



BANKA QENDRORE E REPUBLIKËS SË KOSOVES
CENTRALNA BANKA REPUBLIKE KOSOVA
CENTRAL BANK OF THE REPUBLIC OF KOSOVO

Annual Report 2010

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LIST OF ABBREVIATIONS

ATM	Automated Teller Machine
BEC	Broad Economic Categories
BKT	Banka Kombëtare Tregtare
BPB	Banka për Biznes
CBK	Central Bank of the Republic of Kosovo
CEFTA	Central European Free Trade Agreement
CPI	Consumer Price Index
DJI	Dow Jones Industrial Average
DLE	Department of Labor and Employment
ECB	European Central Bank
EU	European Union
EULEX	European Union Rule of Law Mission in Kosovo
FDI	Foreign Direct Investment
GDP	Gross Domestic Product
HHI	Herfindahl-Hirschman Index
IECS	Interbank Electronic Clearing System
IMF	International Monetary Fund
IPI	Imports Price Index
KEK	Kosovo Energy Corporation
KMB	Komercijalna Banka
KPST	Kosovo Pension Savings Trust
KRK	Credit Registry of Kosovo
MEF	Ministry of Economy and Finance
MLSW	Ministry of Labor and Social Welfare
MTPL	Motor Third Party Liability Insurance
NFA	Net Foreign Assets
NLB	Nova Ljubljanska Banka
NPHSO	Non-profitable Household Service Organizations
NPL	Non-Performing Loans
ODC	Other Depositing Corporations
PAK	Privatization Agency of Kosovo
PCB	Procredit Bank
POS	Point of Sale
pp	percentage point
PPI	Producer Price Index
PTK	Post and Telecommunication of Kosovo
RBK	Raiffeisen Bank Kosovo

ROAA	Return on Average Assets
ROAE	Return on Average Equity
SEE	Southeastern Europe
SKPF	Slovenian Kosovo Pension Fund
SOK	Statistical Office of Kosovo
TEB	Türk Ekonomi Bankasi
TPL	Third Party Liability
UNMIK	United Nations Mission in Kosovo
VAT	Value Added Tax

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Cover Letter

It is my special honor and pleasure to present the Annual Report 2010, which represents a comprehensive report, including the most significant developments in Kosovo's economy, covering the real, fiscal, financial and external sector. The Central Bank of the Republic of Kosovo pays a particular attention, just like to any other duty, to the wider public information, and this is exactly the reason why the CBK staff shows an extraordinary commitment when drafting the Annual Report, making efforts to include each year innovations and new data that explain and disclose all important functions exercised by the CBK. The Annual Report 2010 has also innovations compared to last year's report and it also contains more data, which have been considered to be important to the wider public.

The World economy in 2010 recorded an annual growth of around 5%, which exceeded the preliminary International Monetary Fund forecasts, and this growth was, first of all, driven by the economic growth in the USA and Japan, the growth of industrial production, stabilization of financial markets and growth in the World trade volume.

The first recuperation signs started to emerge in Southeastern Europe countries in 2010, although the economic activity was still fragile and unbalanced among the SEE countries. In 2010, an increase of exports was recorded in these countries, following a drastic decline that was recorded in 2009, and as a result, all SEE countries other than Kosovo recorded a decline in trade deficit, which also brought about a decline in current account deficit.

Kosovo economy in 2010 recorded a real growth of Domestic Gross Product of 4.0%, while the GDP nominal value was euro 4.2 billion. Differently from 2009, where the growth was mainly driven by the increase of public expenditures and decrease of prices, the growth in 2010 was driven by the increase of consumption and investments in private sector. An average increase of prices of 3.5% was recorded during 2010, which was mainly driven by the increase of prices of food products.

A serious problem for Kosovo also in 2010 keeps remaining the high unemployment rate, which is estimated to be around 45%, of course, we have also to consider the fact that a percentage of population reaching the labor age is not included at all in the labor market. We have certainly to take into consideration herein a very high level of participation of informal sector; therefore, this percentage should be smaller. This issue has become more vulnerable by the young structure of Kosovo population, since a significant number of new jobseekers add up in Kosovo on annual basis, while the number of jobs generated within a year is quite low.

Kosovo financial sector did not continue growing as in the previous years, mainly due to a slower growth in banking system, which has the largest share within the financial sector. The growth of bank assets was around 11%, which is mainly driven by lending activity and investments in securities. Slowdown in lending by banks had an impact on banks to orientate a part of their investments abroad, mainly in securities. The increase of investments in securities was also driven by recuperation of international financial markets during this period. Loan structure was dominated by loans to enterprises (over 70%), while among the enterprises the largest part of loans was used by trade enterprises (over 50%).

There is an increase of deposits during 2010 compared to 2009 (annual growth of 11%), yet it was slower than in the previous year. Deposit structure was dominated by household

deposits with over 67% (growth of 7% compared to the previous year), while deposits of enterprises had a share of 27 %.

In spite of challenges faced by the Central Bank of the Republic of Kosovo, it managed to maintain the country's financial stability and it was always proactive in taking numerous measures to ensure a financial stability. The frequency of on-site and off-site examinations has also increased in 2010, in order to closely follow up activities of all financial institutions operating in Kosovo and fulfilling therein one of the most important CBK functions, namely the maintenance of country's financial stability.



Prof. Dr. Gazmend Luboteni

Chairman of the Central Bank Board

Governor's Speech

Kosovo's economy in 2010 continued to grow, based mainly on the growth of consumption and investments. Improvements in the global economy had a significant impact on the growth of Kosovo's exports and received remittances. Inflationary pressures at the global level were also reflected in the Kosovo's economy, due to the high dependency of our economy on imports. Despite the increase of exports, trade deficit remains very high and calls for finding a more sustainable model of growth and economic development for Kosovo.

The country's financial sector continued the increasing trend. Main financial soundness indicators suggest a high level of stability for the Kosovo's banking system. Reaching at 59.7 percent of GDP, banking system assets were among the main contributors to the financing of consumption and investments in the country. Although still high, the degree of the banking system concentration continued its downward trend. At the same time, the insurance industry marked a reduction of tariffs for border insurance policies and an increase of the claims reimbursement level. Kosovo Pension Savings Trust marked a price increase per share units and better return on investments. In close cooperation with the Ministry of Finance, concrete steps were taken in the creation of a modern infrastructure for the securities market.

Besides providing stability for the financial sector, the CBK continued to improve the quality of its services to authorities, financial community and the public. It has improved the quality of supply with euro banknotes and coins and it was completed the full electronization of payment orders for the major CBK customers. Also, the volume and value of interbank payments increased, while the National Payments Council became fully operational. The investment of the CBK assets is made under high security, adequate liquidity and reasonable return on investments. Within the project on the development of the business environment, the Credit Registry started the project of upgrading the credit information, which is expected to result in a reduction of credit risk and consequently of loan interest rates.

In 2010, the Assembly of Kosovo approved the new Law on the Central Bank of the Republic of Kosovo, with more duties and responsibilities for the CBK in providing financial and macroeconomic stability of the country. This year was also marked by the approval of the Law on Deposit Insurance System and initiation for amendments and drafting of other laws relevant to the financial sector (Law on banks, microfinance institutions and non-bank financial institutions, the Law on Compulsory Third Party Liability Insurance, the Law on payment systems, etc.), expected to be approved during 2011. The upgrading of the legal framework of the financial sector is in line with the efforts aimed at the enhancement of the business environment and the generation of new investments by foreign as well as domestic investors.

In the field of statistics, for the first time was started with the reporting of balance of payments statistics to the IMF on quarterly basis, while in the field of economic and financial analysis should be emphasized the compilation of 'stress test' for the banking system, monthly compilation of early warning indicators as well as the compilation and publication of the first issue of the Financial Stability Report for Kosovo. Research work of the CBK employees was awarded for the second time with the prestigious "Olga Radzyner" award for young researchers. All these prove the high competence of the CBK employees in the communication of our work to the domestic and international institutions and public.

Given the fact that the CBK mainly reflects its employees, the management will continue to strongly support the dedication and high level of employees' competences, who together with the CBK Board and Executive Board, had a key role in providing quality work even under the conditions of the management crisis, which the CBK suffered during 2010.

I would like to thank all CBK employees for their precious contribution during 2010. In fact, their dedication makes me even more confident that together we will successfully manage the challenges ahead.



Gani Gërguri

Central Bank Board, Executive Board and Audit Committee

Central Bank Board

Pursuant to the Law on Central Bank of the Republic of Kosovo, the decision making bodies of the Central Bank are: the Central Bank Board, the Executive Board and the Governor.

Pursuant to Article 79, paragraph 2 of Law on the CBK, the Central Bank Board is composed of the Governor, the General Director of Treasury and three (3) non-executive members, whereas the authorities and duties of this Board are defined under Article 35 of Law on the CBK. The Central Bank Board, as of 31 December 2010, was composed of the following members:

Gazmend Luboteni, Chairman of the Central Bank Board;

Lulzim Ismajli, Director of the Treasury (member of the Central Bank Board);

Mejdi Bektashi, member of the Central Bank Board;

The Deputy Governor for Central Banking Operations, Gani Gërguri, has been an Acting Governor as of 26 July 2010.

The Executive Board is composed by the Governor, who is the chairman, and by the Deputy Governors, and is in charge of implementation of the Central Bank policies and its operations. On 31 December 2010, the Executive Board was composed of the following members:

Mr. Gani Gërguri, Deputy Governor for Central Banking Operations and Acting Governor as of 26 July 2010.

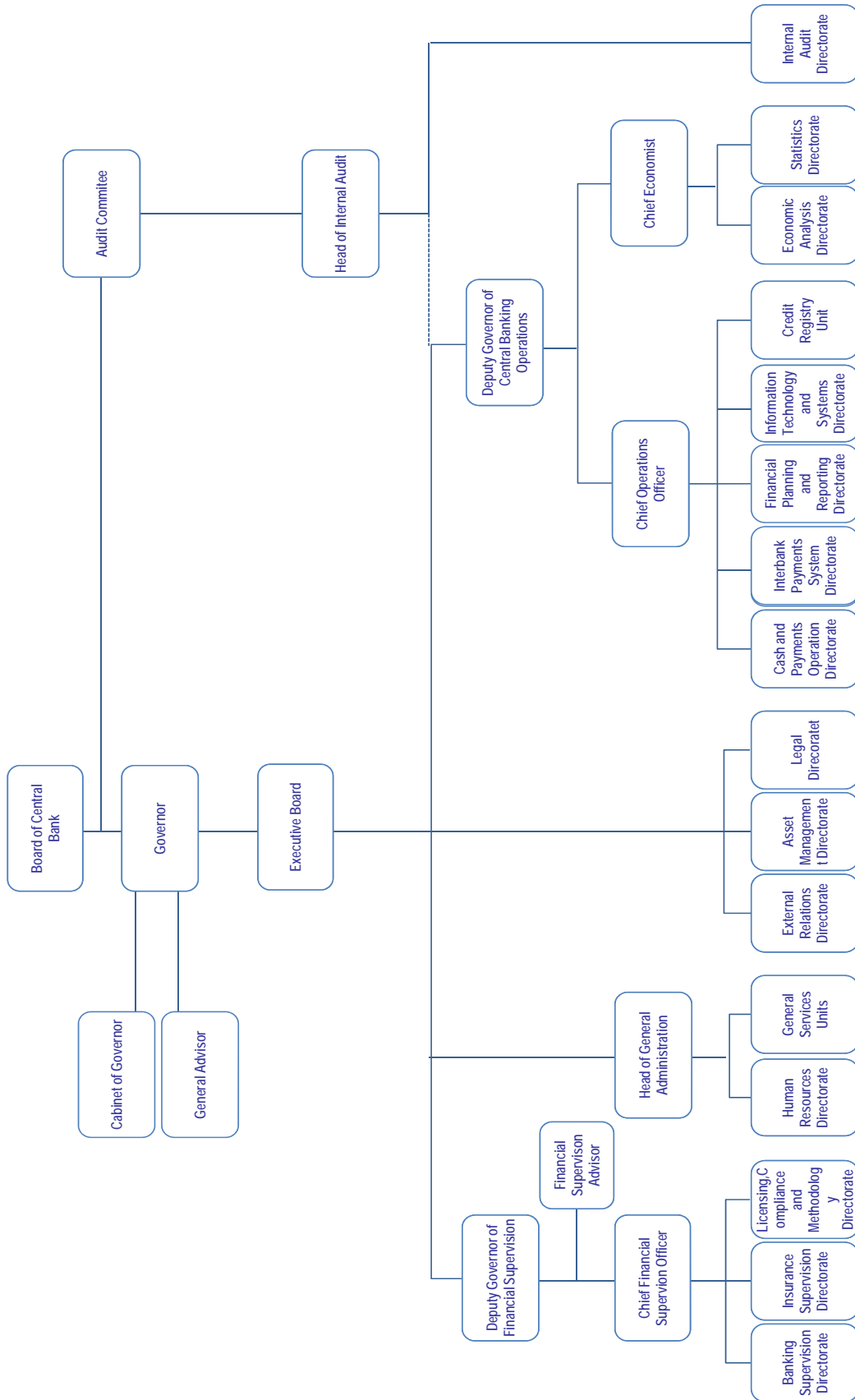
Mr. Nexhat Kryeziu, Deputy Governor for the Supervision of Financial Institutions.

The Audit Committee is appointed by the Central Bank Board and is composed of three members; two non-executive members selected among the Central Bank Board and one member as an external expert being competent in accountancy or auditing area. On 31 December 2010, the Audit Committee was composed of the following members:

Gazmend Luboteni, Chairman of the Central Bank Board.

Sejdi Rexhepi, member of the Central Bank Board.

Organizational Structure of the CBK as of 31 December 2010



1. Executive Summary

Year 2010 may be considered as a year of global economy improvement, which reflects the positive effects of the financial interventions of the respective institutions in the countries affected by the crisis, with the purpose of overcoming the consequences of the global crisis. The global economy recorded a growth rate of 5.0 percent in 2010. The improvement of the performance in the economy was also reflected in the trading activity, which recorded a growth rate of 11.4 percent at the global level, compared to the 11.0 percent decline in 2009. As a result of such improvements, mainly generated by developing countries, economies of Southeastern Europe (SEE) showed the first signs of improvement. Nevertheless, the domestic demand in the SEE countries continues to represent a concerning factor, having not shown solid signs of recuperation, which in effect may hamper the sustainable economic growth for these countries.

Kosovo's economy continued to have a positive growth rate also during 2010. Estimations indicate a real growth rate of 4.6 percent in 2010. Compared to the year 2009, where the public sector was the main driver of the growth, in 2010 the private sector took the lead, by becoming the main generator of economic growth in Kosovo. In 2010, inflation recorded an average rate of 3.5 percent, while the inflationary pressures were more intense during the second half of the year. Similar to the previous years, inflation in Kosovo was mainly a result of the increased food prices, which increased at the global level. As a result of the high dependency of Kosovo's economy on imports, the increase of prices at the global level was considerably reflected also in the price level in Kosovo.

Kosovo's financial sector continued with stability and growth also during 2010. The value of financial sector assets reached at euro 3.2 billion in 2010, recording an annual growth rate of 13.7 percent. Banking system assets continue to represent the largest share of financial sector total assets with a share of 77 percent, while pension funds, as the second largest player in the financial sector, manage over 15 percent of total financial sector assets. Deposits and loans, as the main components of the banking system balance sheet, recorded a growth rate of 11.0 percent and 13.2 percent, respectively. The growth rate of loans in 2010 was higher than in 2009, whereas deposits increased at a lower growth rate. Kosovo's banking system in 2010 continued to have a degree of market concentration, where the three largest banks managed 77.4 percent of the total banking system assets. However, the concentration ratio in banking market has declined continuously during the recent years. Kosovo's banking system maintained the high level of sustainability also in 2010, with a capital adequacy ratio of 18.7 percent. During this year, the share of the non-performing loans to total banking system loans recorded an increase, reaching at 5.9 percent. Nevertheless, the coverage ratio of non-performing loans with loan-loss provisions continues to be high.

Kosovo's balance of payments continues to be characterized with a high current account deficit, while the capital and financial account concluded the year 2010 with positive balances. The ratio between the current account deficit and Gross Domestic Product (GDP) in 2010 was 16.6 percent, which is similar to the previous year. The high level of the trade deficit (45.8 percent of GDP) represents the main contributing factor to the current account deficit. In year 2010, Kosovo's exports grew by 77.8 percent, while imports recorded a growth rate of 10.8 percent. However, the larger weight of exports in the overall amount of traded goods led to a deepening of the trade deficit, in spite of the increase of exports. Nevertheless, the increase of exports during this period led to the increase of the export-to-import ratio at 13.7 percent. The positive balances of the income account and the current

transfers account continued to contribute to the softening of the current account deficit. Within the capital and financial account, 'other investments' recorded a more significant growth, while also foreign direct investments recorded a positive growth rate.

The CBK continued applying the best international practices in the area of licensing, regulation and supervision of the financial institutions. Significant investments have been carried out in this context towards advancing the risk profile-based supervision in financial sector and enhancing the cooperation with central banks and relevant supervision authorities of other countries, such as Turkey, Germany, Austria, Slovenia, Montenegro, etc.

In the area of traditional central bank operation, the CBK has successfully played its role as a government fiscal agent and banker, advancing the processes which relate to account transactions, financial assets management, interbank payment systems and supplying the economy on timely basis with adequate denominations of euro banknotes and coins. Within the Interbank Electronic Clearing System (IECS), a considerable growth both in volume and in value of payment transactions was recorded during 2010. Around 3.9 million transactions with total value of euro 4.66 billion were canalized through IECS during 2010.

Also, during 2010, in cooperation with USAID, preparations have been carried out to further advance the Credit Registry with the purpose of reducing the asymmetry information in the lending area.

Assets' security remains the main pillar of the CBK Investment Policy. Owing to a careful risk profile analysis of institutions and places where the CBK balance assets have been invested, it was ensured not only the necessary liquidity, but also the reasonable return from invested assets. In addition to the Treasury, in 2010, agreements on certain maturity investments have also been reached with other large CBK depositors. CBK Investment Committee as well as Liquidation Committee together with Treasury have assessed on regular basis corresponding banks with purpose of ensuring the fulfillment of criteria required by the CBK investment policy.

Parallel to standard audit envisaged under the Annual Plan of the Head of Internal Audit (HIA), particular reports on development of investments, both in money market and in the securities market have been prepared in 2010. Moreover, based on the Stand-By" arrangement, the government accounts kept within CBK have been audited on regular basis, and the auditing spectrum has been extended towards financial supervision and the information technology area.

2. External Economic Environment¹

2.1. World Economy

According to the International Monetary Fund (IMF) estimations, the world economy recorded an annual growth of 5 percent in 2010 (Table 1). The realized growth rate exceeded the preliminary IMF forecasts (mid 2010) by 0.75 percentage points (pp). This difference mainly resulted from the positive impact of the economic growth in the USA and Japan. The economic growth of these two economies, to a considerable extent, was a result of the increased domestic consumption during the fourth quarter of 2010. Moreover, the growth of industrial production, the stabilization of financial markets as well as the increase of the trade volume globally, had a positive impact the world economy revival. However, the recuperation of the world economy is considered to be imbalanced in terms of the intensity and the geographic position, since developing countries continue to grow at a faster pace, compared with the growth rate of the developed countries.

According to the IMF estimations, in 2010, the economic growth in developed countries reached at 3 percent. USA recorded an economic growth of 2.8 percent, which mainly resulted from the growth of the domestic consumption and the positive impact of the trade activity, since exports continued to grow faster than imports. A positive economic growth was recorded also by Eurozone, which marked an annual growth rate of 1.7 percent, despite the numerous budgetary problems faced by some member states. Among the developed countries, Japan marked the highest economic growth in 2010, recording a growth rate of 3.9 percent. Improvement of economic activity in developed countries mainly relied on the increase of investments, exports and the domestic consumption.

Table 1. World GDP growth rate, in percentage

Description	2009	2010	2011*
World GDP	-0.5	5.0	4.4
Developed countries	-3.4	3.0	2.4
USA	-2.6	2.8	2.8
Euro-zone	-4.1	1.7	1.6
Japan	-6.3	3.9	1.4
United Kingdom	-4.9	1.3	1.7
Developing countries	2.7	7.3	6.5
Russia	-7.8	4.0	4.8
China	9.2	10.3	9.6
India	6.8	10.4	8.2

Source: IMF (2011)

* Projections

Regarding the developing countries, according to the IMF, the economic growth continues to be powerful. In 2010, developing countries on average grew by 7.3 percent, whereas the Asiatic countries and some countries from middle and South Africa led with the highest economic growth rates. The highest growth rate of 10.4 percent was recorded in India,

¹ Developments in the World economy and in the Southeastern Europe are based on these publications: Business Monitor International (2010), ECB (2010), European Commission (2010), (2011), Eurostat (2010), IMF (2010), (2011) and World Bank (2010),

followed by China with a growth rate of 10.3 percent. Economic growth in these countries was constantly supported by expansionary monetary and fiscal policies, high level of domestic consumption and capital inflows.

During 2010, the fiscal policies, especially in developed countries, were oriented towards the consolidation of budgetary expenditures, which previously marked a record high growth as a result of efforts to ameliorate and prevent the financial crisis. The deterioration of public finances was more significant in Eurozone, where some of the member states are facing high budget deficit rates.

Countries like Ireland and Greece, being unable to refund the public debt, were forced to ask for assistance from other countries and international financial institutions. In the course of attempts to prevent the deepening of the budgetary crisis, in May 2010, the EU member states decided to establish the European Financial Stability Mechanism. In order for this mechanism to be functional, EU member states, European Central Bank (ECB) and the IMF allocated an amount of euro 750 billion, which was designated to overcome the potential budgetary crises. Moreover, the majority of the Eurozone member states have initiated deep fiscal reforms, basing the fiscal consolidation in two areas: cutting down the budgetary expenditure or achieving a balance between the decrease of revenues and expenditures. However, the fiscal consolidation in some Eurozone member states by rapid decrease of the government expenditures might bring about other consequences to the economies of these countries, such as by slowing down the economic growth and increasing the unemployment rate.

Financial sector in the global level continued to mark positive results during 2010, with a significant support by expansionary monetary policies. The activity in the stock markets during this year was characterized by a growing trend and lending to both the financial and the real sector continued to grow, although at a lower level than before the financial crisis emerged. Nevertheless, the problems of the Eurozone countries with public debt led to the increase of investors' uncertainty in financial markets. High rates of budget deficit in some of the Eurozone countries negatively affected the credit ranking of these countries, and consequently, the premium risks for Credit Default Swaps (CDS) and guarantees recorded a considerable increase. Premiums for CDS of the countries like Ireland and Greece were up to 5 pp higher than those of Germany, which are characterized with the lowest level of riskiness. In addition, aiming at stabilizing and restoring the trust in the financial markets, in May 2010, for the first time in its history, the ECB decided to intervene in the bond markets, by buying state and private bonds, in order to influence the debt costs and increase the liquidity in the markets. The ECB's action was accepted with full optimism by investors, since these measures helped in neutralizing the turbulences that had overwhelmed the European markets.

Base interest rate in the Eurozone remained at the level of 1.0 percent, which is set since May 2009, after the decision of the ECB to decrease it from 2.0 percent. In addition, the marginal rate of lending and deposits remained unchanged at 1.75 and 0.25 percent, respectively.

Also, the financing rates set by the USA Federal Reserve remained unchanged, ranging from 0.00 to 0.25 percent. Whereas, interest rates in the interbank market marked an increase during 2010, where three-month EURIBOR recorded a growth rate of 1.02 percent (0.712 percent in December 2009) and the three-month LIBOR recorded a growth rate of 0.749 percent (0.605 percent in December 2009).

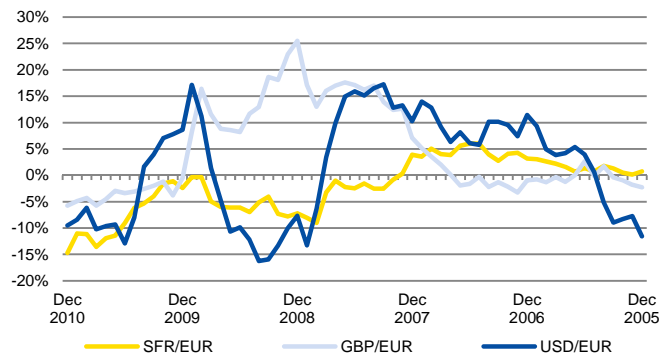
In the end of 2010, the price index in the USA recorded an annual growth rate of 1.5 percent, whereas based on statistics published by EUROSTAT the annual growth rate of the price index in the Eurozone was 2.2 percent.

During 2010, the stock markets in USA and Japan were characterized with improved performance. In December 2010, the stock exchange market index in the USA (*Standard & Poor's 500*) and in

Japan (*Nikkei 225 Stock Average Index*) recorded an increase of 11.8 and 0.84 percent, respectively, compared to December 2009. Whereas, the stock exchange market index that summarizes the European stocks (*Dow Jones Euro Stoxx*) recorded a decrease of 2.82 percent.

In the end of 2010, Euro recorded a significant annual depreciation against the main global currencies (Figure 1). The exchange rate with the US Dollar and British Pound recorded an annual depreciation rate of 9.5 percent (1.322 USD/EUR) and 5.7 percent (0.848 GBP/EUR), respectively. The highest depreciation rate of euro was recorded against the Swiss Franc by 14.7 percent (1.281 SFR/EUR).

Figure 1. Annual change of Euro against SFR, GBP and USD



Source: ECB (2011)

2.2. Southeastern Europe

Two years after the financial global crisis emerged, the Southeastern Europe (SEE) countries² started to show the first signs of the economic recuperation. However, it should be underlined that the improvements in the economies of SEE countries are still fragile and not balanced among them. Improvements in the global economy in 2010, especially the recuperation of EU countries' economies, resulted in the growth of SEE countries exports. Nevertheless, these economies continue to face a low level of domestic demand compared to the pre-crisis period, which has reflected into a higher unemployment rate and application of rather conservative lending policies by banks. During 2010, most of the SEE countries reported positive GDP growth rates, and, according to the European Commission's estimations, the average GDP growth for the entire region in 2010 was 1.7 percent.

In 2010, exports of the SEE countries started to recover after experiencing a drastic decline in 2009. The increase of domestic consumption, especially in the EU countries, which are the key trading partners of these regional countries, had a positive impact in most of these countries, which reported two-digit growth rates of exports. As a result, all SEE countries, except Kosovo, reported a decline of trade deficit, which consequently contributed in the reduction of the current account deficit.

During 2010, all of the SEE countries concluded the year with negative budget balance. However, the budget deficit to GDP ratio increased only in Croatia, reaching at 5.7 percent (4.1 percent in 2009) and in Serbia, reaching at 4.5 percent (4.3 percent in 2009). Other

² Albania, Bosnia and Herzegovina, Bulgaria, Croatia, Kosovo, Macedonia, Montenegro, Romania and Serbia.

countries, through the measures taken to consolidate the fiscal sector, have successfully decreased the budget deficit. During 2010, countries such as Kosovo, Bosnia and Herzegovina, Serbia and Romania signed agreements with the IMF to obtain financial support. In addition, in 2010, Albania and Serbia emitted securities to finance the budget with an amount of euro 300 million and euro 199 million, respectively. Public debt of SEE countries further increased in 2010, reaching at 43 percent of GDP, compared to 41 percent of GDP in 2009. Albania marked the highest rate of public debt to GDP ratio in 2010, which reached at 61.9 percent (60.6 percent in 2009), followed by Montenegro with 49.4 percent (43.5 percent in 2009) and Bosnia and Herzegovina with 43 percent of GDP (39.1 percent in 2009).

