BPK

BANKING AND PAYMENTS AUTHORITY OF KOSOVO
AUTORITETI BANKAR DHE I PAGESAVE TË KOSOVËS
BANKARSKI I PLATNI AUTORITET KOSOVA

BPK BULLETIN

(Structure of Financial Sector)

Research and Statistics Department

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ABBREVIATIONS:

ATM	Automated Teller Machine;
BOP	Balance of Payments;
BR	Branch;
CRK	Credit Registry of Kosovo;
BPK	Banking and Payments Authority of Kosovo;
GDP	Gross Domestic Product;
HQ	Headquarter;
HHI	Herfindahl-Hirschman Index;
IMF	International Monetary Fund;
IT	Information Technology;
ITRS	International Transactions Reporting System;
KCIS	Kosovo Credit Information System;
MU	Mobile Unit;
NIM	Net Interest Margin;
POS	Point of Sales;
RWA	Risk Weighted Assets;
ROAA	Return on Average Assets;
ROAE	Return on Average Equity;
SB	Sub-branch;
UNMIK	United Nations Mission in Kosovo.

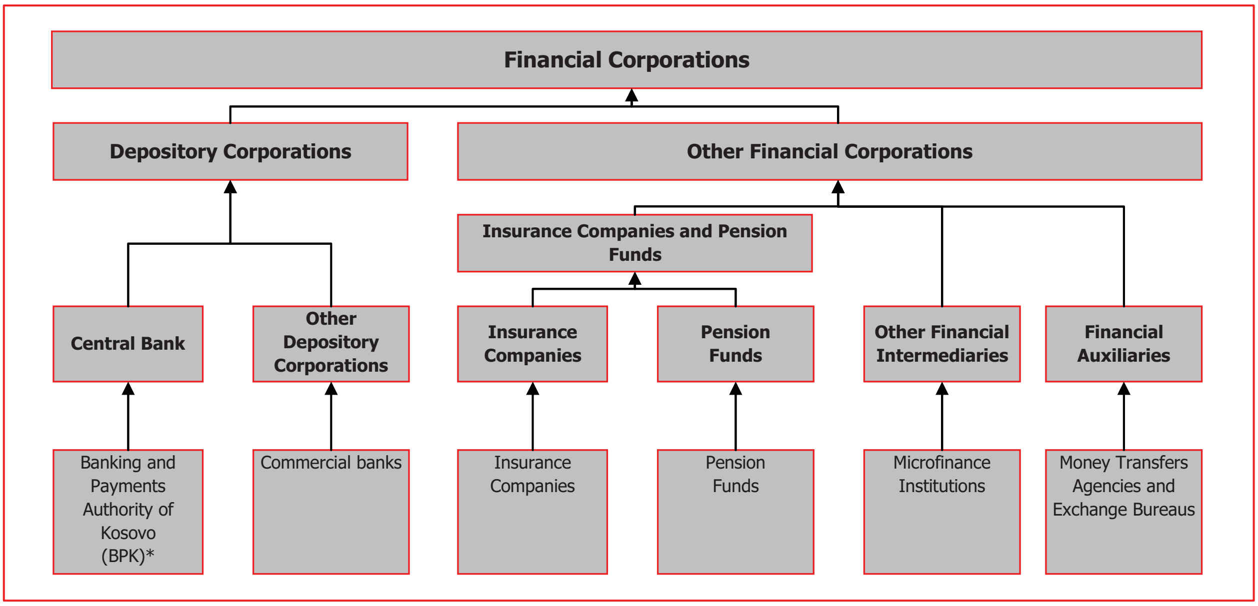
Contents

1. INTRODUCTION

One of the responsibilities of the Banking and Payments Authority of Kosovo (BPK) is to present to the public the information on the evolving financial and other sectors situation. As a result, the BPK publishes the second issue of its Bulletin, which covers not only the main developments in the commercial banking sector, but also a number of developments related to the insurance companies, the pension funds and other financial intermediaries operating in Kosovo. Furthermore, additional attention has been paid to the ongoing projects (Credit register, Kos-Giro Payments and ITRS) developed by the BPK that facilitate better functioning of the financial sector in terms of increasing the intermediary role of financial institutions, improving the performance of the payments system and improving balance of payments statistics.

Financial sector in Kosovo (excluding BPK) is dominated by commercial banks, which compose around 87% of total financial sector assets. The share of insurance companies, pension funds and other financial intermediaries in total assets of financial corporations is around 5%, 1%, and 7%, respectively. From the semi-annual perspective, the assets of the financial sector grew 8.1%. In particular, banking sector assets grew 7.3%, insurance companies 8.7%, pension funds 31.8% and other financial intermediaries 25.4%. The following scheme shows the structure of the financial sector in Kosovo, which is expressed using the terminology provided by the IMF Manual on Monetary and Financial Statistics.

Scheme 1. The structure of financial corporations in Kosovo*



[*] The BPK performs some of the functions of the central bank.

The financial corporations sector consists of all resident corporations or quasi-corporations principally engaged in financial intermediation or in auxiliary financial activities, which are closely related to financial intermediation. They can be split into sub-sectors according to their specific activities. Financial Corporations (FC) comprise Depository Corporations (DC) and Other Financial Corporations (OFC).

Other Depository Corporations (ODC) consists of all resident financial corporations, except the central bank (BPK), whose principal activity is financial intermediation and which have liabilities in the form of deposits or financial instruments that are close substitutes for deposits. In Kosovo this is represented through actually seven licensed commercial banks.

Other Financial Corporations (OFC) comprise Insurance Companies, Pension Funds, Other Financial Intermediaries (Microfinance Institutions) and Financial Auxiliaries (money transfer agencies and exchange bureaus). Insurance companies (IC) consist of incorporated, mutual and other entities whose principal function is to provide life, accident, sickness, fire or other forms of insurance to individual institutional units or groups of units. Currently, there are 8 insurance companies licensed in Kosovo.

In the category of Pension Funds (PF) are included those institutions, which are constituted in such a way that they are separate institutional units from the units which create them. They are established for purposes of providing benefits on retirement for specific groups of employees. They have their own assets and liabilities and they engage in financial transactions in the market on their own account.

Other financial intermediaries (OFI) consist of all resident corporations engaged in financial intermediation except depository corporations, insurance corporations and pension funds. Financial corporations included in this breakdown are those which raise funds on financial markets, but not in the form of deposits, and use them to acquire other kinds of financial assets. These include those engaged in financing investment or capital formation; for example, investment corporations, corporations engaged in financial leasing, corporations engaged in the provision of personal finance or consumer credit. These financial institutions in Kosovo are engaged in lending to small-scale business and individuals, mainly in rural areas and the funding is provided mainly by donors.

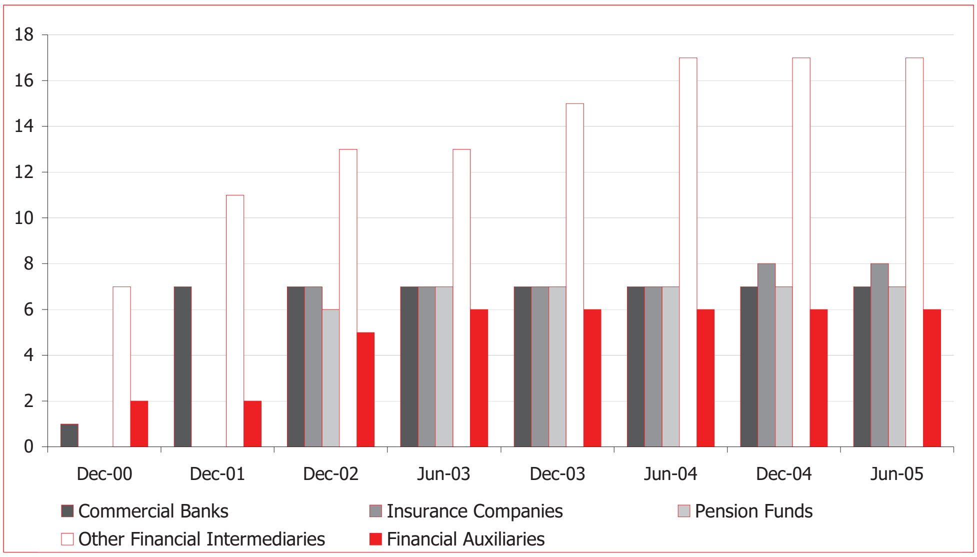
2. FINANCIAL SECTOR IN KOSOVO

2.1. General Characteristics of the Financial Sector

Financial sector in Kosovo is bank based. The share of commercial banks assets to total financial sector assets at the end of June 2005 was around 87%, which is almost the same composition on a year-on-year basis. At the end of June 2005, the assets of the financial sector amounted at EUR 947 million, a 27.4% increase compare to the same period of year 2004. Financial sector loans (mainly commercial banks lending) correspond to a 47.5% growth on a year-on-year basis, while deposits grew at 24.6%, showing the reason behind the decline in the financial sector net foreign assets.

The financial sector in Kosovo, as of end-June 2005 consisted of 45 financial corporations (excluding BPK). Regarding the structure of financial corporations, number of commercial banks remained the same (7), since 2001. However, commercial banks have increased their network of branches. At the end of June 2005, there were 214 banking units, of which 58 were branches (relative to 49 in June 2004), 146 sub-branches (relative to 121 in June 2004), and 3 mobile units.

Figure 1. Number of individual financial corporations (excluding BPK)

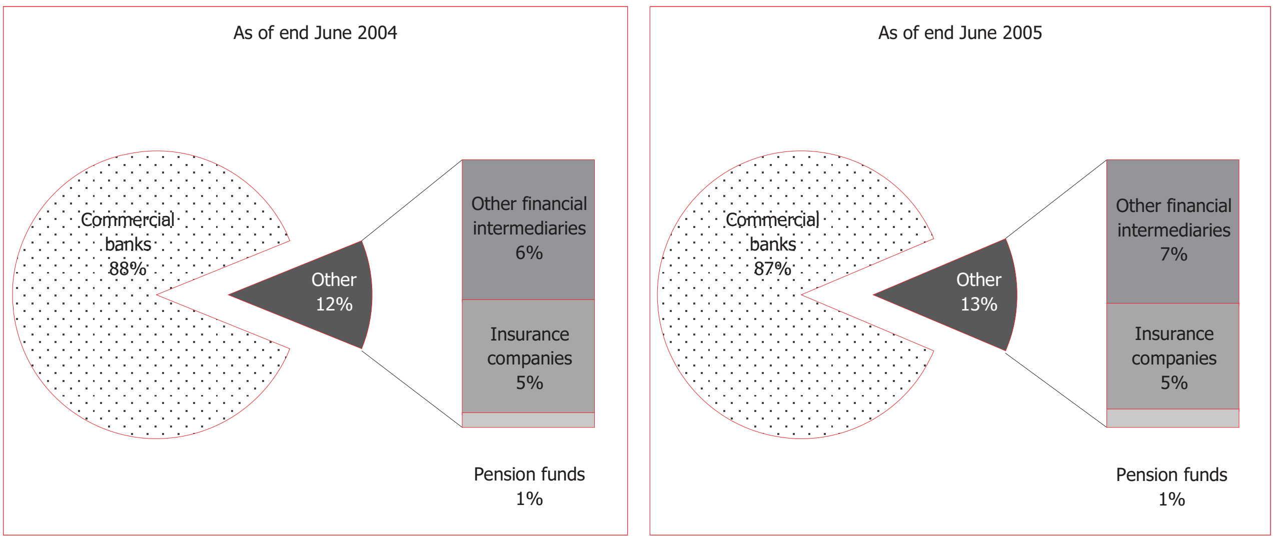


Regarding Other Financial Corporations, during the period December 2002 – June 2004, there were 7 insurance companies. During the second half of year 2003, a domestic insurance company was bought by a foreign insurance company. Two licenses of insurance companies (branches of foreign insurance companies) were revoked by the end of year 2004 and beginning of 2005. In the meantime, BPK has licensed three new insurance companies, two of which during the second half of 2004, and one in the beginning of 2005. As of June 2005, there were 8 insurance companies operating in Kosovo. Concerning pension funds, it comprises 7 corporations, excluding mandatory scheme - KPST. The share of the pension funds assets to the total assets of the financial sector, at end June 2005, was 1% (same as in June 2004). All pension fund assets (EUR 7.2 million out of EUR 7.6 million) are held with depository corporations, mainly with BPK, and dominated by transferable deposits.

Other Financial Intermediaries started to operate since 2000, initially counting 7 corporations. The OFIs number increased by 17 corporations, at the end of June 2004, and remained the same at the end of June 2005. The OFIs are lending to the real sector, mainly based on the funds received from donations. Since June 2003 there are 6 corporations representing financial auxiliaries.

Financial sector total assets (consolidated figure), as of June 2005, reached its peak amounting at EUR 946.9 million. Financial sector assets, compared to the end 2004, increased by 8.1% against the increase by 18.0% experienced in December 2004 relative to June 2004. Most important contributor in the pace of financial sector assets (June 2005 – December 2004) are commercial banks contributing by 5.9% (against 16.4% in period December 2005 – June 2004), while other financial corporations contributed by 2.2% (against 1.6% in period December 2005 – June 2004). On a year-on-year basis, financial sector assets increased by 27.4%, mainly driven by the contribution of commercial banks at 23.3%.

Figure 2. The structure of the financial sector in Kosovo



As shown in figure 2, the share of commercial banks assets to total assets of the financial sector reached 87.2%, as of June 2005, which is slightly lower compare to June 2004 (87.8%). Compare to the end of June 2004, the share of other financial corporations assets to total assets of financial sector increased from 12% to 13%, at the end of June 2005. This slight increase arises mainly due to the increase of the share of the assets of other financial intermediaries in the total assets of the financial sector (from 6% to 7%), whereas the share of the assets of insurance companies as well as pension funds, at the end of June 2005, remained the same with that at the end of June 2004. In terms of total assets of other financial corporations, other financial intermediaries represents the main category with assets amounted at EUR 66.3 million (June 2005), a 25.4% increase compare to the end of June 2004.

Total assets of insurance companies at the end of June 2005 amounted at EUR 47.6 million, a 8.7% increase compare to the end of year 2004, respectively a 24.3% increase compare to the end of June 2004. As regards to the pension funds assets (supplementary schemes), as of June 2005, these assets amounted at EUR 7.6 million, compare to EUR 5.8 million (December 2004), respectivelly EUR 4.3 million (June 2004).

Non-capital links between commercial banks and other financial corporations suggest that commercial bank liabilities to these corporations at end of June 2005 counted for 3.5% of bank liabilities, showing increase from 2.9% in December 2004 and 1.9% in June 2004. While from other financial corporations' perspective in June 2005, their share of assets at commercial banks reached 24.4%. This ratio shows increase comparing it in year-on-year perspective (+22.5%) and relative to the end of 2004 (+14.0%).

Regarding the financial sector (including BPK) position versus other sectors of the economy (external, fiscal and real sector), financial corporations' net foreign assets, at the end of June 2005, amounted at EUR 638.5 million, a 7.8% decrease on a year-on-year basis. Compare to the end of 2004, this represents a marginal decrease (-0.1%) giving a sign that sharp decline was recorded in period June-December 2004 (decrease by -7.7%). The main component of net foreign assets are claims on nonresidents amounted at EUR 701.1 million at end of June 2005, against EUR 720.3 million in June 2004. At the end of June 2005, 86.1% of total claims on nonresidents were represented by deposits and securities, whereas at the end of June 2004, this stood for 86.6%. Since mid of 2004, commercial banks and BPK started to shift their portfolio abroad from deposits (decreasing from 70.6% of total claims on nonresidents in June 2004, to 48.9% in June 2005) into investments in securities other than shares (increasing from 16.1% of total claims on nonresidents in June 2004, to 37.2% in June 2005).

The financial corporations' claims to the domestic sector continued to record impressive growth amounting at EUR 278.5 million (June 2005), compare to the EUR 26.1 million (June 2004). This sizeable growth is attributed to the decreased liabilities to the fiscal sector and increased claims to the real sector. At the end of June 2005, the deposits of fiscal sector within financial sector (mainly at the BPK) amounted at EUR 246.1 million, a 25.7% decrease compare to the same period of 2004. As regards to the claims (lending) to the real sector, on annual basis, there is a considerable growth amounted at EUR 516.2 million, or 47.5%.

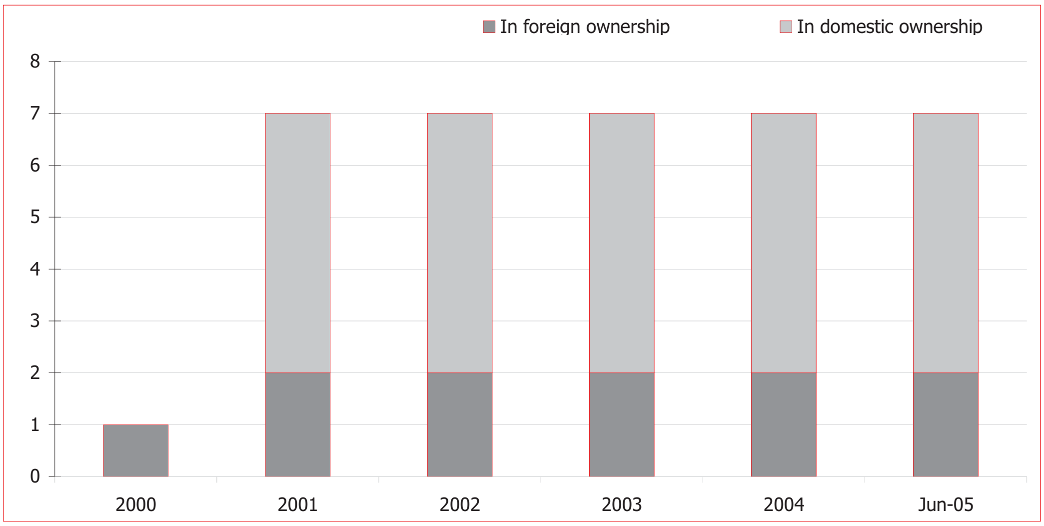
The total deposits at financial sector amounted at EUR 720.1 million, a 24.6% increase on year on year basis, whereas compare to the end of 2004, this increase reached at 6.6%. This increase is attributed to the increased other deposits (time and savings), with a contribution of 22.8%. The share of other deposits to total deposits increased by 8.6 percentage points, covering 57.5% of total deposits at financial sector as of end June 2005 (48.9%, June 2004). The growth of other deposits by 46.7% is mainly due to the contribution of household sector (by 24.6%) and non-financial corporations (by 13.0%). Transferable deposits showed a moderate pace of growth 3.5%, while their share to total deposits decreased by 8.7 percentage points, representing 42.5% of total deposits at the end of June 2005. Household sector recorded increase of its share to total transferable deposits from 43.4% (June 2004) to 52.0% (June 2005).

