

COUNTERCYCLICAL CAPITAL BUFFER ASSESSMENT OF THE MATERIALITY OF THIRD COUNTRIES



28 JUN 2024

Pursuant to a decision of the Board of Directors of the Banco de Portugal of 4 June 2024, the 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 end-June 2025, 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 that was designed with the aim of increasing the resilience of the banking sector against system-wide cyclical risks from excessive credit growth. This note summarises the main results of the 2024 identification exercise, based on supervisory data with reference date of 31 December 2023, and presents the updated list of material third countries.²

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. The 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 exposures secured by mortgages on immovable property. This means that they do not comprise direct exposures to public sector entities or to financial institutions. Moreover, the analysis does not include exposures of the Portuguese banking system via credit granted to Portuguese non-financial corporations whose activity is, to some extent, dependent on third countries (i.e. indirect exposures to third countries are not considered).

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. 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 of 31 December. This means that a sustained decrease in exposures' materiality for a long period (three years) for all metrics considered should be observed. Exit criteria were designed to be more conservative than entry criteria.

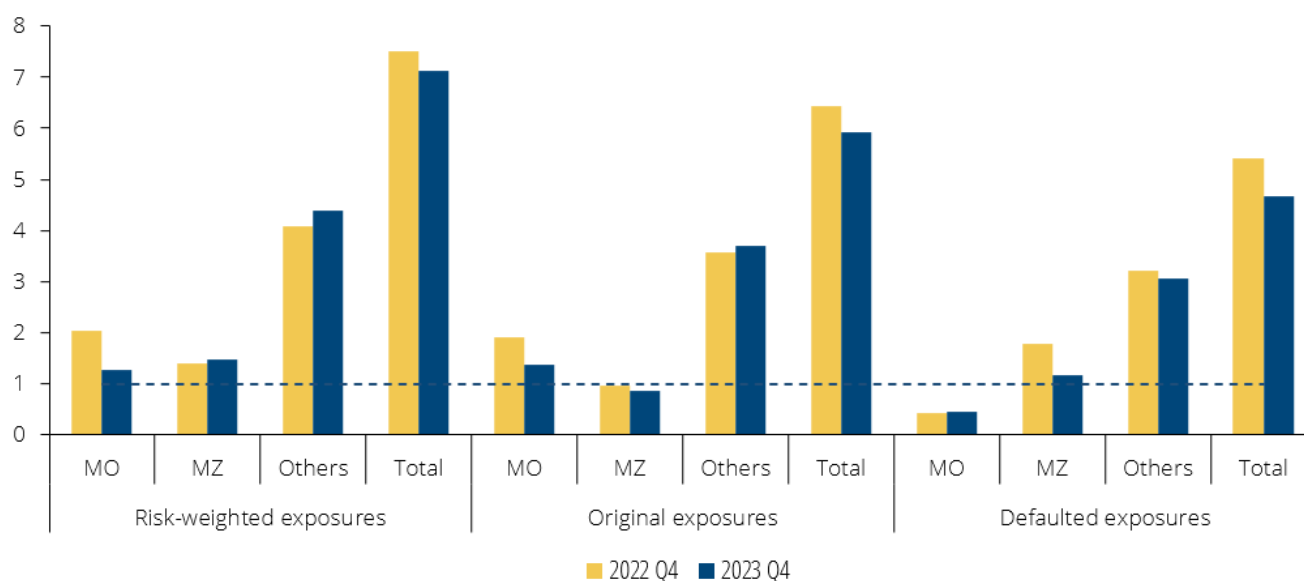
Based on the following assessment, the Banco de Portugal determined the list of material third countries for the Portuguese banking system in 2024, which remains unchanged vis-à-vis 2023, and comprises Macao and Mozambique. This decision of the Banco de Portugal will be in force until end-June 2025 and results simultaneously from the fact that (i) no other third country meets the entry criteria, and (ii) the abovementioned two countries do not fulfil the exit criteria.

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 [Institution-specific countercyclical capital buffer \(30 December 2016\)](#).

In the last quarter of 2023, relative exposures decreased in comparison to the previous year (Chart 1). Relative defaulted exposures registered the highest fall, from 5.4% to 4.7%, followed by relative original and risk-weighted exposures, which decreased from 6.4% to 5.9% and from 7.5% to 7.1%, respectively. The change in relative risk-weighted and original exposures is driven by decreases in relative exposures to Macao, while the decrease in relative defaulted exposures can be mainly attributed to the decrease in relative exposures to Mozambique. When focusing on Macao, relative risk-weighted exposures and relative original exposures decreased significantly (-0.8 p.p. and -0.5 p.p., respectively), while relative defaulted exposures increased (+0.02 p.p.), compared with the last quarter of 2022. Regarding Mozambique, relative risk-weighted exposures increased (+0.07 p.p.), while relative original exposures and relative defaulted exposures decreased (-0.1 p.p. and -0.6 p.p., respectively).

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



Sources: COREP and Banco de Portugal calculations. | Notes: (a) Based on COREP data with reference date of 31 December 2023. The assessment is based on data available up to 4 April 2024. (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: MO – Macao; MZ – Mozambique. (d) Others refers to the remaining third countries.

According to the quantitative criteria defined to exclude a country from the list of material countries, Macao and Mozambique should remain on the list of material third countries for the Portuguese banking system given that exit criteria are not met (Table 1). Based on the risk-weighted exposures, the relative exposures are above the 1% threshold in the second and third quarters of 2023 as well as the 8-quarter and 12-quarter averages. When focusing on the original exposures, the relative exposures for Mozambique were below the 1% threshold in the second and third quarters of 2023, signalling a decrease of relative exposures compared to 2022. Similarly, the metrics for Macao were below the 1% threshold in the case of relative defaulted exposures. However, according to the exit criteria, this is not sufficient to remove these countries from the list of material countries.

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				
	2023			Average over the last 8 quarters	Average over the last 12 quarters	2023			Average over the last 8 quarters	Average over the last 12 quarters	2023			Average over the last 8 quarters	Average over the last 12 quarters
	Q2	Q3	Q4			Q2	Q3	Q4			Q2	Q3	Q4		
Macao	1.44	1.50	1.26	1.66	1.58	1.50	1.58	1.37	1.69	1.62	0.45	0.50	0.45	0.40	0.39
Mozambique	1.31	1.51	1.47	1.42	1.36	0.85	0.92	0.87	0.94	0.90	1.62	1.32	1.16	2.06	2.22

Source: COREP (Banco de Portugal calculations). | Notes: (a) Based on COREP data with reference date of 31 December 2023. The assessment is based on data available up to 4 April 2024. (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 third countries identified as material for the Portuguese banking system in 2024 is currently monitored by the ESRB.³ Therefore, the Banco de Portugal will monitor the cyclical systemic risk of all identified material third countries, using the set of macroeconomic and financial indicators described in the methodology adopted by the Banco de Portugal.

This list shall be updated annually on the basis of the criteria established to guide the entry/exit of countries into/from the list. The tentative date for the next release of the list of material third countries for the Portuguese banking system is 30 June 2025.

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 23 June 2022, includes Brazil, China, Hong Kong, Mexico, Russia, Singapore, Switzerland, Turkey, United Kingdom, and United States of America. The cyclical systemic risk in these countries is, therefore, directly monitored by the ESRB.