The relatively high unemployment rates continued to characterize the economies of the SEE countries also during 2010. The countries with the highest unemployment rate in the region include Kosovo (around 45 percent), Bosnia and Herzegovina (around 43.2 percent) and Macedonia (around 31.7 percent).

Regarding the currencies of SEE countries, in 2010, the Albanian Lek depreciated against Euro by 1.2 percent, reaching at 138.8 ALL/EUR, whereas the Serbian Dinar depreciated against Euro by 10.6 percent, reaching at 106.7 RSD/EUR. Croatian Kuna (7.39 HRK/EUR) and Macedonian Denar (61.5 MKD/EUR) were more stable against Euro during this period.

3. Kosovo Economy

3.1. Real Sector

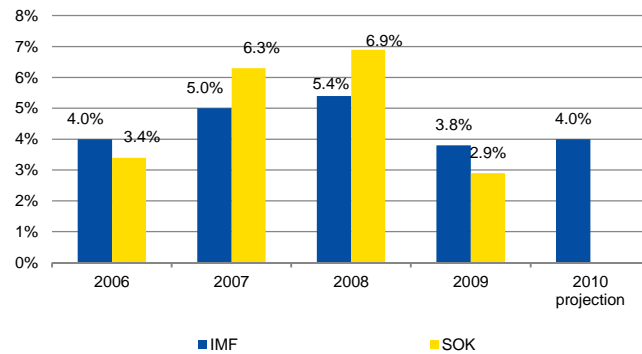
Kosovo's economy continued with the increasing trend also during 2010, marking a higher real growth rate than in the year 2009. The improvement of the performance of the global economy in 2010 has positively affected the economy of Kosovo, making the private sector the key promoter of the economic growth in Kosovo. Kosovo's banking system had quite a significant role in financing the domestic consumption and investments. Another significant contributor which has financed the domestic consumption in the country, were the migrants' remittances, which also increased as a result of the improvements in the developed economies. In spite of continuous economic growth, the domestic production remains at a very low level, thus making the country's economy highly dependent on the import of goods from abroad, which has continually brought about high rates of current account deficit. Despite the facilities for the development of trade, created by the use of Euro as official currency and the participation in the Central European Free Trade Agreement (CEFTA), yet Kosovo faces trade problems in relation with the regional countries, such as Serbia and Bosnia and Herzegovina, which are not implementing the free trade agreement with respect to Kosovo. However, Kosovo's trade with other countries marked a very positive trend during 2010, especially with regard to exports, due to the increase of the demand in global economy.

The relatively high unemployment rate in Kosovo remains one of the main challenges of the economy. The SOK Labour Force Questionnaire (2009) suggests that the unemployment rate in Kosovo in 2009 was around 45 percent of the labour force. Based on the actual trend of the economic growth and the ability of the economy to absorb the pressure from new entrants in the labour market, it may be considered that the unemployment rate is not expected to drop significantly in the short-run.

3.1.1 Gross Domestic Product³

The Gross Domestic Product (GDP) of Kosovo is estimated to have recorded a real growth rate of 4.0 percent in 2010. The nominal GDP in 2010 amounted at euro 4.2 billion (IMF, 2011). Contrary to year 2009, when public sector was the key promoter of the economic growth, in 2010, the private consumption and investments were the main drivers of economic growth in the country. The share of private consumption in the total consumption in Kosovo was 84.2 percent in 2010 compared to 83.7 percent in 2009. Private sector also dominates the overall structure of investments in the country, with a share of 66.0 percent to total investments, whereas public investments recorded a share of 34.0 percent. In

Figure 2. Real GDP growth



Source: IMF (2011) and SOK (2010a)

³ The data source for GDP is the International Monetary Fund, World Economic Outlook, April 2011.

comparison with the previous year, the share of public investments to total investments in Kosovo recorded a slight decline.

The increase of private and public sector consumption led to a higher growth rate of the overall consumption in 2010, compared to year 2009. The real growth rate of total consumption in 2010 was 3.3 percent (0.9 percent in 2009). Also overall investments in Kosovo marked positive developments during 2010, recording a real growth rate of 7.8 percent (9.8 percent in 2009). Private sector investments recorded a real growth of 5.9 percent in 2010, compared to the 2.2 percent growth rate in the previous year. The increase of private sector investments has resulted from the increase of both domestic and foreign investments. Public sector investments also contributed to the increase of total investments in the country, although growing with a slower pace compared to year 2009. The annual real growth rate of public investments in 2010 was 11.7 percent, compared to the growth rate of 29.0 percent in 2009 (IMF, 2011).

As a result of the relatively large volume of Kosovo's imports compared to the volume of exports, the negative trade balance continues to have a negative impact in the Kosovo's GDP. The deepening of the trade deficit by 4.5 percent during 2010, led to a more significant negative impact of the trade deficit on the GDP in 2010. Despite the low base, Kosovo's exports in 2010 recorded a significant growth rate, reaching the highest level in the postwar period. Kosovo's imports from abroad also marked an increase during 2010, which may reflect an increase of domestic demand, taking into consideration that imports in 2009 had marked a decline.

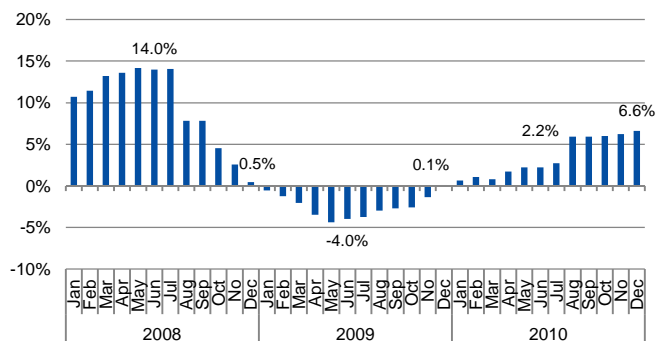
3.1.2. Prices

In year 2009, Kosovo was characterized with deflation. Whereas, following the inflationary pressures in the global level during 2010, also Kosovo's economy recorded an increase of the inflation rate, which took place especially during the second half of the year (Figure 3). The Consumer Price Index (CPI) during 2010 recorded an average annual growth rate of 3.5 percent, whereas, the annual growth rate in the end of the year (December 2010 compared to November 2010) reached at 6.6 percent.

The increase of prices in Kosovo mainly reflects the increase in the food prices during 2010, which in the same time represent the largest item in the consumer's basket in Kosovo. The average annual increase of food prices during 2010 was 4.7 percent. The increase of housing prices and the prices of public services, such as electricity, water, heating, etc., have also contributed to the increase of overall price level in Kosovo.

Price fluctuations in Kosovo are to a considerable extent driven by changes in the prices of imported goods, due to the high dependency of the country's economy on the import of goods from abroad. In 2010, the average annual growth rate of the Imports Price Index (IPI) was 6.0 percent (Figure 4).

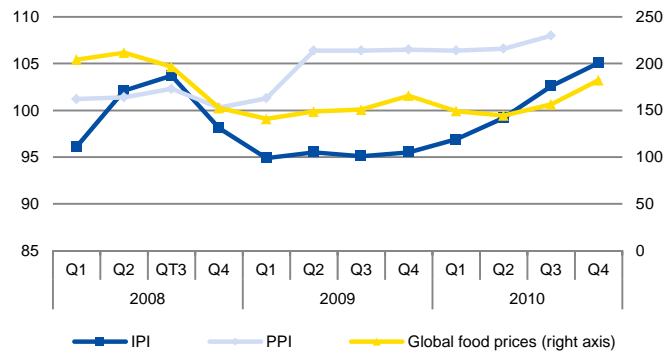
Figure 3. Consumer Price Index, annual change



Source: SOK (2011)

On the other hand, the Producer Price Index (PPI) during 2010 was relatively stable, marking an annual growth of 2.1 percent (average December 2010 – December 2009). Based on the current developments of the food prices and the prices of fuel derivatives at the global level, the inflationary pressures are expected to remain present in the Kosovo's economy also during 2011.

Figure 4. Indices of import, producer, and global food prices



Source: CBK (2011)

3.1.3. Labour Market

According to the SOK Labour Force Questionnaire (2009), the unemployment rate in Kosovo in 2009 was 45 percent⁴ and it represents one of the main challenges for the economy. As a result of the young structure of Kosovo's population, a large number of young people enter into the labour market every year, while the number of new jobs generated within the year remains relatively small. Based on the statistics of the Ministry of Labour and Social Welfare (MLSW), during the period 2004-2010, on average 25,000 people per year have been registered as new jobseekers, whereas the average number of new working places reported to the MLSW for each year was around 7,500.

According to the MLSW data, the number of registered jobseekers in 2010 decreased to 335,260, which represents an annual decline of 1.1 percent. The structure of registered jobseekers is dominated by unqualified jobseekers (63.6 percent), followed by jobseekers with secondary education (34.6 percent), whereas jobseekers with university qualification comprise only 1.8 percent of total registered jobseekers. The structure of jobseekers by gender appears to be balanced, with 47 percent of jobseekers being females. The unemployment in Kosovo has mainly a long-term character, where more than 90 percent of jobseekers have been unemployed for a period longer than 12 months. This makes the unemployment problem in Kosovo even more concerning due to the risk of human capital devaluation, which further diminishes the probability for an eventual employment for the unemployed people and at the same time decreases the general productivity of the labour force in the country.

Although data on the labour market in Kosovo are quite limited, it is estimated that 80 percent of employees are engaged in the private sector. On the other hand, the public sector also represents an important employer, absorbing around 20 percent of total employees in Kosovo. Employment through the intermediation of the MLSW in 2010 was at a lower level compared to the previous year. Through the intermediation of the MLSW, 6,787 jobseekers were employed in 2010, compared to 7,239 jobseekers employed in 2009.

3.2. Fiscal Sector

Kosovo's budget ended the year 2010 with a deficit of euro 93.2 million, compared to the deficit of euro 85.5 million in 2009. The budget deficit to GDP ratio in 2010 reached at 2.2 percent.

⁴ In the absence of data for 2010, the labour market statistics are presented based on the Labor Force Questionnaire 2009.

In 2010, Kosovo for the first time entered into a financial arrangement with the IMF. The IMF granted the first 'Stand-By-Arrangement' loan to Kosovo at the amount of euro 108.9 million (SDR 92.6 million), which is equivalent to 157 percent of the Kosovo's quota in the IMF.⁵ This arrangement was aimed at addressing the budgetary needs, and, according to the agreement, the IMF is expected to distribute the granted loan to Kosovo budget in six installments, throughout a period of 18 months. During 2010, Kosovo withdrew the first installment amounting at euro 22.1 million, whereas the issuance of the remaining five installments is subject to the quarterly reviews of the program implementation. According to the program, the Government of Kosovo is expected to comply with the IMF recommendations, which are mainly related to the rationalization of budget expenditures and the enhancement of efficiency in the public administration. Following the approval of the program with the IMF, Kosovo is expected to receive further budget donations and loans from other international institutions.

3.2.1. Budget Revenues

Budget revenues in 2010 amounted at euro 1.17 billion, or 2.8 percent higher compared to year 2009. The budget revenues to GDP ratio in 2010 stood at 27.9 percent, which represents a lower ratio compared to the average for the countries in the region in year 2009 (34.2 percent).

Border revenues continue to dominate the structure of budget revenues, comprising 59.3 percent of total budget revenues in 2010. Net revenues collected from border taxes reached at euro 699.4 million euro, recording an annual growth of 10.3 percent (5 percent in 2009). The increase of the volume of the border revenues was also driven by the increase of imports, which in 2010 grew by 10.8 percent (0.4 percent in 2009). Within the border taxes, the border VAT represents the largest category (30.7 percent), amounting at euro 361.3 million. Excise revenues (including tobacco excise) represent another important category of border revenues, which amounted at euro 232.4 million or 19.7 percent of total border revenues in 2010. Compared to 2009, the excise revenues recorded an annual growth of 12.4 percent.

Net revenues from local taxes in 2010 amounted at euro 194.2 million (annual growth of 6.9 percent). Within the revenues from local taxes, the largest share is represented by domestic VAT revenues (48.9 percent of local taxes revenues), which in 2010 reached at euro 95 million. Compared to year 2009, the domestic VAT revenues recorded an annual growth of 25.3 percent. One of the factors that may have contributed to the better collection of domestic taxes is also the implementation of the project on the installation of fiscal cashiers. Fiscal cashiers started to be installed by enterprises in Kosovo for the first time in in March 2010. The number of fiscal cashiers that have been installed during year 2010 has reached at 12,000. Taxes on corporate revenues represent another important category of domestic revenues, composing 26.7 percent of total domestic revenues. Revenues collected through this category of taxes reached the amount of euro 51.9 million in 2010, marking a decline of 6.3 percent. Revenues from personal income taxes, in year 2010, reached at euro 44.2 million (22.8 percent of total domestic revenues), recording an annual growth of 12.8 percent. Another category of domestic taxes, that comprises a lower share of total revenues from domestic taxes (2.2 percent), consists of taxes on individual business, which in 2010 generated euro 25.5 million and marked an annual growth of 23.9 percent. In 2010, the own source revenues amounted at euro 100.5 million (8.5 percent of total budget revenues),

⁵ See Annual Report 2009, Box 1, page 33.

marking an annual growth of 39.8 percent. The structure of the own source revenues is composed by the central level and municipal level revenues. In 2010, own source revenues from the central level amounted at euro 48.5 million, whereas own source revenues from the municipal level generated euro 52.0 million for the budget of Kosovo. Regarding one-off revenues, in 2010, the PTK transferred an amount of euro 85 million as a dividend to the budget of Kosovo, compared to euro 200 million transferred in 2009.

3.2.2. Budget Expenditures

Budget expenditures in 2010 amounted at euro 1.27 billion, recording an annual growth of 3.2 percent, which represents a slower growth rate compared to the growth of the previous year (29.6 percent). Budget expenditures to GDP ratio in 2010 stood at 30.1 percent, which represents a lower share compared to the average of the region (35.3 percent of GDP in 2009). In 2010, budget expenditures dedicated for consumption accounted for 11.2 percent of GDP, whereas capital outlays accounted for 10.8 percent of GDP.⁶

Similarly to previous years, capital outlays in 2010 absorbed the largest share of the budget expenditures, comprising 35.8 percent of total budget expenditures. Capital outlays in 2010 amounted at euro 455.3 million, recording an annual growth rate of 13.7 percent. The largest part of capital outlays during 2010 was designated for infrastructure investments (57 percent of total capital outlays), which were mainly related to the construction of the Morinë-Merdarë highway, whose construction started in April 2010. The second largest category of budget expenditures in 2010 were wages and salaries, which amounted at euro 311.4 million (24.5 percent of total expenditures). Wages and salaries represent the category that marked the highest increase within the budget expenditures, recording an annual growth rate of 17.8 percent. Subsidies and transfers represented the third largest category, with a share of 19.9 percent in total budget expenditures. Subsidies and transfers in 2010 reached at euro 252.7 million. This category marked an annual decrease of 1.6 percent. The reduction of this category in 2010 is mainly attributed to the decline of subsidies for public enterprises from euro 82 million in 2009 to euro 56 million in 2010. Basic pensions, which comprise the largest share of subsidies and transfers, reached at euro 95 million in 2010 from euro 86 million in 2009.

Goods and services in 2010 were the category with the smallest share within budget expenditures, amounting at euro 162.6 million (12.8 percent of total budget expenditures), which is an annual increase of 7.1 percent. The increase of expenditure for goods and service is mainly due to the increase of contractual expenses and the expenses for maintenance and refurbishment.⁷

Since year 2009, budget expenditures have started to contain also other financings as a separate item, which includes loans granted to public enterprises and the servicing of the foreign debt (7.1 percent of total budget expenditures). In 2010, loans to public enterprises amounted at euro 60 million, of which the largest part was extended to KEK. In addition, during 2010, Kosovo serviced foreign debt at the amount of euro 10.1 million. Moreover, the US Government helped reducing Kosovo's foreign debt by the amount of euro 9.8 million.

⁶ Consumption expenditures include wages and salaries, and goods and services, whereas capital outlays refer to the public investments.

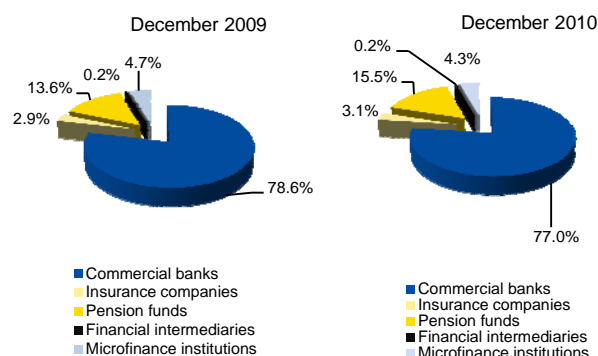
⁷ These expenditures include the expenses for education, training and advocacy services, maintenance of buildings and road infrastructure, etc.

3.3. Financial Sector

3.3.1 General Characteristics

Kosovo's financial sector was characterized with a slower growth during 2010. The total value of financial sector assets (without considering CBK) reached at euro 3.2 billion in 2010, which represents an annual growth of 13.7 percent (24.2 percent in 2009). Commercial banks and pension funds remain the key players in the financial sector, managing 77 and 15.5 percent of total financial sector assets, respectively (Figure 5).

Figure 5. Structure of financial system assets by sectors



Source: CBK (2011)

The remaining part of assets is shared between microfinance institutions (4.3 percent), insurance companies (3.1 percent) and financial auxiliaries (0.2 percent).

The number of financial institutions operating in Kosovo's financial market in 2010 was similar to the previous year (Table 2). A slight change was noted however in the number of financial auxiliaries, which mainly operate as currency exchange bureaus.

Table 2. Number of financial institutions

Description	2007	2008	2009	2010
Commercial banks	7	8	8	8
Insurance companies	10	11	11	11
Pension funds	2	2	2	2
Fin. auxiliaries and microfinancial inst.	46	45	46	49

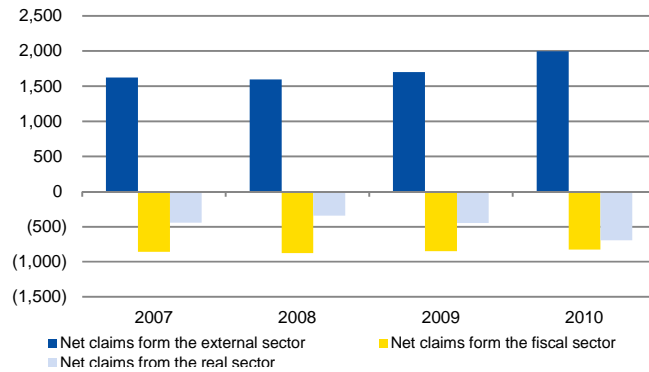
Source: CBK (2011)

The financial corporations' survey (including CBK) indicates a higher growth of Net Foreign Assets (NFA) in 2010 compared to 2009 (Figure 6). In December 2010, the value of NFA was around euro 2 billion, which represents an annual growth of 17.3 percent (6.7 percent in 2009). The total value of claims to the external sector in 2010 was euro 2.4 billion, the largest share of which was invested in deposits (52.7 percent) and securities (22.0 percent). Deposits and securities are mainly invested by the CBK (59.2 percent), commercial banks (32.4 percent) and pension funds (8.4 percent).

On the other hand, liabilities to the external sector reached at euro 392.5 million in 2010, an annual growth of 17 percent. These liabilities consist mainly of non-resident deposits in commercial banks in Kosovo (22.2 percent) and foreign loans to financial institutions operating in Kosovo (42.8 percent). The receivers of these loans are mainly commercial banks and microfinance institutions. The other part of liabilities is mainly related to Special Drawing Rights (SDR) and the IMF quota.

Financial sector claims to the domestic sector reached euro 765.9 million in 2010, an annual increase of 33.5 percent compared to the previous year. Claims to the domestic sector mainly consist of financial sector claims to the real sector and the liabilities to the fiscal sector. Kosovo’s financial sector has only liabilities to the fiscal sector (no claims), which consist of government deposits in the CBK (98.6 percent) and government deposits at commercial banks (1.4 percent). In 2010, financial sector claims to the real sector reached euro 1.59 billion (an annual growth of 12.0 percent). These claims mainly consist of loans issued by commercial banks and microfinance institutions. Taking into account the liabilities to the real sector, which mainly consist of deposits at commercial banks, the financial sector net claims to the real sector maintained a negative balance of euro 693.9 million (Figure 6).

Figure 6. Net claims of the financial sector, in millions of euro

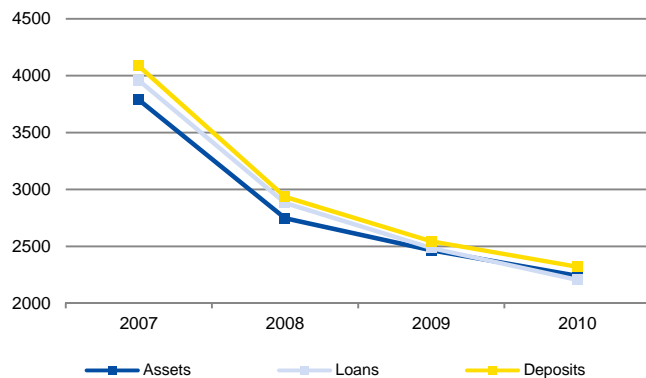


Source: CBK (2011)

3.3.2. Structure and Activity of the Banking System

The structure of Kosovo’s banking system in 2010 remained similar to the previous year, both regarding the number of banks and their ownership structure. In 2010, there were eight commercial banks operating in the Kosovo’s banking system, of which six foreign-owned banks and two domestically-owned. The foreign-owned banks continue to dominate the banking market in Kosovo, managing 90.2 percent of total banking system assets (91.1 percent in 2009). The remaining share of assets is managed by the domestically owned banks (9.8 percent in December 2010). Kosovo’s banking system continues to be characterized by a high degree of market concentration, with around 77.4 percent of total banking system assets being managed by the three largest banks. Nevertheless, the continuous growth in the activity of smaller banks was reflected in a constant decline of the degree of concentration in the banking market. The degree of market concentration in the banking system, measured through the Herfindahl-Hirschman Index (HHI) for total assets, was 2,241 in 2010, which compared to 2009, indicates that the concentration ratio is lower by 224.1 HHI points (Figure 7).

Figure 7. HHI for assets, loans and deposits



Source: CBK (2011)

Unlike in the previous year, when commercial banks were obliged to undertake measures to reduce their operational expenditures due to the slowdown in the intermediary activity of the banking system, in 2010, the banking system expanded its infrastructure. In 2010, the number of branches and sub-branches of commercial banks reached at 303, which represents an annual increase of 16 units. Moreover, compared to the previous year, the

number of employees in the banking system marked an increase. In 2010, the banking system had 3,768 employees (3,626 employees in 2009). A slower growth trend was observed in terms of the number of ATMs and POSs installed by commercial banks (Table 3).

The number of current accounts in commercial banks recorded a slower growth during 2010, reaching 1.40 million in December 2010 compared to 1.36 million in December 2009. While in 2009 the number of current accounts recorded an annual growth of 12.9 percent, in December 2010, the increase of the number of current accounts slowed down to 2.5 percent. A rapid growth trend characterized the 'e-banking' accounts, which in 2010 reached 55,292 compared to 40,924 in 2009.

Table 3. Banking System Network

Description	2007	2008	2009	2010
The number of branches and sub-branch.	227	279	287	303
The number of employees	2,855	3,762	3,626	3,767
The number of ATMs	155	240	339	415
The number of POSs	0	3,426	5,251	6,194
The number of e-banking accounts	8,746	13,051	40,924	55,292

Source: CBK (2011)

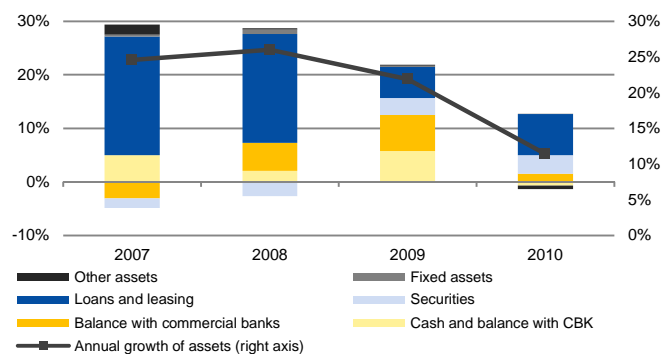
As regards to the interbank payments system, the number and value of transactions continued to increase, reflecting an increase of the economic activity as well as an increase in the use of bank accounts by individuals and businesses, which, among others, contributes positively to the reduction of the economic informality in the economy. The number of total transactions reached at 3.9 million in 2010 (annual growth of 4.4 percent), while a more significant growth was noticed in the value of transactions. Driven by the government transactions, more specifically by the transfer of Post and Telecommunication of Kosovo (PTK) dividend, the value of total interbank payment transactions reached euro 4.7 billion in 2010, an annual increase of 17.2 percent.

3.3.2.1 Banking sector balance sheet

i. Assets

In 2010, the value of total assets managed by commercial banks in Kosovo reached euro 2.5 billion, which indicates an annual growth of 11.4 percent (21.9 percent in 2009). While loans and investments in securities continue to be the key contributors to the overall growth of banking system assets, commercial banks' balances with the CBK had a negative contribution to the growth of total assets. Loans and investments in

Figure 8. Contribution to asset growth by categories, in percentage



Source: CBK (2011)

securities contributed with 7.7 and 3.5 pp, respectively, to the growth rate of total assets in 2010, while the balance of commercial banks with the CBK contributed negatively with 1.3 pp during the same period (Figure 8). The gradual recovery of the global economy from the last year financial crisis has increased the confidence of commercial banks, which was reflected in a faster increase of loans and, at the same time, in a decline of commercial banks' reserves at the CBK. The share of banking system assets to GDP increased to 59.7 percent in year 2010, marking an increase of 2.7 pp compared to the previous year. The activity of commercial banks that operate in Kosovo's banking market is highly concentrated in the financial intermediation activity inside the economy, while 19.7 percent of total assets are invested in the external markets.

Lending activity continues to represent the main activity of Kosovo's banking system. In 2010, lending activity was characterized with a faster growth trend, compared to the previous year, when lending marked a slowdown. In 2010, total banking sector loans amounted at euro 1.46 billion, reflecting an annual increase of 13.2 percent compared to the increase of 8.9 percent in 2009 (Table 4). In the end of 2010, loans accounted for 59.4 percent of total banking system assets (58.5 percent in 2009).