3. COMMERCIAL BANKS

3.1. The Structure of Commercial Banking Sector

The banking sector remains the largest component of Kosovo's financial sector. As of June 2005, compared with the end of 2004, Kosovo banking sector has not experienced any changes with respect to the number of banks. In total, seven commercial banks continue to operate. However, banks have expanded their operating network, showing increase in number of banking units and growth in their total assets.

Figure 3. Number of banks



To facilitate the analysis of the banking sector, banks have also been classified into two groups and are commented in the boxes of different chapters. The breakdown of banks into groups was based on the ownership structure (box 1) which also captures the size effect (foreign-owned banks being largest in size as well). Thus, as of end June 2005, Group I consisted of two banks with full foreign ownership whereas Group II consisted of five banks with majority domestic ownership (although there are some minority foreign shareholders in this group). The ownership structure of the commercial banking sector in Kosovo has not undergone any changes since 2001.

Box 1. Composition of bank groups

Group I	Group II
ProCredit Bank (PCB)	New Bank of Kosovo (BRK)
Raiffeisen Bank of Kosovo (RBKO)	Bank for Private Business (BPB)
	Economic Bank (BE)
	Kasabank (KSB)
	Credit Bank of Pristina (BKP)

Table 1 shows classification of banks in terms of their asset size. In 2001 there was only one bank with assets exceeding EUR 100 million. However, with the increase in banking sector activity the number of banks with assets above EUR 100 million increased to 3 at end of June 2005, of which two are banks with foreign ownership, and one belonging to domestic ownership.

Table 1. Commercial bank assets, by size

Assets	Number of Banks				
	2001	2002	2003	2004	Jun-05
Over 100 EUR million	1	1	1	2	3
Over 60 - up to 100 EUR million	0	0	2	1	0
Up to 60 EUR million	6	6	4	4	4

With respect to their size of assets, as of June 2005 Group I banks managed 64.8% of total commercial banking sector assets, which is an increase by 2.5 percentage points, compared with end 2004.

Table 2. Commercial bank assets, by ownership, in EUR million, unless otherwise indicated

Gr.	Banks	2000	Share in %	2001	Share in %	2002	Share in %	2003	Share in %	2004	Share in %	Jun-05	Share in %
I	In foreign ownership	102,964	100.0	385,315	74.2	344,380	73.1	370,869	63.8	494,539	62.0	552,234	64.6
II	In domestic ownership	-	0.0	133,670	25.8	126,813	26.9	210,614	36.2	302,528	38.0	302,885	35.4
	Banking sector total	102,964	100	518,985	100	471,193	100	581,483	100	797,067	100	855,119	100

3.1.1. Geographical Distribution of Banking Units

As of end June 2005, there were 214 banking units (branches, sub-branches and mobile units) operating in Kosovo. Banks have expanded their operating network with 7 new operating units (compare to the end of 2004), respectively 35 new operating units (compare to the end of June 2004). As presented in the table 3, sub-branches continuously show expansion totaling 146, at end of June 2005.

Table 3. Commercial banks operating network, by region

Description		Dec-02	Jun-03	Dec-03	Jun-04	Dec-04	Jun-05
Prishtina							
	HQ	7	7	7	7	7	7
	BR	2	1	3	5	7	12
	SB	17	28	31	42	47	47
	MU	0	0	0	1	1	1
Prizreni							
	BR	8	7	7	8	8	8
	SB	8	16	16	22	26	26
	MU	0	0	0	0	0	0
Peja							
	BR	13	13	14	14	14	14
	SB	11	12	13	14	21	22
	MU	0	0	0	0	0	0
Gjilani							
	BR	14	13	13	14	14	14
	SB	18	22	23	26	30	31
	MU	1	0	1	1	2	2
Mitrovica							
	BR	5	5	6	8	10	10
	SB	7	10	14	17	20	20
	MU	1	0	0	0	0	0
Total							
	HQ	**7**	**7**	**7**	**7**	**7**	**7**
	BR	**42**	**39**	**43**	**49**	**53**	**58**
	SB	**61**	**88**	**97**	**121**	**144**	**146**
	MU	**2**	**0**	**1**	**2**	**3**	**3**

With respect to their regional distribution of banking units, as of June 2005 their largest concentration was in Pristina region covering 31.3% of total banking units in Kosovo. The second largest concentration was the region of Gjilan accounting for 22.0% of banking units operating in Kosovo; whereas three remaining regions cover mutually comparable shares, Peja (16.8%), Prizren (15.9%), and Mitrovica (14.0%).[1]

As of end June 2005, the largest semi-annual growth was recorded for by the number of banking units in Pristina region which grew with 5 banking units against end 2004 (or increase by 12 units compared with the same period of 2004). Peja region recorded the increase of 1 banking unit compared with end 2004 (or increase by 8 units compared with June 2004). In Gjilan region the number of banking units grew with 1 new unit compared with end 2004 (or increase by 6 units against the same period of 2004). In Mitrovica and Prizren there was no change in the number of banking units compared with end 2004, and they show an increase compared with June 2004 by 5 and 4 new banking units, respectively.

The increase in the banking units was accompanied by the increase in the number of ATMs by commercial banks in Kosovo. ATMs were first introduced by banks with foreign ownership at end 2002 enabling their clients to use the banking services throughout 24 hours. However, since 2004 onwards, banks with domestic ownership introduced the ATMs too, increasing the number of ATMs to 52 in total (which is 9 ATMs higher

[1] The analysis is based in five main regions of Kosovo which are: Pristina, Peja, Prizren, Mitrovica and Gjilan. The municipalities throughout Kosovo comprise particular region (e.g. Ferizaj is included in the Gjilan region).

compared with end 2004). Similar to the banking units, ATMs are also concentrated in Pristina region, which by the end June 2005 accounted for 44.2% of all ATMs. 15.3% of total ATMs are accounted for by Prizren region whereas, Peja, Gjilan and Mitrovica region account for around 13.5% of total ATMs in Kosovo.

Apart from ATMs and other products such as credit and debit cards (Visa, Master Card, and Maestro Card), commercial banks in Kosovo introduced POS terminals in different stores throughout Kosovo, which in turn might have contributed to the decrease in cash transactions. The installation of POS was initiated by banks with foreign ownership, which account for 100% of total POS terminals throughout Kosovo. By the end June 2005, number of POS terminals throughout Kosovo reached 215, with 80.5% being concentrated in Pristina region. 7.0% of total POS terminals are located in Peja region whereas Prizren and Gjilan region have mutually comparable shares accounting for 6.5% and 6.0%, respectively.

3.1.2. Employment

As of June 2005 the banking sector network expansion was accompanied with the increase in employment. The number of employees in the commercial banking sector reached 2.225, which is the increase by 159 employees compared with end 2004, and increase by 423 employees compared with June 2004.

Labor productivity indicator (table 4), expressed by the number of employees per banking unit, shows no change in June 2005 compared with end 2004. The number of employees per banking unit remained at 10. Total banking sector assets managed by an employee show a slight decrease from EUR 385,430.00 at end 2004 to EUR 384,323.00 in June 2005. On the other hand, loans managed by an employee increased with 15.8% in June 2005 amounting at EUR 209,550.00, pointing to the increase in the lending productivity (compared with end 2004, which amounted at EUR 181,015.00). This increase is due to the increase in the lending activity of commercial banks. On the deposit side, the volume of deposits managed by an employee increased with 0.6% compared with end 2004, and as of June 2005 they reached EUR 333,579.00.

With respect to the assets managed by a banking unit, the indicator shows a slight increase to 3,996 thousand EUR in June 2005 against a decrease by 2.7% in 2004 compared with 2003, which points to a slight improvement in the productivity in the banking sector in Kosovo with respect to this indicator. The reason behind this development of this productivity indicator is the faster growth of assets of the banking sector relative to the growth of the number of banking units.

The increase in productivity was marked in the lending activity. The ratio of loans per banking unit increased with 20.5% in June 2005 compared with end 2004 amounting to 2,179 thousand EUR. On the other hand, deposits managed by a banking unit increased slightly in June 2005 compared with end 2004 and reached EUR 3,468,283.00, which corresponds to the increase by 4.7%.

Table 4. Commercial banks selected indicators

Description	2001	2002	2003	2004	Jun-05
No. of banking units					
No. of employees	637	1,393	1,676	2,068	2,225
No. of employees per banking unit	23	13	11	10	10
Total Assets					
Per banking unit, in EUR thousand	18,535	4,284	3,956	3,851	3,996
Per employee, in EUR thousand	815	338	347	385	384
Number of citizens per banking unit	66,679	17,264	13,136	9,488	9,341
Number of citizens per employee	2,931	1,363	1,152	950	898
Loans					
Per employee, in EUR thousand	41	62	139	181	210
Per banking unit, in EUR thousand	926	786	1,583	1,808	2,179
Deposits					
Per employee, in EUR thousand	773	307	307	332	334
Per banking unit, in EUR thousand	17,581	3,884	3,497	3,313	3,468

The "bankarisation" indicator, which measures the number of inhabitants served by a banking unit, experienced a decrease by 1.5% in June 2005 compared with end 2004. Number of inhabitants served by a banking unit reached 9,341 from 9,488 in 2004. Compared with 2003, the number of inhabitants served by a banking unit fell by 28.9 (or 3,795 inhabitants) whereas compared with 2002 it decreased by 45.9% (or 7,923 inhabitants) which in turn shows the improvement in banking services provided in Kosovo. The indicator measuring the number of citizens per employee reveals similar picture. As of June 2005, the number of inhabitants per employee decreased with 5.4% compared with end 2004 reaching 898 inhabitants per employee. The number of inhabitants per employee in June 2005 fell by 22.1% (or 254 inhabitants) compared with 2003 and by 34.1% (or 465 inhabitants) compared with 2002.

Number of accounts in commercial banks at end of June 2005 reached 594.487. The ratio of number of accounts to number of inhabitants living in Kosovo is around 0.3 meaning that around 30% of the Kosovo population has accounts in commercial banks. Share of household current accounts in total accounts has decreased and in June 2005 stood at 81.8% from 89.1% in 2002. However, there was an increase in the number of household current accounts from 145 thousand in 2002 to 489 thousand in June 2005. As regards to other categories, current accounts of corporations or legal entities represented increase from 12.484 accounts at end 2002 to 44.492 accounts at end of June 2005. Regarding the saving accounts, they increased from 5.197 accounts at end of 2002 to 60.915 accounts at end of June 2005.

Box 2. Productivity indicators by bank groups

Group I banks outperform banks of Group II in productivity indicators per employee in terms of total assets, deposits and loans per employee. In terms of loans per employee, Group I showed an increase by 21.0%, while group II represented smoothed increase by 8.2%.

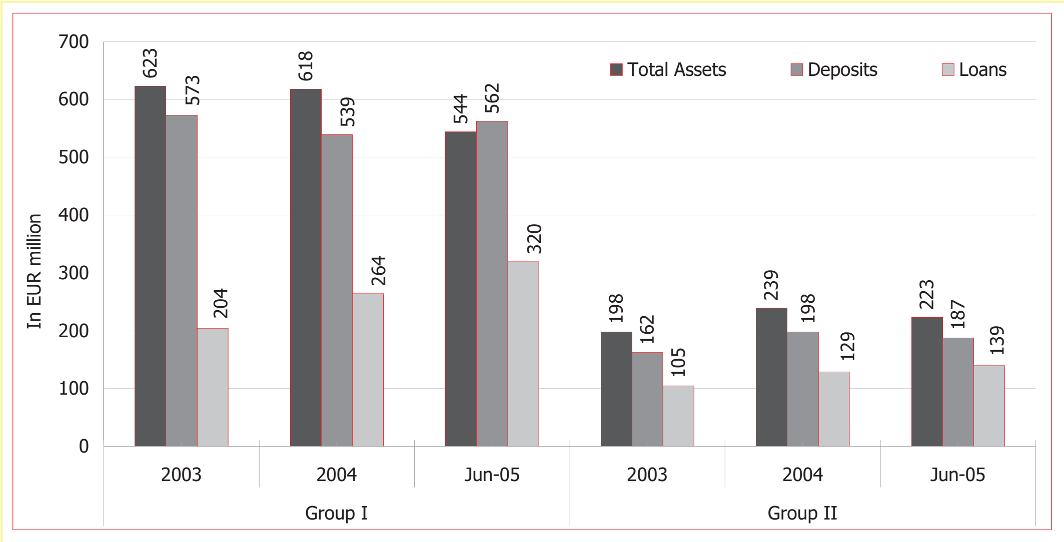
Productivity indicators per employee of banks in June 2005 (with respect to assets, loans and deposits) and change in percentage against end 2004 (in parentheses):

Group I	
Assets	543,912 EUR (-12.0%)
Loans	319,543 EUR (+21.0%)
Deposits	562,001 EUR (+4.3%)
Group II	
Assets	223,201 EUR (-6.5%)
Loans	139,194 EUR (+8.2%)
Deposits	187,469 EUR (-5.3%)

Group I banks experienced an increase in both loans and deposits per employee, while for Group II this is so only for loans per employee. The Group II banks total loans and deposits managed per employee represented 43.6% (which is -5.2 percentage points compared to the level in 2004) and 33.4% (-3.4 percentage points compared to the level in 2004), respectively of the level reached by Group I. Regarding the assets managed by employee, the relative position of Group II diminished with 2.4 percentage points compared to 2004, reaching 41.0% of the level attained by Group I.

From the figure 4 can be seen that, compared to end 2004, loans per employee increased for both bank groups. Group I banks show an increase in deposit per employee figure, pointing to the increase in deposit taking and lending activity. The shift in the composition of the balance sheet in favor of lending to the domestic economy is the main explanation why total assets per employee of group I banks has decreased to EUR 544.000 million from EUR 623.000 and EUR 618.000 million at end 2003 and 2004. !!!???

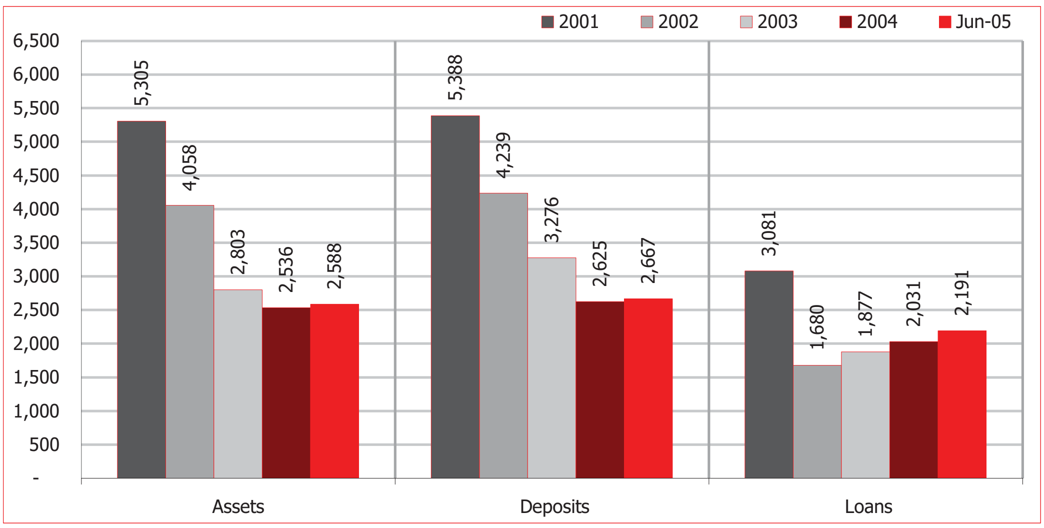
Figure 4. Commercial bank productivity indicators



3.1.3. Concentration in the Banking Activity

Competition in the commercial banking sector in Kosovo is shown by using the Herfindahl-Hirschman Index (HHI) that measures the concentration in the commercial banking sector.[2] As indicated in the figure 5, in June 2005 the increase in the HHI and hence the decrease in competition was recorded for the assets of the banking sector, deposits and lending activity.

Figure 5. Commercial banks Herfindahl-Hirschman Index



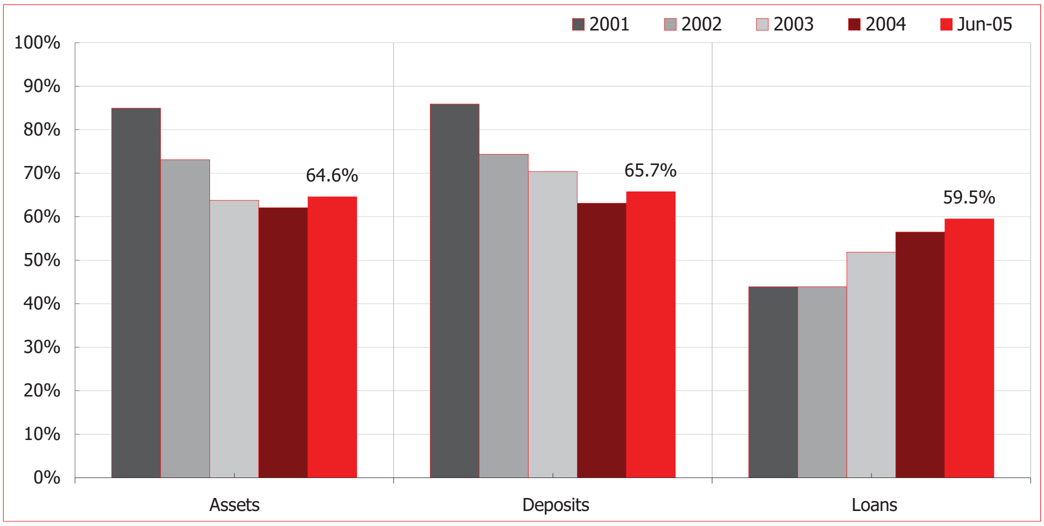
[2] See notes on methodology for the calculation of this indicator

The HHI for the concentration of assets in the banking sector experienced a slight increase in June 2005 reaching 2,588 points from 2,536 points in 2004, following the decrease from 2,803 in 2003. Similarly, the HHI index for the concentration in deposit-taking experienced an increase in June 2005 to 2,667 from 2,625 points at end 2004, following the decrease from 3,276 in 2003.

