13 March 2025

EXPLANATION FOR THE COUNTERCYCLICAL CAPITAL BUFFER RATE FOR THE REPUBLIC OF SERBIA

Pursuant to Article 14, paragraph 1, item 11) of the Law on the National Bank of Serbia (RS Official Gazette, Nos 72/2003, 55/2004, 85/2005 – other law, 44/2010, 76/2012, 106/2012, 14/2015 and 40/2015 – CC decision and 44/2018) and Section 436 of the Decision on Capital Adequacy of Banks (RS Official Gazette, Nos 103/2016, 103/2018, 88/2019, 67/2020, 98/2020, 137/2020, 59/2021, 67/2022, 137/2022, 48/2023, 110/2023 and 102/2024, hereinafter: Decision on Capital Adequacy), the NBS Executive Board, at its meeting of 13 March 2025, decided to keep the countercyclical capital buffer (CCyB) rate for the Republic of Serbia at 0%, having in mind that the credit-to-GDP ratio is below its long-term trend. By keeping the CCyB at 0%, the NBS continues to support the lending market amid the still uncertain macroeconomic developments globally.

The CCyB is additional Common Equity Tier 1 capital that banks are required to maintain above the prescribed regulatory minimum in the amount equal to their risk-weighted assets multiplied by the specific countercyclical buffer rate. This instrument mitigates the cyclical dimension of systemic risk, creating an additional buffer of Common Equity Tier 1 capital during periods of pronounced credit growth, which can be released when systemic risks materialise.

The NBS sets the CCyB rate for the Republic of Serbia on a quarterly basis, taking into account the reference guide, applicable guidelines and recommendations of the European Systemic Risk Board and other variables it considers relevant for monitoring the cyclical dimension of systemic risk. In accordance with Section 436, paragraphs 2 and 3 of the Decision on Capital Adequacy, the guide for setting the CCyB rate is the deviation of the share of loans in GDP from long-term trend (credit-to-GDP gap). The CCyB rate for the Republic of Serbia is set in line with the recommendation for setting the CCyB rate of the European Systemic Risk Board (ESRB/2014/1).

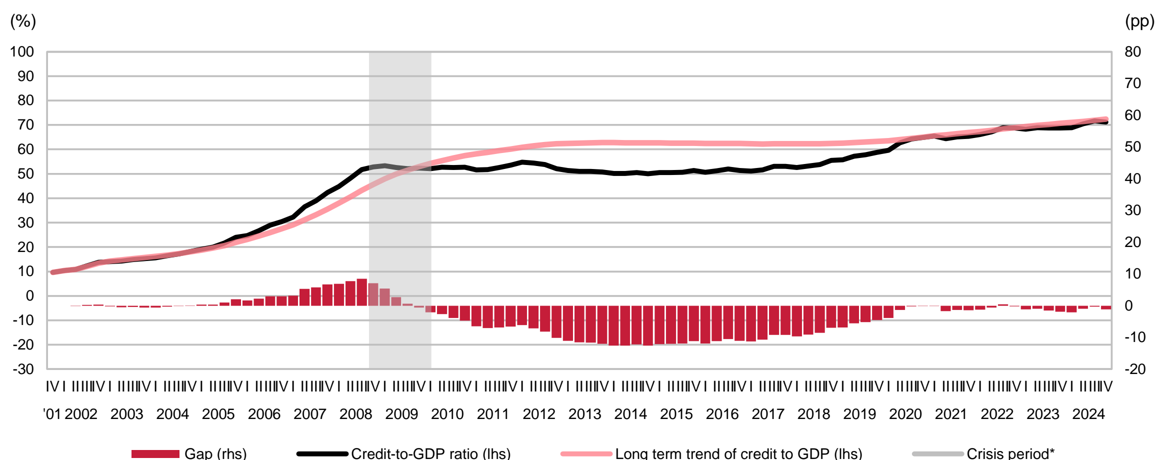
Chart 1 shows the share of credit to the non-government sector in GDP,[1] the long-term trend and the estimated credit-to-GDP gap. After a period of credit expansion between 2000 and 2008, in late 2009 the credit-to-GDP gap entered the negative territory. Lending growth in place since 2014 brought the share of credit in GDP close to its long-term trend. Since 2020, the share has oscillated around its long-term trend. According to December 2024 data, the

[1] https://www.stat.gov.rs/vesti/statisticalrelease/?p=16869&a=09&s=090202

credit-to-GDP ratio is slightly below its long-term trend, with a gap of -1.2 pp. The gap widened by 0.7 pp y-o-y and narrowed by 0.9 pp q-o-q. As the estimated gap value is below the threshold of 2 pp, which would potentially indicate excessive lending activity, the CCyB rate reference guide in Q4 2024 measured 0%.