Table 4. Structure of banking system assets

Description	2007		2008		2009		2010	
	In millions of euro	Participation (%)	In millions of euro	Participation (%)	In millions of euro	Participation (%)	In millions of euro	Participation (%)
Cash and balance with CBK	189.0	13.2%	218.2	12.1%	322.7	14.6%	307.5	12.5%
Balance with commercial banks	208.1	14.5%	283.9	15.7%	405.6	18.4%	439.0	17.9%
Securities	78.9	5.5%	40.5	2.2%	97.0	4.4%	173.4	7.1%
Loans and leasing (gross)	892.1	62.2%	1,183.4	65.4%	1,289.0	58.5%	1,458.7	59.4%
Fixed assets	27.2	1.9%	39.0	2.2%	43.1	2.0%	44.1	1.8%
Other assets	39.7	2.8%	43.1	2.4%	46.7	2.1%	32.5	1.3%
Total	1,435	100%	1,808	100%	2,204	100%	2,455	100%

Source: CBK (2011)

Due to the slowdown of lending activity, in 2009, commercial banks diverted a part of their investments towards the external markets, namely in investments in securities. These investments continued to grow also in 2010, driven mainly by the recovery of the international financial markets during this period. Investments in securities amounted at euro 173.4 million in 2010 (euro 97.0 million in 2009), increasing their share to total assets to 7.1 percent (4.4 percent in 2009). This represents the highest share of securities to total banking sector assets since 2006. The structure of banks' investments in securities mainly consists of investments in government bonds (83.1 percent), financial corporations (16.7 percent) and non-financial corporations (0.2 percent).

ii. Structure of loans

The recovery of the world economy and, consequently, the improvement of banks' perceptions on the domestic economic environment were reflected in a higher growth rate of loans in 2010 compared to 2009. In 2010, loans extended to the domestic economy amounted euro 1.46 billion, which is an annual growth of 13.2 percent compared to the growth rate of 8.9 percent in 2009 (Figure 9). Loans to households continued to have the highest growth, marking an annual increase of 25.5 percent. Loans to enterprises continued to grow at lower rate compared to household loans. Nevertheless, the annual increase of 8.7 percent indicates a faster growth rate of loans to enterprises during 2010, compared to the previous year.

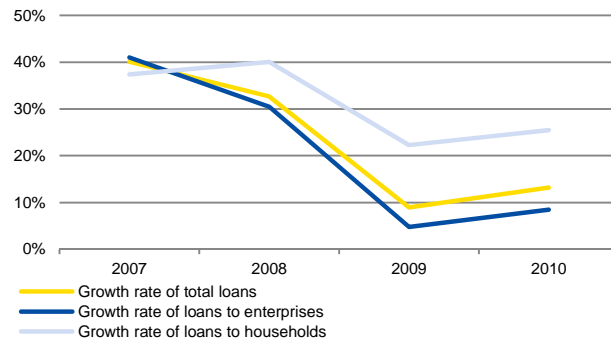
The structure of loans during 2010 was dominated by loans issued to enterprises, which in 2010 represented 70.5 percent of total loans issued by the banking system (Figure 10). Household loans during the last two years have increased their share to total loans. In 2010, the share of household loans to total banking system loans reached at 29.5 percent, compared to 26.7 percent in 2009. This increase is mainly attributed to the fact that loans to enterprises incurred a more significant reduction of the growth rate, while the growth rate of loans to households, despite the slowdown, was more approximate to the previous periods.

The sectorial distribution of loans remained similar to the previous years, with the services sector absorbing the largest share of loans issued to enterprises (70.1 percent of total loans to enterprises). Within services, the majority of loans are issued to the trade sector (50.8 percent of loans to enterprises), followed by loans issued to the industry sector, including mines, production, industry and construction, which received 26.1 of total loans issued to enterprises. The agriculture sector continues to participate only with a low share, receiving only 3.7 percent of total loans issued to enterprises (Figure 11).

Loans issued to the trade sector and financial services were characterized with an increasing trend in 2010, while lending to other sectors recorded a slowdown compared to the previous year (Figure 11). Reaching the amount of euro 521.6 million, loans to the trade sector marked an annual increase of 13.7 percent in 2010 (4.9 percent in 2009). Loans issued to enterprises that provide financial services amounted at euro 22.1 million, compared to euro 10.6 million in the previous year. Lending to the industry sector recorded a slowdown of the growth rate during 2010, with loans to the manufacturing sector recording an annual

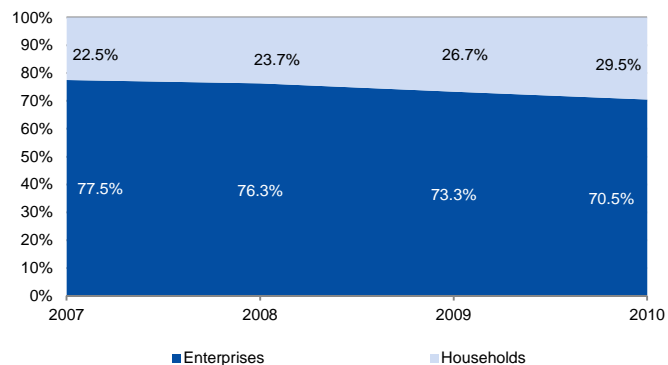
growth of 5.8 percent (29.9 percent in 2009), and loans to the construction sector recording an annual growth of 22.5 percent (35.9 percent in 2009). In 2010, loans issued to the manufacturing sector amounted at euro 126.8 million, that indicates a share of 12.3 percent in total loans issued to enterprises. During the same period, loans to the construction sector reached at euro 109.1 million, representing 10.6 percent of total loans to enterprises.

Figure 9. Growth rate of loans by sectors, in percentage



Source: CBK (2011)

Figure 10. Structure of loans, in percentage



Source: CBK (2011)

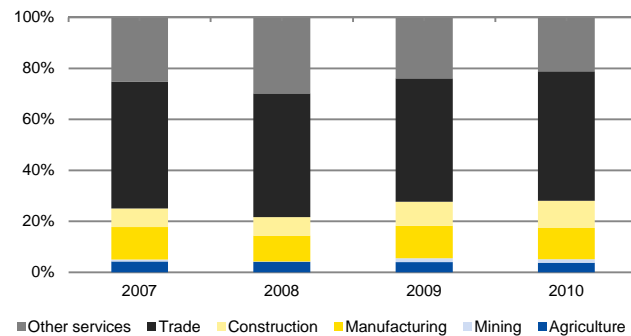
Regarding the maturity, the structure of loans issued by the banking system remains dominated by longer maturity loans. In 2010, loans with maturity of over two years and up to five years represented 43.5 percent of total loans, followed by loans with maturity of over five years, which represented 25.4 percent of total loans. Loans with maturity of over two years represented 73.1 percent of total loans in the banking system (Figure 12). Loans with maturity of up to one year also have a considerable share in total banking sector loans, composing 20.6 percent of total loans. The remainder is shared among loans with maturity from one to two years (6.3 percent) and over ten years (4.3 percent). In 2010, it has been noticed a decline in loans with maturity from one to two years. Amounting at euro 91.2 million, loans with maturity from one to two years recorded an annual decline of 37.1 percent. As a consequence, the share of loans with maturity from one to two years to total loans decreased by around 5.0 pp.

iii. Liabilities

The structure of banking system liabilities during 2010 was dominated by deposits collected within the domestic economy, which represent the main source of finance for commercial banks in Kosovo. In 2010, deposits represented 78.9 percent of the total liabilities of the banking system (Table 5). The trend of deposit growth in 2010 was slower compared to year 2009. Amounting at euro 1.93 billion, deposits in the banking system recorded an annual growth of 11.0 percent in 2010, which was lower compared to the growth rate of 20.8 percent in 2009. The slowdown of the deposit growth in 2010 mainly reflects the withdrawal of government deposits from commercial banks.

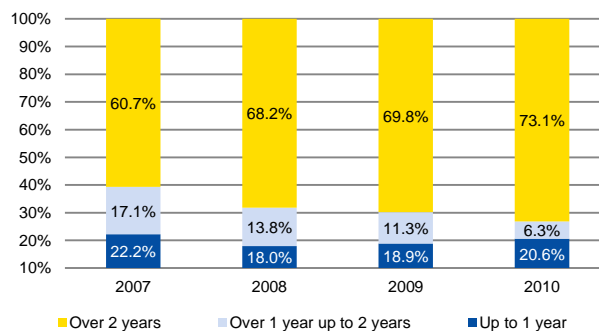
Another important source of finance for commercial banks in Kosovo consists of own resources, which in 2010 composed 9.4 percent of total liabilities in the banking system. Own resources marked an annual increase of 12.7 percent, mainly due to the increase of shareholders capital, which comprises around 73.9 percent of total own resources. In 2010, banking sector liabilities to the external sector in the form of subordinated debt reached at euro 33.5 million (euro 24.4 million in 2009). Nevertheless, the share of the subordinated debt to total liabilities continues to be low at only 1.4 percent. The continuous increase of the subordinated debt and placements from commercial banks that operate in the external markets indicates a tendency of increasing the use of external funding by commercial banks operating in Kosovo.

Figure 11. Structure of loans by economic activity, in percentage



Source: CBK (2011)

Figure 12. Structure of loans by maturity, in percentage



Source: CBK (2011)

Table 5. Structure of banking system liabilities

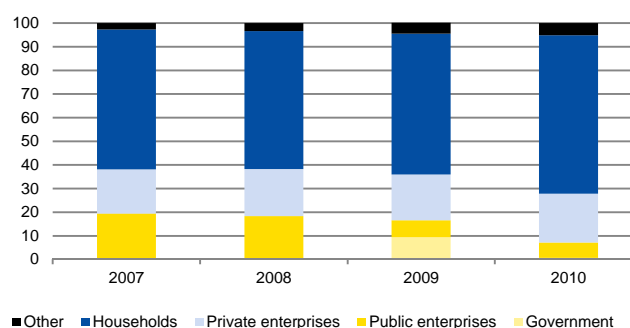
Description	2007		2008		2009		2010	
	In millions of euro	Participation (%)	In millions of euro	Participation (%)	In millions of euro	Participation (%)	In millions of euro	Participation (%)
Balance with other banks	25.8	1.8	34.9	1.9	58.5	2.7	56.8	2.3
Deposits	1,143.1	79.6	1,444.1	79.9	1,744.9	79.2	1,937.0	78.9
Other borrowings	2.7	0.2	0.0	0.0	0.0	0.0	0.0	0.0
Other liabilities	103.7	7.2	129.8	7.2	171.7	7.8	197.3	8.0
Subordinated debt	7.0	0.5	7.0	0.4	24.4	1.1	33.5	1.4
Own resources	152.7	10.6	192.5	10.6	204.6	9.3	230.6	9.4
Total	1,435	100.0	1,808	100.0	2,204	100.0	2,455	100.0

Source: CBK (2011)

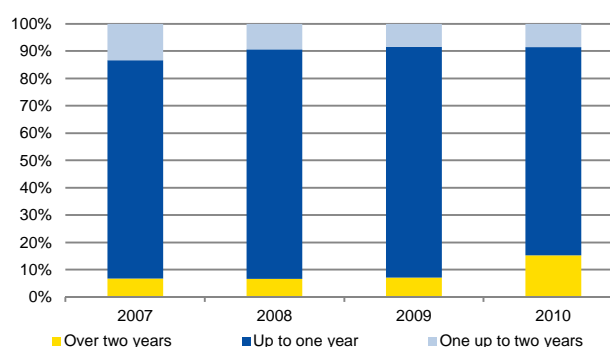
iv. Structure of deposits

The largest share of deposits in the banking system of Kosovo consists of household deposits, which in 2010 reached the amount of euro 1.3 billion. Household deposits recorded an annual growth of 25.0 percent in 2010, compared to the growth of 23.3 percent in the previous year. Reaching at euro 526.6 million, the deposits of enterprises recorded an annual growth of 14.0 percent. In 2010, the structure of enterprises' deposits was dominated by the deposits of private enterprises (76.0 percent of total enterprises' deposits). Regarding the government deposits, the continuous withdrawal during 2010 led to a decline in the value of these deposits to euro 11.7 million, compared to the value of euro 164.9 million in 2009.

Regarding the structure of deposits at the banking sector in 2010, household deposits increased their share to total deposits by 7.5 pp (67.1 percent of total deposits), whereas the deposits of enterprises increased their share by 0.7 pp, accounting for 27.2 percent of total deposits in 2010 (Figure 13). The increase in the share of household deposits mainly reflects the decline in the share of government deposits during 2010. The share of government deposits to total banking system deposits in the end of 2010 was 0.6 percent, which indicates a decline of 8.8 pp compared to year 2009. Non-resident deposits in Kosovo's banking system continued to increase, reaching an amount of euro 84.8 million, which is an annual growth of 32.3 percent. In terms of the currency, the structure of deposits in the banking system of Kosovo is mainly dominated by the Euro denominated deposits, which

Figure 13. Structure of deposits by sectors, in percentage

Source: CBK (2011)

Figure 14. Structure of time deposits by maturity, in percentage

Source: CBK (2011)

account for 94.5 of total deposits. The large share of Euro deposits indicates a low level of exchange rate risk for the banking system of Kosovo.

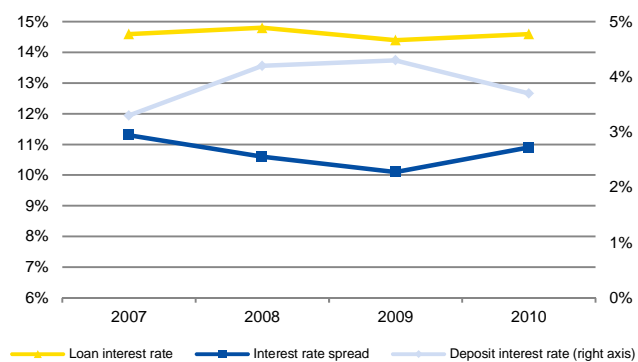
In terms of the maturity, the structure of deposits has remained similar compared to the previous periods. Time deposits continue to attain the largest share, composing 47.7 percent of total deposits. The remaining share consists of transferable and saving deposits that in 2010, composed around 34.6 and 17.6 percent of total deposits, respectively.

The structure of time deposits remains dominated by deposits with short term maturity. In 2010, deposits with maturity up to one year represented 76.2 percent of total time deposits, followed by deposits with maturity of over two years, which represented 15.3 percent of total time deposits (Figure 14). The remaining share of time deposits mainly consists of deposits with maturity of over one year and up to two years, which represented 8.5 percent of total time deposits in 2010. It is worth mentioning that in 2010, deposits with shorter maturity decreased their share to total time deposits, while deposits with longer maturity increased their share. Thus, deposits with maturity of up to one year decreased their share by 8.3 pp, while deposits with maturity of over two years increased their share by 8.2 pp. The persistent growth of deposits with longer maturity will have a positive impact in the extension of longer-term lending and at the same time, it will improve the liquidity position in the banking system. The approval of the law on the deposit insurance is expected to affect positively the depositors' trust towards the commercial banks, which may contribute to the further increase of longer maturity deposits.

3.3.2.2 Interest rates

The movements of interest rates in 2010 were characterized with a decline of interest rates on deposits, while interest rates on loans recorded a slight increase. The average interest rate on deposits (12-month moving average) decreased from 4.3 percent in 2009 to 3.7 percent in 2010, while the average interest rate on loans increased to 14.6 percent in 2010 from 14.4 percent in 2009 (Figure 15). The decline of deposit rates during 2010 may be a result of the slowdown of lending activity by the banking sector, which has reduced the demand for deposits. The interest rate spread in the end of 2010 reached at 10.9 pp, which represents an annual increase of 0.8 pp.

Figure 15. 12-month moving average of interest rates



Source: CBK (2011)

Interest rates on household deposits and enterprise deposits were similar during 2010. The highest average interest rate on enterprise deposits in December 2010 was 5.14 percent, which is offered for deposits amounting over euro 250 thousand and with a maturity of over two years. In the same period, the highest average interest rate for household deposits reached at 5.14 percent, which also applies to deposits with maturity of more than two years. Regarding the average interest rates on loans, loans to enterprises maintain higher interest rates compared to household loans. Standing at 13.8 percent, the average interest rate on loans to enterprises was by 1.4 pp higher than the average interest rate on household loans.

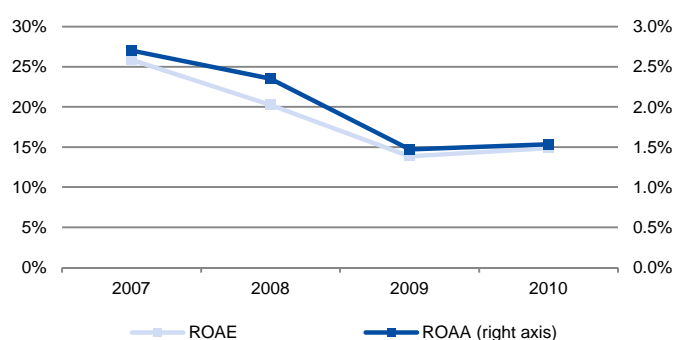
3.3.2.3 Banking system performance

Kosovo's banking system concluded year 2010 with a net profit of euro 32.9 million, which is for 30.3 percent higher compared to the previous year. Considering the decrease of the net profit of the banking system in 2009, the increase of the net profit in 2010 indicates a considerable improvement in the performance of this system.

The increase of profit mainly resulted from the faster increase of lending activity during 2010 compared to the previous year, considering that interest income represents the main source of banking sector income. The slowdown of the banking system expenditures growth during this period has also contributed to the increase of profit. Despite the increase of the net profit, the

Return on Average Assets (ROAA) remained at the same level with the previous year, standing at 1.5 percent (Figure 16).⁸ Whereas, Return on Average Equity (ROAE) reached at 14.9 percent in 2010, compared to 13.9 percent in 2009.

Figure 16. Banking system performance indicators



Source: CBK (2011)

Table 6. Income statement, in millions of euro

Description	2007	2008	2009	2010
Income				
Interest income	117.9	155.7	163.2	175.8
Non-interest income	39.5	39.3	38.2	41.4
Total income	157.3	195.0	201.5	217.2
Expenditures				
Interest expenditures	26.0	38.1	52.2	55.2
Non-interest expenditures	19.9	21.9	32.6	36.0
General and administrative expenditures	69.7	86.0	87.0	88.0
Total expenditures	115.6	146.0	171.8	179.2
Net income				
Net operating income	41.7	49.0	29.6	37.9
Net income before tax	41.3	47.6	28.9	37.2
Tax provisions	7.9	11.2	3.6	4.3
Net profit/loss within the period	33.5	36.4	25.3	32.9

Source: CBK (2011)

Banking system income amounted at euro 217.2 million in 2010, which represents an annual growth of 7.8 percent (3.3 percent in 2009), indicating an upward trend of banking system income compared to year 2009. The increase of income in this period mainly resulted from the increase in the lending activity that led to an increase of revenues from loan interest. The structure of the banking sector revenues continues to be dominated by interest income from loans, which in 2010 represented 80.1 percent of total banking system

⁸ Based on net assets.

income. Interest income recorded an annual growth of 7.7 percent in 2010 (4.4 percent in 2009), amounting at euro 157.8 million. Moreover, unlike the previous year, year 2010 marked an increase of non-interest income. The non-interest income reached at euro 43.1 million, recording an annual growth rate of 8.1 percent in 2010. The largest share of this category of income consists of the income from commissions.

Banking system expenditures in year 2010 amounted at euro 179.2 million. The increasing trend that characterized banking system expenditures during 2009 was considerably slowed down in 2010 (4.3 percent in 2010 compared to 17.7 percent in 2009). The slowdown was present in almost all banking expenditure categories. For example, interest expenditures in 2010 amounted at euro 55.2 million and increased by only 5.8 percent (37.0 percent in 2009). The slowdown of interest expenditures during 2010 was mainly a result of the slowdown evidenced in the deposit growth. Moreover, the slowdown of interest expenditures might have also resulted from the decline of deposit interest rates during 2010. Non-interest expenditures in 2010 amounted at euro 36 million, recording a growth rate of 10.4 percent, which is lower than the growth rate of 49.2 percent that was recorded in 2009. Within non-interest expenditures, provision expenses represent the largest category, which in 2010 amounted at euro 28.3 million and recorded an annual growth of 10.3 percent. The increase of provision expenses reflects the increase of non-performing loans in 2010. General and administrative expenditures represent the largest category of total banking system expenditures (49.1 percent of total expenditures). In 2010, this category of expenditures amounted at euro 88.1 million, which is a similar level to the previous year. The slowdown of the banking system expenditures during this year mainly reflects the measures undertaken by the banking system against the significant decline of profit in 2009.

The lower growth rate of banking system revenues compared to the growth rate of banking sector total assets led to a decline in the ratio between banking system income and total assets in the past two years (9.3 percent in 2009, 8.8 percent in 2010), suggesting that commercial banks were less efficient in income generation from the use of their assets. On the other hand, the efficiency of commercial banks, expressed by the average value of assets managed by an employee, increased during 2010. For example, in 2009, the average amount of assets managed by an employee was euro 637.2 thousand, while in 2010 this amount increased to euro 680.1 thousand. This difference reflects the rapid expansion of banking system assets in relation to the number of employees.

3.3.2.4 Banking system risks

i. Liquidity risk

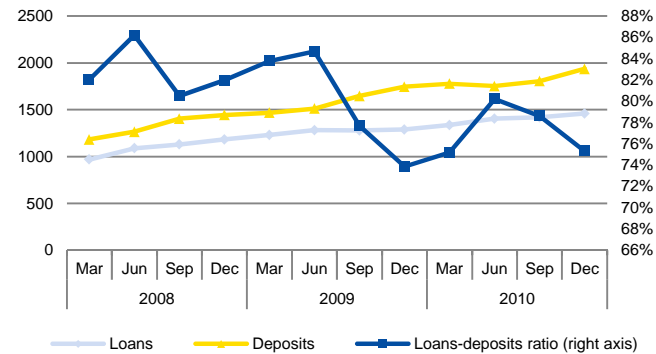
Domestically collected deposits continue to be the main source of finance for the activity of Kosovo's banking system. As a result, Kosovo's banking system is characterized with a low level of sensitivity against changes in the cost and availability of funds in the international financial markets. In December 2010, the share of banking system deposits to total banking sector liabilities was 78.9 percent, which represents a decline of 0.3 pp compared to December 2009. Own resources also have an important role in the financing of the banking operations, accounting for 9.4 percent of total liabilities. Whereas, placements from commercial banks operating abroad and the subordinated debt have a lower share, composing only 2.3 percent and 1.4 percent of total liabilities, respectively.

Liquidity indicators for the Kosovo's banking system constantly have shown a satisfactory liquidity position. The faster growth of loans relative to deposits during 2010 led to a higher loan to deposit ratio, which in December 2010 reached at 75.3 percent compared to 73.9 percent in 2009 (Figure 17). Despite the increase, the current ratio between loans and deposits is in accordance with the recommendations of the CBK, which recommends that commercial banks operating in Kosovo should have a loan to deposits ratio of around 80 percent.

At the same time, the increase of the banking system liquid assets to total assets ratio shows a slight improvement of liquidity in the banking system. In December 2010, liquid assets accounted for 37.5 percent of total banking system assets, which is an increase of 0.15 pp compared to the previous year.

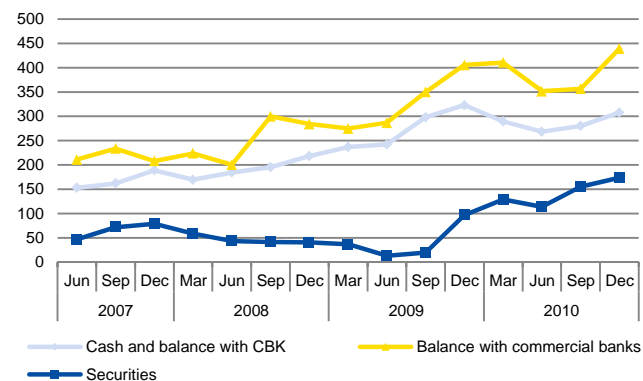
The structure of liquid assets in the Kosovo's banking system is composed of cash and balance with CBK, balance with commercial banks abroad and investments in securities (Figure 18). In the end of 2010, assets under the category 'cash and balance with CBK' reached at euro 307.5 million, which is a decline of 4.7 percent compared to December 2009. Whereas, the category 'balance with commercial banks' mainly consists of assets invested in

Figure 17. Banking system loans and deposits, in millions of euro



Source: CBK (2011)

Figure 18. Liquid assets, in millions of euro



Source: CBK (2011)

placements to banks operating abroad by banks operating in Kosovo. In December 2010, this category had a value of euro 439.0 million, which represents a growth of 8.2 percent compared to the same period of 2009. During 2010, banks continued to increase investments in securities abroad, a trend that started since year 2009. In December 2010, banking system assets invested in securities reached at euro 173.4 million, which represents an annual growth of 78.8 percent compared to December 2009. The satisfactory performance of financial markets globally was a key determinant that encouraged banks to increase investments in securities. Also, the slowdown credit growth within the country contributed to the increase of investments in securities by increasing the availability of assets to be invested in the external markets.

ii. Credit risk

The reflection of the global crisis in Kosovo during 2009 has had an impact on borrowers' solvency, thus affecting negatively the quality of banking system loan portfolio. In 2010, in spite of the fact that Kosovo's economy was estimated to have marked a higher growth rate

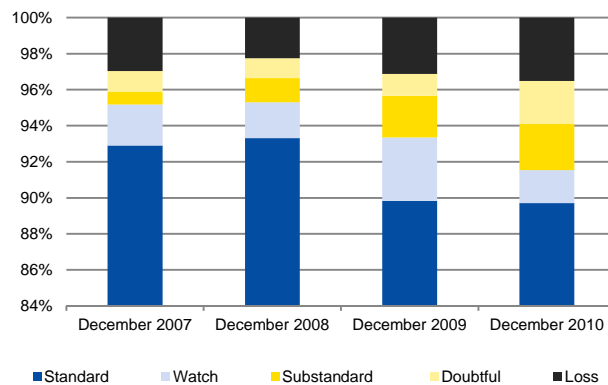
compared to the previous year, the share of non-performing loans to total loan portfolio continued to increase.

The deterioration of the loan portfolio quality, in spite of a higher economic growth rate during this year, to some extent, can be explained by the specific nature of non-performing loans, which do not react automatically to the improvements in a country's economy. The increase of the share of non-performing loans to total loans during 2009 and 2010, to some extent, can also be attributed to the "base effect", driven by the credit tightening in response to the increase of uncertainty on the performance of the real sector of the economy. Credit tightening led to lower growth rate of total loans compared to the growth rate of non-performing loans.

Regarding the structure of loans in terms of quality, in 2010 it was noticed a migration of loans from the 'standard' category (which represents loans that have no return problems) towards the categories of poor quality.⁹ In December 2010, loans classified as 'substandard' represented 2.6 percent of total loans, recording an increase of 0.3 pp compared to 2009, while loans classified as 'watch' recorded decline (Figure 19).