The increase in concentration index and hence the decrease in competition was recorded for the lending activity. The HHI in the lending activity, after increase to 1,877 points (end 2003), it experienced another increase by 160 points (June 2005) compared with end 2004 reaching 2,191 points. HHI on lending activity, after a drop in 2002, experienced a continuous increase (by on average 170 points) reaching 2,191 as of June 2005.

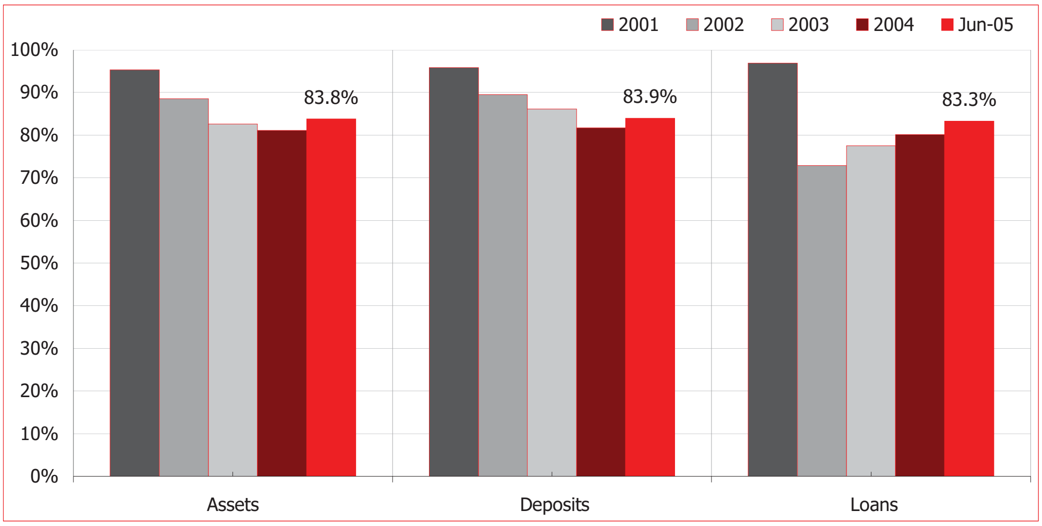
Although, until 2004 the concentration for assets and deposit-taking was falling and hence the competition increasing relative to loans, in June 2005 the movements of the three types of measures of concentration have shown similar trend, pointing to the fall in competition.

Figure 6. The share of two largest banks in total banking sector assets, loans, and deposits (C2)



The competitiveness in the banking sector is also measured as the concentration of the two largest banks (C2) and the four largest banks (C4). Figure 6 presents the changes in the share of the two largest banks assets, deposits and loans in total banking sector assets, deposits and loans. As depicted in the figure, the market share of the two largest banks fell gradually until end 2004 (in terms of their assets and deposits), whereas their market share in lending activity increased gradually. Particularly, in June 2005, the market share of two largest banks in terms of assets increased by 2.5 percentage points compared with end 2004 and reached 64.6%. The share of two largest banks deposits in total banking sector deposits decreased from 70.4% in 2003, over 63.1% in 2004, to 65.7% in June 2005. The market share of the two largest banks in total banking sector loans reached 59.5% from 56.4% in 2004 and 51.8% in 2003.

Figure 7. The share of four largest banks in total banking sector assets, loans, and deposits (C4)



Similar tendencies were shown for the market share of four largest banks (C4). The concentration C4 for the assets first decreased from 82.6% in 2003 to 81.1% in 2004 and then increased again in June 2005 to 83.8%. Similarly, the concentration C4 for the deposits fell from 86.1% in 2003 to 81.7% in 2004, whereas it increased to 83.9% in June 2005. As regards to the lending activity, there is a different pace relative to the deposits and assets. Namely, excluding the year 2001 which represented period of establishing of the new commercial banks, since 2002 there is continuous increase of C4 to total loans of the commercial banks, when at end of June 2005 the share accounted for 83.3% (from 77.5% in 2003).

In general, these concentration indicators, being a crude measure of competition, show that there was a decrease in competition within the banking sector for the period until June 2005 in terms of both assets and deposits. On the other hand, the concentration on lending activity is following the increasing trend following the previous years, although the level of the indicator is lower relative to the indicator for assets and deposits.

3.2. The Structure of Balance Sheet of Commercial Banks in Kosovo

3.2.1. Structure of Assets

Total banking sector assets by the end of June 2005 amounted to EUR 855.1 million, which is EUR 58.1 million higher compared with end 2004. With respect to their share to GDP[3] (end 2004), assets increased from 31.8% of GDP at end 2004 to 34.1% of GDP in June 2005.

[3] IMF staff estimates of GDP (AIDE MEMOIRE, July 2005).

Total assets of the banking sector in June 2005 grew for 8.2% compared with end 2004. The largest contribution to the growth of assets in June 2005 was recorded for by loans (11.4%) followed by cash and balances with BPK (1.2%) while other items recorded smaller contribution. By the end of June 2005, bank balances with other commercial banks generated negative contribution to the growth of assets with 5.5%.

Table 5 shows the developments of the structure and changes in the share of each category of assets. As indicated, liquid assets (cash, balances with BPK, balances with banks abroad and investments in foreign securities) of the banking sector represented 43.5% of total assets amounting at EUR 382.9 million as of end June 2005. Cash and balances with BPK grew with 8.6% in June 2005 compared with end 2004, amounting at EUR 126.3 million and made up 14.4% of total banking sector assets.

Table 5. Commercial banks balance sheet – assets, in EUR thousand, unless otherwise indicated

Description	Dec. 2003		Jun. 2004			Dec. 2004			Jun. 2005		
	Amount	Share in %	Amount	Share in %	Change	Amount	Share in %	Change	Amount	Share in %	Change
Cash and balances with BPK	106,180	18.0	102,371	15.1	-3.6	116,293	14.3	13.6	126,282	14.4	8.6
Cash	46,611	7.9	52,862	7.8	13.4	43,293	5.3	-18.1	50,545	5.7	16.8
Balances with BPK	59,569	10.1	49,509	7.3	-16.9	73,000	9.0	47.4	75,736	8.6	3.7
Balances with commercial banks	106,205	18.0	113,365	16.8	6.7	185,849	22.9	63.9	144,958	16.5	-22.0
Securities	119,620	20.3	115,713	17.1	-3.3	111,778	13.8	-3.4	111,721	12.7	-0.1
Gross loans and lease financing	232,773	39.5	313,684	46.4	34.8	373,668	46.0	19.1	466,249	53.0	24.8
Provisions on loans and lease financing	7,715	1.3	11,710	1.7	51.8	15,947	2.0	36.2	24,378	2.8	52.9
Net loans and lease financing	225,058	38.2	301,974	44.6	34.2	358,392	44.1	18.7	441,871	50.2	23.3
Fixed assets	12,265	2.1	12,650	1.9	3.1	15,056	1.9	19.0	16,753	1.9	11.3
Other assets	12,155	2.1	18,913	2.8	55.6	10,255	1.3	-45.8	13,533	1.5	32.0
Total assets	589,198	100	676,697	100.0	14.9	812,899	100.0	38.0	879,497	100.0	8.2

Amounting at EUR 466.2 million in June 2005, loans made up the largest share (53.0%) of total assets increasing with 7.0 percentage points compared with end 2004. Although, in June 2005 loans grew for 24.8% compared with end 2004 and 48.6% compared with the same period of 2004, the semi-annual growth experienced a slight slowdown compared with their growth in the same period of 2004 when they grew with 34.8%.

Commercial banks decreased their investments in foreign securities and deposits in commercial banks abroad for 13.7% compared with end 2004 amounting to EUR 256.7 million. Following a considerable decrease in their outstanding amounts, in June 2005, their share in balance sheet total also decreased by 7.4 percentage points compared with end 2004, reaching 29.2% of total assets. This decrease was mainly due to the decrease in balances with other banks (-22.0%), which represented 56.5% of total investments abroad as of June 2005 (16.5% of total assets).

Box 3. Main categories of assets by banking groups

Share of Group I in total banking sector in June 2005 and change in percentage points against end 2004:

54.5% of cash and balances with BPK (+ 6.3 percentage points)

77.9% of placements and investments in securities (+ 3.7 percentage points)

59.5% of loans (+ 3.0 percentage points)

The share of cash and balances with BPK within Group I was 12.5% of total assets at end June 2005, which corresponds to the increase by 1.2 percentage points compared with end 2004. Within Group II, the corresponding share was 19.0%, a decrease by 0.9 percentage points compared with end 2004. The share of placements and investments in securities within Group I decreased in June 2005, compared with end 2004, by 8.4 percentage points and accounted for 36.2% of total assets. Similarly, the corresponding share within Group II assets, relative to the assets mentioned for group I, in June 2005 decreased to 18.7% of total assets, from 25.4% in 2004.

Within Group I, the share of loans as part of their total assets increased from 56.4% in 2004 to 59.5% in June 2005. Loans granted by Group II as a share of their total assets was reduced and accounted for 40.5% in June 2005 from 43.6% at end 2004.

3.2.1.1. Loans Granted by Commercial Banks

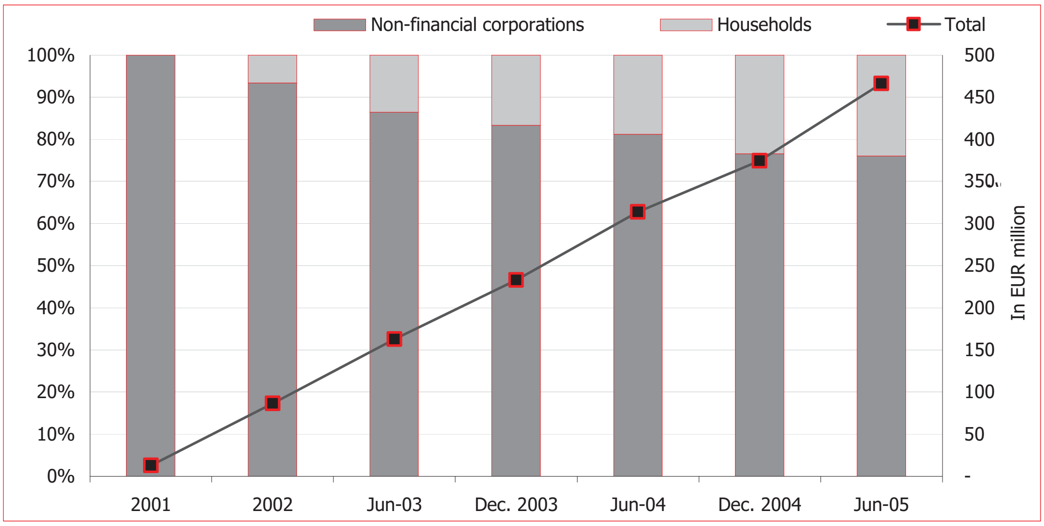
The role of banks in providing intermediation to the domestic economy is continuously increasing. Total banking sector loans grew with 24.6% in June 2005 compared with end 2004, with non-financial corporations being the main beneficiary, although loans granted to households grew faster relative to the loans to non-financial corporations. Trading sector remains the largest beneficiary whereas commercial banks in Kosovo are continuing to direct their lending activity towards longer-term loans, with loans over two years representing 34.2% of total loans in June 2005.

The volume of total gross loans granted by banks in June 2005 reached at EUR 466.2 million, a 24.6% increase compare to the end of 2004. The amount of net loans reached at EUR 441.9 million at end June 2005 that corresponds to the semi-annual increase by 23.3% compared with end 2004. Slower increase in net loans is manly as a result of the higher growth of provisioning for loan losses, which in June 2005 compared with end 2004, grew with 52.9%. The share of loans to GDP[4] increased from 14.9% in 2004 and reached 18.6% in June 2005. The share of loans to domestic economy increased by 7.6 percentage points compared with end 2004 making up 54.5% of total assets by the end June 2005.

[4] IMF staff estimates of GDP (AIDE MEMOIRE, July 2005).

Outstanding amount of loans granted to the non-financial corporations increased from EUR 286.6 million in 2004 to EUR 354.5 million in June 2005 (an increase by 23.7%). Their share in total loans decreased slightly from 76.5% of total loans in 2004 to 76.0% in June 2005. Compared with June 2004, their share decreased with 5.1 percentage points. The reason behind this decrease in the share of loans to non-financial corporations is the growing rate of loans granted to households, which in June 2005 grew for 27.3% compared with end 2004. The outstanding volume of loans granted to households amounted at EUR 111.7 million as of end June 2005, which is EUR 23.9 million higher compared with end 2004. The share of loans granted to households to total loans was 23.9% in June 2005, an increase by 0.5 percentage points compared with end 2004.

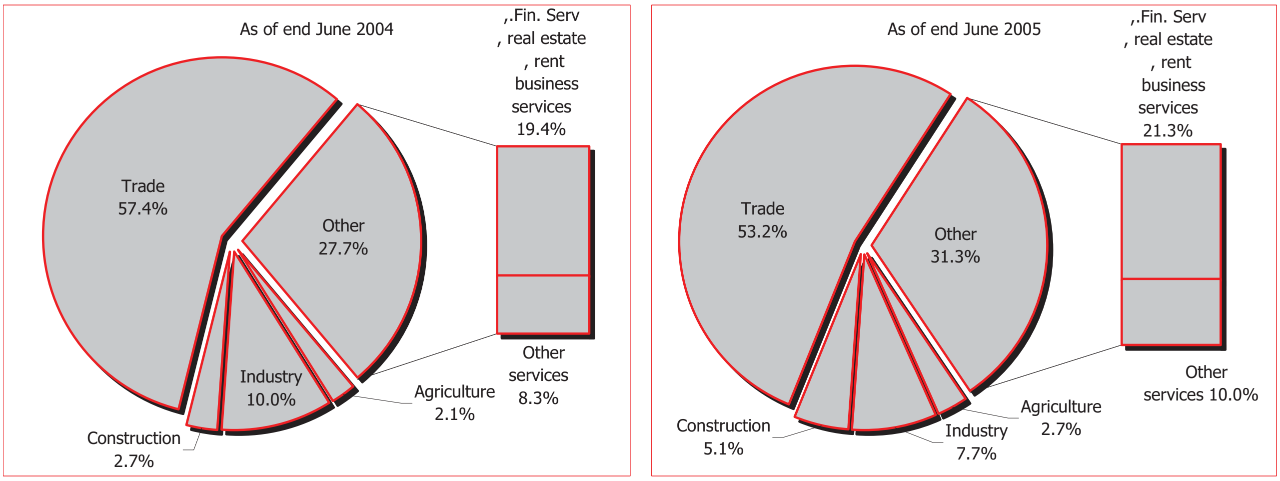
Figure 8. Structure of loans by sector



With respect to the industry structure of loans, trading sector continues to retain its dominant position in total loans (see figure 9). The outstanding amount of loans granted to the trading activity in June 2005 reached EUR 223.9 million corresponding to the increase by 19.0% compared with end 2004, whereas at end 2004 compared with June 2004 they grew with 12.2%. The share of loans granted to trade declined slightly from 54.9% of total loans in 2004 to 53.2% in June 2005.

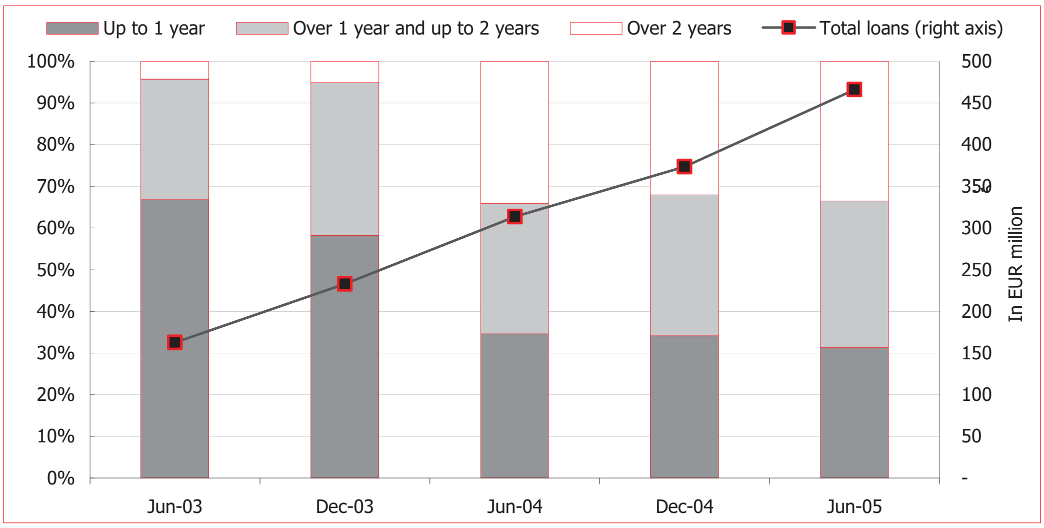
Meanwhile, loans to construction activities increased their share in total loans by 1.7 percentage points reaching 5.1% in June 2005. Significant share of loans is directed towards financial services, real estate, rent, and business services (EUR 89.4 million in June 2005), which increased from 20.1% in 2004 to 21.3% of total loans in June 2005. The share of loans channeled to the industry, mainly manufacturing of textile, food, and related items stood at EUR 32.5 million, showing a decline by 2.2 percentage points and representing 7.7% of total loans in June 2005. Agriculture with outstanding amount of EUR 11.3 million reached the share of 2.7% of total loans.

Figure 9. Structure of loans by industry



The maturity structure of loans shows some changes during the first half of 2005. As illustrated in figure 10, loans with longer-term maturities are gradually increasing their share to total loans. As of June 2005, loans with maturities of up to one year attained EUR 146.0 million, a 14.6% increase compare to its level in 2004. However, their share to total loans is decreasing continuously from 34.6% in June 2004, 34.1% at end 2004 to 31.3% in June 2005. The corresponding share for loans with maturities of over one year and up to two years increased by 1.3 percentage points and in June 2005 reached 35.2% of total loans. The outstanding amount of loans with maturities of over one year and up to two years by the end of June 2005 amounted at EUR 163.9 million, which is EUR 37.4 million higher compare to the level obtained in end 2004. The amount of loans with maturities of over two years attained at EUR 156.3 million, a 30.5% increase on a semi-annual basis (compared with end 2004). Their share in total loans reached 33.5% in June 2005 from 32.1% at end 2004.

Figure 10. Structure of loans by maturity



Box 4. Loans granted by bank groups

Accounting for the largest share in total banking sector assets, Group I banks managed 59.5% of total banking sector loans at end June 2005, which corresponds to the increase by 3.1 percentage points compared with end 2004. Their share in total banking sector loans to non-financial corporations was 57.6%, while their share in total loans granted to households reached 65.3% of total loans.