In addition to the credit-to-GDP gap, other optional indicators were also taken into account when setting the CCyB rate for the Republic of Serbia, in accordance with Section 436, paragraph 4 of the Decision on Capital Adequacy. The optional indicators used relate to the real estate market, external imbalance and banking sector developments.

Chart 1 **Credit-to-GDP ratio and its long-run trend**



Source: NBS.
*Based on SSI.

Real estate market

The latest available data of the Republic Geodetic Authority and the Apartment Price Index (Chart 2) indicate that flat prices continued up in Q3 2024, but at a somewhat slower y-o-y pace than in prior periods. Flat prices increased by 4.7% per annum at end-Q3 2024 (preliminary data), and by 1.2% relative to the previous quarter.[2]

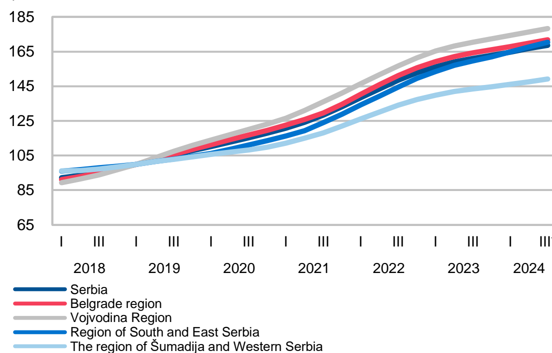
In Q4 2024, the total number of issued permits for new construction increased by 8.1% y-o-y.

The LtV ratio, measured by the ratio of mortgage-backed housing loans for which a flat was mortgaged and the estimated value of the flats, posted an

[2] Republic Geodetic Authority – Report on the Apartment Price Index for Q3 2024 (latest available data).

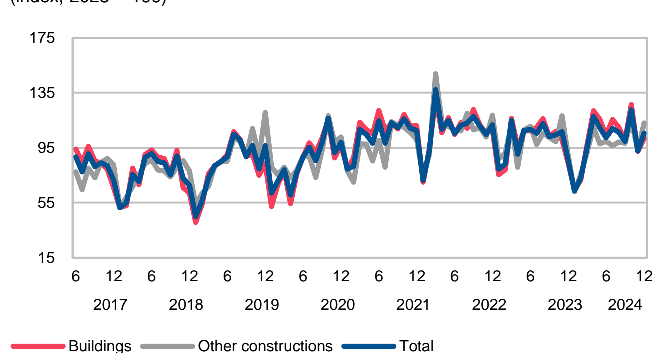
increase in Q4 2024 relative to a quarter earlier and measured 62.6% (61.9% in Q3 2024).[3]

Chart 2 **Apartment price index**
(Q1 2019 = 100)



* The latest data available (preliminary data)
Source: Republic Geodetic Authority

Chart 3 **Indices of the number of newly issued building permits**
(index, 2023 = 100)



Source: Statistical Office of the Republic of Serbia.

The January NBS bank lending survey shows that banks relaxed their credit standards for dinar long-term corporate loans in Q4 2024. Standards for dinar cash loans, refinancing loans and FX-indexed housing loans to households were eased further. On the other hand, standards for FX and dinar short-term corporate loans were tightened. The easing of household loan standards was driven by the lower costs of financing, thanks to monetary policy easing by the NBS and the ECB, the effects of competition and positive economic prospects, while the relaxation of corporate loan standards was propped up by lower funding costs for dinar loans and shorter loan approval procedures. According to banks, corporate demand for dinar and long-term FX/FX-indexed loans increased in Q4 2024. Demand growth was driven by the need to finance investments. Internal financing by companies, and loans of other banks and non-banking institutions, worked in the opposite direction. Household demand for dinar consumer, cash and refinancing loans went up, as did the demand for FX-indexed housing loans. According to banks, demand growth was driven by the need to refinance existing loans, procure durable consumer goods and purchase real estate, with higher wages providing a positive impulse. Banks expect tighter credit standards and lower demand in the corporate sector in Q1 2025, and a further easing of standards and higher loan demand in the household sector.[4]

Indicators of external imbalance

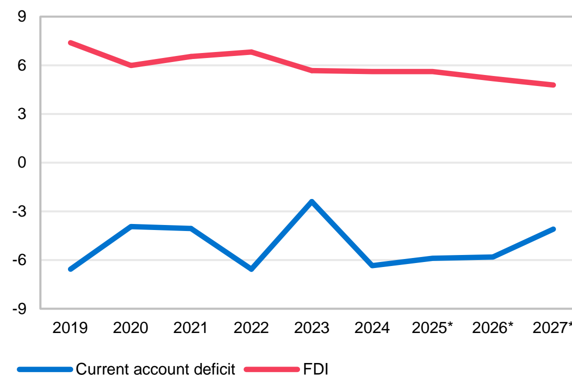
During 2024 the import and export of goods and services rose compared to the previous year. Amid the acceleration of the investment cycle and domestic demand growth, goods and services import picked up to 8.4% in 2024, displaying a more dynamic trend than that of the goods and services export,