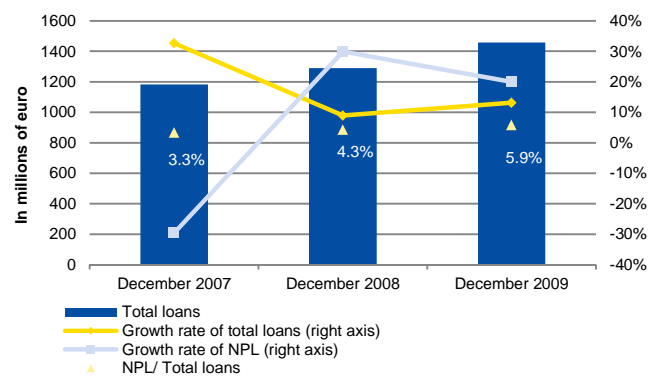
A more significant increase was marked by loans classified as 'doubtful' and 'loss'. These two categories comprise together the Non-Performing Loans (NPL) portfolio. The share of NPL to total loans reached at 5.9 percent in 2010, which indicates an increase of 1.6 pp compared to 2009, when NPL represented 4.3 percent of total loans (Figure 20). Further deterioration of the quality of loan

Figure 19. Structure of loans by classification



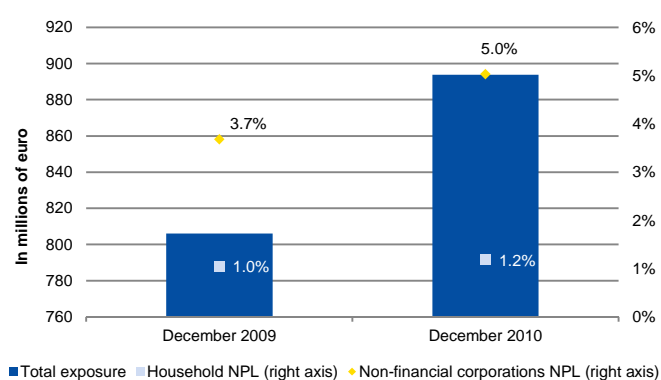
Source: CBK (2011)

Figure 20. Total loans and NPL



Source: CBK (2011)

Figure 21. NPL by sectors



Source: CBK (2011)

⁹ Based on the CBK regulation, loans in Kosovo's banking system are classified in five main categories: standard, observing, substandard, doubtful and loss. Classified loans include: standard, watch, substandard, doubtful and loss loans. Problematic loans include: substandard, doubtful and loss loans. Non-performing loans include: doubtful and loss loans.

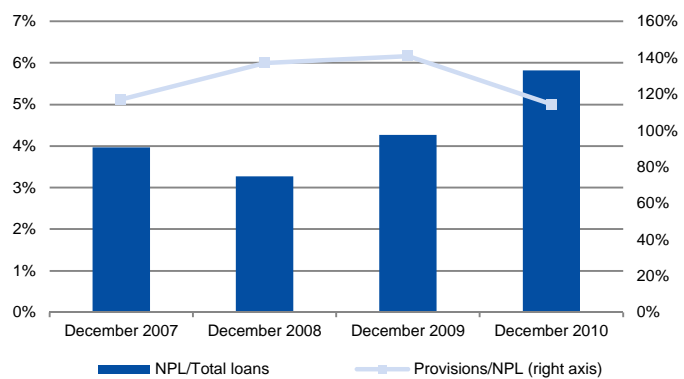
portfolio increases the need for further development of credit risk assessment capacities at the commercial banks, in order to ensure that that further expansion of lending by banks is conducted on sound lending practices, by not jeopardizing the system's performance.

The structure of NPL has constantly been dominated by loans classified as 'loss'. However, in December 2010, the share of these loans to total NPL was 59.5 percent or 12.5 pp lower compared to 2009. Whereas, the share of loans classified as 'doubtful' increased to 40.5 percent of total NPL. In 2010, loans classified as 'loss' increased by euro 10.8 million (27.3 percent), while loans classified as 'doubtful' increased by euro 19 million (122.5 percent).

Regarding the structure of NPL in terms of economic agents, it can be noticed that during 2010, the household loan portfolio has not experienced any change with regard to the quality compared to the previous year (Figure 21). On the other hand, the portfolio of loans designated to non-financial corporations was characterized with higher sensitivity towards economic difficulties that appeared as a consequence of the financial crisis. During this period, 5.3 percent of loans to enterprises were classified as NPL, which represents a growth of 0.2 pp compared to 2009.

Kosovo's banking system has continuously shown to be conservative in terms of NPL coverage with loan loss provisions. In December 2009, coverage ratio of NPL with loan loss provisions stood at 125 percent, whereas the average for the last four years was 130 percent (Figure 22). In December 2010, provisions amounted at euro 93.2 million, compared to euro 77.4 million in December 2009. The high level of NPL coverage ratio indicates that the actual level of NPL does not threaten the stability of the banking system.

Figure 22. NPL and provisions

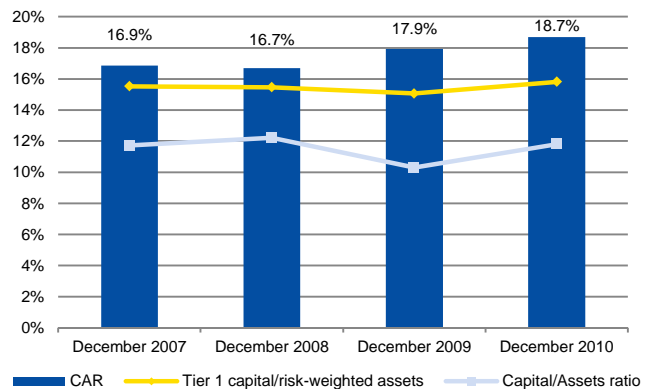


Source: CBK (2011)

iii. Solvency risk

One of the most important indicators for measuring the banking system sustainability is the Capital Adequacy Ratio (CAR). In 2010, Kosovo's banking system increased its CAR to 18.7 percent compared to 17.9 percent in 2009 (Figure 23). This level is quite satisfactory considering that it is well above the minimal level of 12 percent that is required by the CBK regulative. All commercial banks operating in Kosovo are well capitalized and do not have any difficulty to fulfil the criterion of 12 percent for the CAR.

Figure 23. Capital adequacy of banking sector



Source: CBK (2011)

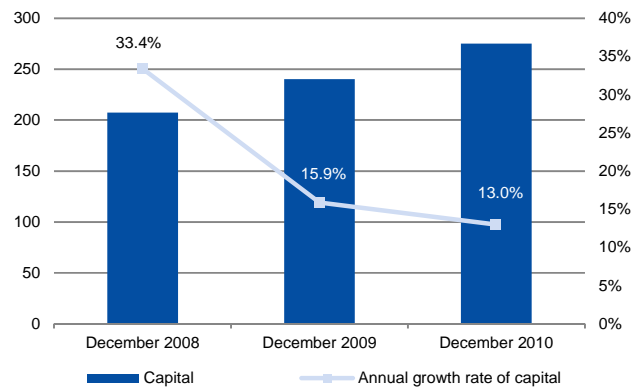
The increase of this indicator during 2010 was driven by the faster growth of capital (13

percent in 2010) compared to the growth of Risk-Weighted Assets (RWA), which increased by 9 percent in 2010. During 2010, banks increased the investments in securities, which convey lower risk compared to other categories, thus contributing to the slowdown of the RWA growth.

In the end of 2010, the total amount of banking system capital was euro 271.4 million, compared to euro 240.2 million in the same period of 2009. Since December 2008, the capital of the banking system followed an increasing trend, but the growth rate continuously slowed down (Figure 24). The main source of financing for the banking system's capital continues to be the shareholders capital with a share of 62.8 percent, followed by the retained profit by banks with a share of 21.9 percent.

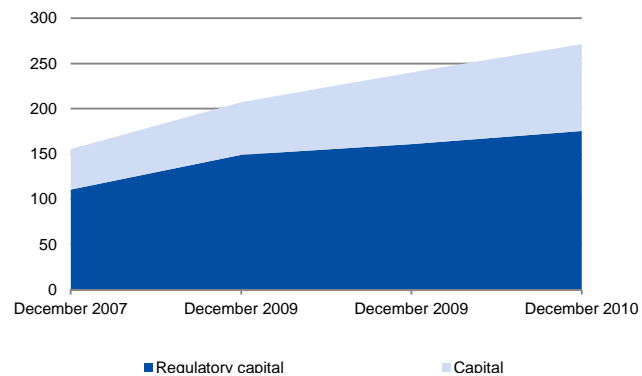
Based on CBK rule number I¹⁰, in December 2010, banks were obliged to maintain the level of capital at euro 175.3 million. However, banks operating in Kosovo continuously kept a higher level of regulative capital than required by the CBK. In December 2010, the total regulative capital was euro 271.4 million, which represents a surplus of regulative capital amounting at euro 96.1 million (Figure 25).

Figure 24. Total banking system capital



Source: CBK (2011)

Figure 25. Total capital and regulatory capital, in millions of euro



Source: CBK (2011)

3.3.2.4.1. Stress-test analysis

The satisfactory position of the Kosovo's banking system with regard to the sustainability against the credit and liquidity risk is confirmed also by the stress-test analysis. The results presented in this report are based on December 2010 data on commercial banks operating in Kosovo. This part provides an analysis of the sensitivity of the banking system against credit risk, combined with the interest rate and exchange rate risks. The sensitivity against the liquidity risk was also tested, based on hypothetical assumptions on the withdrawal of deposits from the banking system.

i. Stress-test results - credit risk

In assessing the banking system sensitivity against the credit risk, it is assumed that the share of Non-Performing Loans (NPL) to total banking system loans will increase by 4.5pp,

¹⁰ According to the CBK Rule 1, banks are obliged to maintain a capital to RWA ratio of at least 12 percent.

from the current NPL level of 5.9 percent in 2010.¹¹ The growth of NPL was also combined with the assumption of a decline of interest rates and depreciation of the Euro currency against.¹² Consequently, it was assessed the impact of these three assumptions on the banking system regulatory capital, risk-weighted assets and, eventually, on the Capital Adequacy Ratio (CAR).

The results from this analysis indicate that under the abovementioned scenario, only one of the banks (out of eight banks operating in Kosovo) would have problems with the regulatory capital ratio, recording a lower than 12 percent CAR, while the necessary amount for the recapitalization of this bank would reach at euro 1.5 million, or only 0.03 percent of GDP. For the banking system in general, the NPL to total loans ratio would reach at 10.4 percent.

Considering the abovementioned results, it can be assessed that the banking system is quite sustainable against possible deterioration in the loan portfolio quality. This is mainly due to the sufficient ratio of provisioning against potential loan losses and the high capital adequacy ratio in the sector in general (capital adequacy ratio was 18.7 percent in December 2010). The system also appears to be sustainable against eventual changes of interest rates and exchange rate. Predominantly fixed interest rates offered by banks for loans and deposits make the sector less sensitive against the interest rate risk. Likewise, since only less than 1 percent of total banking system assets is held on currencies other than Euro, the exchange rate risk is only marginal.

ii. Stress-test results - liquidity risk

In assessing the banking system sensitivity against the liquidity risk, it is assumed a withdrawal of deposits at the rate of 8 percent of total deposits on daily basis for a period of 5 consecutive days. The total amount of deposits withdrawn after 5 days would be equivalent to 34 percent of total deposits in the banking system. Regarding the availability of liquid assets to banks during this period, it is assumed that within a day banks would be able to convert to cash 80 percent of liquid assets and 1 percent of non-liquid assets. It is assumed that banks can use their reserves, but the possibility of financing through other sources was excluded. Thus, through this scenario it was assessed the sufficiency of the available liquid assets to the banking system to cope with such a withdrawal of deposits, without having access to external financing.

Stress-test results suggest that under such hypothetical scenario, liquidity problems would start to emerge after the third day, with only one of the banks facing liquidity shortage. The necessary amount to fulfil the liquidity needs of this bank, under the considered assumptions, would be euro 1.5 million (0.04 percent of GDP). After the fifth day, the liquidity problems would appear in four banks. Total additional liquid assets, necessary to overcome the liquidity problems, would reach at euro 24.1 million or 0.58 percent of GDP (Table 7). After the fifth day, the loan to deposit ratio for the overall banking system would reach at 113.3 percent (assuming that the level of loans remains unchanged).

¹¹ The assumed growth rate of NPL is defined by taking into account the average economic growth rate in Kosovo in the recent years, the assumption on the economic decline of 1.6 percent in 2011 and the coefficient of elasticity between NPL and the output gap (0.8), which is based on an unpublished IMF study titled "CESE Bank Loss Projection and Stress Testing Exercise", July 2010.

¹² For detailed information on the methodology, consult the Financial Stability Report, no. 1, page 53 – 54, CBK (2010).

Table 7. Liquidity risk, results

Description	Number of banks 1/	Necessary additional liquid assets (in thousands of euro)
After the first day	0	0
After the second day	0	0
After the third day	1	1,510
After the fourth day	4	5,907
After the fifth day	4	24,074

1/ Number of banks in need of additional liquid assets

In general, it can be considered that, following such a conservative scenario, Kosovo's banking system appears to have quite good liquidity position. The problems encountered, based on this hypothetical scenario, are isolated in individual banks. The satisfactory ratio between liquid assets and total assets makes the banking system sustainable against a considerable withdrawal of deposits.

Comparing these outcomes with those of June 2010, under the same scenario (withdrawal rate of deposits 8 percent in daily basis for a period of five days), the situation appears to be quite similar. Using June 2010 data, the assumed rate of deposits withdrawal would have an impact in one of the banks after the third day, posing the need for additional liquid assets amounting at euro 2.2 million. After the fourth day, the total amount of required additional liquid assets would be euro 5.8 million, but concentrated in only one bank, while, following the application of the scenario in December 2010 data, the amount of additional liquid assets (almost the same) is distributed in four banks (Table 7).

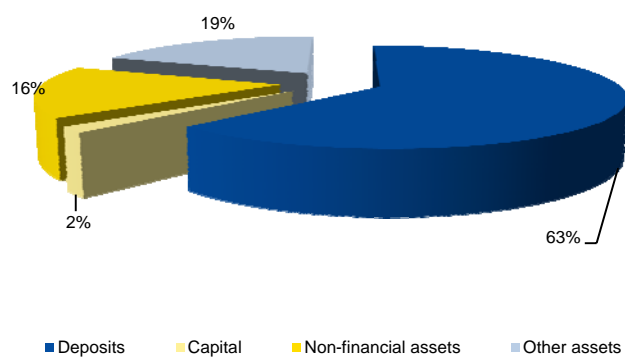
3.3.3. Insurance Companies

The sector of insurance companies in Kosovo continued to expand its activity in 2010. Nevertheless, the share of this sector in total financial sector assets remains relatively small. The number of insurance companies operating in Kosovo at the end of 2010 was 11, of which 10 companies exercise their activity in the non-life insurance services, whereas one company offers life insurance services. Regarding the

ownership structure, eight insurance companies are foreign owned, whereas three other insurance companies are domestically owned, which is similar to the previous year. Concerning the composition of assets in terms of ownership, 77.4 percent of total insurance companies assets are foreign owned, whereas 22.6 percent are domestically owned. During 2010, the insurance company "Dukagjini", which was previously partly foreign owned, in 2010, incurred some changes in its ownership structure, with the Slovenian company "SAVA re" purchasing 100 percent of its shares.

Total assets of the insurance companies in 2010 amounted at euro 97.2 million, which represents an annual growth rate of 9.3 percent. The largest share of insurance companies' assets consists of deposits, comprising 51.5 percent of total assets (Figure 26). Regarding

Figure 26. Structure of assets of insurance companies



Source: CBK (2011)

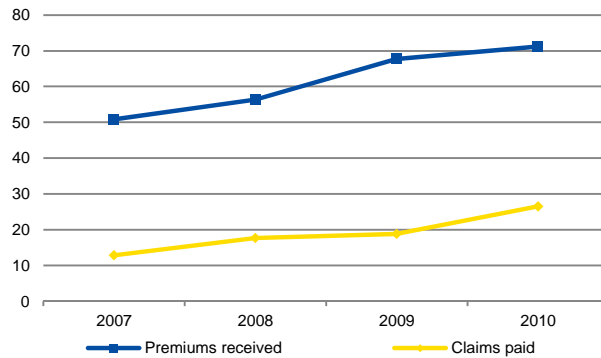
the liabilities, shareholders equity represents the largest category, with a share of 41.8 to total liabilities.

The capital to total assets ratio, which expresses the capital adequacy of insurance companies, was 41.8 percent in 2010, compared to 43.4 percent in 2009. The ratio between capital and technical reserves, which indicates the insurance companies' capacity to cope with potential losses, was 77.7 percent in 2010, compared to 81.5 percent in 2009. The decline in this ratio came as a result of the faster growth rate of the technical reserves, which increased by 12.8 percent, compared to the growth rate of 7.6 percent for the capital.

Net profit of insurance companies in 2010 was euro 1.5 million, compared to the net loss of euro 4.9 million in 2009. The improvement of the financial output of insurance companies during 2010 has been reflected also in the trend of the two profitability indicators, consisting of the Return on Average Assets (ROAA) and the Return on Average Equity (ROAE). Thus, the ROAA reached at 1.6 percent in 2010 from a negative ratio of -5.7 percent in 2009, whereas ROAE reached at 3.9 percent from -12.5 percent in 2009.

The number of the insurance policies issued by insurance companies operating in Kosovo, in 2010 reached at 540.7 thousands, which represents an annual increase of 5.7 percent (Figure 27). The premiums received increased by 5.1 percent, reaching the amount of euro 71.3 million in the end of 2010. However, the growth rate of the value of the received premiums was lower in 2010, compared to the growth rate of 2009, where the annual growth

Figure 27. Premiums received and claims paid, in millions of euro



Source: CBK (2011)

rate was 20.0 percent. The slowdown of the growth rate of the received premiums was driven by the decrease of border insurance fees, which occurred twice during 2010.¹³ Consequently, revenues from the border policies recorded an annual decline of 16.3 percent in 2010, amounting at euro 10.6 million. The activity of insurance companies in Kosovo is mainly focused in the issuing of Third Party Liability (TPL) insurance policies, which in 2010 generated the largest share of the received premiums (57 percent of total premiums). Revenues from TPL policies amounted at euro 40.6 million and recorded an annual growth rate of 11.8 percent. The remaining part of the received premiums comes from voluntary insurance policies, which in 2010 amounted at euro 20 million and recorded an annual growth rate of 6.8 percent. The share of received premiums from voluntary policies to total received premiums stood at 28 percent, which is consistent with the share of voluntary policies in 2009.

The amount of claims paid by insurance companies marked an increasing trend in 2010, reaching at euro 26.5 million euro (annual growth of 40.8 percent). The largest share of the claims paid consists of payments to TPL policyholders (around 72 percent of total claims paid in 2010). The ratio between claims paid and received premiums in 2010 reached at

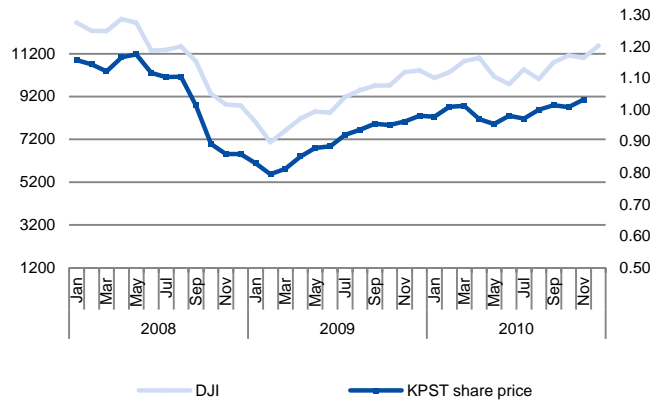
¹³ According to section 8.3 of CBK Rule 3, the insurance companies are entitled to apply for changing the fees only twice a year. In January 2010, the border insurance fee decreased by 12 percent on average and in June 2010 by 15 percent.

37.2 percent (27.8 percent in 2009), reflecting a faster growth of claims paid, compared to the growth of the received premiums by insurance companies.

3.3.4. Pension Funds

Kosovo’s pension system assets in 2010 reached at euro 493.7 million (12.0 percent of GDP), recording an annual growth rate of 29.6 percent. The performance of the pension system in 2010 has improved, compared to the performance in the previous year. This is because the share price of Kosovo Pension Savings Trust (KPST), which manages the largest part of pension system assets, recorded an annual growth rate of 6.2 percent, reaching at euro 1.04 (the basic price during contribution is counted euro 1.0 per share). The performance improvement of KPST investments reflects the positive developments in the international markets of capital during 2010, which is presented in Figure 28, indicating that KPST shares price followed a very similar pattern with the Dow Jones Industrial Index.

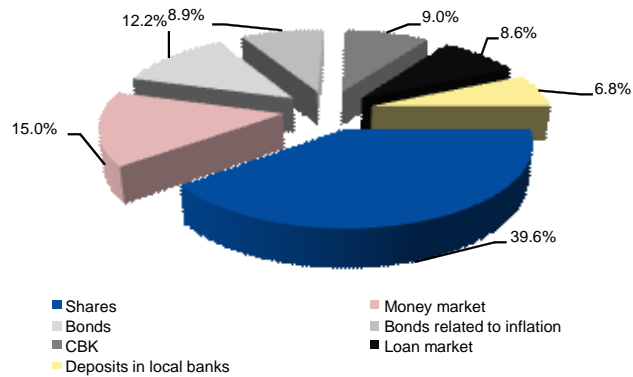
Figure 28. KPST share price and DJI index



Source: Trust (2011), DJI (2011)

From the total of euro 488.5 million of KPST assets, 6.8 percent are invested in commercial banks in Kosovo, whereas 9.0 percent have been deposited in the CBK (Figure 29). The rest of the assets is invested abroad (mainly in the USA, Great Britain and Japan). The largest part of the KPST assets have been invested in shares (around 40 percent), whereas a considerable part has also been invested in the money market (15 percent) and credit default swaps (12.2 percent).

Figure 29. Structure of KPST investments



Source: Trust (2010)

Regarding the assets of the Slovenian-Kosovo Pension Fund, the largest share (over 95 percent) have been invested in bonds and bank deposits, whereas the remaining is kept in cash, shares, etc.

3.3.5. Microfinance Institutions and other Non-Bank Financial Institutions

The number of microfinance institutions (MFI) operating in Kosovo in the end of 2010 was 13, while the number of non-banking institutions was 8. The MFI market in Kosovo was continuously characterized with a relatively high degree of concentration. However, during 2010, the MFI industry marked a decline in the concentration ratio. This is confirmed through the Herfindahl-Hirschman Index for assets, according to which the level of concentration in the MFI market declined to 1,747 points, compared to 2,115 points in 2009. The decline in the degree of concentration in the MFI industry can also be noted in

through the decline of the concentration ratio of the assets of the three largest MFI in the country (Figure 30). The decrease of market concentration ratio in this industry can be an indication of the intensification of competition between microfinance institutions.

The MFI activity continues to be concentrated in crediting the small businesses and households.

The number of loans issued by

these institutions in the end of 2010 reached at 62,683, which represents an annual growth rate of 9 percent. In 2010, the value of loan portfolio issued by MFI reached at euro 116 million, marking an annual growth rate of 6.5 percent. The share of loans issued by MFI to total loans issued by Kosovo's financial sector in 2010 was 7.4 percent, which represents a similar level compared to the year 2009. The average value of a loan issued by MFI in 2010 was euro 1,852, compared to the average value of a loan issued in 2009, that was euro 1,405 in 2009.

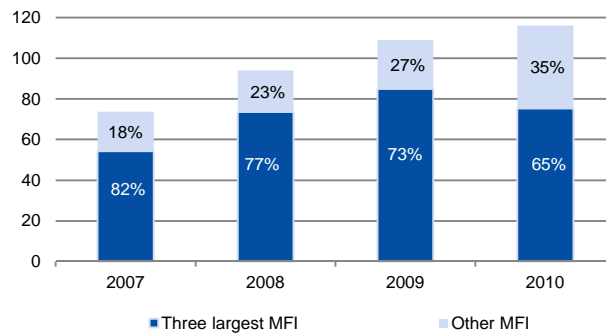
In 2010, the MFI system marked a decrease of performance, compared to the performance of the MFI in 2009 (loss of around euro 2.0 million). Consequently, the performance indicators, such as return on average assets (ROAA) and return on average equity (ROAE) declined during 2010. ROAA in 2010 was -1.6 percent, compared to 1.4 percent in the year 2009, whereas ROAE indicator was -5.5 percent, compared to 4.3 percent in the year 2009.

Financial auxiliaries in Kosovo are composed of Exchange Bureaus and Money Transfer Agencies (MTA). The amount of transfers through MTA during 2010 reached at euro 231.8 million, which is an increase of 2.1 percent compared to year 2009. Out of this amount, 92.1 percent were incoming transfers to Kosovo. Transfers through MTA represent 4.2 percent of total international transfers, whereas the largest part of international transfers is realized through commercial banks (around 78 percent of total transfers)

3.4. External Sector

Kosovo's economy continued to have a high level of current account deficit also during 2010. This year, mainly due to the increase of the negative balance in the goods account and the decrease of the positive balance in services account, the current account deficit recorded an annual growth of 12.4 percent. While Kosovo exports in 2009 recorded a decline, the recuperation of demand in the global economy led to a considerably high growth of exports. Even though the growth rate of exports was higher compared to the growth rate of imports, yet the high weight that imports have in the structure of Kosovo's trade continued to offset the growth effect of exports. As a consequence, trade deficit of Kosovo in 2010 a growth rate of 9.4 percent compared to the previous year. Income and current transfers account continued to contribute positively to the decrease of the current account deficit. The positive balances of income and current transfers account recorded an annual growth of 50.7 percent and 2.6 percent, respectively. At the same time, the capital and financial account recorded a positive balance of euro 448.9 million. The annual decline of 17.3 percent was mainly driven by the decrease of the capital account balance in this period.

Figure 30. MFI Assets , in millions of euro



Source: CBK (2011)

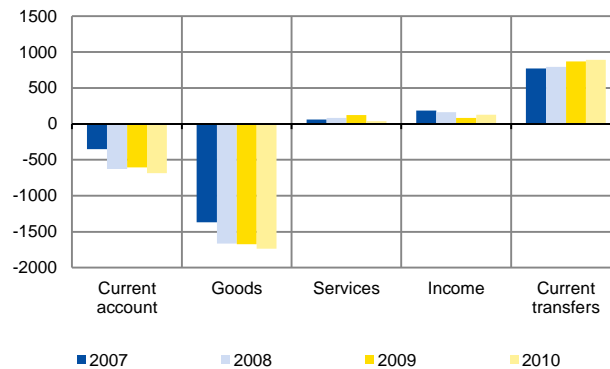
3.4.1 Current account

The negative trade balance of the goods account remains the main cause for the high current account deficit. In 2010, the current account deficit reached at euro 684.4 million, compared to euro 603.5 million in the same period of the previous year (Figure 31).

Recording an annual growth of 9.4 percent, the negative trade balance of goods was the main contributor to the increase of the current account deficit in 2010. On the

other hand, the growth of the positive balance in the income and current transfer accounts continued to contribute on the softening of the current account deficit. Income account recorded an annual growth of 50.7 percent in 2010 (-49.4 percent in 2009). Current transfers balance also increase, recording a growth rate of 2.6 percent in 2010 (9.0 percent in 2009).