Group I banks oriented their lending activity towards non-financial corporations accounting for 73.7% of total Group I loans in June 2005. Within Group II loans, loans to non-financial corporations represented 79.5% of total loans, showing that Group II was more active in lending to non-financial corporations relative to Group I.

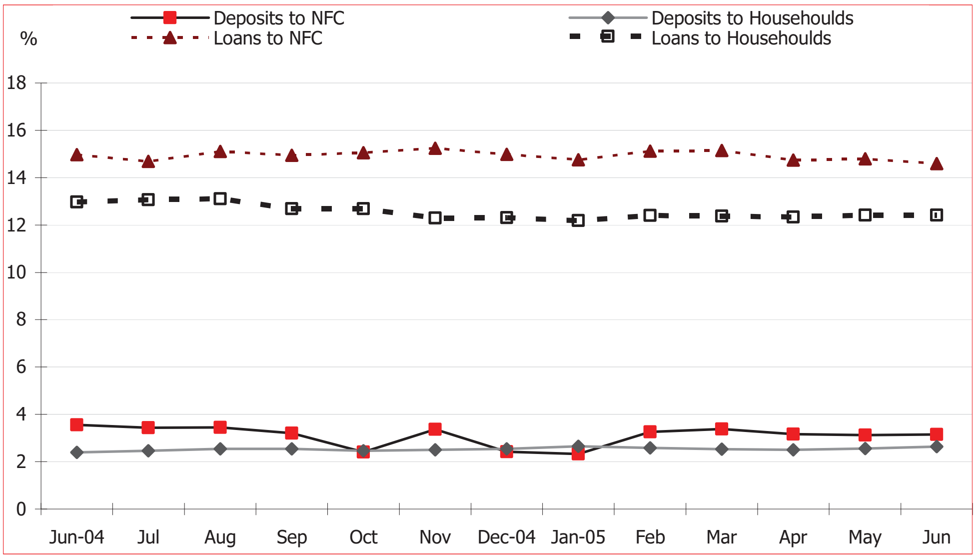
In June 2005, Group I banks attained 36.5% of total banking sector loans with maturities of up to one year. Their share in total banking sector loans with maturities from one year up to two years was 52.1%, while their share in total loans with maturities of over two years in June 2005 reached 88.7%.

Group I banks relative to Group II banks were more active in granting loans with longer-term maturities, given that loans over two years represent 50.0% of Group I total loans. The corresponding share in Group II was 9.3% in June 2005. Loans over one year and up to two years within Group I loans compose 30.8% of total Group I loans while loans with the same maturity represent 41.6% of total Group II loans. Group II banks relative to Group I were more active in shorter term lending with loans up to one year representing 49.1% of Group II loans; whereas the corresponding share in Group I was 19.2%.

Since June 2004 onwards, BPK has started collecting statistical data on effective interest rates on loans and deposits. Interest rates on both, loans and deposits, have not seen significant changes since then. In particular, as of June 2005, average interest rates on deposits ranged from 2.63% to 3.16% depending on the breakdown by sector (household and non-financial corporation).

Average interest rates on loans ranged between 12.41% and 14.59%, with interest rates on loans granted to households being lower compared with the interest rates on loans to non-financial corporations. As shown in the figure 11, the lending/deposit spread is lower for households relative to the spread for non-financial corporations.

Figure 11. Effective interest rates on loans and deposits and their spread



3.2.2. Structure of Liabilities

The bulk of banking sector liabilities comprise of deposits. Within their structure, deposits as well have undergone substantial changes overtime, with transferable deposits reducing gradually their share in total deposits. Remaining still modest, banks are continuing to borrow from other banks and financial institutions. Commercial banks in Kosovo have also experienced a slight decrease on their own funds, which by the end of June 2005 accounted for 7.6% of balance sheet total.

In June 2005, the total amount of deposits attained at EUR 742.2 million which represents a semi-annual (relative to end of 2004) increase of 6.8%, representing a decelerating increase (at end 2004 relative to the June 2004 the increase was 20.3%). Their share to balance sheet total decreased as well, which in June 2005 was 84.4% against 85.5% in 2004.

Representing with a mere 2.1% of balance sheet total, deposits from other banks amounted at EUR 18.7 million as of end June 2005, a 30.9% increase against end 2004 (see table 6). Although they increased continuously, their share in balance sheet total still remains negligible.

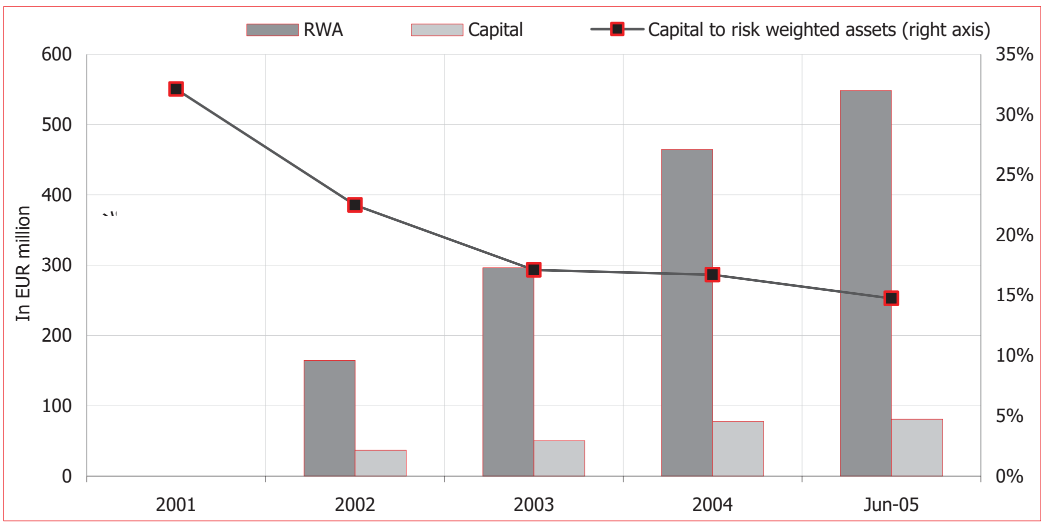
Table 6. Commercial banks balance sheet – liabilities, in EUR million, unless otherwise indicated

Description	Dec-03		Jun-04			Dec-04			Jun-05		
	Amount	Share in %	Amount	Share in %	change	Amount	Share in %	change	Amount	Share in %	change
Balances from other banks	1,751	0.3	11,866	1.8	577.7	14,275	1.8	20.3	18,684	2.1	30.9
Debts to clients	522,938	88.8	583,303	86.2	11.5	696,138	85.6	19.3	749,771	85.2	7.7
Deposits	514,045	87.2	577,519	85.3	12.3	694,739	85.5	20.3	742,213	84.4	6.8
Transferable deposits	314,654	53.4	283,531	41.9	-9.9	278,698	34.3	(1.7)	306,387	34.8	9.9
In EUR	298,416	50.6	273,469	40.4	-8.4	264,895	32.6	(3.1)	291,408	33.1	10.0
In non-EUR	.	0.0	10,062	1.5		13,802	1.7	37.2	14,979	1.7	8.5
Other deposits	199,391	33.8	293,988	43.4	47.4	416,041	51.2	41.5	435,826	49.6	4.8
In EUR	199,391	33.8	283,110	41.8	42.0	406,449	50.0	43.6	424,122	48.2	4.3
In non-EUR	.	0.0	10,878	1.6		9,592	1.2	(11.8)	11,704	1.3	22.0
Other borrowings	8,893	1.5	5,785	0.9	-35.0	1,399	0.2	(75.8)	7,558	0.9	440.2
Other liabilities	17,457	3.0	22,135	3.3	26.8	25,019	3.1	13.0	36,804	4.2	47.1
Subordinated debt	2,045	0.3	2,045	0.3	0.0	9,318	1.1	355.6	7,045	0.8	(24.4)
Own resources	45,007	7.6	57,348	8.5	27.4	68,148	8.4	18.8	67,193	7.6	(1.4)
Total	589,198	100	676,698	100	14.9	812,898	100	20.1	879,497	100	8.2

Other borrowings grew with 440.2% (from a low base) against end 2004 and amounted at EUR 7.6 million, at end June 2005. Meanwhile, their share to balance sheet total reached 0.9% in June 2005 from 0.2% in 2004. Commercial banks' own resources (comprising of share capital, reserves, and profit/loss) amounted at EUR 67.2 EUR million, in June 2005, whereas as of end 2004 it stood at EUR 68.1 million.

Kosovo's banking sector capitalization remained satisfactorily by the end of June 2005. In particular, in June 2005, average capital adequacy of the total banking sector attained 14.7%, representing a decrease by 2.0 percentage points compared with 2004. As it is illustrated in figure 12, capital adequacy experienced a moderate decrease from 2003 to 2004 and followed with the stronger fall at end June 2005.

Figure 12. Capital to risk weighted assets



The decrease in the first half of 2005 was caused by a marked increase in the risk-weighted assets which in June 2005, compared with end 2004, grew with 18.1% while capital increased with 4.0% (see figure 12). This is mainly due to the increase in the lending activity of banks in domestic economy characterized with a greater risk.

Box 5. Main categories of liabilities by bank groups

Share of Group I in total banking sector in June 2005 and change in percentage points against end 2004.

54.9% of total deposits (-8.4 percentage points)
54.2% of own resources (+5.2 percentage points)

Total customer deposits, which represent the largest part of the total deposits, within the Group I balance sheet total, represented 85.2% in June 2005 against 88.7% in 2004. The corresponding share within the Group II was 84.6% in June 2005 from 84.1% in 2004.

Within Group I balance sheet total, the share of own resources experienced an increase by 2.4 percentage points attaining 9.2% at end June 2005. The corresponding share in Group II balance sheet total have not changed compared with 2004 and remained at 11.5%.

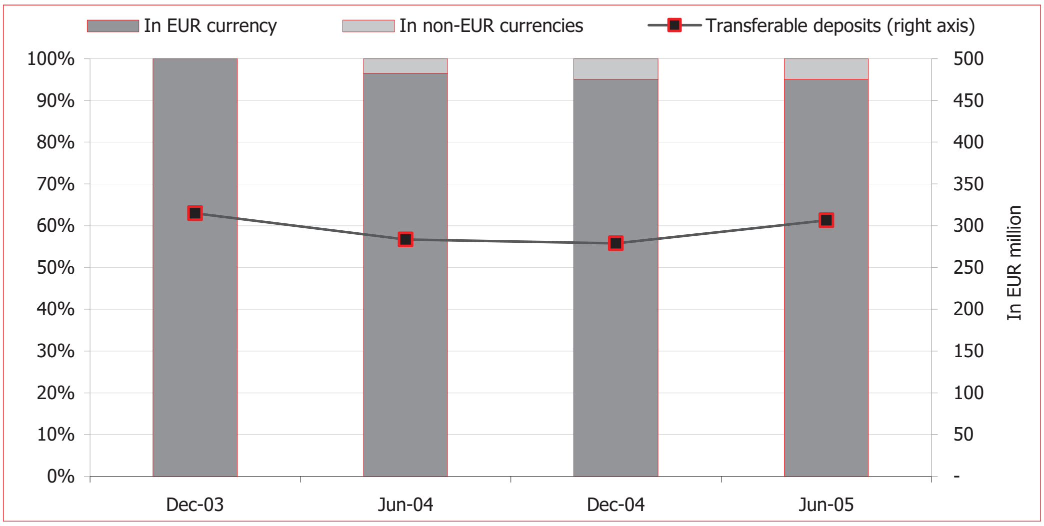
3.2.2.1. Deposit Structure of Commercial Banks

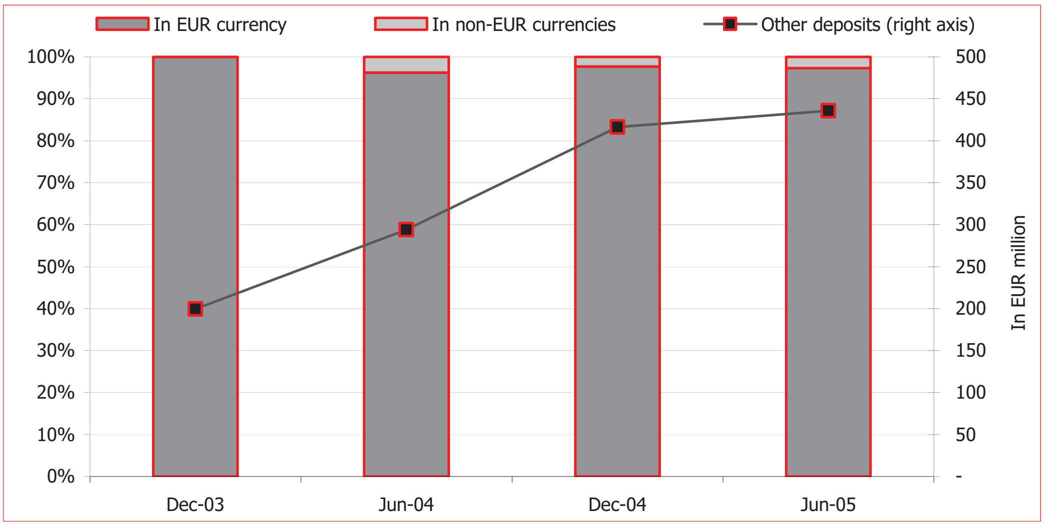
Deposits at the banking sector in Kosovo are continuing to increase. In addition, the structure in favor of longer-term maturities has improved in the period under review. This may confirm that the confidence in the banking system remains satisfactory. Households continue to dominate the composition of deposits. Provided the increase of loans in domestic economy, the intermediary role of banks is improving in general. Regarding the currency structure, non-euro deposits continue to remain negligible.

As of end June 2005, total amount of deposits in the banking sector amounted at EUR 742.2 million, a 6.8% increase against end 2004 while the share of deposits to GDP experienced a further increase from 27.7% (2004) to 29.6% (June 2005).

With respect to the maturity structure of deposits, other deposits (time and savings) continued to increase their share in total deposits in June 2005 reaching 58.7%. This is 6.0 percentage points higher from the level attained in end 2004 and in June 2005 amounted to 435.8 EUR million. The semi-annual growth of other deposits was 4.8% against 49.5% in 2004. This may suggest that further increase in deposits may be achieved at slower growth rates or its peak may be expected in the near future.

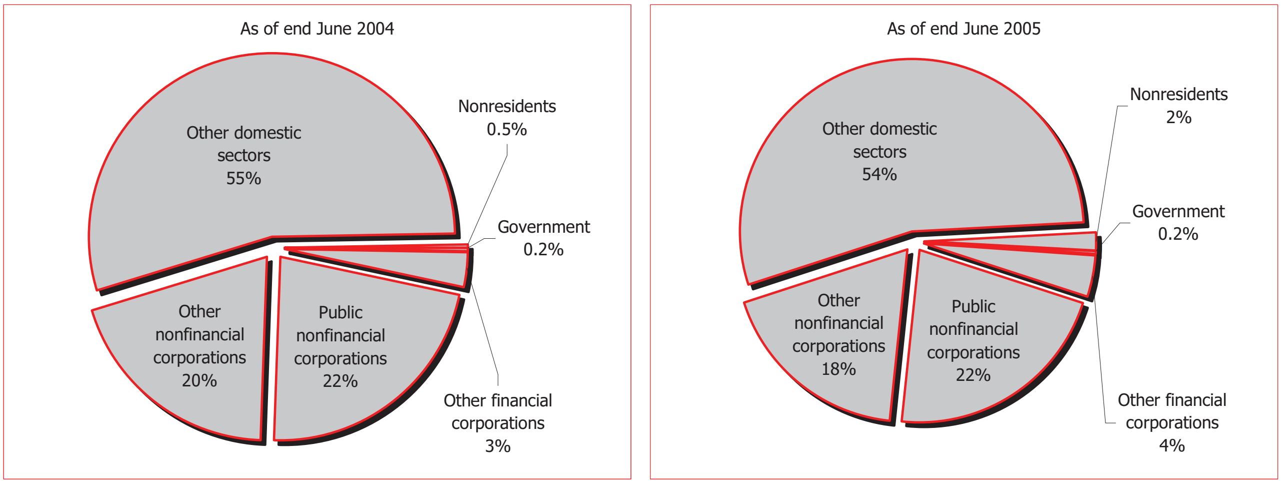
Figure 13. Structure of deposits by maturity and currency





Total amount of transferable deposits in the banking sector attained EUR 306.4 million, a semi-annual increase of 9.9% in June 2005 against 2004 when they decreased with 1.7%. By the end June 2005 they accounted for 41.3% of total deposits. Deposits in euro mainly compose the currency structure of deposits. In June 2005 euro-deposits accounted for 96.4% of total deposits, 0.2 percentage points lower from their level in 2004.

Figure 14 Structure of deposits by sector



Regarding the structure of deposits by sector, households retain the largest share of 56.2% of total deposits. Household deposits attained at EUR 417.4 million by the end June 2005, a 10.4% increase against end 2004. The second largest share is accounted for by the public non-financial corporations (EUR 166.3 million in June 2005 or +9.3% compared with end 2004) accounting 22.4% of total deposits as of June 2005 (0.6 percentage points higher than in 2004). Other non-financial corporations comprising private and socially owned enterprises (the later representing negligible share) amounted at EUR 112.2 million in June 2005 (or -12.1% against end 2004) corresponding to around 18.0% of total deposits. Deposits of other financial corporations (EUR 32.9 million in June 2005 or +23.0% compared with end 2004) recorded a slight increase from 3.8% in 2004 to 4.4% of total deposits in June 2005.

Box 6. Deposit structure by bank groups

Share of Group I in total banking sector in June 2005 and change in percentage points (in parentheses) against end 2004:

67.4% of transferable deposits (+1.4 percentage points)
64.4% of other deposits (+3.3 percentage points)
70.6% of deposits held by households (+0.3 percentage points)
39.3% of deposits held by other non-financial corporations (+2.8 percentage points)
74.2% of deposits held by public non-financial corporations (+6.5 percentage points)
65.9% of total deposits in EUR currency (+2.4 percentage points)
59.9% of total deposits in non-EUR currency (+7.5 percentage points)

<u>By nature of deposits</u>

Within total deposits of Group I, transferable deposits accounted for 42.3%. Compared with end 2004 they experienced an increase by 0.2 percentage points while compared with June 2004 their share declined by 9.8 percentage points. The share of transferable deposits with Group II in total Group II deposits experienced an increase by 2.0 percentage points from the level obtained in 2004 and in June 2005 they accounted for 39.0% of total Group II deposits.

