Mozambique and a decrease in the relative exposures to other third countries not identified as material for the Portuguese banking system.

Compared with the last quarter of 2019, the relative risk-weighted and original exposures to Brazil and Macao have remained barely unchanged. For Mozambique, the relative risk-weighted and original exposures decreased 0.06 p.p. to 1.10% and 0.08 p.p. to 0.75%, respectively. Defaulted exposures increased slightly in all three countries.

Chart 1 • Amount of relevant credit exposures in third countries in relation to the total amount of relevant credit exposures: total and by material third countries | In percentage of the total amount of relevant credit exposures



Source: Banco de Portugal. | Notes: (a) Based on COREP data with reference date of 31 December 2020. The assessment is based on data available up to 25 May 2021. (b) The relevant credit exposures comprise exposures to the private non-financial sector in the banking and trading books of credit institutions subject to own funds requirements associated with credit risk, counterparty risk and free deliveries. (c) Country codes: BR – Brazil; MO – Macao; MZ – Mozambique. (d) Others refers to the remaining third countries.

In 2020, Brazil was included for the first time in the list of material third countries given that the relative defaulted exposures to Brazil met the entry criteria. However, the original and risk weighted relative exposures already exhibited a decreasing path since the end of 2017 with values below the 1% threshold. In 2021, Brazil has met the necessary conditions to be removed because relative defaulted exposures decreased substantially in the four quarters of 2020 (Table 1). The three types of relative exposures are below the 1% threshold in each of the last two quarters of 2020 as well as in the 12-quarters average. However, Brazil is one of the third countries identified by the ESRB as material for the banking system of the European Economic Area and for that reason it is subject to a regular monitoring as regards the emergence of cyclical systemic risk.

Macao and Mozambique remain on the list of material third countries for the Portuguese banking system given that exit criteria are not met.

Table 1 • Entry and exit criteria for the list of material third countries | In percentage of the total amount of relevant credit exposures

Third Countries	Risk-weighted exposures					Original exposures					Defaulted exposures				
	2020			Average over the last 8 quarters	Average over the last 12 quarters	2020			Average over the last 8 quarters	Average over the last 12 quarters	2020			Average over the last 8 quarters	Average over the last 12 quarters
	Q2	Q3	Q4			Q2	Q3	Q4			Q2	Q3	Q4		
Brazil	0.28	0.29	0.30	0.34	0.42	0.25	0.25	0.26	0.29	0.33	0.62	0.61	0.61	0.80	0.89
Macao	1.46	1.37	1.39	1.34	1.35	1.56	1.50	1.48	1.55	1.55	0.32	0.37	0.35	0.27	0.23
Mozambique	1.22	1.24	1.10	1.25	1.27	0.82	0.82	0.75	0.81	0.77	2.52	2.47	2.35	1.95	1.67

Source: Banco de Portugal. | Notes: (a) Based on COREP data with reference date of 31 December 2020. The assessment is based on data available up to 25 May 2021. (b) The relevant credit exposures comprise exposures to the private non-financial sector in the banking and trading books of credit institutions subject to own funds requirements associated with credit risk, counterparty risk and free deliveries. (c) Cells in grey represent relative exposures above 1% for individual third countries. (d) The number of institutions included in each identification exercise may change across quarters.

None of the two third countries now identified as material for the Portuguese banking system in 2021 is monitored by the ESRB.³ Therefore the Banco de Portugal will continue to monitor the cyclical systemic risk of the two identified material third countries, using the set of macroeconomic and financial indicators described in the methodology adopted by the Banco de Portugal. Also, the Banco de Portugal will continue to monitor developments associated with Angola (the country that was excluded from the list of material third countries in 2020) as regards other sources of risk, since there are other types of exposures that render this country relevant for the Portuguese banking system. The Banco de Portugal will only disclose its risk assessment if there is the need to take a decision on the countercyclical buffer rate applicable to exposures to a country included in the list of material third countries.⁴

This list will be updated annually. The tentative date for the next release of the list of material third countries for the Portuguese banking system is 30 June 2022.

³ According to Decision ESRB/2015/3, the current list of material third countries for the Union's banking system, as adopted by the ESRB on 19 June 2020, includes Brazil, China, Hong Kong, Mexico, Russia, Singapore, Switzerland, Turkey, and United States of America. The cyclical systemic risk in these countries is, therefore, directly monitored by the ESRB.

⁴ Decisions cover the recognition of a countercyclical buffer measure implemented by a third country authority or the setting of the countercyclical buffer rate for exposures to a third country.