Figure 31. Current account balance, in millions of euro



Source: CBK (2011)

3.4.1.1 Goods and services

Kosovo's economy continues to increase its trade activity. The degree of trade openness in 2010 reached at 59.3 percent of GDP, compared to 54.3 percent of GDP in 2009. The increase of exports during 2010 resulted in a higher coverage ratio of imports by exports, which reached at 13.7 percent, compared to 8.5 percent in the same period of the previous year (Table 8).

Table 8. Kosovo's trade balance, in millions of euro

Description	2007	2008	2009	2010
Exports	165.1	198.5	165.3	294.0
Imports	1,576.2	1,928.2	1,935.5	2,144.9
Trade balance	-1,411.0	-1,729.7	-1,770.2	-1,850.9
Export to import ratio (%)	10.5	10.3	8.5	13.7
Trade openness (% of GDP)	51.0	55.3	54.3	59.3

Source: CBK 2011

Amounting at euro 1.85 billion, Kosovo's trade deficit recorded an annual growth of 4.6 percent in 2010. The share of trade deficit to GDP in 2010 stood at 45.0 percent compared to 45.8 percent of GDP in 2009.

Kosovo imports during 2010 recorded an annual growth of 10.8 percent, reaching the amount of euro 2.1 billion. The annual increase of fuel prices in the international markets by around 25.0 percent during 2010 affected to some extent the increase of the overall value of imported goods, considering that mineral products represents one of main categories of Kosovo's imports.

Although the increase of prices during 2010 was mainly of global character, Kosovo's economy faced a higher level of inflation compared to the average of the EU and CEFTA

countries. The inflation rate in Kosovo was by around 4.8 pp higher than in the CEFTA and EU countries, leading to an appreciation of the Kosovo's Real Effective Exchange Rate (REER) in this period. In 2010, Kosovo's REER appreciated against the Eurozone countries by 1.4 percent and by 2.2 percent against the CEFTA countries.

Kosovo's exports in 2009 were characterized by a significant decline driven mainly by the global crisis which had a considerable negative effect on the on the sales of base metals industry, namely nickel minerals. The recovery of the world economy in 2010 resulted in a stronger external demand for base metals. As a result, the increase of base metal prices during 2010 had a positive impact on the production level and led to the increase of the volume and amount of sales. Considering that 90 percent of metals exported from Kosovo are nickel minerals, Kosovo's exports in 2010 recorded an annual growth of 77.8 percent, reaching the value of euro 294.0 million.

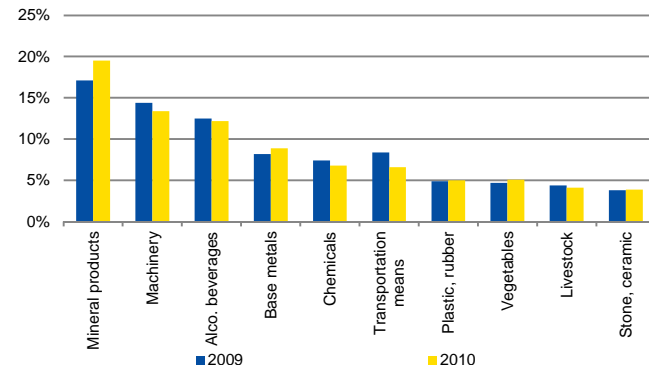
The structure of imports in 2010 was similar to the previous year (Figure 32). However, differently from last year, when imports of mineral products (mainly fuel) recorded an annual decline of 12.5 percent, the import of mineral

products in 2010 recorded an annual growth of 26.5 percent, thus contributing by around 4.5 pp to the overall growth of imports. The share of mineral products to total imports in 2010 increased to 19.5 percent (17.1 percent in 2009). The import of machinery and equipment products also recorded an annual growth of 3.4 percent in 2010, but its share to total imports decreased to 13.4 percent (14.4 percent in 2009). Base metals and food products remain important categories of Kosovo imports, and their share to total imports in 2010 was 8.9 and 12.2 percent, respectively.

The structure of exports in 2010 was dominated by base metals, with a share of 63.0 percent of total exports, compared to 53.5 percent in December 2009 (Figure 33). The recovery of external demand and the increase of prices in the metal industry in international markets had a positive impact in the significant growth of base metals exports, which, in December 2010, reached at euro 185.2 million (euro 88.4 million in December 2009), contributing by 58.6 pp to overall growth of Kosovo's exports.

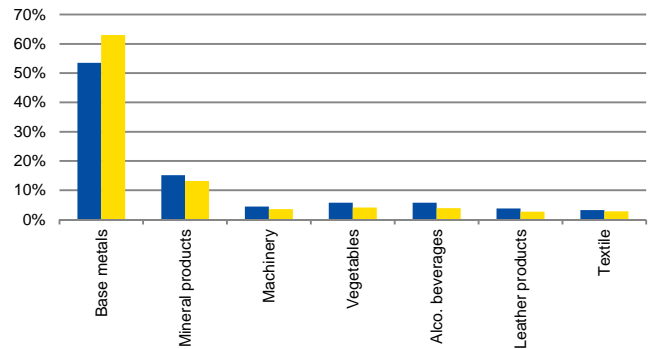
The increase of overall exports in 2010 was also due to the growth by 55.3 percent of mineral products exports, which represented 13.2 percent of total exports. Machinery and equipment exports (mainly consisting of the exports of electricity) represent 3.6 percent of

Figure 32. Main categories of the structure of imports, in percentage



Source: CBK (2011)

Figure 33. Main categories of the structure of exports, in percentage



Source: CBK (2011)

total exports. Unlike last year, when machinery and equipment export recorded an annual decline of 18.0 percent, exports of this category recorded an annual growth of 48.8 percent in 2010.

The classification of the imported products according to their final use or Broad Economic Categories (BEC) was similar to the previous year. According to this classification, the intermediate goods represent the largest

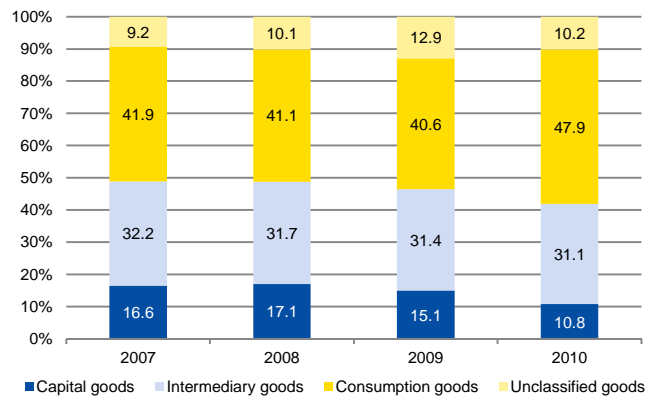
category with a share of 47.9 percent of total imports, followed by consumption goods with a share of 31.1 percent of total imports (Figure 34). The relatively high share of intermediate goods in the overall imports indicates that the production activity in the Kosovo's economy considerably depends on the import of raw materials from abroad. Also, the increase of the share of consumption goods to total imports continuously indicates a low level of domestic production. The share of capital goods to total imports decreased to 10.8 percent in 2010 compared to 15.1 percent in 2009, in spite of the faster growth of investments in the country during 2010.

The structure of Kosovo's trading partners in 2010 was similar to the previous years. In 2010, Kosovo realized around 74.7 percent of total trade with the European Union (EU) and with CEFTA member countries. The recovery of the demand in EU countries, especially in the second half of 2010, made Kosovo exports to these countries record a higher growth compared to export to the region countries. The noncompliance with CEFTA

agreement, for political reasons, by Serbia and Bosnia and Herzegovina continued to obstruct Kosovo's exports to these countries also during 2010. In addition to the problems related to the implementation of the CEFTA agreement, as of end 2010, also Kosovo's status as a favored country for trade with EU has expired, thus presenting another obstacle for Kosovo's firms to penetrate the external markets.

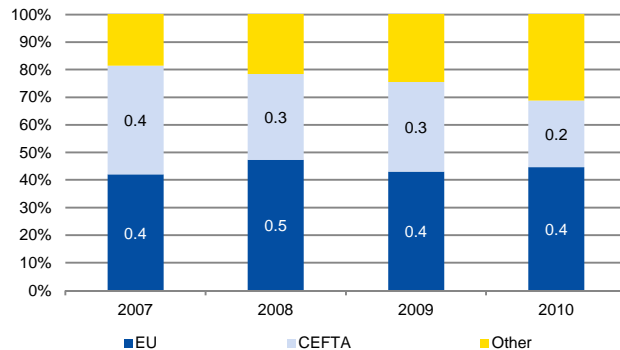
Kosovo's exports towards EU reached at euro 131.5 million in 2010, which represents an annual growth of 84.4 percent. Consequently, the share of Kosovo's exports to EU increased to 44.7 percent, compared to 43.1 percent in the previous year (Figure 35). Among the EU countries, Italy represents the main destination for Kosovo's exports, with a share of 27.3 percent of total exports. The largest part of exports to Italy consists of nickel minerals. Exports to Germany, Austria and Slovenia have also increased their share to total exports.

Figure 34. Imports by BEC



Source: CBK (2011)

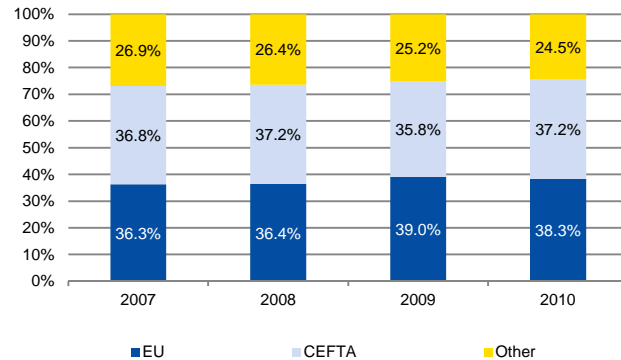
Figure 35. Structure of exports by trading partners, in percentage



Source: CBK 2011

The distribution of Kosovo's exports among CEFTA member countries in 2010 was similar to the previous year, while the share of exports to CEFTA countries in the overall amount of Kosovo's exports decreased 24.1 percent in 2010 from 32.4 percent in 2009. Among the regional countries, the largest share of Kosovo's products continues to be exported in Albania and Macedonia (11.0 and 8.9 percent of total exports, respectively). It is worthy to mention that despite obstructions imposed by Serbia and Bosnia and Herzegovina, exports to these two countries marked a slight increase in 2010. During this year, exports to Bosnia and Herzegovina reached at euro 1.9 million (euro 1.2 million in 2009), whereas exports to Serbia reached at euro 3.8 million (euro 3.5 million in 2009).

Figure 36. Structure of imports by trading partners, in percentage

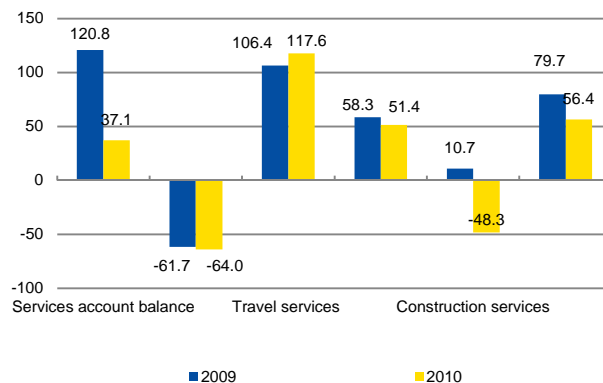


Source: CBK 2011

EU and CEFTA countries represent the main trading partners for Kosovo also in terms of imports. Until December 2010, around 38.3 percent of total goods imported by Kosovo came from the EU member states (Figure 36). The largest share of imports comes from Germany (12.8 percent of total imports) and Greece (4.7 percent of total imports). Among the CEFTA countries, most of the imported goods come from Macedonia and Serbia, with a share of 14.7 and 12.1 percent in total imports, respectively.

The account of trade in services had a positive in 2010, but differently from the previous years, the balance of this account recorded a significant decline. In 2010, the balance of trade in services amounted at euro 37.1 million, compared to euro 120.8 million in the previous year (Figure 37). The decrease in the balance of services in this period mainly reflects the slower growth of income from the sale of services to nonresidents, compared to the

Figure 37. Services account, in millions of euro



Source: CBK (2011)

growth of payments for services purchased by Kosovo residents. In 2010, the services account generated income amounting at euro 515.0 million, with an annual growth of 20.1 percent. At the same time, the total payments for services purchased abroad by Kosovo residents reached at euro 477.9 million, which represents an annual growth of 55.2 percent. The increase of payments for construction services, namely the construction services for the first segment of Morinë-Merdarë highway, were the main driver of the significant decrease of the services balance in this period. The income from construction services reached at euro 52.0 million in 2010 (euro 15.7 million in 2009), whereas the payments for construction services reached at euro 100.3 million (euro 5.0 million in 2009).

In December 2010, income from travel services recorded an annual growth of 18.2 percent, representing around 43.2 percent of total services income. However, the increase of payments for travel services (mainly travels for summer holidays) by 28.1 percent led to an increase of travel services by 10.4 percent. In addition to travel services, communication and government services (services provided to embassies and to military presence of NATO) and all the other services reported a negative balance in 2010.

3.4.1.2. Income and current transfers

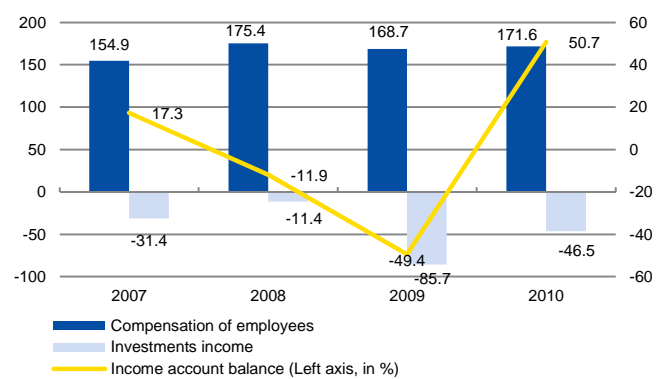
Income account in 2010 recorded a positive balance of euro 125.1 million, which represents an annual growth of 50.7 percent. The inflows in the income account amounted at euro 188.4 million in 2010, which represents a growth of 3.3 percent. At the same time, outflows reached euro 63.3 million, which represents a decrease of 36.3 percent. A dominant category within the income account remains the compensation of employees, which in 2010 represented 93.5 percent of total income, whereas income from investments of Kosovar residents abroad represented 6.5 percent of total income in this category.

The income from compensation of employees in 2010 was euro 171.6 million, which represents an annual growth of 1.7 percent (Figure 38). The balance of the compensation of employees account reached at euro 176.1 million in 2010 (euro 169.7 million in 2009), whereas the compensation of non-resident employees working in Kosovo reached at euro 4.5 million (euro 0.9 million in 2009).

In 2010, as a result of inflows amounting at euro 12.3 million and outflows amounting at euro 58.8 million, the category of investment income recorded a negative balance of euro 46.5 million (85.7 million in 2009). Inflows in the category of investment income mainly consist of investments of domestic institutions in international markets (KPST, commercial banks and CBK), while outflows mainly consisted of the income generated by foreign companies operating in Kosovo, such as commercial banks, other foreign enterprises, etc.

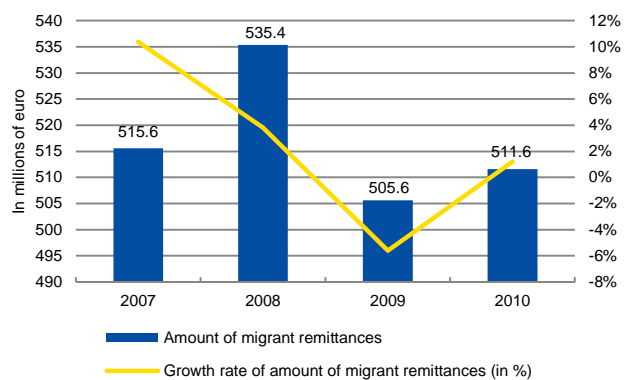
Current transfers continue to represent a category of particular importance in the Kosovo's balance of payments, which continuously contributes into the narrowing of the current account deficit.

Figure 38. Income account balance, in millions of euro



Source: CBK (2011)

Figure 39. Value of migrant remittances received in Kosovo, in million of euro



Source: CBK (2011)

Current transfers balance reached at euro 888.9 million in December 2010, which represents an annual growth of 2.6 percent. Current transfers of private sector are dominated by migrant remittances, which represent around 47.3 percent of total private sector transfers in the country. In December 2010, the balance of migrant remittances reached at euro 420.2 million, which represents an annual growth of 6.3 percent. The growth

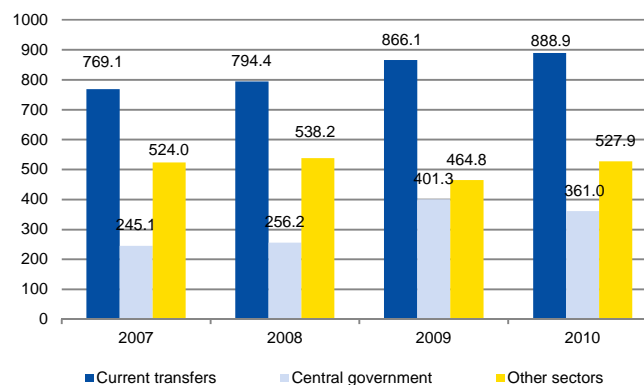
of migrant remittances balance is attributed to the significant decline of remittances outflows from Kosovo's economy, compared to the level of inflows. While the value of total transfers from Kosovo economy recorded an annual decline of 17.2 percent, the value of total transfers received in the category of migrant remittances recorded an annual growth of 1.2 percent, reaching at euro 511.6 million (euro 505.6 million in the previous year) (Figure 39). The recovery of the Eurozone economies, where the largest part of Kosovo emigrants are settled, is expected to have a positive impact on the level of migrant remittances inflows to Kosovo, which mainly come from Germany, Switzerland, Italy and Austria. At the same time, the balance of government sector transfers (donors, EULEX and UNMIK) reached at euro 361.0 million, marking an annual growth of 10.1 percent (Figure 40).

3.4.2 Capital and Financial Account

The capital and financial account during 2010 was characterized with a positive balance of euro 448.9 million (euro 543.0 million in 2010). The decline of the capital and financial account was driven by the capital account, which in 2010 was reduced to euro 25.4 million from 108.2 million in 2009. Regarding the financial account, the positive balance of euro 423.5 million during 2010 was by 2.6 percent lower compared to 2009

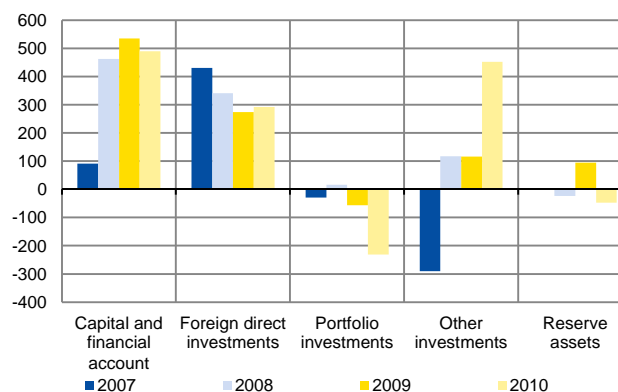
(euro 434.8 million). Among the factors which mostly contributed to the decrease of the financial account balance was the increase of portfolio investments in external markets, which in 2010 reached at euro 231.0 million. The high growth of portfolio investments is mostly attributed to the significant growth of investments by pension funds and commercial banks. On the other hand, the category of other investments had a significant positive effect on the financial account as a result of the withdrawals of deposits from abroad by monetary authorities, commercial banks and other economic sectors. Increase is noticed also in the level of FDI (net), which in 2010 recorded an annual growth of 10.8 percent (Figure 41).

Figure 40. Current transfers, in millions of euro



Source: CBK (2011)

Figure 41. Financial account, in millions of euro



Source: CBK (2011)

3.4.2.1 Foreign Direct Investments

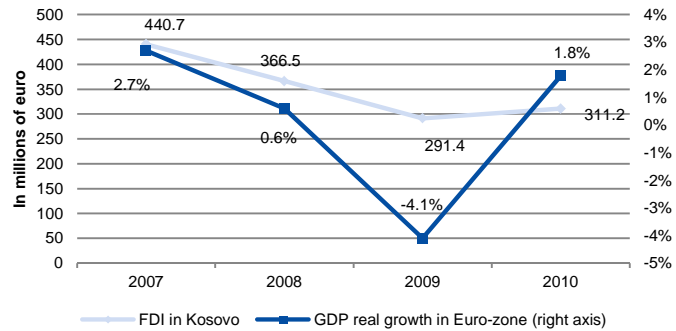
The FDI account reached the amount of euro 307.9 million in 2010, which is an increase of 9.6 percent compared to year 2009. The direct investments of Kosovo's residents abroad declined to euro 3.4 million in 2010, compared to 10.5 million in 2009. Whereas, the amount of FDI received in the Kosovo's economy in 2010 reached at euro 311.2 million, compared to euro 291.4 million in 2009 (Figure 42).

The difficulties related to the access of Kosovo's firms in a part of regional market, caused by Serbia and Bosnia and Herzegovina, remain an important challenge for Kosovo in attracting new FDI. The level of FDI in Kosovo has followed a similar trend with the real economic growth rates of EU economies, which represent the main source of FDI for Kosovo (Figure 42).

Capital investments represent the main category of FDI in Kosovo, followed by the category of other investments within the FDI. Capital investments, which compose 70.5 percent of total FDI, reached at euro 221.8 million in 2010 (euro 211.1 million in 2009). The category of other investments within FDI is mostly composed of intercompany loans. This FDI category reached at euro 49.5 million in 2010 (euro 23.2 million in 2009), accounting for 15.9 percent of total FDI in Kosovo. Another important category of FDI in Kosovo consists of the reinvested earnings of foreign businesses operating in Kosovo. The reinvested earnings reached at euro 43.4 million (euro 57.2 million in 2009), representing 13.8 percent of total FDI in Kosovo.

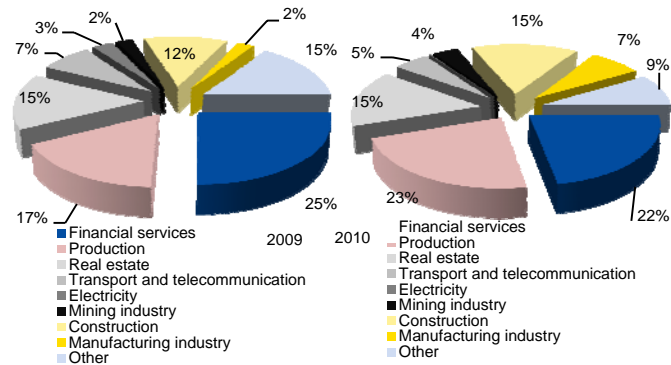
The structure of FDI by economic activity incurred some slight changes during 2010 (Figure 43). In 2010, the manufacturing sector represented the sector with the largest FDI inflows

Figure 42. Foreign direct investments in Kosovo and the economic growth in Euro-zone



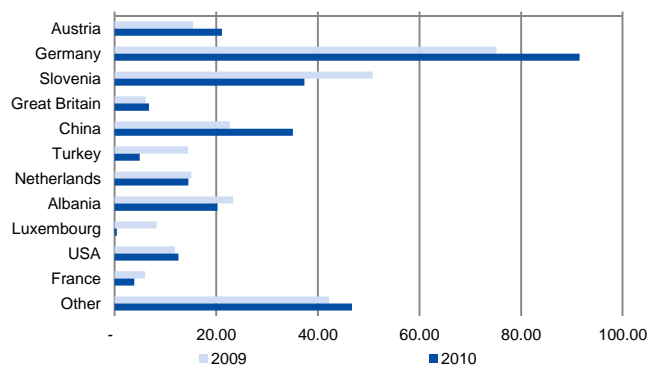
Source: IMF (2011) and CBK (2011)

Figure 43. Structure of FDI by economic activity



Source: CBK (2011)

Figure 44. FDI by country of origin



Source: CBK (2011)

(23.0 percent of total FDI). Another important sector with regard to the amount of received FDI consists of the financial sector, which absorbed 22.1 percent of total FDI in Kosovo. The FDI in the financial sector are mainly composed of reinvested earnings of financial institutions that operate in Kosovo. The real estate sector (15 percent of total FDI) and the construction sector (15 percent of total FDI) also represented important sectors for the attraction of FDI in Kosovo during 2010.

The origin of foreign investors in Kosovo is mainly from the EU countries. Germany continues to be the country where most of the FDI come from, followed by Slovenia which represents the second country in terms of the volume of investments in Kosovo. An important share of FDI in Kosovo also comes from Austria and China (Figure 44).

3.4.2.2 Portfolio Investments, Other Investments and Reserve Assets

Portfolio investments abroad recoded a considerable growth in 2010, reaching at euro 231.0 million (euro 56.5 million in 2009). Out of euro 231.0 million, 66.9 percent consist of the investments of pension funds, while the remaining 33.1 percent are investments in international financial markets by commercial banks operating in Kosovo.

These investments are mostly oriented in money market instruments (for example, in securities), while a smaller part of them is invested in other instruments of capital markets. The recovery of global financial markets can be considered as the most important factor that resulted in the increase of portfolio investments during 2010.

The balance of “other investments” in 2010 was positive, amounting at euro 390.4 million compared to euro 116.2 million in 2009. Within the other investments category, assets represented 62.1 percent of total investments, while liabilities composed 37.9 percent. A considerable growth within the other investments category was recorded in the side of assets as a result of the higher level of investments abroad, mostly in money market instruments invested by commercial banks, monetary institutions and other sectors. Liabilities, on the other hand, continue to be dominated by the trade credit, which represents 43.1 percent of total liabilities within the other investments category. In the end of 2010, the amount of trade credit was euro 63.7 million, which compared to the previous year represents a decline of 39.9 percent. The decline of the trade credit may indicate a better solvency of firms in Kosovo during 2010, compared to year 2009. Reserve assets of Kosovo in the end of 2010 recorded an annual growth of euro 46.9 million.

4. Supervision of Financial Institutions

As of its establishment, CBK has a licensing, regulatory and supervising authority over all financial institutions in Kosovo, and as such it contributes towards development and modernization of financial sector in Kosovo. Currently, the financial sector in our country consists of banking industry, insurance industry, pension funds and other financial institutions (microfinance institutions, non-bank financial institutions, exchange bureaus for currencies and payments and money transfer institutions).

Even in 2010, taking for granted the best international standard in financial sector development, CBK continued to invest in promoting licensing effectiveness and efficiency and the financial supervision regulative aiming at further promotion of a competitive financial sector based on economy market.

Based on Basel Core Principle on effective supervision of banking system, in 2010, steps have been taken towards capacity building for risk profile-based supervision in banking sector, aiming at a supervising synergy which is expected to be reflected in a more effective coordination of micro-prudential and macro-prudential supervision. Also, with purpose to establish as fair as possible the risk-based solvency, good steps have also been taken in the insurance industry towards adoption of basic principles set forth under Solvency II framework.