Group I banks, relative to Group II, were less active in attracting deposits with longer maturities given that in June 2005 their share within Group I deposits was 57.7% while the corresponding share within Group II deposits was 61.0%.

Group I banks, relative to Group II, are also less active in attracting deposits in non- EUR currency, which in June 2005 accounted for 3.3% of total deposits while for Group II they accounted for 4.2%. However, the largest share of total deposits in non-EUR currency is concentrated in Group I.

By nature of client

In June 2005, deposits of other domestic sectors (mainly households) comprise 60.2% of total deposits of Group I. The corresponding share in Group II was 47.9%, an increase by 4.3 percentage points compared with 2004. Deposits of public non-financial corporations, being the second largest depositors, accounted for 25.2% of total Group I deposits while their share in Group II in June 2005 fell to 16.7% from 19.0% in 2004. Deposits of other non-financial corporations represented 9.0% of total deposits of Group I (-1.6 percentage points compared with end 2004) while this share in Group II was 26.6% (-4.8 percentage points compared with end 2004). Deposits of other financial corporations accounted for 2.3% of Group I deposits while the corresponding share in Group II reached 8.4% in June 2005 from 5.9% in 2004.

3.3. Financial Performance of Commercial Banks

As of June 2005, commercial banks have experienced a slight deterioration regarding their financial performance indicators. Commercial banks have experienced a slight decline in their profit in June 2005 compared with June 2004, and as a result, their return indicators attained lower values, with ROAA and ROAE declining by 0.9 percentage points and 14.2 percentage points, respectively compared with end 2004. [5]

[5] The values on profit are annualized figures for 2005.

3.3.1. Structure of Income and Expenditures

After tax profit of the total banking sector reached at EUR 3.1 million, in June 2005, which is EUR 2.5 million lower from the value attained in the same period of 2004 (decrease by around 45%). Before tax profit of the banking sector reached EUR 4.6 million which corresponds to 30.8% decrease compared with the same period of 2004. This decrease was mainly on account of the slower increase of income relative to the expenditure increase.

Table 7 presents each component of the total banking sector structure of income and their annual percentage change. As the table illustrates, net interest income[6] in June 2005 attained EUR 26.4 million, an increase by 31.7% against June 2004. On the other hand, net non-interest income experienced a decrease by 136.9% in June 2005 against the same period of 2004, and as a result amounted at EUR -1.5 EUR million.

General and administrative expenses amounted at EUR 20.5 million by the end of June 2005, and compared with June 2004 they grew with 34.8%. Since June 2004, general and administrative expenses generated positive contribution with 20.1% to the growth of total expenses and as a result by June 2005 they represented 52.0% of total expenditures.

Net income from other banking activities such as net gain/losses from dealing securities, net gain/losses from dealing in foreign exchange and, net gain/losses from foreign currency revaluation, by June 2005 grew with 39.6% against June 2004, and amounted at EUR 237,400.00

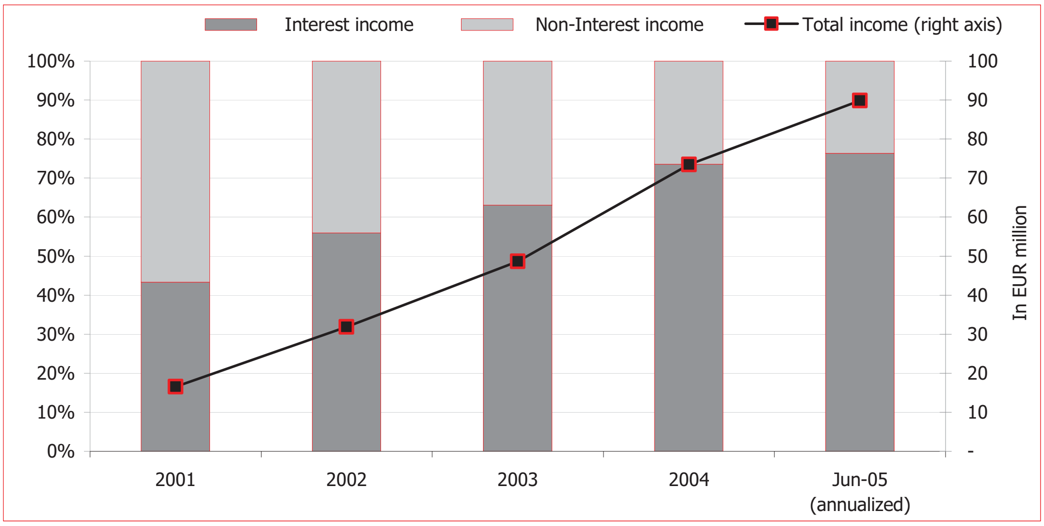
Table 7. Commercial banks income statement, in EUR million, unless otherwise indicated

Description	Jun-03	Dec-03	Jun-04	y-o-y % change	Dec-04	y-o-y % change	Jun-05	y-o-y % change
INCOME								
Interest income	13,355	30,695	24,311	82.0	53,999	75.9	33,361	37.2
Non-Interest income	7,932	17,984	8,471	6.8	19,449	8.1	10,410	22.9
TOTAL INCOME	**21,287**	**48,679**	**32,782**	**54.0**	**73,448**	**50.9**	**43,771**	**33.5**
EXPENDITURES								
Interest expenditures	1,946	5,279	4,277	119.8	9,978	89.0	6,975	63.1
Non-Interest expenditures	4,696	10,223	6,822	45.3	14,939	46.1	11,956	75.3
General and administrative expenses	11,639	25,379	15,215	30.7	33,952	33.8	20,504	34.8
TOTAL EXPENDITURES	**18,281**	**40,881**	**26,314**	**43.9**	**58,869**	**44.0**	**39,435**	**49.9**
NET INCOME								
Net operating income	3,006	7,798	6,468	115.2	14,579	87.0	4,336	-33.0
Provision from taxes	958	1,912	981	2.4	2,104	10.0	1,464	49.3
Net profit / loss for period	2,400	6,801	5,630	134.6	12,955	90.5	3,109	-44.8
Less: dividents	...	...	...	...	...	...	...	...
Retained profit for period	2,400	6,801	5,630	134.6	12,955	90.5	3,109	-44.8

[6] Net interest income is the difference between interest income and interest expenditures.

Structure of Income. Total income of the banking sector by June 2005 grew with 33.5% against the same period of 2004, amounting at EUR 43.7 million. The largest contribution to the growth was recorded for by interest income (+27.6%), while non-interest income contributed with 5.9% (see figure 15).

Figure 15. Structure of income



With respect to the interest income, income from loans contributed with 37.0% to the growth of total income from interest. By June 2005, they amounted at EUR 30.1 million, a 42.6% increase compared with June 2004. Their share to total interest income increased from 86.9% in June 2004, 89.1% at end 2004, to 90.3% in June 2005.

Income from placements with other banks generated positive contribution by 1.9% to the growth of total interest income, whereas by the end June 2005 they amounted at EUR 1.9 million. They grew with 31.1% against June 2004 accounting for 5.8% (-0.3 percentage points compared with June 2004) of total interest income.

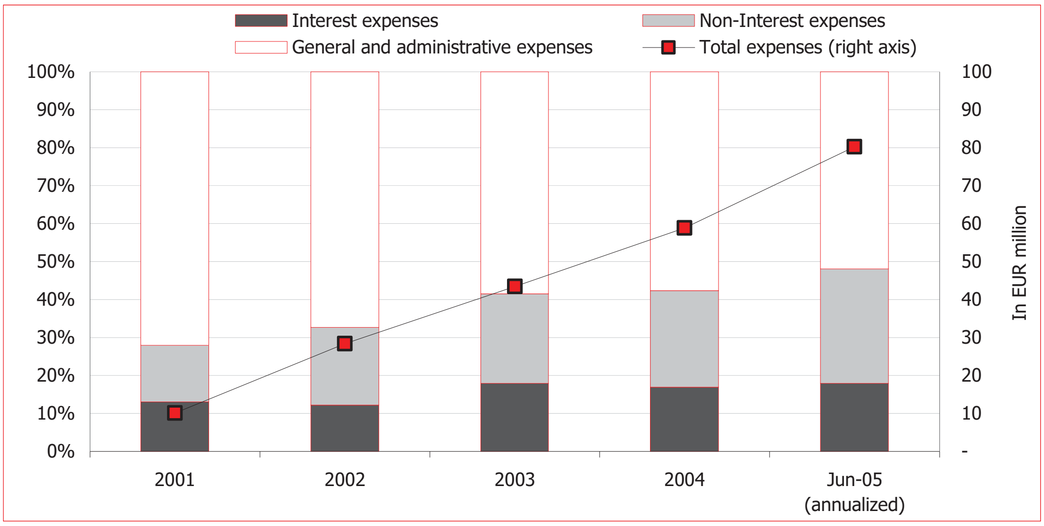
Regarding income from investments in securities, they amounted at EUR 1.3 million, a 23.8% decrease compared with June 2004. Owing to this decrease, they generated negative contribution by 1.7% to the growth of income from the interest. In June 2005, their share to total interest income decreased by 3.1 and 2.4 percentage points compared with June 2004 and end 2004, respectively.

Income from fees and commissions contributed with 15.4% to the growth of non-interest income. By June 2005, they amounted at EUR 8.8 million, a 17.3% increase compared with June 2004. However, their share to total non-interest income fell to 84.9% in June 2005 from 89.0% and 90.1% in June 2004 and end 2004, respectively.

Other operating income contributed with 7.5% to the growth of non-interest income, while in June 2005 they amounted at EUR 1.6 million. In June 2005 compared with June 2004, they grew with 67.8% and, as a result, their share increased to 15.1% or 4.0 percentage points higher from the level they had in June 2004.

Structure of Expenditures. Regarding the growth of expenditures in June 2005, the major contribution was regarded for by general and administrative expenses (20.1%), while non-interest expenditures contributed with 19.5% and interest expenditures with 10.3%.

Figure 16. Structure of expenditures



With respect to the structure of expenditures, interest expenses in June 2005 amounted at EUR 6.9 million, a 63.1% increase against June 2004. As a result, interest expenditure increased their share to 17.7% in June 2005 from 16.9% at end 2004 (see figure 16) and 16.1% in June 2004.

Within the structure of interest expenditures, interest expenses on deposits grew with 61.0% compared with June 2004, amounting to around EUR 6.3 million. Their share to total interest expenditures at end June 2005 reached 90.0% which is 1.1 percentage points lower from the level obtained in June 2004. Interest expenses on borrowings contributed with 7.5% to the growth of interest expenses. Interest expenses on borrowings amounted at EUR 0.7 million which corresponds to the increase by 84.2% compared with June 2004. Due to this considerable increase, their share to total interest expenditures reached 10.0% in June 2005 from 7.4% at end 2004.

Growth of non-interest expenses is mainly attributed to the provisions for loan losses, which in the meantime contributed with 66.9% to the growth of non-interest expenses. Provisions for loan looses amounted at EUR 9.6 million by June 2005 while they grew with 91.2% compared with June 2004. As a result, their share to non-interest expenditures increased by 6.7 and 5.9 percentage points compared with their share in June 2004 and end 2004, respectively. By June 2005, they accounted for 80.0% of total non-interest expenses.

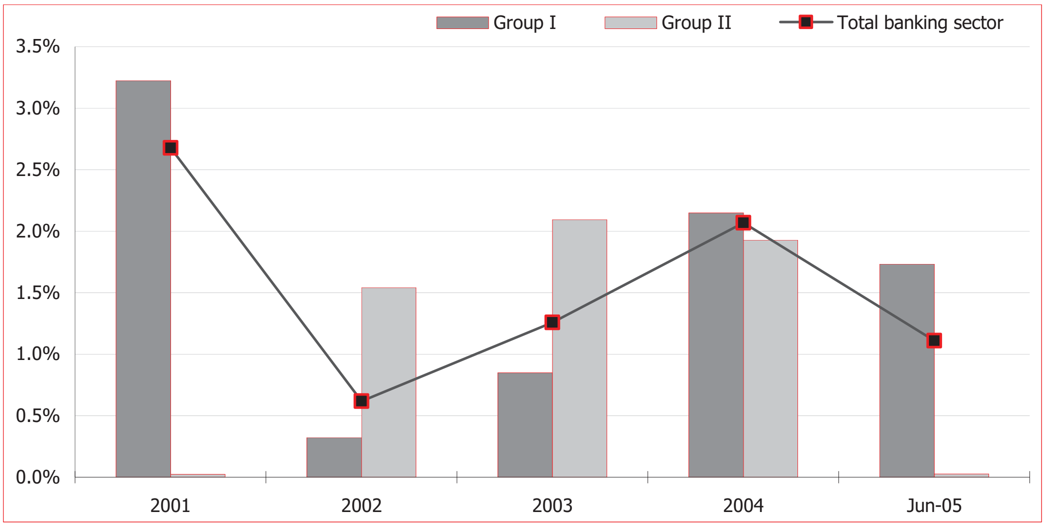
Depreciation of fixed assets grew by 31.4% compared with June 2004, and in June 2005 amounted at EUR 2.4 million. Their share to non-interest expenses was 26.6% and 25.9% in June 2004 and at end 2004, respectively and fell to 20.0% in June 2005.

The largest share of expenditures is recorded for by general and administrative expenses accounting for 52.0% in June 2005, a decrease by 5.8 and 5.7 percentage points compared with June 2004 and end 2004, respectively. Thus, by June 2005, general and administrative expenses amounted at EUR 20.5 million, an increase by 34.8% against June 2004.

3.3.2. Profitability and Efficiency

Profitability of the banking sector during the period under review showed a slight weakening. In particular, return on average assets[7] (ROAA), which is used to measure the efficiency with which the banking sector uses its assets, was characterized by a decline in June 2005 to 1.1% which is 0.96 percentage points lower from the level obtained at end 2004 (see figure 17). The reason behind this fall is the decrease in the ratio of both groups of banks in general and of Group II in particular.

Figure 17. Return on average assets



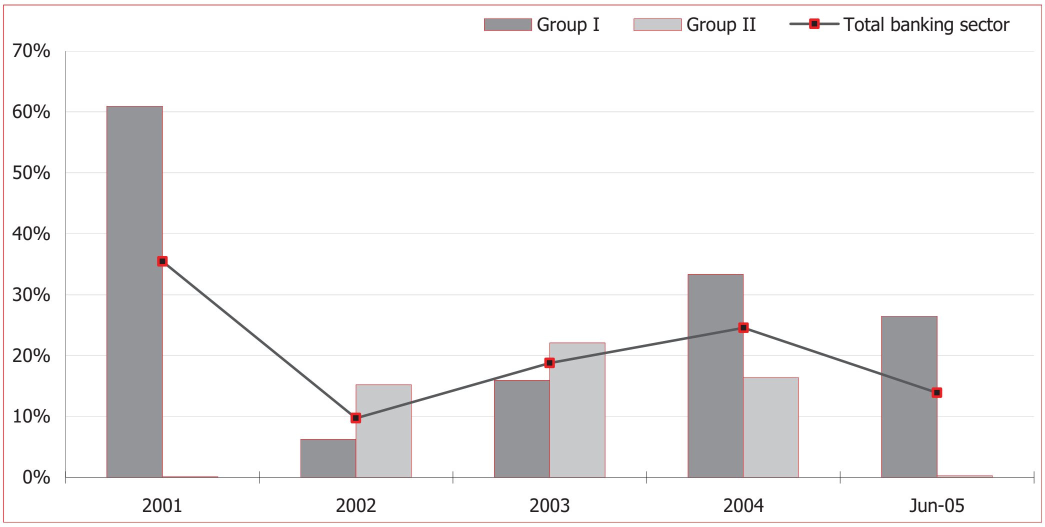
The corresponding ratio for Group I banks is characterized by a 0.4 percentage points decrease compared with 2004, and in June 2005 remained at 1.7%. On the other hand, the ratio for Group II banks, relative to Group I, decreased much faster in June 2005 reaching 0.03%, or 1.9 percentage points lower from the level obtained at end 2004. This decrease in the ratio is manly on account of the fall in the net profit after taxes of the total banking sector and an accompanying faster increase in assets.

[7] ROAA is measured using net profit after tax. Data on net profit after tax for June 2005 are annualized.

Similar tendencies were seen in the ratio between net profits after tax and average equity (ROAE). In particular, in June 2005 the ratio fell to 13.9% from 24.6% in 2004. Fall in net profits after tax and parallel increase in average assets of the total banking sector caused the fall in the ratio. The ratio for the Group I banks decreased by 6.9 percentage points in June 2005 against 2004 when they reached 33.4%.

As illustrated in figure 18, the rate of return on average equity at end-2004 was 24.6%, which corresponds to 5.8 percentage points increase compared with end-2003. As it the case with return on average assets, due to a decrease of net profit after tax and a concurrent moderate increase in equity, the banking sector ROAE in 2003 reached 24.6% whereas in 2002 it stood at 18.8%. Group II recorded a significant downturn on their ROAE falling from 16.4% in 2004 to 0.2% in June 2005.

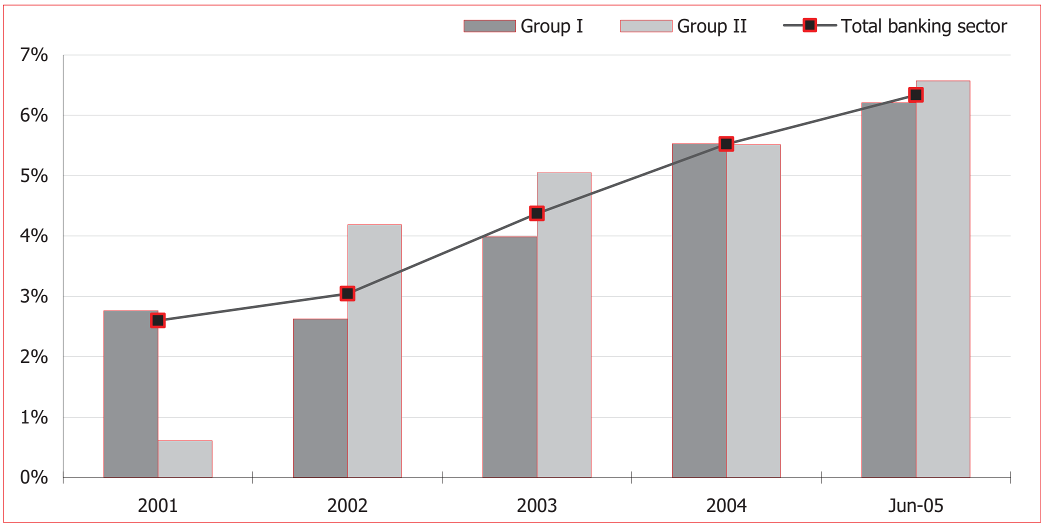
Figure 18. Return on average equity



On the other hand, total banking sector net interest margin (NIM) continues with its upward trend in 2005 as well. The total banking sector NIM increased from 5.5% at end 2004 to 6.3% in June 2005. This may be due to the change in the composition of the asset structure of the total banking sector in favor of loans granted to the economy characterized with higher interest rates.