[3] Source: NBS Real Estate Database
[4] Report on the Bank Lending Survey, Q4 2024.

which measured 4.8%. Against such backdrop, the current account deficit rose to 6.3% of GDP from its historical low of 2.4% of GDP last year. The current account deficit rose compared to the previous year due to the implementation of investments planned within the "Leap into the Future – Serbia Expo 2027" programme and growth in the disposable income of households, and partly to the low external demand. Even so, the current account deficit was fully covered by the FDI inflow.[5]

High FDI inflow to Serbia continued in 2024, when total FDI touched a record high EUR 5.2 bn or 6.4% of GDP (EUR 4.6 bn net), an increase of 14% from the previous highest level in 2023. Around four-fifths of the FDI inflow were in the form of equity capital and reinvested earnings, which confirms the determination of foreign investors to continue their prevalently long-term financial investments in Serbia. FDI remained diversified across geographies and projects, contributing to growth in productivity, employment, and competitiveness of the economy. By activity, the bulk of investments was chanelled to construction, mining, manufacturing, and professional, scientific, innovation and technical activities. In the years ahead, it is expected that FDI inflow will average around 5.5% of GDP, staying diversified across geographies and projects and directed chiefly to export-oriented sectors.[6]

Chart 4 **Current account deficit and FDI**
(in % of GDP)



* NBS projection, February 2025

Source: NBS.

Main banking sector indicators

The banking sector is well capitalised and highly liquid. At end-Q4 2024, the capital adequacy ratio at the banking sector level equalled 21.3%, well above the regulatory minimum.[7]

At end-Q4 2024, the loan-to-deposit ratio (LtD) measured 0.80. Keeping this indicator at levels below 1 means that banks largely rely on domestic, stable sources of funding, such as deposits.

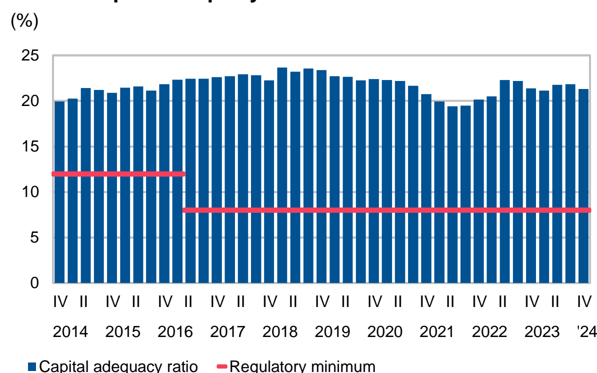
[5] Inflation Report, February 2025.

[6] Inflation Report, February 2025.

[7] Since 30 June 2017, the minimum CAR is 8% (minimum Tier 1 capital is 6% and minimum Common Equity Tier 1 capital is 4.5%). Also, in addition to meeting these conditions, a bank shall maintain its capital at all times at the level necessary for the coverage of all risks to which the bank is or may be exposed in its operation, i.e. at least in the amount necessary for maintaining the increased capital adequacy ratios – if the National Bank of Serbia, in accordance with Section 5 of this Decision, has set capital adequacy ratios for a bank higher than the prescribed ones.

Chart 5 **Capital adequacy ratio**

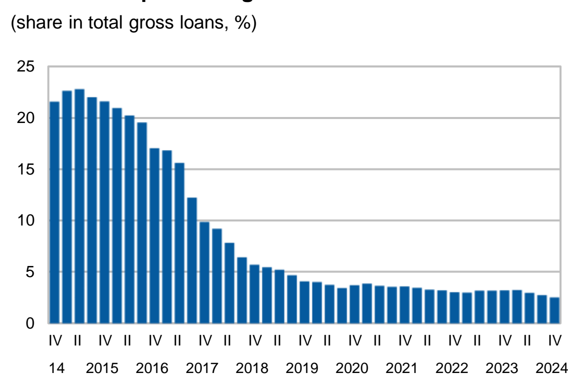
(%)



Source: NBS.

Chart 6 **Non-performing loans**

(share in total gross loans, %)



Source: NBS.