In accordance with its duties and authorities established by law, CBK in 2010 initiated a revision of legislation relating to all key constitutive systems of financial sector. Law on Deposit Insurance System in Kosovo was adopted in the end of 2010, while the functionality of deposit Insurance Fund will be completed in 2011. Also, the first versions have been drafted for the law on commercial banks, microfinance institutions and other financial non-bank institutions, then the draft law on compulsory motor third party liability insurance, the draft law on general insurances and it is worked on the amendment of law on pensions.

4.1. Licensing and Methodology

One of the main CBK functions is to ensure supervision and regulation of financial institutions, with purpose to establish a sound, sustainable, competitive and reliable financial system and which provides a wide range of financial services. The direct responsibility for accomplishment of this mission falls on directorates, such as Licensing and Methodology Directorate, Bank Supervision Directorate and Insurance and Pension Supervision Directorate.

4.1.1. Licensing

Criteria and conditions to obtain a license for exercising banking and financial activities by banks and other financial institutions in the Republic of Kosovo are established under Law No. 03/L-209 on Central Bank of the Republic of Kosovo and other sublegal acts adopted by the CBK. Pursuant to legislation governing its statutory functions, CBK has authority to set criteria for licensing of financial institutions and to reject those which do not fulfill these standards.

Licensing criteria established under legislation, aim at ensuring a fair financial market and regulated through a process based on the principle of justice, honesty and equality. Licensing conditions and criteria are of supervising character and do not intend creating barriers against investors. Entry of foreign investors in financial market of the country

proves the CBK open policy towards foreign investment, without violating the legal requirements.

CBK strategy in the area of financial institutions licensing is focused on attraction of investors having good financial situation, who fulfill the ethical and professional criteria to be fit and proper for shareholders and management, who are capable of run an approach towards a prudent development of the business in order to protect clients' interest, thus facilitating strengthening of the financial system and enhancement of reliability on it.

Licensing and Methodology Directorate in its licensing and regulating activity for commercial banks, insurance companies, intermediaries, supplementary pension funds and other financial and non-financial institutions, is guided by principles which are in compliance with the European Union directives and the best international practice, as presented under "Core Principles for Effective Banking Supervision" published by the Bank for International Settlements (BIS), and Core Principles for Effective Insurance Supervision published by the International Association of Insurance Supervisors (IAIS).

Licensing activity of financial supervision during 2010 included changes in opening new bank branches and other financial institutions in Kosovo; changes in structure of ownership and shareholding capital of banks and insurance companies; increasing services and banking products and insurances; amendment of normative acts, such as statutes of banks and insurance companies; changes and new appointments of administrators and senior management of banks and insurance companies, expansion of exchange bureaus network and money transfer agencies network.

Banks and insurance companies constantly worked in expanding their activities towards diversification of baking and insurance products, offering numerous investment and selection opportunities to their clients. During 2010, eight (8) banks with 321 branches and sub-branches continued to exercise their activities, whereas in insurance market there have been eleven (11) insurance companies, ten (10) non-life insurance companies and one life insurance company.

The CBK Governing Board approved during 2010 a preliminary license for the insurance company "Grawe Kosova" for life insurance, as well as the change in ownership structure of the insurance company "Dardania".

a) Microfinance Institutions

By the end of 2010, thirteen (13) microfinance institutions and eight (8) other non-bank financial institutions were operating in Kosovo. During 2010, upon the request of the institutions and pursuant to legal applicable regulative, the registration of "Cordaid" as microfinance institutions with is head office in Gjakova and "PTK" as non-bank financial institution with is head office in Prishtina has been withdrawn.

b) Insurance Intermediaries

By the end of 2010, there have been four (4) insurance intermediaries. Upon the request of the institutions and pursuant to legal applicable regulative, the licenses of Insurance Intermediaries "Intel Broker" and "Intel Service" with their head offices in Prizren, "Incoming" L.L.C and "Nic Holding" L.L.C with their head offices in Prishtina, were withdrawn.

c) Exchange Bureaus and Money Transfer Agencies

During 2010, the CBK Executive Board approved the registration of three (3) new Exchange Bureaus for currency exchange activities: “Kujtimi” in Peja, “Adis” in Prizren and “Aral” in Shtime. Twenty six (26) exchange bureaus and three (3) money transfer agencies were operating in Kosovo in the end of 2010.

Table 9. Banks licensing activity, 2006 – 2010

Description	2006	2007	2008	2009	2010
Prior licensed	7	8 ^[1]	8	9	8
Preliminary approvals *	2	1	1	0	0
Revocation/w ithdraw al of license	-1	0	0	-1	0
Rejected	1	0	0	0	1
Total	8	9	9	8	8

[1] Merging of banks NLB-KSB and NLB-BRK was effective on 2 January 2008

Source: CBK 2011

Table 10: Insurance Companies licensing activity, 2006 – 2010

Description	2006	2007	2008	2009	2010
Prior licensed	8	9	9	11	11
Preliminary approvals	1	0	2	0	1
Rejected	0	0	0	0	1
Total	9	9	11	11	12

Source: CBK 2011

Table 11. Pension funds licensing activity, 2006 – 2010

Description	2006	2007	2008	2009	2010
Compulsory pension funds	1	1	1	1	1
Supplementary pension funds	6	1	0	0	0
Individual pension funds	1	2	1	1	1
Total	8	4	2	2	2

Source: CBK 2011

Table 12. Microfinance and non-bank financial institutions registration activity, 2006 – 2010

Description	2006	2007	2008	2009	2010
Prior registered	19	18	19	22	20
Registered	1	1	4	0	0
Withdrawal of registration	-2	0	-1	-2	-2
Total	18	19	22	20	18

Source: CBK 2011

Table 13. Insurance intermediaries licensing activity, 2006 - 2010

Description	2006	2007	2008	2009	2010
Agents/operators	784	347	479	528	679
Insurance brokers	2	2	2	4	3
Damage adjusters	2	2	3	4	1

Source: CBK 2011

Table 14. Money transfer agencies registration activity, 2006 – 2010

Description	2006	2007	2008	2009	2010
Prior registered	2	3	3	3	3
Registered	1	0	0	0	0
Total	3	3	3	3	3

Source: CBK 2011

Table 15. Money exchange bureaus registration activity, 2006 – 2010

Description	2006	2007	2008	2009	2010
Prior registered	6	16	23	21	23
Registered	10	7	0	2	3
Withdrawal of registration	0	0	-2	0	0
Total	16	23	21	23	26

Source: CBK 2011

4.1.2 Methodology

The process of supplementation of legal framework in the area of financial regulation and supervision continued to be revised and updated, in order to ensure an effective financial supervision in compliance with application of Basel Committee principles and standards, the European Commission directives and the best international standards. The aim of supplementation of relevant regulations and rules is to ensure establishment of a well regulated environment, without undue burdens to financial services users.

With purpose of revising the financial supervision regulations, based on the support by technical assistance, a Commission is established to prepare the new regulatory and supervision framework according to new Basel Committee standards for banking supervision. Thus, working groups have been set up within the financial supervision to work actively on supplementation of relevant regulations and drafting internal policies and procedures. In cooperation with the technical assistance provided by the IMF, it was worked on the draft law on banks licensing, regulation and supervision, which project is expected to be finalized during 2011.

4.2. Banking Supervision

Kosovo banking system also continued with a sustainable growth during 2010, but with a slower trend compared to 2009. The value of total banking system assets reached at euro 2.237 billion. Total assets increased by 11.0 percent compared to last year's growth ratio of 21.5 percent.

A slower growth of assets level in the current year is mainly attributed to a slower growth of deposits, driven to a considerable extent by withdrawal of PTK dividend deposits from bank accounts and crediting of the Treasury account (Ministry of Economy and Finance) by euro 233¹⁴ million during 2010.

A faster growth in total assets in 2010 was marked by medium and small classified banks, compared to large (systematic) banks. Small banks (G3)¹⁵ recorded a higher growth ratio with euro 39.7 million or 45.3 percent, compared to medium banks (G2)¹⁶ the growth of which is accounted to be euro 95.7 million or 31.6 percent and large banks (G1)¹⁷ with a growth of euro 95.8 million or 5.6 percent. Following these changes, the share of medium banks (G2) and small banks (G3) in total banking system assets increased to 17.1 respectively 5.5 percent from 14.4 and 4.2 percent that was in 2009, whereas the share of large banks decreased from 81.4 percent in 2009 to 77.4 percent in 2010.

The abovementioned changes add value to the interbank competition, increasing the impact of small and medium banks in the system. The supervision activity was also adapted to these changes during the year, increasing the focus on financial performance supervision and more frequent examinations in group-banks with faster growth trend.

a) Off-site Examination Unit

Pursuant to its duties and responsibilities, the Off-site Examination Unit is engaged at constant monitoring of risk profile in financial institutions. Reports and periodical

¹⁴ This amount does not include earned profit.

¹⁵ Includes banks with a share in market <3% of total assets

¹⁶ Includes banks with a share in market of 3%-10% of total assets.

¹⁷ Includes banks with a share in market >10% of total assets.

analyses¹⁸ on developments in financial institutions facilitated identification of areas needing a more significant supervision consideration. Distribution of resources and the supervision activity focus on financial supervision is realized on this ground.

It was continuously monitored during 2010 the tendency of indicators with higher tendency, with a particular focus on the control of liquidity ratios following the withdrawal of euro 233 million by the Treasury in the name of PTK dividend. A significant attention was also paid to the performance of parent banks, in context of subsidiaries and branches of banks operating in Kosovo, in order to obtain timely information on possible impact from the parent banks. A particular consideration this year was also given to credit exposures abroad by commercial banks. .

b) On-site Examination Unit

14 full examinations and 16 examinations focused on financial institutions have been conducted during 2010.

Table 16. Examinations conducted by banking supervision during 2010

Financial institutions – comprehensive and focused examinations		
Description	Comprehensive	Focused
Banks	8	13
Microfinance institutions	3	1
Non-bank institutions	3	2
Total	14	16

Source: CBK 2011

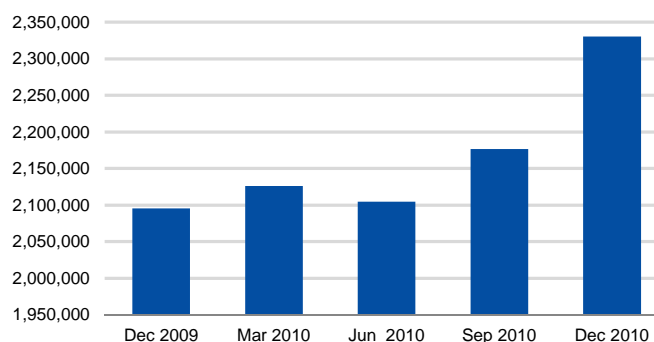
In spite of deterioration of loan portfolio quality (the growth of non-performing loans from 4.4 percent in December 2009 to 5.9 percent in December 2010) and the need to maintain liquidity levels following the withdrawal of PTK funds, the banking system continued to be liquid, profitable and well solvent. Examinations conducted during the year are mainly focused on the manner of management of banking risks, with a special emphasis on credit and liquidity risk. Banks were required to provide contingency liquidity plans and access to additional financing resources in case of necessity.

c) Banking System Profile

Total assets in 2010 increased to around 231 million or 11.0 percent compared to last year. The key items of banking system assets evidenced the following changes:

“Cash and balance with CBK” recorded a decline of around euro 14.6 million or 4.5 percent; namely cash recorded a growth of around euro 15 million or 16.8 percent, whereas the balance with CBK

Figure 45. Amount of assets in banking sector - total equities in thousands of euro



Source: CBK (2011)

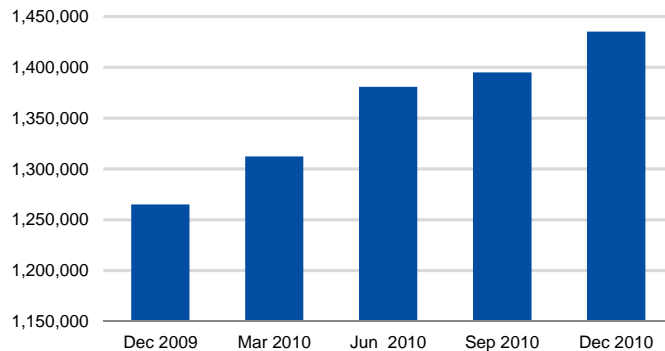
¹⁸ Weekly, Monthly, Quarterly and Bi-Annual

evidenced a decline of euro 29.6 million or 12.7 percent. Following this change, the share of item 'cash and balance with CBK' in total banking system declined from 15.4 percent that was last year to 13.2 percent in 2010.

“Requirements against banks/placements” recorded a growth of around euro 15.1 million or 3.6 percent compared to the previous year. However, the growth of placements was considerably slower compared to last year, where these were increased with around euro 140 million or 49.3 percent. A slower growth of placements decreased their weight within the total equity from 20.2 percent in the previous year to 18.9 percent in 2010. A faster growth of placements during the previous year was mainly driven by conservative approach by banks in granting new loans, which came as a result of the assessment on the impact that the global financial crisis could have on the economic conditions in general and its direct effect in refunding loans. Similar to the previous year, in 2010, CBK was also active in following a rather conservative approach in terms of existing limits of exposures abroad by banks and financial institutions. In this aspect, the requests by banks to increase the placements ratios within a financial institution over the limit of 20 percent of tier I capital have been rejected in most cases. This policy (applied in 2009 and continued in 2010 as well) was imposed to CBK taking into consideration the new circumstance created in global financial markets as a result of crisis overwhelming the world financial markets.

Investments in securities is an equity item which recorded the highest growth last year, namely euro 76.4 million or 78.8 percent. This inclination to the growth ratio of securities is mainly attributed to the decline of weight of Cash and balance with CBK and Placements with other banks within the equities, as well as the improvement of conditions in international financial markets during 2010. This made the share of securities within the equities to increase from 4.6 percent that was last year to 7.5 percent in current year.

Figure 46. Loans trend in banking sector - total loans, in thousands of euro



Source: CBK (2011)

“(Gross) Loans and Leasing” recorded a growth of euro 170.4 million or 13.5 percent compared to last year. Growth of loans in the current year continued with a faster trend compared to the previous year, recording a growth of 13.5 percent, while the growth last year was 9.2 percent. A faster growth of loans during the current year was reflected by the increase of share in total (net) loans within the total equity from 56.6 percent that was last year to 57.5 percent in current year.

Loans classified as “standard” increased to euro 154.5 million or 13.6 percent, while loans classified as “observing” decreased to euro 20.2 million or 43.6 percent during 2010. At the same time, loans classified as “substandard” increased to euro 6.9 million or 23.0 percent, while loans classified as “suspicious” increased to euro 18.6 million or 118.4 percent. Loans classified as “loss” increased to euro 10.7 million or 27.0 percent.

As a result of the abovementioned developments, the loans quality indicators recorded the following changes: ‘delayed loans¹⁹ / total loans’ decreased from 10.4 percent that were in 2009 to 10.3 percent in 2010, ‘problematic loans²⁰ / total loans’ increased from 6.7 percent to 8.5 percent, while ‘non-performing loans²¹ / total loans’ evidenced a growth from 4.4 percent to 5.9 percent. These developments in loans quality have impacted on the growth of loan reserve compared to last year by euro 18.7 million or 23.9 percent.

Financing resources (liabilities) of banking system evidence the following changes by items:

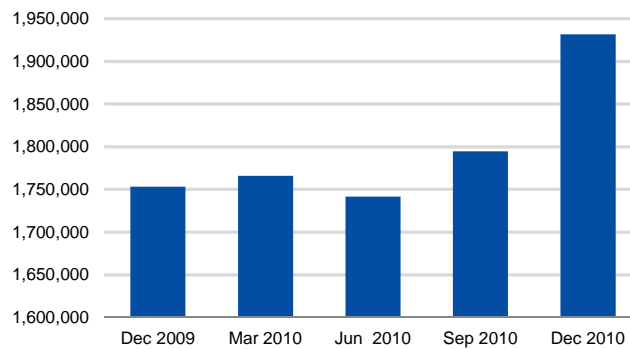
‘Total Deposits’ recorded a growth of euro 178.6 million or 10.2 percent compared to last year. Interest free deposits increased to euro 141.3 million or 36.9 percent, while interest deposits increased to euro 37.2 million or 2.7 percent compared to last year. Within the structure of interest free deposits the following changes have been recorded: bank deposits decreased to euro 3.8 million or 52.9 percent, individual deposits increased to euro 52.1 million or 22.4 percent, while the enterprise enterprises increased to euro 93.2 million or 65.5 per cent.

Whereas, within the structure of interest deposits the following changes have been recorded: bank

deposits increased to euro 253 thousand or 8.0 percent, individual deposits increased to 220.1 million or 26.5 percent and enterprise deposits decreased to euro 183.1 million or 34.2 percent.

Deposits keep the highest weight that their position has within the equities. In the current year, the share of total deposits in total liabilities in banking sector is evidenced around 92.2 percent.

Figure 47. Deposits trend in banking system - in thousands of euro



Source: CBK (2011)

d) Regulatory Capital Structure – Capital Adequacy Ratio

The total of regulatory capital²² in banking system also continued a growing trend during the current year. The value of total regulatory capital is reported to be around euro 271.4 million, which represents a growth in absolute amount of around euro 30.1 million or 12.5 percent compared to 2009, where the key contribution was given by profits generated during the year amounting at euro 32.9 million. In 2010, three (3) banks of the system distributed the shareholders’ dividends from reinvested profits of last years amounting at euro 18 million of which 5 million returned to equities. Some of the commercial banks during the year increased fresh capital amounting at euro 5 million as well as tier II capital through interdependent debts amounting at euro 6.5 million.

Constant growth of regulatory capital ratio made the financial sector have very good capital adequacy indicators, recoding higher ratios than the minimal ratio required by CBK. The

¹⁹ Delayed loans include loans classified as: observing, substandard, suspicious and loss loans.

²⁰ Problematic loans include loans classified as: substandard, suspicious and loss loans.

²¹ Non-performing loans include loans classified as: suspicious and loss loans.

²² Regulatory capital = first tier capital + second tier capital.

capital adequacy indicators respectively “tier I capital / total risked assets” and “total capital / total risked assets” in 2010 is evidenced to be 15.6 percent respectively 18.7 percent from 15.0 and 18.0 percent that were in 2009. The growth of capital adequacy indicators is attributed to the growth of total capital by a faster trend compared to the growth of total risked assets. While the total capital recorded a growth of around euro 30.1 million or 12.5 percent (supported by constant growth increase of profits), the total of risked assets increased to around euro 113.9 million or 8.5 percent (resulting from constant growth of loans and investments in securities as well as placements ratio) compared to 2009.

e) Banking System Liquidity

Banking system in general continued to have satisfactory liquidity indicators, although this indicator compared to last year reflects a declining tendency. In 2010, the indicators “liquid assets / total assets” and “liquid assets / total deposits are estimated 37.3 and 45.0 percent, compared to 38.8 and 46.4 percent that were in 2009. This has mainly come as a result of slow growth trend of total deposits, driven to a considerable extent by the abovementioned withdrawal of PTK dividend and by rapid growth of total loans.

f) Banking System Profitability

The banking system net profit outcome in the end of 2010 is reported to be around euro 32.9 million, which compared to 2009 is by euro 5.5 million or 20.0 percent higher. The key factors influencing on the increase of profits were: the increase of interest income with a faster trend compared to 2009, respectively by euro 11.2 million or 6.8 percent and the net increase from provisions with around euro 4.0 million or 15.7 percent compared to 2009. The abovementioned factors had an impact on the performance of profitability indicators; respectively the return from average assets (ROAA) and the return from average equities (ROAE) evidenced a slight growing trend, from 1.5 percent and 13.9 percent that were in the end of 2009 to 1.5 percent and 14.9 in the end of 2010.

g) Performance of Microfinance Institutions

The number of Microfinance Institutions (MFI) and Non-bank Institutions (NBI), the activity of which is lending, was seventeen (17) in the end of 2010.

Loans active portfolio in the end of 2010 was euro 115.8 million, which represents an annual growth of euro 6.5 million or 5.9 percent. Loans, as the key activity of these institutions, consist around 92.7 of total equities. Loan portfolio during 2010 recorded deterioration in quality. Loans quality indicators, respectively the ratio between problematic loans and total loans, as well as the ratio between non-performing loans and total loans is evidenced at the ratios of 4.4 percent and 3.6 percent, while in the end of 2009, these ratios were evidenced with 3.1 percent and 2.6 percent, respectively. Also, due to weaknesses evidenced in corporate management, CBK had to appoint a temporary administrator in one of this institution in the beginning of 2011.

Negative movements in microfinance sector in 2010 are also noticed in profitability indicators. Return from average assets (ROAA) and return to average equities (ROAE) recorded negative ratios of minus 1.6 percent, respectively minus 5.5 percent. These indicators recorded a significant decline compared to the ratios of 1.4 percent, respectively 4.3 percent in last year driven by a considerable growth of provisions expenditure from the loss of loans, with an annual growth of euro 3.5 million or 117.6 percent.

h) Cooperation with other Regulatory and Supervision Authorities

Cooperation with foreign regulatory and supervision authorities was followed by more significant intensity. Thus, a joint examination of the respective banks was done with colleagues from Bank Regulatory and Supervision Agency of Turkey (“BRSA”), the supervisory newsletter exchange took place on quarterly basis with Financial Supervision Agency of Austria (“FMA”), then the mutual information exchange with Central Bank of Slovenia. Bank of Albania, communication and cooperation with Federal Financial Supervision Agency in Germany (BaFin) in order to initiate conclusion of a Memorandum of Understanding between the two institutions, which is expected to be signed in the beginning of 2011.

It is also worth mentioning the Central European Bank project for strengthening macro and micro-prudential supervision which added value to supervisory capacity building, and it also contributed to exchange of experiences and disclosure of the best practice and standards on financial supervision. On the other hand, this project will continue to be implemented during 2011 with the second component, where CBK will benefit a technical assistance in improving the early warning system and macro “stress-test”, as well as the third component to point out the interstate cooperation aspect with other supervision authorities by simulating crisis situations.

4.3. Insurance Supervision

The number of insurance companies operating in insurance industry during 2010 was 11, of which, ten are non-life insurance companies and one life insurance company. Regarding the ownership structure, four companies were of foreign ownership, four of mixed ownership, while three of them were insurance companies being completely under local ownership.

In the course of changes in ownership structure during 2010, two insurance companies with mixed ownership structure (local and foreign) were completely transformed into foreign companies.

The total number of insurance policies issued in the end of 2010 reached at 542,097 or 6 percent more than in 2009. The structure of insurance portfolio for 2010 is characterized by 47.6 percent of compulsory motor insurance policies, then 35.6 percent of border insurance policies and around 16.6 percent of other (voluntary) insurance policies. Life insurance market still remains with a small share in total insurance portfolio (0.25 percent of policies of insurance portfolio in 2010).

Gross written premiums during 2010 were characterized with 56.13 percent of compulsory motor liability insurance, then other (voluntary) insurances with 28.25 percent and border insurance with 14.64 percent. Life insurance market still remains low with a share of only 0.98% in gross written premiums in 2010.

A considerable growth both in number and in value was recorded by losses paid during 2010. The number of paid losses during 2010 reached at 60,112 losses or 56.5 percent more than 2009, while the value of paid losses in 2010 was euro 28.1 million or 40.87 percent compared to that in 2009 which was 39.34 percent. The abovementioned indicators show a considerable increase in payment of losses in 2010 compared to the previous year which comes as a result of additional and effective CBK supervision on the control of payment of losses with purpose to protect the policyholders.

Taking into consideration the role and objectives of Insurance Supervision Directorate in protection of policyholders’ (clients) interests and protection of financial sector

sustainability in general, this directorate performed a risk-based supervision in 2010 by conducting direct on-site examinations as well as off-site monitoring.

Off-site monitoring is based on monthly, quarterly and annual reports, whereby different financial indicators have been assessed, which show the maintenance of activity of insurance companies, as follows: minimal solvency margin, financial power–liquidity, calculation of technical reserves, risk exposure, maximal risk hold by insurance companies, reinsurance quality and other relevant financial indicators.

Table 17. On-site examination conducted during 2009

Description	Comprehensive examinations	Focused	Examinations of Points of Sale
Insurance companies	3		
Insurance intermediaries	3	41	126

Source: CBK 2011

Table above shows a proactive approach in insurance supervision during 2010. On-site examinations are mainly concentrated on focused examinations, always based on insurance companies activity which have been identified and assessed of their higher risk activities. Insurance supervision orientation towards focused examinations during 2010 was estimated to be quite effective. In particular, positive results have been achieved in payment of losses, financial sustainability, and promotion of corporate management quality and of the entire insurance market reregulation.

In addition to activities which resulted from the operational plan of insurance supervision, as of 2010, CBK started implementation of the Administrative Instruction²³ on certification of technical reserves for non-life insurance companies. According to this instruction, the non-life insurance companies will be obliged to submit to CBK on quarterly and annual basis the technical reserves certified by a certified company's or foreign actuary and based on this the CBK will assess and safeguard the reserve adequacy, and in case of inadequacy, the insurance companies will have to increase their reserves.

During 2010, CBK issued the "Manual for establishment of green card compensation fund", whereby insurance companies have been obliged to open bank accounts in commercial banks. Consequently, as of July 2010, insurance companies started to allocate 20 percent of border insurance income by contributing to the establishment of the abovementioned fund.

With purpose of a higher security of assets of collateral, possessed by insurance companies in form of deposits in commercial banks, CBK addressed during 2010 all companies and commercial banks to open escrow accounts for collateral deposits.

a) Financial performance of insurance system

The insurance industry performance during 2009 recorded a sustainable financial growth.

The table above shows that gross written premiums marked an increase of 7.85 percent in 2010 compared to 2009.

²³ Instruction issued by CBK in December in 2009.

Table 18. Gross written premiums

Description	2009	2010	Difference in %
Motor liability	35,461,834	40,221,123	11.83%
Border insurance	12,983,207	10,491,743	-23.75%
Voluntary insurance	17,224,304	20,244,145	14.92%
Returns	-1,365,724	-1,878,507	27.30%
Gross written premiums	64,303,621	69,783,389	7.85%

Source: CBK 2011

A significant growth marked the voluntary insurance which reached at 14.9 percent compared to 2009. Orientation towards voluntary insurance indicates an encouraging developing ratio in Kosovo insurance system.

Border insurance premiums during 2010 recorded a decline of 23.75 percent compared to 2009 and this is a result of decrease of border insurance fees by CBK. Within the two last years (2009 and 2010), these fees decreased by 50 percent.

Insurance system equities in Kosovo during 2010 recoded a growth of 9.20% compared to 2009. The share of insurance system equities in total equities of financial sector is around 7.10 percent. Within the general equities, a considerable growth was recorded by fixed equities (27.22 percent), because of investment in immovable properties by the insurance companies.