As the figure 19 illustrates, Group II banks outstand Group I in terms of NIM. In particular, NIM for the Group II in June 2005 attained 6.6% from 5.5% in 2004. On the other hand, Group I banks' NIM increased from 5.5% in 2004 to 6.3% in June 2005. This increasing trend for Group II relative to Group I was driven by the fact that assets of Group II grew slower relative to the growth of net interest income.

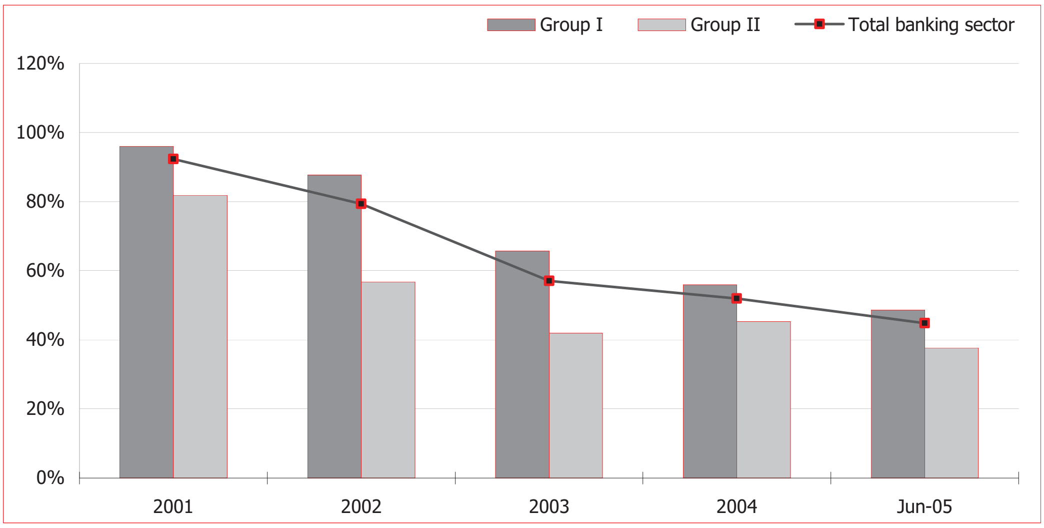
Figure 19. Net interest margin



3.3.3. Liquidity

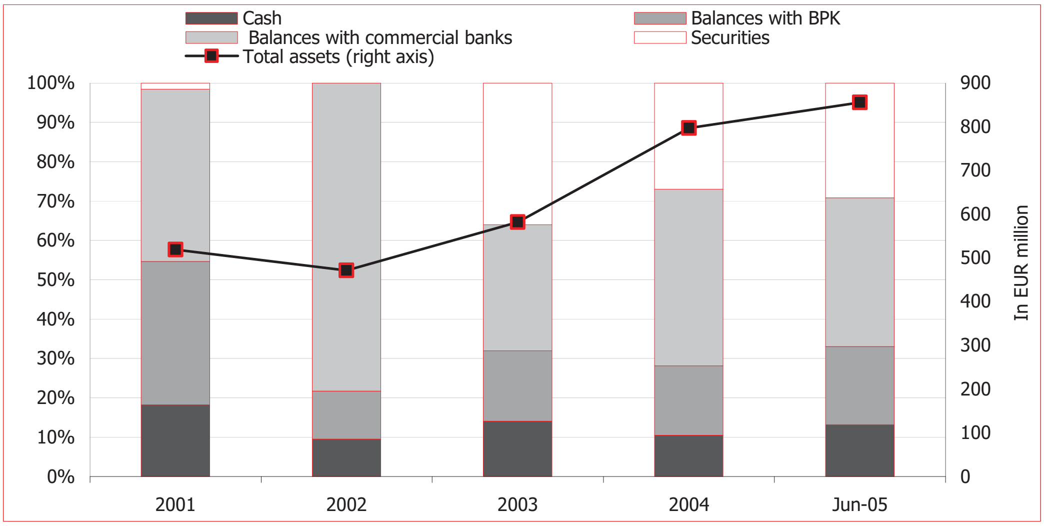
Liquidity position of the total banking sector remains strong. Ratio of liquid assets (which includes cash, balances with BPK, balances with other banks, and investments in securities) to total banking sector assets in June 2005 has fallen by 7.1 percentage points compared with 44.8% at end 2004 (see figure 20). The decrease in the ratio was driven by the continuous fall in the liquid assets. In particular, this decrease can also be seen from the structure of assets of the banking sector which has changed, mainly in favor of lending to the economy of Kosovo.

Figure 20. Liquid assets to total assets



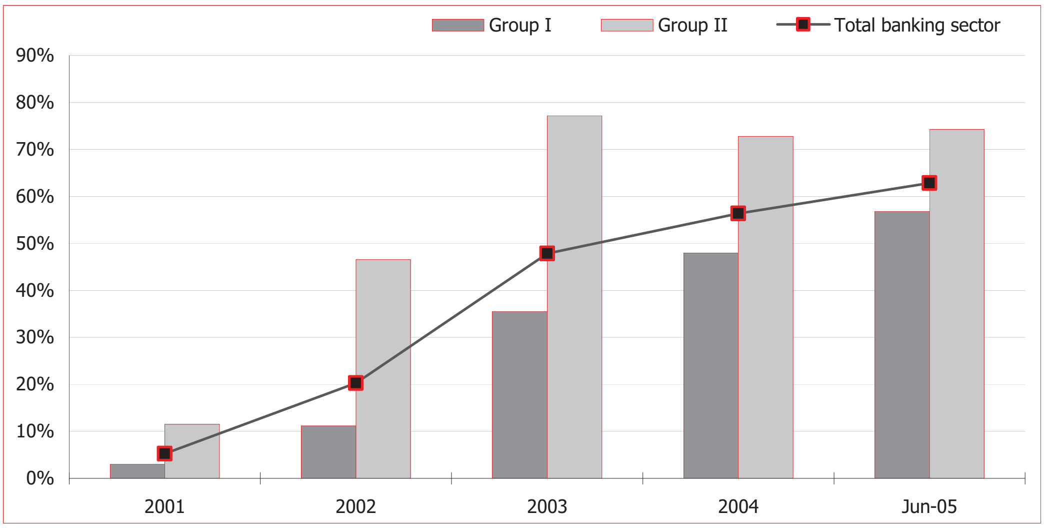
Similar decline in the ratio was recorded for both bank groups. Group II ratio of liquid assets to total assets fell by 7.6 percentage points from the level they had in 2004 and in June 2005 it reached 37.7%. Similarly, the ratio of liquid assets to total assets of Group I reached 48.7% in June 2005, 7.3% decrease compared with 2004. Total liquid assets of the banking sector in June 2005 decreased by 7.5% against 3.0% in 2004. The decrease was mainly driven by the decrease in liquid assets of Group II, which in June 2005 fell by 13.0% against 2004. On the contrary, liquid assets of Group I increased by 1.4% in June 2005 compared with 2004.

Figure 21. Structure of liquid assets



With respect to the composition of liquid assets, commercial banks by June 2005 increased their investments in securities by 49.7% compared with 2004 (see figure 21). The increase in the investments in securities was mainly at the expense of balance with other banks, which in June 2005 decreased by 35.0% compared to end 2004. However, by June 2005 the largest share in total liquid assets was accounted for balances with other banks (37.9% of total liquid assets) while investments in securities remained the level at 29.2%. The remaining share accounted for cash and balances with BPK (including reserve requirements).

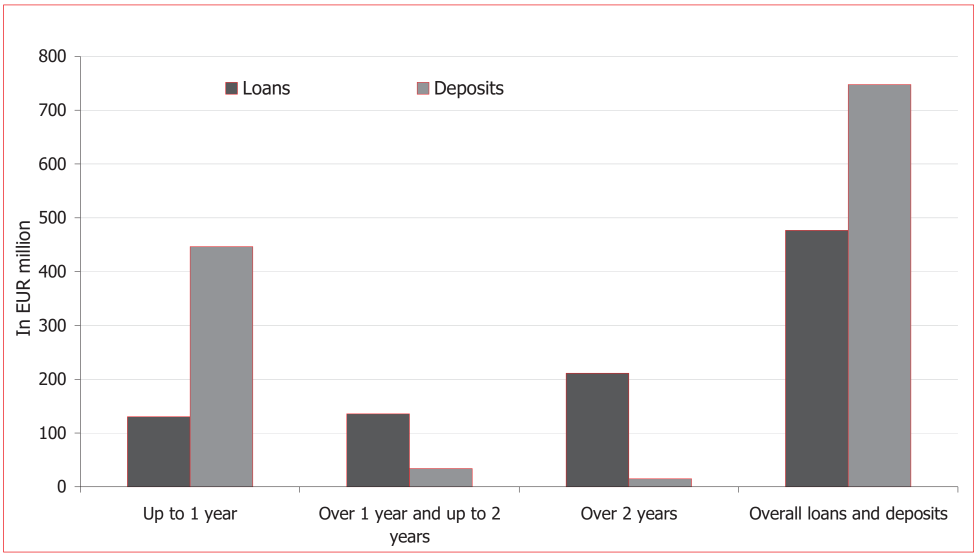
Figure 22. Loan to deposit ratio



The liquidity position of the banking sector is revealed by the ratio of loans to deposits as well. Particularly, the ratio of loans to deposits increased in June 2005 by 6.5 percentage points compared with 2004 remaining the level at 62.8%. This continuous increase, although at a slower rate, was driven by the faster increase of loans accompanied with the moderate increase in deposits.

With respect to the defined groups of banks, Group II recorded the largest ratio of loans to deposits. Specifically, the ratio for Group II increased from 72.8% in 2004 to 74.2% in June 2005. Group I remained the level at 56.9% in June 2005 representing an increase by 8.9 percentage points compared with the level obtained in 2004.

Figure 23. Maturity breakdown of commercial banks lending and deposits, as of June 2005



As depicted in the figure 23, loans with the maturity of up to 1 year at end June 2005 totaled around EUR 130 million, or 29.1% of deposits with the same maturity. This ratio is much lower compared with June 2004, when counted for 40.5%. The decrease in the ratio is more contributed from increase in deposits (from EUR 268.3 million in June 2004, through EUR 398.4 million in December 2004 to EUR 446.4 million in June 2005), than increase in loans (from EUR 108.5 million in June 2004, through EUR 127.4 million in December 2004 to EUR 130.1 million in June 2005).

In June 2005, loans with maturity of over 1 year and up to 2 years totaled at EUR 135.7 million which is approximately four times higher (402.0%) than deposits with the same maturity whereas compared with June 2004 (413.5%) this share have experienced a slight decrease. The same situation corresponds also for loans and deposits with maturity of over 2 years. Loans with maturity of over 2 years amounted at EUR 211.1 million compared with deposits which amounted at EUR 14.7 million.

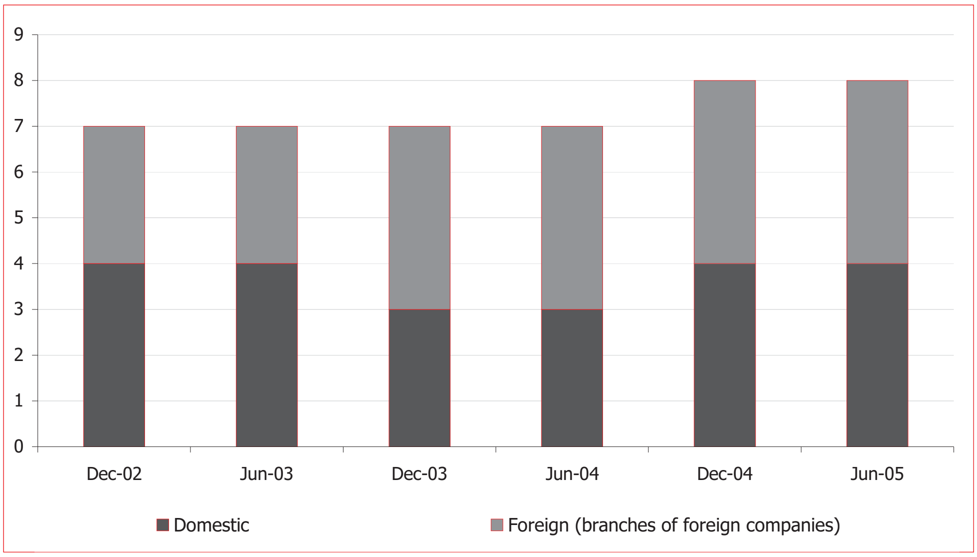
4. OTHER FINANCIAL CORPORATIONS

4.1. Insurance Companies

Insurance market in Kosovo is rather small and represents 5% of total financial sector assets (as of end June 2005). Regarding the trend of insurance companies' assets, at end of June 2005 they stood at EUR 47.5 million, a 24.3% increase relative to the June 2004, or comparing with end of 2004 there is decelerating increase of 8.7%. Concerning the products offered by insurance companies, until know these companies are engaged only in non-life insurance, dominated by car insurance.

As of June 05, there were 8 insurance companies operating in Kosovo. Concerning ownership structure of these companies, four are branches of foreign companies and four are domestic companies established in Kosovo.

Figure 24. Number of insurance companies



As presented in the figure 23, during the period June – Dec 2003 a domestic company shares were bought from a foreign company, increasing of foreign owned insurance companies from 3 to 4. Till end of 2004 the number remained the same, while at end of March 2005, BPK licensed a new insurance company (as branch of foreign insurance company).

Prepayment of premiums and reserves at end of June 2005 totaled at EUR 22.7 million. In year-on-year perspective they increased by 27.3% and 32.0% compared with December 2004 and June 2004, respectively.

Being the main position in the insurance companies' balance sheet, prepayment of premiums represents increase also in the share of total balance sheet. The highest ratio corresponds to 47.8% for period June 2005, against 35.3% and 41.3% in December 2004, and June 2004, respectively.

Table 8. Insurance companies' assets, by size[8]

Description	Dec-02	Jun-03	Dec-03	Jun-04	Dec-04	Jun-05
Over 10 million	1	1	1	0	1	1
Over 5,5 - up to 10 million	2	3	4	4	3	5
Up to 5,5 million	3	2	1	2	3	1

At the beginning of operations most insurance companies were at the level of up to around EUR 7.5 million of total assets, while only one company exceeded EUR 10 million assets (around 11 EUR million). Increase in the number of insurance companies with below EUR 5.5 million assets, in period 2003-2004, is due to the establishment of the new company with foreign ownership.

From the surveys perspective, insurance companies relations with external sector shows that net foreign assets at end of June 2005 counted for EUR 3.9 million. The amount is made up from claims on nonresidents, dominated from foreign shares and other equities. Insurance companies' claims on depository corporations at end June 2005 counted for EUR 39.4 million, a 39.0% increase on year-on-year perspective, while 10% is increase in their assets to depository corporations compared with end 2004. The share of claims on BPK to total claims on depository corporations, at end of June 2005, accounted for 46.6% representing continuous decrease from June 2004 when counted for 62.5%. As a result, there is increase in the claims on other depository corporations as share to depository corporations from 37.5% in June 2004 through 53.4% in June 2005.

We will use ownership criteria, separating domestic and foreign insurance companies making some comparisons in the direction of market share and other selected indicators.

Box 7. Composition of insurance companies groups

Group I	Group II
Insig	Dukagjini
Sigal-Drini	Siguria
Sigma	Kosova e Re
	Dardania

[8] Excluding the balance sheet of the recently established one insurance company.

Looking into the assets of domestic companies (group II), as depicted in the table 9, share to total assets is higher. Since December 2002, group II on average accounted 57% of total assets. In the year-on-year basis, assets of insurance companies experienced highest increase by 24.3% contributed 17.0% from group I and 7.4% from group II. Mainly, the contribution of group I is due to the establishment of new foreign insurance company.

Table 9. Insurance companies' assets, by ownership[9], in EUR thousand

Description	Dec-02	Jun-03	Dec-03	Jun-04	Dec-04	Jun-05
Group I	20,927	17,838	23,642	13,637	18,836	20,142
Group II	24,388	24,752	25,542	24,641	24,962	27,456
TOTAL ASSETS	**45,315**	**42,590**	**49,184**	**38,278**	**43,798**	**47,598**

Based on the table 10, insurance companies' premiums received at end June 2005 stood at EUR 25.3 million, a 36.7% increase compare to the same period of the previous year. Looking on year-on-year perspective, at end 2004 amount of premiums received reached at EUR 39.1 million, a 5.4% increase relative to the end of 2003, against the increase of 20.1% in the period 2003 – 2002. However, comparing end 2004 with end 2002 and end of 2001, we see accelerated growth in received premiums by 26.5% and 25.3%, respectively.

Increase in the amount of the premiums received from insurance companies, is accompanied with increase in the number of policies sold. At end 2004, they reached its peak numbering for 370.1 thousand policies sold, showing permanent increase from 179.8 thousand at end 2001. As regards to the structure, "Third party liabilities" policies are dominating with 65.2% of total policies sold at end 2004, while, at the end of June 2005, this ratio is even higher (3.2 percentage points).

Amount of claims paid by insurance companies, at end of June 2005, reached around EUR 4 million, a 3.4% increase compare to the June 2004. The same follows end of 2004 compare with previous years. Namely, EUR 6.7 million accounts for end of 2004 compared with EUR 5.8 million, EUR 3.9 million and EUR 2.6 million at the end of 2003, 2002, and 2001, respectively. Same as it is the case with premiums received, "Third party liability" (TPLs) dominates within total claims paid with its share at 90%.

However, claims paid from insurance companies represent substantial smaller amount versus the premiums received. The gap can be stressed correctly comparing the ratio of premiums paid relative to the premiums received. The ratio for the period end 2004 was 17.2%, representing highest ratio since the beginning of operations, compared with 15.8%, 12.7%, and 8.5% at end 2003, 2002, and 2001, respectively.