The share of NPLs in banking sector loans fell to a new record low in December 2024 (2.5%) despite the multidimensional crisis we have faced in the past five years. Since August 2015, when the NPL Resolution Strategy was adopted and which in turn produced a number of measures aimed at bringing NPLs down, the share of NPLs contracted by 19.7 pp. The share of NPLs in total loans was 0.2 pp lower at end-Q4 2024 than at end-Q3 the same year, while compared to end-2023 it decreased by 0.7 pp. The NPL ratio drop to a new record low indicates that the tightening of financial conditions in the prior period did not have any major adverse consequences on the quality of banks' assets.

Assessment of systemic risk of the Serbian financial system

The Systemic Stress Indicator (hereinafter: SSI) was developed with a view to identifying periods of elevated stress and the level of systemic risk in the financial system of the Republic of Serbia. The SSI covers a series of indicators which capture the level of financial stress in six key segments of the Serbian financial system: FX market, government securities market, money market, capital market, banking sector and the international environment.

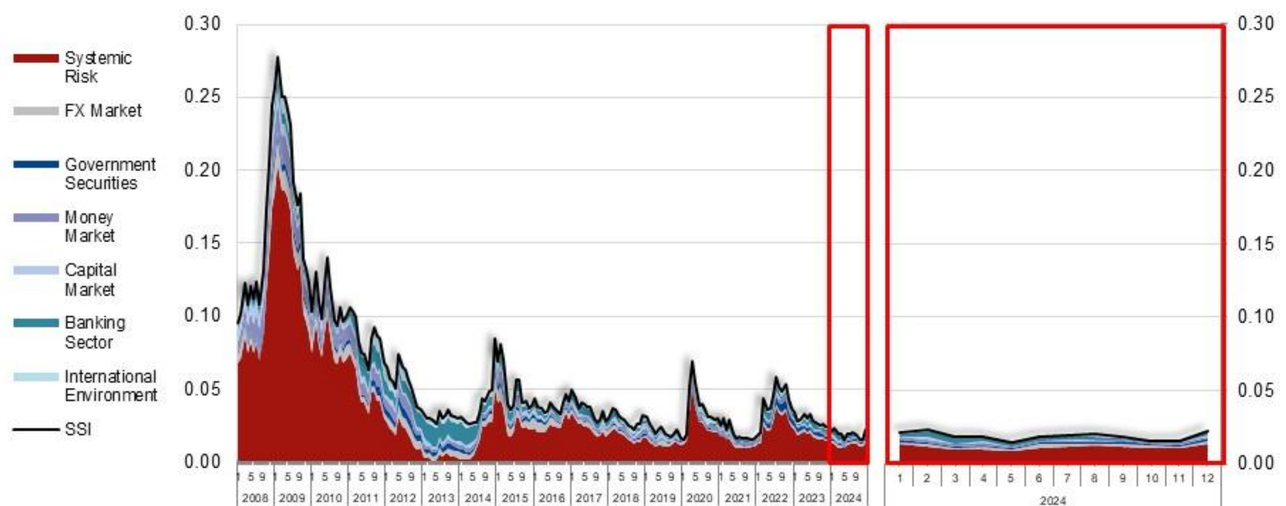
At end-Q4 2024, the SSI recorded a slightly higher value (0.022) relative to the quarter before, as well as a slightly lower value (0.024) relative to December 2023. The lower values of the SSI in Q4 2024 are largely attributable to movements in the international environment amid a decrease in the composite risk premium, as well as the fact that the global economy has turned out to be more resilient than initially forecast.

The NBS will continue to act cautiously and to make timely decisions to preserve and strengthen the achieved financial system stability. The strengthening of domestic macroeconomic fundamentals in the prior period and the continuous improvement of the regulatory framework for banks helped

to maintain a stable, well-capitalised and highly liquid banking sector in Serbia. The results of macroprudential solvency and liquidity stress tests carried out on data from September 2024 also confirm the stability of our banking system.

In early October 2024, Standard & Poor's increased Serbia's credit rating to BBB- whereby Serbia joined the ranks of investment grade countries for the first time in its history. The decision reflects Serbia's favourable macroeconomic prospects and improved resilience to external shocks thanks to responsible economic policy pursuit, which is expected to continue in the years ahead, as well as expectations that risks to financial stability in Serbia will remain low, supported by a well-capitalised, profitable and liquid banking system.

Chart 7. **Systemic stress indicator dynamics and contribution of the most important factors to the Systemic stress indicator**



Source: NBS.

At the end of January 2025, Fitch Ratings maintained the positive outlook for investment grade, keeping the credit rating at BB+. The decision on maintaining Serbia's positive outlook was underpinned by a sound policy mix, including a record of prudent fiscal management, robust economic growth outlook, strenghtened FX reserves and stronger GDP per capita compared to the peer group medians.