Table 19. Insurance system equities in Kosovo

Equities	2009	2010	Difference in %	Share in 2010	Share in 2009
Cash	59,267,448	61,108,295	3.01%	62.89%	67.18%
Liquid assets	17,882,681	20,290,650	11.87%	20.88%	20.27%
Fixed assets	11,011,670	15,130,416	27.22%	15.57%	12.48%
Intangible equities	62,804	639,573	90.18%	0.66%	0.07%
Total equities	88,224,603	97,168,934	9.20%	100.00%	100.00%

Source: CBK 2011

b) Solvency ratio (payment capacity)

Insurance system during 2010 resulted in sustainable financial performance. The solvency ratio during 2010 by euro 21,130,756 above ²⁴the minimal margin of euro 6,600,000 required under CBK Rule VIII (section 9). Compared to 2009, the solvency ratio in 2010 was euro14,751,505, which indicates a growing tendency of solvency ratio.

²⁴ Minimal solvency margin is-20% of 3 mil euro - collateral = 600,000 euro

Table 20. Liquidity ratio in insurance system in Kosovo

Description	2010
Liquid equities – cash/Total equities	63%
Total liquid equities (cash) / Technical reserve	130%
Total liquid equities (cash) / Total liabilities	107%
Investment income / Total income	6%
Non-TPL / Gross written premiums	9%

Source: CBK 2011

The insurance system in general during 2010 resulted in sustainable liquidity indicators. As indicated in the table above, liquid equities in cash in relation to technical reserves were 130 percent, while in relation to total liabilities they were 107 percent. Tightening of liquidity during 2010 mainly resulted as a consequence of rapid growth trend of total technical reserves compared to last year, and the implementation of the Manual on calculation methodology of technical reserves issued by CBK.

c) Corrective actions

Corrective actions have been undertaken during 2010 against the insurance companies depending on discrepancies/violations found out. In July 2010, CBK issued Orders against the insurance companies on execution of payment of losses treated but not settled.

Because of issuance of compulsory motor liability insurance policies in violation with CBK legal regulative, respectively Direction No.008/2004, fines in the amount of euro 38,000 have been imposed on insurance companies by CBK. In this context, CBK has also issued written warnings to senior officers of the respective insurance companies.

During 2010, CBK issued Orders against insurance companies with purpose of fulfilling the deficit found out through the relevant financial analyses. Then, based on direct examinations performed on insurance companies, during 2010, CBK issued Orders against the respective companies with purpose of improvement of situation pursuant to the legal regulative. Also, with purpose of verification of adequacy of insurance system staff, during 2010, CBK issued communications and undertook corrective measures in case of identification/confirmation by competent authorities on the inadequacy of respective individuals.

d) International cooperation in the area of supervision

CBK in cooperation with the technical assistance provided by the relevant financial international institutions, respectively the World Bank, Ministry of Economy and Finance and the insurance industry prepared the draft law on compulsory motor liability insurance, which draft law was forwarded to Kosovo Assembly for adoption. It is expected that this law will consolidate and further advance the legal ground on compulsory insurance market.

Also, in cooperation with the technical assistance provided by the World Bank, CBK initiated a project for Assessment of Core Insurance Principles, which project assesses 28 core insurance principles in total and provides a concrete Action Plan with purpose of implementation of recommendations deriving from the assessment. This will certainly

contribute towards a more effective supervision in compliance with the international insurance principles and directives, which are relevant to Kosovo industry development.

To this end, parallel to detailed revision of Regulation 2001/25 on Insurances which will serve as a ground for preparation of the general Law on Insurances, and supplementation of insurance industry rules pursuant to law, as of the end of 2010, CBK, supported by the technical assistance provided by the World Bank, initiated drafting of the general law on insurance regulation and supervision, which law will also contain concepts of both Solvency I and Solvency II.

In the international cooperation area, with purpose of exchanging experiences and supporting professional development, CBK signed in 2010 an Agreement on cooperation/exchange of information with Insurance Supervision Authority of Bulgaria and with the Insurance Supervision Agency of Montenegro. At the same time, it continued cooperation in form of official visits to respective countries, which CBK has a Memorandums of Understanding (MoU) with.

4.4 Pension Supervision

Pension system in Kosovo functions pursuant to Law 03/L-084 amending UNMIK Regulation 2005/20 on Pensions in Kosovo. The said law provides a three-pillar pension structure, which structure provides:

Basic pension provided to all elderly Kosovars aged over 65, funded by Kosovo Consolidated Budget revenues (known as Pillar I);

Invested pensions, funded by mandatory fully funded contributions by employers and employees for current employees (known as Pillar II) and;

Voluntary pension schemes, funded by voluntary individual contributions (known as Pillar III).

Pursuant to Law 03/L-084 on Pensions in Kosovo, the second pillar is funded by mandatory monthly contributions: the employees contribute by 5 percent of their wage and the employers contribute by another 5 percent. Payments are transferred to individual accounts of participants in Kosovo Pension Savings Trust (Trust).

It is worthy to underline that during 2010, in cooperation with the World Bank technical assistance, it was worked on finalization of the new draft law on pensions in Kosovo.

a) Operators

Pillar II (Kosovo Pension Savings Trust (Trust) – the Trust is established to administer this new system, the second pillar. A Managing Board, with its seven members, supervises the Trust performance. Board members are selected by panel composed of CBK, Auditor General and Permanent Secretary of MEF, and they are appointed by Kosovo Assembly following a consultation with the Government.

Trust investments during 2010 had a satisfactory return. The value of contributions invested by the Trust only in one year reached at euro 26 million, or a growth of 5.18 percent net return from investments. The value of Trust share in the end of 2009 was euro 0.9818, while this value in the end of 2010 reached at euro 1.0327, which is higher by 5 percent. The number of beneficiaries, who started withdrawing pensions from their accumulated savings, increased considerably during 2010. From 2,177 new beneficiaries who withdrew pensions in 2009, this number in 2010 reached at 2,738. The value of assets

under Trust management increased almost to euro 115 million only during 2010. The value of total assets under Trust management reached almost at euro 490 million in the end of 2010, from euro 375 million in the end of 2009. In the end of year, respectively on 31 December 2010, the largest part of Trust assets was under the management of asset managers, such as “Vanguard” (39.73 percent), “Fortis GLF” (15.35 percent), “Schroders” (12.38 percent), European Credit Management (8.64 percent), while another part of assets was deposited in three commercial banks and in CBK. The value of Trust share in the end of 2009 was euro 0.9818, while this value in the end of 2010 reached at euro 1.0327. This positive change implies a direct growth in value of contributors’ savings and it determines the number of shares that would be bought by new contributions in the future.

Pillar III, Slovenian-Kosovo Pension Fund (SKPF) is established as a shareholding company “Prva Group” from Ljubljana and Corporation “Dukagjini” from Peja, on 4 September 2006, pursuant to Law 03/L-084 amending UNMIK Regulation 2005/20 on Pension in Kosovo. SKPF was licensed as Supplementary Pension Fund and as Pension Asset Manager, while assets under SKPF management as of 31 December 2010, reached at euro 3,616,889, while the number of contributors was 3,242 and the unit value was equal to euro 120.91.

In compliance with legal applicable regulative, for the saving period, SKPF assets have mainly been invested in credit default swaps (75.49 percent), then in shares (1 percent), in deposits (20.84 percent), in cash (1.95 percent) and other (0.72 percent).

Likewise the other financial institutions, the pension system operators, both the Trust and SKPF have been subject to on-site and off-site examinations conducted by Insurance and Pension Directorate within CBK.

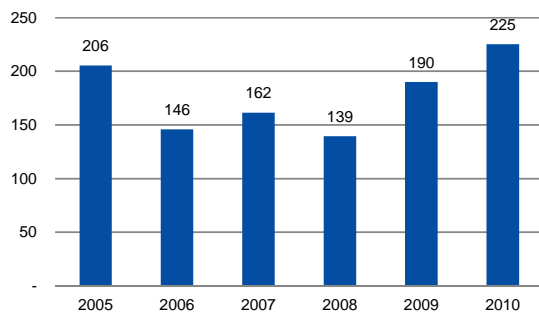
5. Services provided to the Authorities, to the Financial Community and to the Public

The Central Bank of the Republic of Kosovo (CBK) provides the basic services which are to be offered by a central bank to the state institutions, financial institutions and wide public. In general these services have to do with cash flow, account transactions, managing the financial means, interbank payment system, credit registration as well as economic statistics and analysis.

5.1. Operations and Cash Management

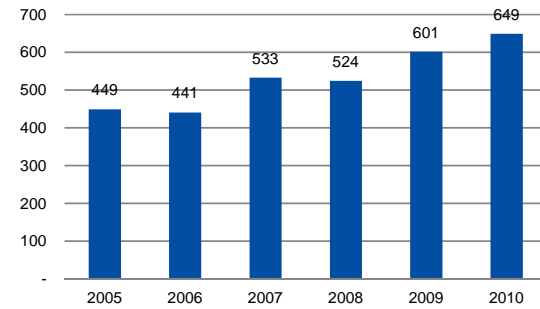
As of its establishment, CBK was vested the authority to provide proper supply of banknotes and coins to the domestic economy, for execution of cash transactions. Since Euro is a currency that is being used in Kosovo, the CBK responsibilities with respect to operations and cash management are related to Euro in first place.

Figure 48. Cash supply (amount), in millions of euro



Source: CBK (2011)

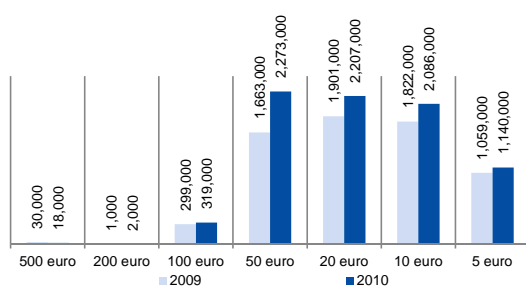
Figure 49. Cash admission (amount), in millions of euro



Source: CBK (2011)

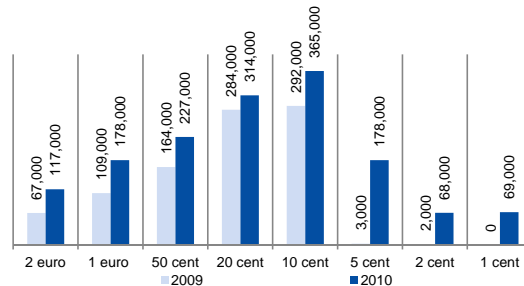
Regarding general amount, cash supply during 2010, had an increase 18.4 percent compared to 2009, whereas the structure of the cash supply in accordance to denominations, that is determined by the requirements of banking sector in first place, did not have any evident change from year 2009 to year 2010. As to the euro banknotes, low denominations (5, 10, 20 and 50 euro) kept dominating, while higher denomination volumes of 200 and 500 euro remain evidently lower. As to the euro coins, supply is mainly dominated by the coins with medium value from 5 eurocent to 50 eurocent, while lower denominations than the two previous ones recorded a considerable growth compared to 2009.

Figure 50. Supply with euro banknotes by denominations (number of pieces)



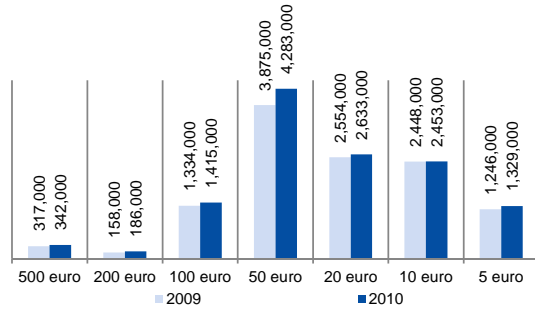
Source: CBK (2011)

Figure 51. Supply with euro coins by denominations (number of pieces)



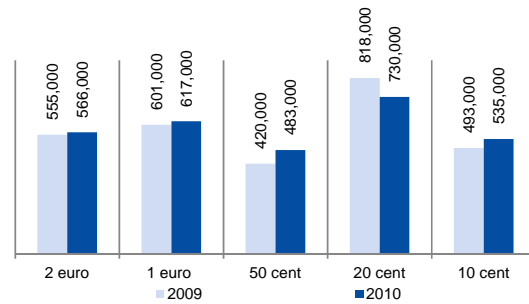
Source: CBK (2011)

Figure 52. Euro banknotes received by denominations (number of pieces)



Source: CBK (2011)

Figure 53. Euro banknotes received by denominations (number of pieces)



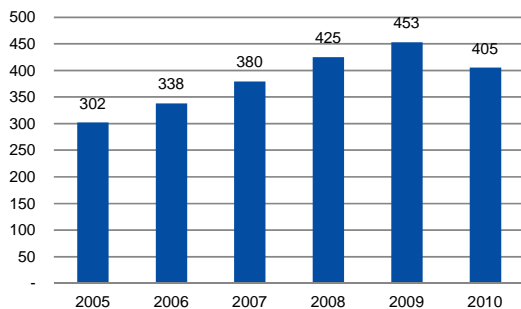
Source: CBK (2011)

As presented in the figures above, without a significant change from the previous year, CBK supplied commercial banks and other institutions with approximately 804 million pieces of euro banknotes (in an approximate amount of euro 225 million) and over 1.5 million pieces of euro coins (in an approximate amount of euro 0.3 million).

On the other hand, during 2009, the overall value of cash received as deposits marked a considerable increase of 7.9 percent compared to the previous year. CBK received around 12.6 million pieces of euro banknotes (an average of 50,500 pieces of banknotes per day) and around 2.94 million pieces euro coins (an average of around 12,000 pieces of coins per day) as cash deposits from commercial banks and other institutions. Expressed as a value, these deposits have approximately reached the amounts of euro 648 million and 2.2 million, respectively. The structure of euro banknotes and coins received does not have a great difference compared to previous year.

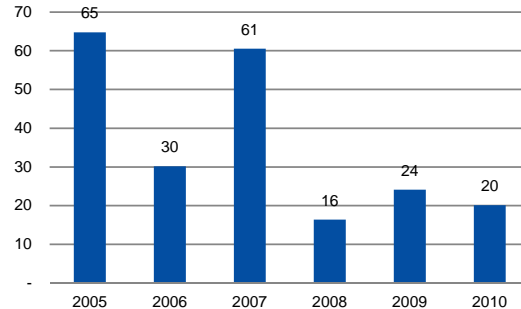
Same as in previous years, in 2010, the deposited cash was in evidently higher amount than the cash supply. In fact, by reaching at nearly euro 423.7 million, the variation of cash deposit was a bit higher compared to the previous year when it was around euro 411 million.

Figure 54. Export of cash (value) in millions of euro



Source: CBK (2011)

Figure 55. Import of cash (value) in millions of euro

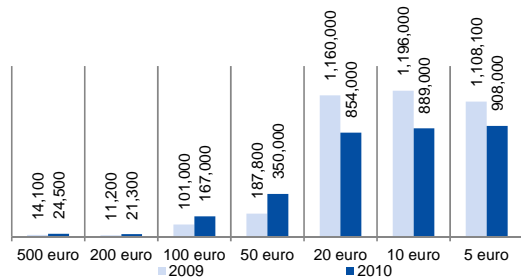


Source: CBK (2011)

Since, the CBK keeps in its treasury only the minimum required level of cash by remitting the overflow to the Euro-zone banks, wherein they are refunded into the interest assets, the annual increase of the deposited cash against the cash supplies, has also resulted in net increase of cash remittances outside the country. The net remittances of cash outside the country in 2010, reached the amount of euro 405.3 million being a bit lower than in previous year, when they were euro 429 million.

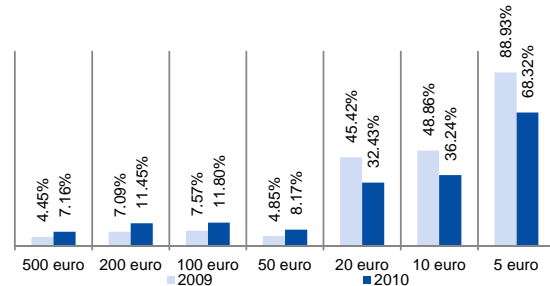
The cash export and import situation during the recent years are depicted in the two figures above.

Figure 56. Number of outdated banknotes withdrawn from circulation (number of pieces)



Source: CBK (2011)

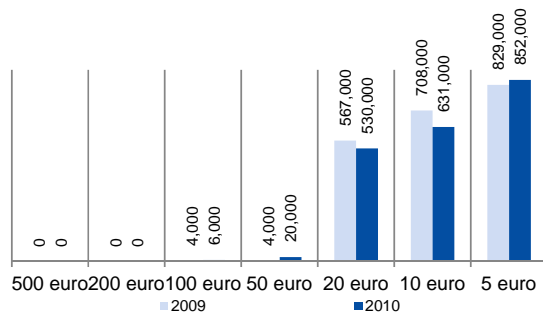
Figure 57. Proportion of outdated banknotes from the total received ones



Source: CBK (2011)

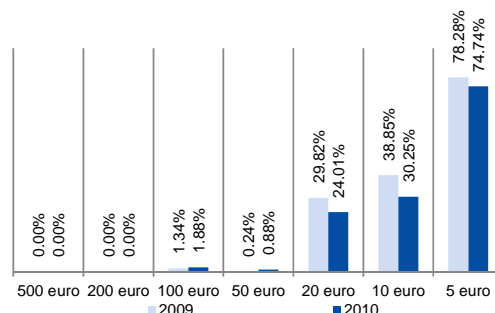
The cash operations kept being executed through modern processing equipment and in compliance with standard rules. All the cash received by commercial banks and other institutions are processed and classified in accordance to the extent of their age. During the year, around 3.2 million euro banknotes (25 percent of deposited euro banknotes number) were classified as outdated and were excluded from the circulation by being remitted towards the central Euro-zone banks. Such capacity of considerable outdated euro banknotes excluded from circulation has evidently contributed to the improvement of the quality of cash in circulation in the Republic of Kosovo. Banknotes that mainly were classified as highly outdated and were excluded from circulation were those of denominations 20, 10 and 5 euro, due to their higher circulation in the economy.

Figure 58. Supply of new banknotes (number of pieces)



Source: CBK (2011)

Figure 59. Proportion of new banknotes induced in circulation from the total supplied



Source: CBK (2011)

The quality of cash in circulation was also improved through the supply of banks and other institutions with completely new euro banknotes, which were brought from Euro-zone. During 2010, CBK supplied the banking sector with over 2 million pieces of new euro banknotes (25 percent of the overall number of euro banknotes supplied). Most of the new banknotes supplied were those of low denominations (20, 10 and 5 euro), and mainly commercial banks were supplied with them aiming at equipping their ATM machines. In addition, all the used euro banknotes that were supplied were of the highest standard quality (proper quality for ATMs).

Regarding measures against the counterfeiting, the CBK proceeded on following up the cases of counterfeit money in 2010. Furthermore, it proceeded with its cooperation with authorities in charge to advance the reporting of cash suspected as counterfeit and with organizing relevant trainings for the staff of financial institutions operating in cash. It is worth mentioning, the regular meetings of Counterfeit Money Analyzing Central Committee, which is composed of three CBK senior representatives and three Kosovo Police senior representatives. Furthermore, CBK published in its website educational material on security features of euro banknotes. Such materials aim at wider public education, and in particular of persons handling cash in different economic sectors.

5.2. Account Maintenance and Transactions

CBK provides banking services to Department of Treasury of the Ministry of Finance (Treasury) and other institutions of Government the Republic of Kosovo, such as Privatization Agency of Kosovo (PAK), particular public entities, banks and other financial institutions, international financial institutions and international organizations. In 2010, similarly to the previous years, these services consisted mainly of account maintenance and transactions execution, excluding any form of crediting.

Table 21. Amount of transactions by their main types (in thousand of euro)

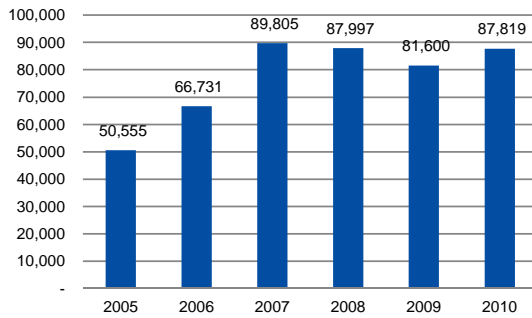
Types of transactions	2005	2006	2007	2008	2009	2010
Cash transactions	+249,904	+295,100	+371,745	+385,113	+411,055	+423,658
Deposits	456,279	440,975	533,178	524,346	601,207	648,911
Withdrawals	206,375	145,875	161,433	139,233	190,152	225,253
Local payments	+129,854	+228,668	+358,182	+78,078	+41,169	+392,587
Incoming domestic payments	828,633	998,128	1,055,472	1,076,145	1,225,527	1,568,021
Outgoing domestic payments	698,779	769,460	697,290	998,067	1,184,358	1,175,434
International payments	-221,008	-65,543	+13,124	-364,795	-463,816	-408,689
Incoming international payments	100,592	260,267	335,613	203,113	202,755	326,319
Outgoing international payments	321,600	325,810	322,489	567,908	666,571	735,008

Source: CBK 2010

The largest number of accounts in CBK is kept in the name of PAK and Treasury, regarding transactions, while those in cash are executed mainly in relation to banks; payment transactions has mostly to do with the Treasury and PAK. In fact, all commercial banks generate themselves local payment transactions as their own basic products, whereas the other financial institutions being CBK clients, conduct the largest number of their payments through commercial banks, where they keep current accounts. All commercial banks also generate themselves the international payments, but they do through CBK only the international transfer of their funds.

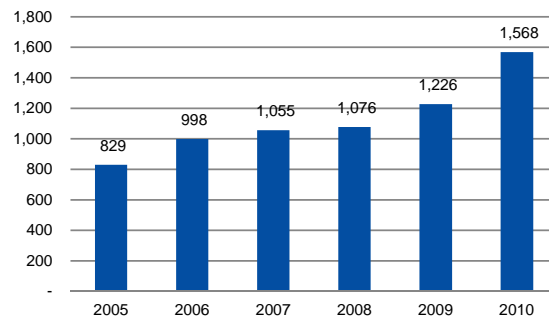
During 2010, CBK kept promoting and advancing the processes of transactions execution and Treasury and PAK reports. Types of payments and ways of communications have been adapted to their demands and it is worthy to mention the complete automation of payment order.

Figure 60. Volume of domestic incoming transactions, number



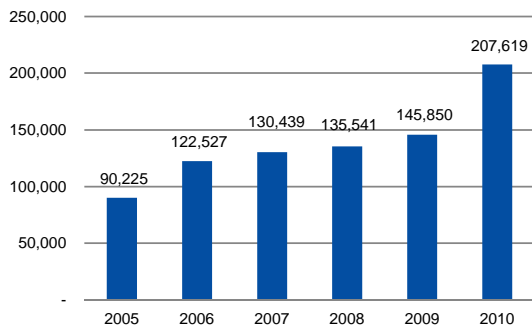
Source: CBK (2011)

Figure 61. Value of domestic incoming transactions, in million of euro



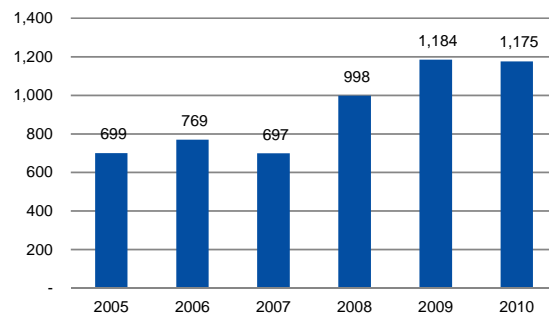
Source: CBK (2011)

Figure 62. Volume of domestic outgoing transactions, number



Source: CBK (2011)

Figure 63. Value of domestic outgoing transactions, in millions of euro



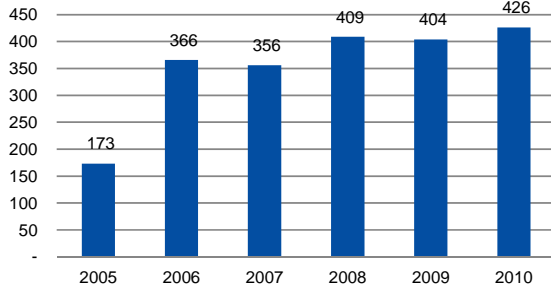
Source: CBK (2011)

Most of local payments are interbank payments, which are canalized by CBK through Interbank Electronic Clearing System (IECS) as direct participant in it.

During 2010, through IECS, CBK issued in the name of its clients around 208 thousand outgoing payment orders (a growth of 42 compared to the previous year), and received in their accounts around 88 thousand incoming payment orders (a growth of 8 percent compared to the previous year). Expressed in value, the outgoing payment orders in 2010 reached at euro 1.17 billion (a decrease of 1 percent compared to the previous year) and the incoming payment orders reached around euro 1.56 billion (a growth of 28 compared to the previous year). CBK also remained the largest participant in IECS both in terms of value and volume of transactions.

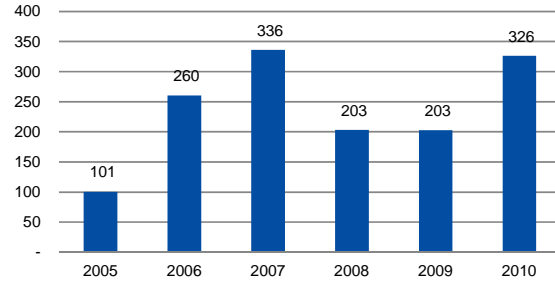
Regarding the international payments in 2010, the largest number of them was executed by CBK upon the Treasury order. On the other hand, considering their value, the largest number of them was executed by CBK relate to the transfer of commercial banks funds. Annual data on international transaction for the last five years are presented in the following figures.

Figure 64. Volume of international incoming transactions, number



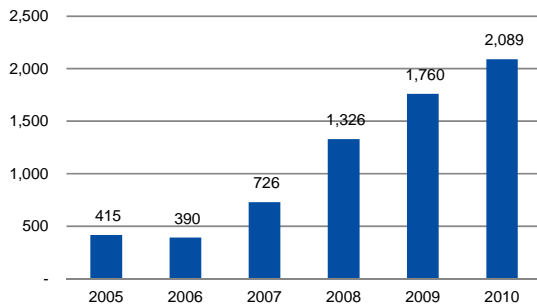
Source: CBK (2011)

Figure 65. Value of international incoming transactions, in millions of euro



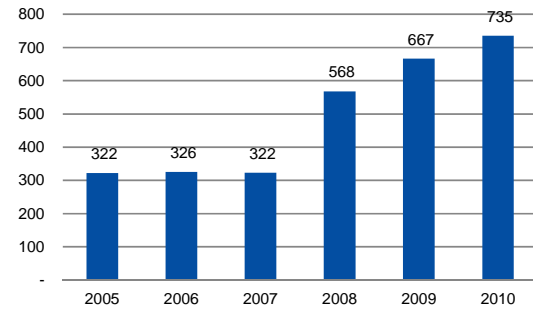
Source: CBK (2011)

Figure 66. Volume of international outgoing transactions, number



Source: CBK (2011)

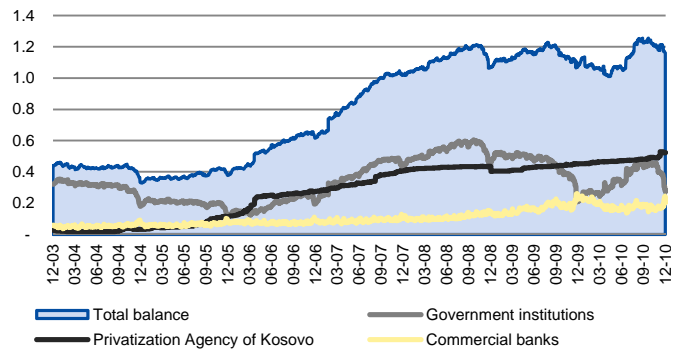
Figure 67. Value of international outgoing transactions, in millions of euro



Source: CBK (2011)

Deposits of the Kosovo Government institutions along with the deposits of PAK compose the major part of the overall deposits held in CBK by the end of 2010. On 31 December 2010, deposits of institutions of Kosovo Government and of PAK reached the amount of nearly euro 800 million. Current account and time deposit assets are included in this amount.