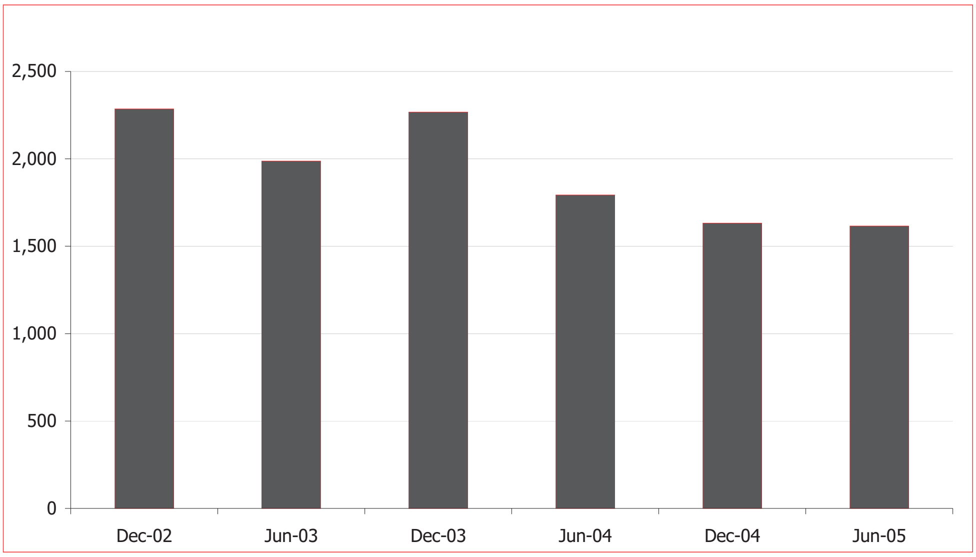
Table 10. Insurance companies activity, in EUR thousand

Description	Dec-02	Dec-03	2004 Jun	2004 Dec	Jun-05
Amount of premiums received					
TPL	27,231	29,163	14,119	28,739	18,072
Border policies	3,686	6,557	3,485	8,604	2,156
Other	66	1,340	932	1,747	5,019
TOTAL	**30,983**	**37,060**	**18,536**	**39,090**	**25,247**
Number of policies sold					
TPL	175,008	199,223	106,960	241,901	123,987
Border policies	72,358	62,073	38,371	120,609	48,446
Other	67	3,827	3,257	8,423	7,129
TOTAL	**247,433**	**265,123**	**148,588**	**370,933**	**179,562**
Amount of claims paid					
TPL	3,540	5,576	3,125	6,163	3,865
Border policies	395	272	317	580	106
TOTAL	**3,935**	**5,848**	**3,442**	**6,743**	**3,971**

Note: Data are cumulative within a calendar year.

Increase in the activity of the insurance companies (figure 25) is followed by the increase in the competition among the companies also, concentrated only in non-life insurance activities. The HHI index, measured by total assets (except for end 2003 when it increased to 2.268 points), in the following periods decreased to the level of 1.616 points at the end of June 2005. Until now (June 2005), there is no insurance company dealing with life-insurance activities.

Figure 25. Insurance companies Herfindahl-Hirschman Index



4.2. Pension Funds

In Kosovo the pension schemes are defined at three levels:

- Basic pension - as mandatory scheme, paid by the Pension Administration financed through Consolidated Budget of Kosovo;

- Individual Savings Pension - as mandatory scheme, managed by the Kosovo Pension Savings Trust (KPST) and financed through compulsory minimal contributions of employers and employees.

- Supplementary schemes consist of three sublevels: a. Individual Savings Pension (managed by KPST complemented with additional voluntary contributions paid by the employer or the employee, or both); b. Supplementary Employers Pensions (provided to employees by their employer); c. Supplementary Individual Pensions, provided to natural persons from licensed pension provider.

The two mandatory schemes (basic and individual savings pension), based on international practices and definitions do not form part of the sub-sector of pension funds, but belong to the central government and social security sector respectively.

As of end June 2005 there are 7 pension funds operating in Kosovo. Except one pension fund[10] which is established in 2003, all remaining were established during 2002, which funds belong to supplementary schemes. However, amount collected at end of June 2005 amounted at EUR 7.6 million, showing continuous increase from EUR 1.5 million in June 2003, or on average at EUR 1.5 million on semi-annual basis.

As regards to the mandatory schemes, amounts collected (by Kosovo Pension Saving Trust) by this scheme, at end of June 2005, amounted at EUR 110.2 million. However, this amount represents increase for around 38% and 94% relative to end of 2004 and the same period of the previous year, respectively. The amount collected from KPST is mainly invested abroad (Western European countries) in mutual funds/unitrust funds investments[11]. Looking into the trend, average increase in the amount of these funds is for by EUR 22.7 million on semi-annual basis.

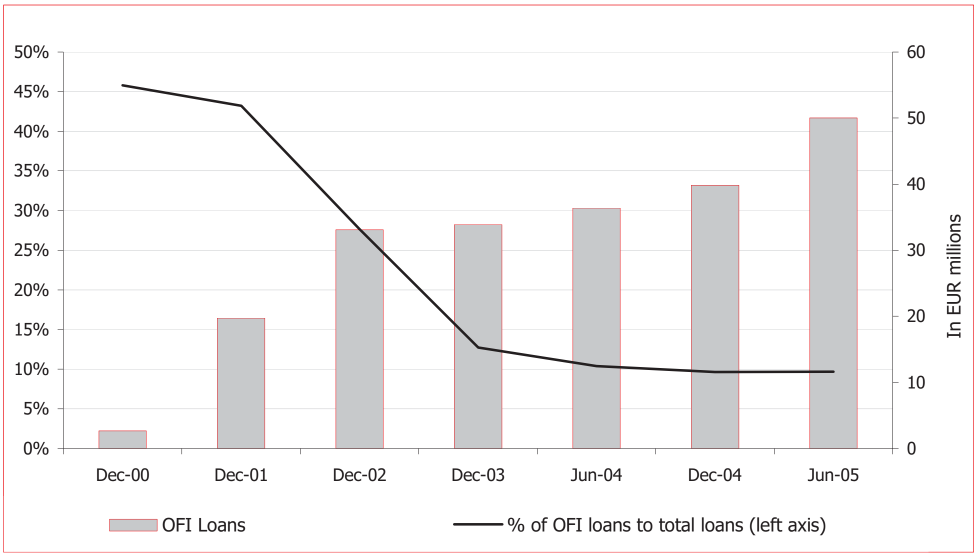
4.3. Other Financial Intermediaries

In addition to commercial banks, other financial intermediaries participate in lending to the real sector with respectable satisfactory share. As presented in the figure 26, the ratio of OFIs lending to total financial sector lending has fallen continuously compared to previous periods. The decrease of the ratio is due to the faster increase in the lending of commercial banks. At the end of June 2005, other financial intermediaries loans

[10] Pension Fund "Ramiz Sadiku".
[11] ABN AMRO Funds (Interest Growth Fund – EURO hedged) and VANGUARD (Global Index Fund – EURO hedged). Source: Pension Funds Supervision Department - BPK.

amounted at EUR 49.9 million, a 37.4% increase on year-on-year basis, and representing around 10% of total loans granted by financial sector in Kosovo.

Figure 26. Other financial intermediaries lending activity



Regarding the number of loans extended by other financial intermediaries, at end of June 2005, they counted for around 24.3 thousand loans compared with 22.3 thousand loans in December 2004, and 20.7 thousand loans in June 2004. Since June 2004, average monthly increase in the number of loans extended from other financial intermediaries, is for by 291 new loans per month. Average amounts of loans show a decline from 570.6 EUR in June 2004, 559.2 EUR in December 2004 standing at 487.6 EUR per loan.

5. BPK PROJECTS

5.1. Credit Registry of Kosovo

The first credit registry in Kosovo was established under the name Kosovo Credit Information Service – KCIS in 2001 by several credit providing institutions. The KCIS has collected data from credit providing institutions about the credit record of borrowers in order to enhance the assessment of credit applications. It was organized as a not-for-profit association in accordance with UNMIK Regulation 1999/22 On Registration and Operation of Non-Governmental Organizations. It was a voluntary initiative, and as such the transmitting of data was on a voluntary basis.

The BPK in 2004 undertook the development of the KCIS. Specifically, the Banking Rule No. XXVIII On Credit Reporting was approved by the BPK Governing Board in November 2004 to make the reporting of credit information by the credit providing institutions compulsory, and to regulate the data collection on credit reports of potential borrowers. At the same time, the BPK initiated the development of a contemporary IT system for the credit registry. The work on development of the credit registry IT system continued in 2005, while the BPK also has involved in the project and familiarized with the credit registry all credit providing institutions (commercial banks and micro finance institutions). In the meantime, credit registry was renamed and called 'Credit Registry of Kosovo' (CRK). Further to Banking Rule No. XXVIII and based on the developed CRK system, the BPK prepared Operational Instructions for the CRK. The testing phase is expected to be completed in November 2005 and it is planned that at the beginning of 2006 the CRK system will become functional.

The CRK system is designed as a web-based application and is accessible online and in real time by authorized staff of credit providing institutions. The credit providing institutions have to enter in the system approved credits within one working day following the date of their approval. Subsequently, they have to update status of each credit on a monthly basis and this within 5 working days following the last working day of the previous month.

Credit providing institutions can obtain from the system a summary report on level and status of outstanding credits of each credit applicant. They will also be advised of collateral in case of collateralisation. In addition, they will obtain relevant information on credit applicant's relation to other outstanding credits. Nevertheless, in order to maintain the secrecy of their business, credit providing institutions do not get advised of the terms of approved credits or the identity of the credit providing institutions that approved them. For entering/updating the information the credit providing institutions will not be charged. For obtaining credit reports on individual credit applicants they will be charged nominal fees according to a monthly descending scale.

Also, each person that is the subject of credit has the right to obtain his details registered at the CRK. Such a request should be addressed in writing to the BPK, and for each such a request a nominal fee is payable.

All data registered in the CRK is secured according internationally accepted best principles for data protection. The privacy of each and every person's data is guaranteed. The data will be kept in the system up to three years after the last entry. When a physical or legal person ceases to exist, the information will be kept up to three years in the system. All the data older than three years will be archived.

The CRK will not be used only for the purposes of facilitating assessment of credit application by the credit providing institutions, but also for supervisory purposes by the BPK. The Bank Supervision Department of the BPK will obtain on a monthly basis detailed reports on outstanding credits in relation to each credit providing institution. These reports will be verified against the books of credit providing institutions.

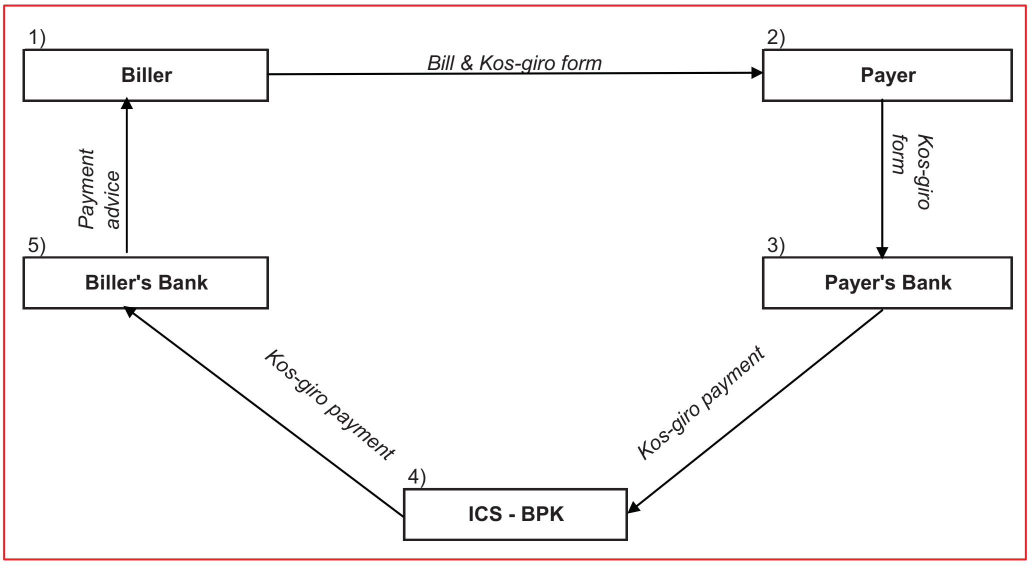
The BPK project on Credit Registry is among the projects designed to provide better infrastructure in the functioning of the financial market. This will provide the tool to the credit providers for better assessment of the borrower creditworthiness and risks and, as a result, may facilitate lending in Kosovo economy in terms of the volume and costs to the Kosovo economy.

5.2. Kos-Giro Payments

The development of the giro payment scheme has been one of the major projects of the BPK since 2004. The Kosovo scheme for giro payments, known as the Kos-giro, is a milestone in the development of low value / high volume retail payments. It is designed to facilitate bill payments through standardization and automation of an efficient scheme for all the participants involved: the BPK, commercial banks, large billers and payers.

The Kos-giro is based on internationally accepted standards and provides a way for the payer to pay bills to the biller through the banking system. The payer at the bank pays bills either from an account or in cash. From the perspective of the banking system, Kos-giro is linked to the Interbank Clearing System (ICS), and enables efficient processing and clearing of multiple credit transfers to single accounts.

Scheme 2. Kos-Giro payments, information flow



The principal use of Kos-giro is for regular periodic payments like utility bills, taxes, or subscription fees. Kos-giro consists of:

- a standardized payment form, which is attached to a regular bill by the billers
- a standardized and efficient (automated) way of processing the payment by the commercial banks
- a standardized and efficient way of providing payment details by the commercial bank to the biller for automated reconciliation

In relation to Kos-giro introduction, the BPK has had product development and management role, and it is responsible for maintenance and development of the scheme. The BPK started to develop the Kos-giro scheme in 2004 in close cooperation with the IMF, seven commercial banks and the two largest utilities (billers) in Kosovo: Electricity Company - KEK and post and telecom company - PTK. A pilot started to run at the end of 2004, with other billers joining in (the Water Utility – Batllava, Heating Utility – Termokos, UNMIK Customs, Municipality of Pristina Property Tax, Car Registration). The Kos-giro was officially launched in August 2005.

The Kos-giro has positive impacts for the BPK, commercial banks, large billers, and payers. First, it positively contributes to the principal objectives of the BPK by enhancing the efficiency of the domestic payment system and the liquidity in the economy. The Kos-giro enriched the payment system with a modern payment scheme, which contributes to the reduction of the cash in circulation, the increase of deposits in commercial banks, and the improvement of the overall liquidity. Second, it enables the commercial banks to improve customer services and to process payments faster and more efficiently. Third, for the large billers, it offers improved efficiency and cost savings, as well as more timely and accurate information on their financial and overall position. Finally, the Kos-giro provides the payer with one more choice to pay the bills, which is efficient as well as convenient.

5.3. International Transaction Reporting System

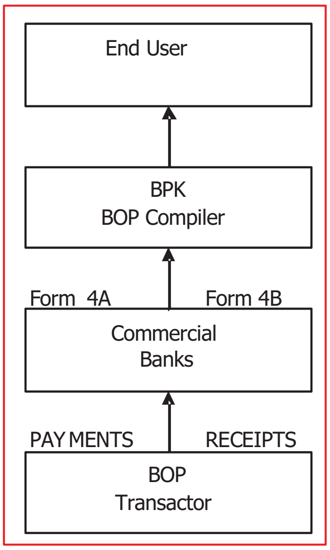
Banking and Payments Authority of Kosovo starting from September 2005 has launched the project on International Transaction Reporting System (ITRS). ITRS measures individual balance of payments (BOP) transactions passing through the commercial banks. The aim of this project is to collect the necessary information with the purpose of compiling the BOP for Kosovo.

A country's balance of payments tracks payments to and receipts from nonresidents. BOP is "a statistical statement that systematically summarizes, for a specific time period, the economic transactions of an economy with the rest of the world" (Balance of Payments Manual, IMF 1995). The ITRS developed by the BPK covers transactions above the threshold of 10,000 EUR. Hence, the ITRS is a partial system meaning that certain balance of payments transactions are not recorded. This is in the fuction minimizing the reporting burden for commercial banks and at the same time covering significant amount of transactions with rest of the world.

As presented in the scheme 3, bank clients will provide the information through Payment Order to the commercial banks for payments to and receipts from nonresidents on the amount (above threshold of 10,000 EUR), purpose of transaction, sector, and other information required in the form. These data are collected by the commercial banks and transmitted to the BPK for BOP compilation. In addition, commercial banks report their own account transactions with nonresidents in a separate ITRS module.

The ITRS will not cover all the transactions needed for BOP compilation. The BPK is continuing efforts to build the infrastructure with other relevant institutions for collecting data on international transactions in order to capture transactions with nonresidents. As a result, the BOP statistics will improve in terms of scope and accuracy of the data. This will serve to end users (researchers, policymakers and other relevant parties) in understanding better the external sector of Kosovo economy and propose policy gudelines.

Scheme 3. ITRS flow



6. NOTES ON METHODOLOGY

Figure 1. Number of individual financial corporations (excluding BPK)

The figure shows types of financial corporations licensed from BPK, and operating in Kosovo. Terminology used in the figure is based on the "Manual on Monetary and Financial Statistics" IMF 2000. BPK as institution is not included in the presentation. Source for the number on individual types of financial corporations are banking, insurance, and pension supervision department.

Figure 2. Structure of the financial sector in Kosovo

The figure 2. is compiled using consolidating the balance sheet of all financial corporations except BPK. Removing all their capital and non-capital links between the financial corporations, is presented the ratio of each type of financial corporations to total assets of the financial sector in Kosovo. Source for the data are Statistical Bank Report, insurance corporations and pension funds department of the BPK.

Figure 3. Number of banks

According to the ownership structure, commercial banks in Kosovo are classified into two groups: foreign owned and domestic owned, and thus named as Group I and II, respectively. Group I comprises banks which have more than 50.0 % of foreign ownership whereas Group II comprises those banks which are in majority domestic ownership. The figure shows the number of banks during the period 2000-2004, which also captures the ownership structure. The data on the number of banks in Kosovo are obtained from the Banking Supervision Department.

Table 1. Commercial bank assets, by size

The table shows the comparison between groups of banks with respect to their size of assets, which also capture the ownership structure of the banking sector in Kosovo. The source of data is BS schedule (Statistical Bank Report, BPK)

Table 2. Commercial bank assets, by ownership

The table shows the comparison between asset sizes of group of banks with respect to their ownership structure. Banks are divided into two groups according to their ownership. Then their assets are summed up and, in turn, their share to total banking sector assets is calculated. The source of data is BS schedule (Statistical Bank Report, BPK)

Table 3. Commercial banks network, by region

The table presents the distribution of banks' head quarters, branches, sub-branches, and mobile units among the regions of Kosovo on annual and semiannual basis.

Table 4. Commercial bank selected indicators

The banking sector productivity is measured on the year-on-year basis using the number of employees, volume of assets/loans/deposits managed by employee and banking unit. The number of employees per banking unit was calculated as the ratio between the number of employees for the total banking sector and the total number of banking units for the total banking sector. The ratio of total assets managed by the banking unit and by an employee is calculated in the same manner. Total banking sector loans per employee/banking unit and deposits per employee/banking unit is measured as the ratio between total banking sector loans (deposits) and total number of employees/banking units.

The ratio between the number of citizens[12] and the number of banking units and/or number of employees is calculated to capture the "bankarisation" degree in Kosovo. The schedule Balance Sheet (Statistical Bank Report) is the source for data on the amount of assets, loans, and deposits whereas Banking Supervision Department is the source of data on the number of banking units and the number of employees.

Figure 4. Commercial bank productivity indicators

In order to capture the labour productivity for the particular banking group, the ratios of assets, loans, and deposits per employee are calculated. The calculations were made in the similar way as for the total banking sector but the figures are divided by banking groups.

Figure 5. Commercial banks Herfindahl-Hirschman Index (HHI)

The concentration of assets, loans and deposits for the each bank is calculated using the formula of HHI.
This formula is calculated as follows:

[12] The data for the number of citizens is taken from the IMF staff estimates.

$$HHI = \sum_{i=1}^{7}\left(\frac{Assets_i\ (deposits_i, loans_i)}{Total\ banking\ \sec tor\ assets\ (deposits, loans)}\cdot 100\right)^2$$

Where i represents the number of banks. The HHI is calculated by squaring the market shares of each bank and then summing the results. Schedule BS is the source for the data on the amounts of assets, deposits, and loans.

Figure 6. The Share of two largest banks in total banking sector assets, loans, and deposits (C2)

The criterion of banks asset size was used for selecting of two largest banks in the banking sector in Kosovo. Accordingly, the share of the two largest banks assets to total assets was calculated as a ratio between the sum of assets of the two largest banks and the total banking sector assets. The same was applied for calculating the share of the two largest banks to total deposits and total loans. Note that the share of two largest banks does not capture the same banks for different years, and hence it relies on the asset size of banks. The schedule BS is the source of data on the assets, deposits and loans (Statistical Bank Report, BPK).

Figure 7. The Share of four largest banks in total banking sector assets, loans, and deposits (C4)

The criterion of banks asset size was used for selecting of four largest banks in the banking sector in Kosovo. Accordingly, the share of the four largest banks assets to total assets was calculated as a ratio between the sum of assets of the four largest banks and the total banking sector assets. The same was applied for calculating the share of the four largest banks to total deposits and total loans. The schedule BS is the source of data on the assets, deposits and loans (Statistical Bank Report, BPK).

Table 5. Commercial banks balance sheet - assets

The table presents each category of assets in volume and their share in total assets for the particular period. In addition, the change for each item in the year-on-year basis is calculated, showing the percentage change of the item relative to the balance reported in the preceding period (which in this case is percentage change in semiannual basis). Schedule BS is the source for the data on the amount of assets for the banking sector in Kosovo.

Figure 8. Structure of loans by sectors

The sectoral diversification of the loan exposure is presented by the type of beneficiaries such as non-financial corporations and households. First, the share of loans for each category in total banking sector loans is calculated and presented by bars in the figure. Then, total loans for each sector are added up and presented with a line which corresponds to the right axis of the figure. The schedule BS/LBM is the source of loans by institutional sectors.

Figure 9. Structure of loans by industry

The table shows the industrial diversification of loan exposure during the course of 2004 and June 2005. Total loans extended by industrial sector of each bank are added up and then the share of loans extended to each industry in total loans extended is calculated for each year. Schedule BS/LBI (Loans By Industry) is the source of data for the amounts of loans extended.

Figure 10. Structure of loans by maturity

The maturity structure of loans is reported for the period 2001-June 2005 for the total banking sector in Kosovo. Loans are split up by their maturity and presented by bars which represents their shares in total loans, whereas the line corresponds to the total banking sector loans presented in volume. Schedule BS/LBM (Loans by Maturity) is the source of data for the maturity structure of loans.

Figure 11. Effective interest rates on loans and deposits and their spread

The figure shows the developments of lending and deposits interest rates since June 2004 onwards on the monthly basis. The effective interest rate is the average interest rate weighted over all maturities and type of product.[13]

Table 6. Commercial banks balance sheet - liabilities

The calculation of commercial banking sector liabilities is made in the same manner as the calculation of assets. First, each category of the liability side of balance sheet is stated in volume. Second, for each category of balance sheet the share in balance sheet total is stated in the second column of the corresponding year. Finally, the change in balance sheet categories indicates their percentage change relative to their balance recorded in the preceding year. Schedule BS is the source of data on the amount of the liability side of total banking sector balance sheet.

[13] For detailed explanation for effective interest rate calculations see www.bpk-kos.org: Monthly Statistics Bulletin, issue of November 2004. The distinction is made for households and non-financial corporations.

Figure 12. Capital to risk weighted assets

The ratio is calculated in accordance with the rule on Capital Adequacy of Banks. The figure illustrates the ratio between the consolidated total capital and the risk-weighted assets and then multiplied by 100. This calculation is made by the Banking Supervision Department of the BPK based on the amended rule on capital adequacy.

Figure 13. Structure of deposits by maturity and currency

The structure of deposits by maturity and currency is computed in the following manner. Breakdown of deposits with respect to the sectors is made into the non-financial and households which are then presented by bars. This criterion is used in both cases, structure of deposits by maturity and currency. The line corresponds to the transferable deposits in first case and other deposits in second case. The right panel of figure shows the breakdown of deposits by sector. The schedule BS/DBM (Deposits by Maturity) is the source for the amount of data on deposits.

Figure 14. Structure of deposits by sector

The sectoral distribution of deposits is presented with charts for the three periods, on the semiannual basis. The deposits of each sector for each bank are added up and thus calculated as a share in total deposits in commercial banks.

Table 7. Commercial banks income statement

Each category of the income statement is summed up for the total banking sector. Additionally the change in the income statement is the percentage change for the each item in comparison to the statement recorded in the preceding year. Schedule IS (Income Statement) banking supervision department is the source of the data on the amounts of income statement items for the banks.

Figure 15. Structure of Income

The figure plots the structure of the particular component of income for the total banking sector. It shows the amounts for the total income represented by the line and corresponds to the right axis and the share of each component of the income structure to the total income presented by bars. The Schedule IS the source of data on the banks' income.

Figure 16. Structure of expenditures

Same as in the previous figure, the structure of expenditures for the total banking sector is plotted, with interest expenditures, non interest expenditures, and the general and administrative expenses presented by bars. The bars in the figure show the share of each expenditure component while the line presents total expenditures stated in volume. Schedule IS is the source of data on the expenses of banking sector.

Figure 17. Return on average assets

The ratio between the after-tax profit and the average assets is calculated for each group of banks as follows. First, the after tax profit for each bank recorded for the particular period is added up for all banks in the group of banks. Than the banks' assets are added up for each group. Then the amounts thus calculated are divided and multiplied by 100. The same applies for the total banking sector. The average assets are calculated as the sum of the monthly assets for each bank for the particular year. Schedule IS is the source of data for the profit after tax whereas BS is the source for the amount of assets for the banking sector.

Figure 18. Return on average equity

The ratio between after tax profit and average equity for each group of banks is calculated as follows. First, the after tax profit for the particular period is added up for each defined group of banks. Then the average equity is calculated and added up for each group. The summed amounts are thus divided and multiplied by 100.

The average equity is expressed as arithmetic mean, which is calculated as the sum of the monthly averaged equity for the particular year for each bank. Schedule IS is the source for data on the banks' profits and schedule BS is the source for data on equity.

Figure 19. Net interest margin

To analyze the profitability of defined group of banks as well as the total banking sector, the ratio between banks' interest margin and total assets is calculated. The interest margin is measured using the following formula: (Interest Income – Interest Expense). This amount thus is divided by total assets of a particular group and multiplied by 100. The schedule IS and BS is the source of data for the interest income and interest expenses and for total assets.

Figure 20. Liquid assets to total assets

Each bank group ratio between liquid assets and total assets is calculated as follows. First, liquid assets of each bank are added up in the banks group. Second Total assets for each bank group are added up. The sum of liquid assets of each bank group and total assets of each banks group are expressed as a ratio and thus multiplied by 100.

Liquid assets are calculated as the sum of the cash, balances with BPK, accounts with other banks, placements abroad and security investments. Schedule BS is the source for data on liquid assets and for total assets for each bank and thus bank group.

Figure 21. Structure of liquid assets

The figure plots the components of liquid assets as a share in total liquid assets for each year. Total assets are presented by line which corresponds to the right axis (in volume).

Figure 22. Loan to deposit ratio

The ratio between loans granted and customer deposits received is calculated as follows. First, total loans granted by each bank are added up for the particular group and for the particular period. Second, the customer deposits received for each bank in the bank group are added up for the specific period. The totals then are expressed as a ratio and multiplied by 100. The ratio for the total banking sector is calculated in the same manner. Schedule BS/LBM is the source for the data on loans granted whereas schedule BS/DBM is the source for the data on deposits.

Table 9. Insurance companies assets, by size

The table on insurance companies assets by size illustrates the comparison between categories of the companies based on the size of their assets. There is distinction regarding the ownership criteria. Thresholds used are based on functional approach. The source of data is balance sheet of insurance companies reported to the insurance companies supervision department of the BPK.

Table 10. Insurance companies assets, by ownership

Same as with the table 2, criterion for the distinction between insurance companies is ownership criteria. Source for the table are the companies balance sheets reported to the respective supervision department of the BPK.

Figure 26. Other financial intermediaries lending activity

As stated, except commercial banks, also other financial intermediaries, known as micro financial institutions, are lending to the domestic economy, mainly to the households. Using the data from banking supervision department, in the figure 26 is presented the outstanding amount of their loans to the domestic economy, and the share of their lending to total loans extended from financial sector.

7. LIST OF FINANCIAL CORPORATIONS IN KOSOVO[14]

Commercial banks

(As of June 2005)

PROCREDIT BANK

Address: Skenderbeu Street, Pristina

Phone: ++381 38/ 240 248

Fax: ++38138/ 248 777

E-mail: info@procreditbank-kos.com

Website: www.procreditbank-kos.com

Balance Sheet

(Outstanding amounts, end of period, in thousands of EUR)

Assets	Amount
Cash on hand and balances with BPK	45,076
Securities	111,721
Deposits and placements with commercial banks	59,188
Net loans to non-financial institutions	138,781
Fixed assets	4,324
Other assets	4,849
TOTAL ASSETS	**363,939**

Liabilities	Amount
Costumer deposits	320,744
Borrowings	15,363
Other liabilities	9,231
Total liabilities	345,338
Equity	18,600
TOTAL LIABILITIES	**363,939**

[14] Ordering of financial corporations within a sub-sector is made based on the date of establishment;

NEW BANK OF KOSOVO

Address: Mother Teresa No. 54, Pristina
Phone: ++381 38/223 976
Fax: ++381 38/225 871
E-mail: brk-bank@brk-bank.com
Website: www.brk-bank.com

Balance Sheet

(Outstanding amounts, end of period, in thousands of EUR)

Assets	Amount
Cash on hand and balances with BPK	9,367
Deposits and placements with commercial banks	21,398
Net loans to non-financial institutions	23,193
Fixed assets	678
Other assets	1,420
TOTAL ASSETS	**56,056**

Liabilities	Amount
Costumer deposits	48,405
Borrowings	...
Other liabilities	1,652
Total liabilities	50,057
Equity	5,999
TOTAL LIABILITIES	**56,056**

BANK FOR BUSINESS

Address: Vellusha street, no.6, Pristina
Phone: ++381 38/ 244 666
Fax: ++38138/ 243 656, 243 657
E-Mail: hq@bpb-bank.com
Website: www.bpb-bank.com

Balance Sheet

(Outstanding amounts, end of period, in thousands of EUR)

Assets	Amount
Cash on hand and balances with BPK	10,035
Deposits and placements with commercial banks	9,084
Net loans to non-financial institutions	28,578
Fixed assets	1,358
Other assets	2,214
TOTAL ASSETS	**51,269**

Liabilities	Amount
Costumer deposits	45,789
Borrowings	753
Other liabilities	339
Total liabilities	46,881
Equity	4,388
TOTAL LIABILITIES	**51,269**

ECONOMIC BANK

Address: UCK Street No. 5, Pristina
Phone: ++381 38/248 997
Fax: ++381 38/229 253
E-mail: -
Website: www.bankaekonomike.com

Balance Sheet

(Outstanding amounts, end of period, in thousands of EUR)

Assets	Amount
Cash on hand and balances with BPK	6,522
Deposits and placements with commercial banks	13,250
Net loans to non-financial institutions	19,402
Fixed assets	766
Other assets	540
TOTAL ASSETS	**40,480**

Liabilities	Amount
Costumer deposits	34,835
Borrowings	...
Other liabilities	406
Total liabilities	35,241
Equity	5,239
TOTAL LIABILITIES	**40,480**

RAIFFEISEN BANK KOSOVO

Address: UÇK Street 51, Pristina
Phone: ++381 38/ 226 400, 401
Fax: ++38138/ 226 408
E-mail: info@raiffeisen-kosovo.com
Website: www.raiffeisen-kosovo.com

Balance Sheet

(Outstanding amounts, end of period, in thousands of EUR)

Assets	Amount
Cash on hand and balances with BPK	23,770
Deposits and placements with commercial banks	28,753
Net loans to non-financial institutions	130,341
Fixed assets	3,188
Other assets	2,245
TOTAL ASSETS	**188,297**

Liabilities	Amount
Costumer deposits	163,783
Borrowings	2,000
Other liabilities	4,663
Total liabilities	170,446
Equity	17,851
TOTAL LIABILITIES	**188,297**

CREDIT BANK OF PRISTINA

Address: Tirana Street Nr. 29, Pristina
Phone: ++381 38/249 851
Fax: ++381 38/248 468
E-mail: -
Website: -

Balance Sheet

(Outstanding amounts, end of period, in thousands of EUR)

Assets	Amount
Cash on hand and balances with BPK	11,432
Deposits and placements with commercial banks	2,769
Net loans to non-financial institutions	29,242
Fixed assets	1,304
Other assets	2,154
TOTAL ASSETS	**46,901**

Liabilities	Amount
Costumer deposits	40,045
Borrowings	...
Other liabilities	1,765
Total liabilities	41,810
Equity	5,091
TOTAL LIABILITIES	**46,901**

KASABANK

Address: Pal Palucaj No. 1, Pristina
Phone: ++381 38/543 688
Fax: ++ 381 38/543 699
E-Mail: -
Internet: www.kasabank.com

Balance Sheet

(Outstanding amounts, end of period, in thousands of EUR)

Assets	Amount
Cash on hand and balances with BPK	20,080
Deposits and placements with commercial banks	10,277
Net loans to non-financial institutions	72,227
Fixed assets	5,069
Other assets	525
TOTAL ASSETS	**108,178**

Liabilities	Amount
Costumer deposits	91,226
Borrowings	6,805
Other liabilities	122
Total liabilities	98,153
Equity	10,025
TOTAL LIABILITIES	**108,178**

Insurance Companies

DARDANIA
Pristina
Mother Teresa str.

DUKAGJINI
Pristina
Bulevardi i Dëshmorëve str.

KOSOVA E RE
Pristina
Fazli Graiqevci str. No.5

SIGURIA
Pristina
Qamil Hoxha str No.15

INSIG - Tirana
Branch “INSIG”
Pristina
Pejton str. No.4

SIGAL - Tirana
Branch “Sigal - Drini”
Prizren
Vellusha e Poshtme str. No.16

SIGMA - Tirana
Branch "SIGMA"
Pristina
Pashko Vasa str.

CROATIA
Pristina
Str.Fehmi Agani, str. No 69, D/1-2

Pension funds

KOSOVO ELECTRIC COMPANY
Pristina
Nena Tereza str. No.36

POST AND TELECOMMUNICATIONS OF KOSOVO[15]
Pristina
Dardania str.

BANKING AND PAYMENTS AUTHORITY OF KOSOVO
Pristina
Garibaldi str. No.33

[15] PTK Pension fund is comprised from two pension funds. Pension fund PTK “A” and PTK “B”.

RAMIZ SADIKU
Pristina
Fehmi Agani str.

PROCREDIT BANK
Pristina
Skenderbeu str.

KOSOVA
Pristina
Nena Terezë str

Other financial intermediaries

ABU APMP
Pristina
Bedri Shala str, 38C

FINCA Kosovo
Prizren
Komuna e Parisit str No.23

KOSOVO ENTERPRISE PROGRAM
Pristina
Bedri Pejani str. No.4

BESLIDHJA
Pristina
Lidhja e Prizrenit str. No.15

MERCY CORPS INTERNATIONAL
Pejë
M.Popoviq str. No.150/3 67/A

BALKANACTIE
Shtime
Tirana str.

INTERNATIONAL ORGANIZATION FOR MIGRATION
Pristina
Ismail Qemaili str.18

START
Drenas
Rasim Kiqina str. No. 5

GRAMEN TRUST
Pejë
Marshal Tito str. No.154

CORDAID
Gjakovë
Nena Terezë str.

MFI - Ce.L.I.M
Gjakovë
UCK str. No.

DEG
Pristina

KOSINVEST
Podujevë
Zahir Pajaziti str. No.96

KREDITIMI RURAL I KOSOVES
Pristina
Procredit Bank Building 3rd Floor

PERSPEKTIVA 4
Klinë
Lidhja e Prizrenit str.

MESHTEKNA
Dragash

KOMITETI I BOTES ISLAME
Podujevë

Financial auxiliaries

PROCREDIT BANK WESTERN UNION
Pristina
Skenderbeu str.

UNIONI FINANCIAR TIRANA
Pristina
Pejton, Perandori Justinian str. No.1E

EURO-B
Drenas
Lagja e re str. No.2

ABD
Pristina
19 Nentori str. No.8

EURO-CUFA
Pristina
Marevci str. No.43

NBS
Pristina
Marevci str. No.45