Figure 68. Deposit motion of the key account-keepers of the CBK, in billions of euro



Source: CBK (2011)

Among other accountholders, the commercial banks and insurance institutions are the most important ones in regard to the deposits level that are kept in the CBK account. Deposits of commercial banks and of insurance institutions kept in CBK mainly have to do with their regulatory obligations. On 31 December 2010, deposits of commercial banks and of insurance institutions reached an amount of nearly euro 210 million.

Level of deposits of Kosovo Pension Savings Trust (KPST) kept in CBK decreased during 2010. It reached an amount of nearly euro 40 million at the end of the year. This decrease came due to the increase of their external placements.

5.3. Asset Management

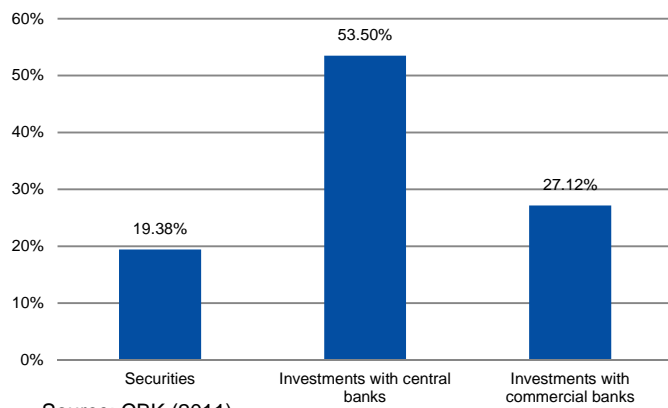
Asset Management and CBK Investment Policy

Pursuant to its Law (Article 1, paragraph 1.6), CBK is authorized to act as a fiscal agent of the Government, whereas pursuant to Law on Public Finance Management and Responsibilities (Article 7), CBK is authorized to invest the Government assets. This form of financial investments enables the return on investments, generating assets paid from interest, which are then collected in Kosovo Consolidated Budget.

In practice, deposited funds mainly belong to Government institutions, Ministry of Economy and Finance (budget revenues), Privatization Agency of Kosovo (PAK) as well as financial institutions (mandatory liquidity reserves).

Management of Treasury investments is done by CBK in cooperation with Treasury through Liquidity Committee which meets on regular monthly basis. PAK started time bank deposits with maturity up to one year as of August 2010. These investments are carried out in accordance with Investment Policy and Interest Rate Policy approved by the CBK Board. CBK is also in charge of management of funds deposited by public agencies, financial institutions and donor organizations.

Figure 69. CBK investment report

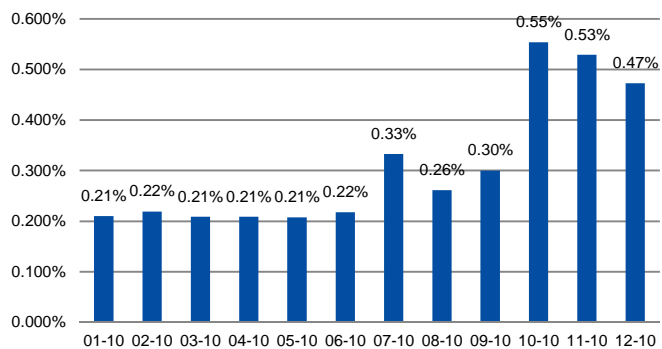


Source: CBK (2011)

Investment Policy approved by the CBK Board is followed by the Management, and under its control, is implemented by Asset Management Directorate. Since a large part of funds under management are assets of public funds, or can be returned with a short period of time, a particular concentration was given to *security*, *liquidity*, and finally the *return to investments*.

All assets are invested in central and commercial banks which are in the EU countries. Among these three central banks of these countries with which CBK cooperates are: Central Bank of German (Deutsche Bundesbank), Bank of France (Banque de France) and Central Bank of Luxembourg (Banque Centrale du Luxembourg) which have a minimal credit risk and six commercial banks of the EU member states. Investment by the end of 2010 was carried on in financial instrument and bank deposits.

Figure 70. Monthly average ratio provided by corresponding banks to CBK portfolio



Source: CBK (2011)

27.12 percent of assets of total portfolio have been invested in central banks of Euro-zone countries, 53.50 percent of assets in commercial banks of the Euro-zone countries whereas in securities have been invested 19.38 percent of total assets, where according to the Investment Policy this exposure is allowed up to 70 percent. Furthermore, in relation to the Investment Policy, the combined exposure in commercial banks did not exceed 60 percent of the total CBK investment portfolio.

Average interest rates given by banks, which CBK cooperates with, are characterized by a positive change in second half of the year, namely from the seventh month up to the end of 2010. The first half of the year is characterized by an average interest rate of 0.21 percent with differences in interest rates.

Investment Risk Management

Risk Management is conducted through the monthly evaluation of the banks, which CBK cooperates with. All investment activities take place with banks fulfilling the criteria envisaged in the Investment Policy. Despite the financial crisis, continuous assessments on financial sustainability conducted by International Financial Agencies revealed that all banks, which CBK cooperates with, do fulfill the criteria of the Investment Policy under the main evaluation categories *Aa*.

CBK invested assets within the instruments of the cash market. During 2010, special attention was dedicated to the risk distribution, where the highest concentration of invested assets was in central banks of the European Union countries with a maturity up to one year. According to the CBK Investment Policy, the credit risk is managed through proportional distribution, based on evaluations done by international financial agencies. According to evaluations carried on banks, which CBK cooperates with, banks which fail to fulfill the risk classification criteria have been removed from the approved list. No investment has been carried out with banks, which CBK cooperates with, without the Investment Committee consideration, review and approval, which meets on regular monthly basis. Determination of investment limits for each bank, which CBK cooperates with, and for the country where it is invested is strictly limited. Risk analysis and auditing of asset management functions are conducted on regular basis.

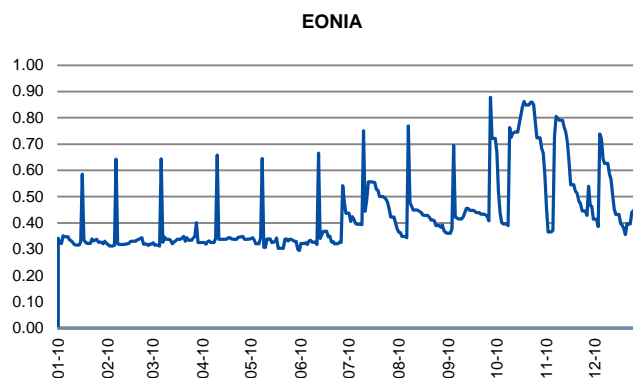
The accepted deposits by the CBK were paid on the basis of the CBK Interest Rate. According to this Policy the return from investments achieved by CBK is on average the minimum of provided interest rates, where the CBK keeps a difference which contributes to the return from its investments.

Developments in global financial market

Public debt crisis that overwhelmed EU in the second quarter of 2010 created conditions for funds to be concentrated in short-term investments in money market.

A considerable growth in returns from investments in short-term and long-term securities was recorded in European countries under turbulence, such as Ireland,

Figure 71. EONIA motion throughout the year



Source: CBK (2011)

Greece and Portugal. Returns from investments serve as a good benchmark and at the same time as a good point to compare the financial instruments of EU countries with Germany, which sustained a considerable expansion that was more significant during the last quarter of 2010. While return from investment in short-term securities of Germany reached the point of 0.40 percent, those of Portugal culminated at 4 percent. In November 2010, return from investment 10-year credit default swaps of Ireland increased to 9 percent. This is because the main countries of Europe, Germany and France agreed that private investors should pay for risks taken during investments in Ireland to avoid the entire burden fall on EU taxpayers. In July 2010, all state and corporate credit default swaps in Ireland were sold due to a risk of infection of the other European countries.

EONIA (Euro Overnight Index Average) started relatively low in the first part of 2010, but it had a growing trend during the third and fourth quarters, making overnight investments of CBK portfolio generate satisfactory profits. In October 2010, the decline of EONIA driven by turbulences in European debt market was compensated by a considerable growth in the end of the year. One-week and one-month interest rates given by corresponding banks have also recorded a growing trend, making short-term investments the most favorable category of asset invested in CBK portfolio. Average EONIA for 2010 was 0.44 percent, while it reached the highest point of 0.87 percent on 30 September 2010.

European Central Bank (ECB) kept maintaining key refunding ratio of 1 percent throughout 2010. Keeping short-term ratios relatively low, ECB created simultaneously conditions for an accommodating monetary policy in the region. This oriented investors towards capital markets that were more liquid and created other conditions for the credit default swaps prices to continue declining. Establishment of the financial assistance mechanism, respectively the European Financial Stability Facility, in May 2010, which aimed at assisting the Euro-zone countries in emergency liquidity needs, it created a stability in the market making the returns from investment in securities of Portugal, Spain and Ireland start decreasing in the end of 2010. Liquidity injection in European market to save Ireland and preparation to intervene in Portugal created a temporary security in money market. Private investors and institutions benefited from the instable situation, buying Portuguese and Greek securities which provided high returns.

During this period, CBK invested a small part of assets in debt market in short-term instruments, generating profits and maintaining a low level of market risk and failure risk.

Commercial banks of EU countries outside the public debt crisis had a stable performance and satisfactory returns throughout 2010. Among the category with sustainable performance are included banks of Austria, Germany, France, Netherlands and Scandinavian countries. Considering their risk return profile, investments in short-term deposits of CBK were concentrated in the safest banks in this region. Average time horizon for investments in short-term deposit in 2010 was 9 days.

5.4. Interbank payment System

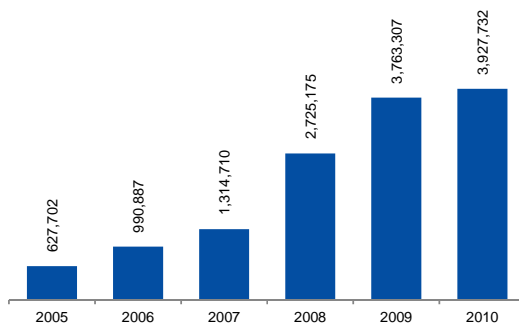
Interbank Electronic Clearing System

Development of an efficient and safe system for domestic payments, as a key standard of the financial infrastructure, is one of the CBK primary functions. Interbank Electronic Clearing System (IECS) operated by CBK is the only interbank payment system in the Republic of Kosovo. IECS functions as a hybrid system which enables interbank channeling of a wide range of payment instruments.

In 2010, an increase was marked in volume, as well as in IECS transaction ratio and a further advancement was carried out, where we must especially emphasize launching the direct debit scheme. Another important development in the area of payments system was the preparation of the Strategy for developing a national payment system and beginning of its application.

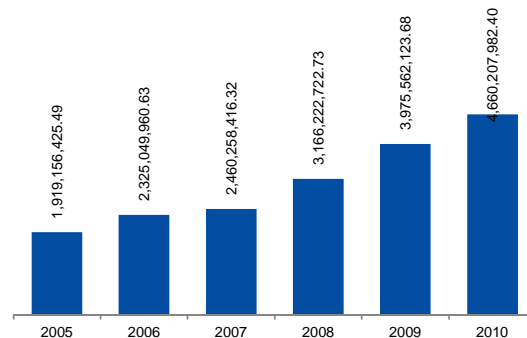
Among the developments of particular importance were automation of communication between IECS and the central system of CBK and initiation of some analytical studies for the future development needs.

Figure 72. IECS transaction number



Source: CBK (2011)

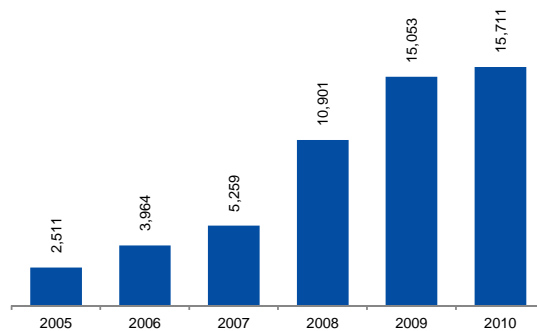
Figure 73. IECS transaction value



Source: CBK (2011)

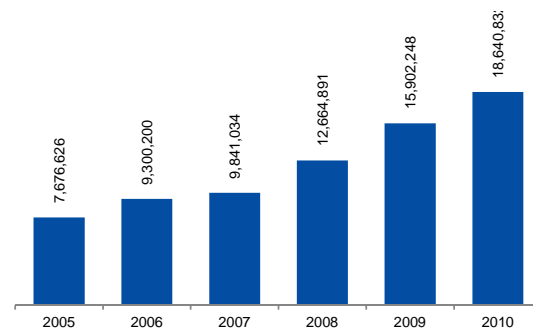
In continuation, the volume and amount of transactions prescribed through the IECS were increased by reflecting the relative payment increase without cash and the increase of confidence in the domestic banking system. As in previous years, in 2010, the annual increase of volume as well as amount of IECS transactions was evident. Around 3.9 million transactions with an overall amount of euro 4.66 billion were channelized through IECS during 2010.

Figure 74. Average daily IECS transaction number



Source: CBK (2011)

Figure 75. Average daily IECS transaction value

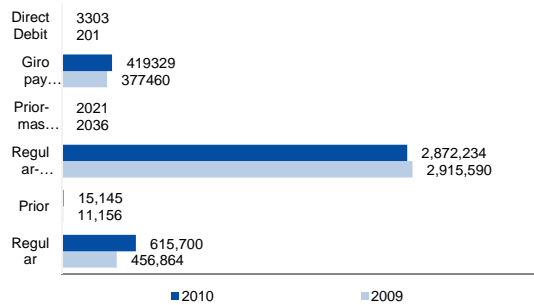


Source: CBK (2011)

The transaction volume increased by 4 percent and transaction amount increased by 17 percent compared to IECS transaction in the previous year. IECS considerable transaction increase can be seen also from the average daily data. The increase of IESC transactions can be seen from daily data. In 2010, the IECS daily transaction amount was around euro 18.6 million, compared to around euro 15.9 million in 2009. Furthermore, in 2010 the IECS daily transaction volume was nearly 15.7 thousand, compared to around 15.1 thousand transaction in 2009. One of the factors that impacted on the increase of the value of IECS transactions, were fiscal transactions from the Post and Telecommunication of Kosovo. Whereas, the increase of the number of interbank payments during this year was not as significant as in the previous years.

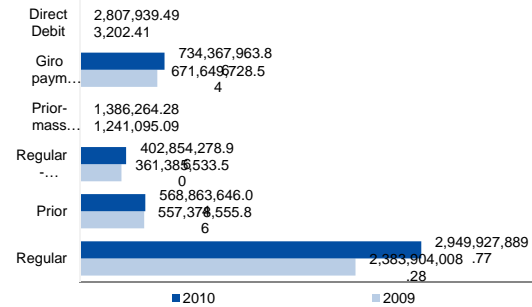
There are some specific types of IECS transactions, such as prior (individual and massive), Kos-Giro and Direct Debit. The comparable volume and the amount levels for 2010 and 2009 are presented in the figures below.

Figure 76. Annual transaction volume of IECS, by their types



Source: CBK (2011)

Figure 77. Annual transaction value of IECS, by their types



Source: CBK (2011)

Regular payments compose around 89 percent of IECS transactions volume and around 72 percent of the IECS transactions value. They are channelized through the IECS either as individual transactions (one-to-one) or as massive transactions (one-to-many or many-to-one). They are processed through regular clearing sessions and cleared on net basis.

The Kos-Giro transactions represent a special type of regular transactions, which are also processed through clearing sessions and cleared on the net basis. They are channelized through the IECS as massive transactions (many-to-one). While regular individual transactions are meant for payments in general the massive regular payments are meant for payments and collections of different enterprises and institutions, the Kos-Giro transactions are meant for standardized and automated cashing of the large recipient institutions. A growth was recorded during 2010 both in their volume and amount.

Priority transactions (urgent) are processed and immediately cleared on the gross basis. Same as regular transactions, prior transactions can be channelized through IECS or as individual or massive transactions. They still represent a small part of overall IECS transactions. In 2010, in reference to their volume, they represented less than 1 percent of IECS transactions, while in terms of their amount; they achieved to represent more than 12 percent of IECS transactions. This type keeps mainly being used for urgent payment transactions and for those with high amounts.

Direct Debit as a new payment instrument and scheme in Kosovo was launched in 2009. Direct Debit scheme provides an advanced method of periodical automated payment from bank account. Periodical payments that are executed through this scheme have to do, in first place, with regular services in regard with residential or working buildings such as electrical supply, water supply, telephony, heating, maintenance, etc. As a new type of IECS transactions this is not still used as much as other types. During 2010, Direct Debit represented less than 1 percent of both in volume and amount of IECS transactions. During 2011, three new companies joined the Direct Debit scheme.

In framework of IECS operation advancement, it should be emphasized that in the end of 2010, with the finalization of implementation of CBK basic banking system development, it was done the automation of interfaces with IECS, which resulted in efficiency and security increase.

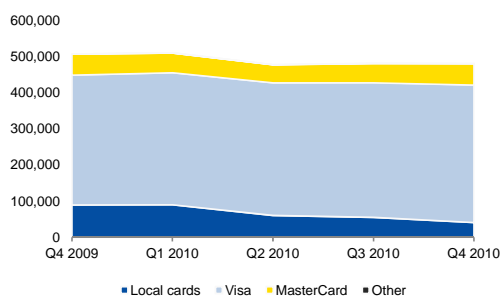
General developments, payment system analysis and supervision

In the course of implementation of the National Payment Development Strategy, during 2010, it was initially constituted the National Payment Council (NPC), as envisaged under its relevant pillar. NPC is composed of representatives from CBK, Treasury/MEF, KBA and commercial banks represented in KBA Governing Board. It has a formal structure with CBK Governor/Deputy Governor as Chairman and the secretariat is also provided by CBK. Appointed representatives of the stakeholders are their Chief Executive Officers. NPC aims at supporting the establishment of sustainable and efficient clearing and payment of securities in Kosovo. It also can serve as forum for cooperation and establishment of necessary conditions in regional and international payment system. A particular working group on reduction of cash payments in Kosovo was consolidated and started operating within NPC. During 2010, all working groups on all other pillars envisaged under the strategy have been constituted: i) legal framework, ii) large amount and urgent payments, iii) low amount payments, iv) governmental transactions, v) securities, vi) monetary market, vii) remittances, viii) supervision of payment system. It was also worked on preparation of terms of reference for new payment systems (pillars ii, iv, v and vi) and in drafting a law on payment system (pillar i).

In the supervision and analysis area, with purpose of reviewing the analytical indicators on payment indicators in Kosovo, the Reporting Methodology on Payment Instruments was reviewed and supplemented during 2010. This methodology aims at:

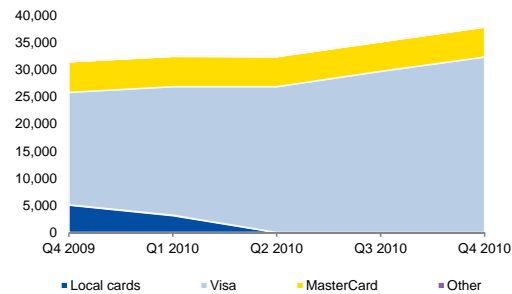
Collection and processing of periodical data and establishment of a database on payment instrument utilization in Kosovo.

Figura 78. Number of debit accounts by type



Source: CBK (2011)

Figure 79. Number of credit accounts by type



Source: CBK (2011)

Monitoring the developments in payment system area in order to assess the risk ratio contained therein and to ensure transparency in agreements relating to payment instruments and services.

Advancing publications on payment instruments in accordance with reports from the Central European Bank and International Clearing Bank, aiming at publication of data on Kosovo in relevant editions in a near future.

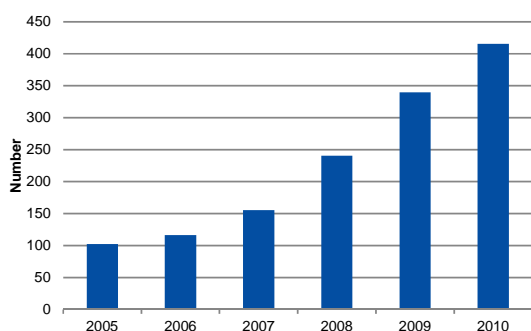
Analyzing the developments in payment instruments area in Kosovo vis-à-vis Southeastern Europe and Central European countries.

From the data collected and analyzed during 2010, it was created a clear picture on the level of development in national payment system. In general, it is noticed that the payment infrastructure and instruments are developing with a rapid trend. The number of payment function cards has constantly increased. The network of bank terminals in Kosovo is also increasing. Around 481 thousand debit cards, around 38 thousand credit cards and over 8

thousand prepaid cards have been reported in December 2010. These cards could have been used in more than 400 ATMs terminals and in more than 6,100 POS terminals distributed throughout Kosovo.

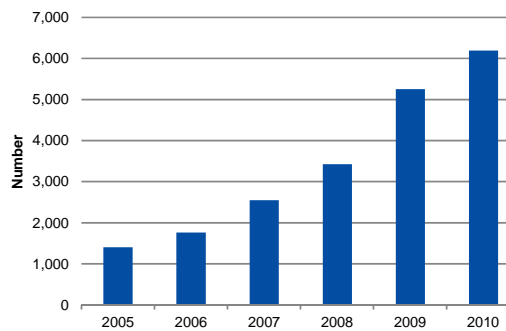
Compared to the previous year, both the number of two types of ATM terminals and the number of POS terminals increased by around 20%.

Figure 80. Number of ATM terminals



Source: CBK (2011)

Figure 81. Number of POS terminals



Source: CBK (2011)

During last year, all banks in Kosovo started providing e-banking services to their clients. From the bank reports, it results that the total number of clients' bank accounts being valid to conduct payments was around 1.4 million in the end of 2010, of which over 50 thousand or around 4 percent use e-banking. Out of accounts using e-banking, 84 percent are individual accounts and 16 are commercial accounts. Compared to the previous year, the increase of total number of these accounts was 23 percent. The number and value of transfers executed through e-banking is also increasing.

Regarding the number of terminals in 1 million residents, Kosovo stands under the average of the regional countries, but the annual trend of increase in the number of terminals is above the average of these countries. The same situation also applies to bank cards.

Table 22. Comparative table of payment instruments and terminals

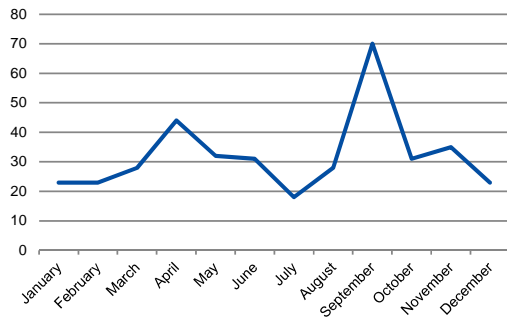
Description	Kosovo	Albania	Czech Republic	Turkey	Slovenia	Bulgaria	Hungary	Bosnia	Montenegro	Croatia	Macedonia
Residents	2.1	3.16	10.51	74.8	2.04	7.54	10.02	3.77	0.62	4.42	2.04
Surface (km ²)	10,887	28,748	78,865	783,562	20,273	110,879	93,028	51,197	13,812	56,594	25,713
Density per km ²)	193	110	133	95	101	68	108	74	45	78	79
ATM	415	741	3,573	23,952	1,786	5,471	4,748	1,355	295	3,601	832
per 1 million residents	198	234	340	320	875	726	474	359	476	815	408
per 100 km ²	4	3	5	3	9	5	5	3	2	6	3
POS	6,194	4,370	77,797	1,731,397	36,720	59,449	70,960	16,259	7,202	85,804	31,447
per 1 million residents	2,950	1,383	7,402	23,147	18,000	7,884	7,082	4,313	11,616	19,413	15,415
per 100 km ²	57	15	99	221	181	54	76	32	52	152	122
Credit Cards	37,922	23,844	1,536,882	44,392,600	122,811	1,050,566	1,505,439	-	56,935	2,044,621	188,612
per 1 million residents	18,058	7,546	146,230	593,484	60,201	139,332	150,243	-	91,831	462,584	92,457
Debit Cards	480,659	543,141	7,811,609	64,661,900	2,611,307	6,631,214	7,266,081	-	318,875	6,489,163	1,021,370
per 1 million residents	228,885	171,880	743,255	864,464	1,280,052	879,471	725,158	-	514,315	1,468,136	500,672
E-Banking	40,924	15,034	-	5,169,129	-	-	-	52,000	18,155	919,009	296,914

Source: CBK (2011) and central banks or supervision authorities of relevant countries

5.5. Credit Registry

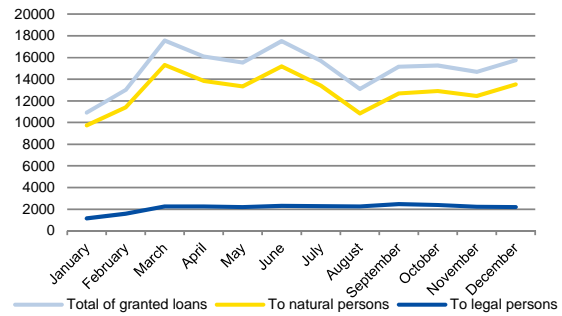
Supplying the lending and borrowing institutions with individual credit information through the Credit Registry of Kosovo (CRK) is an important service developed and managed by the CBK.

Figure 82. Number of generated certificates



Source: CBK (2011)

Figure 83.. Number of loans reported on monthly basis during 2010



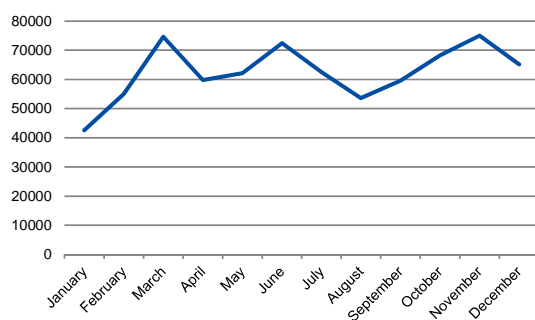
Source: CBK (2011)

CRK is designed as an internet-based application which can be accessed directly in real time by certified officers of lending institutions. Certified officers of lending institutions report to the CRK the relevant data on granted loans and update the data on regular basis until the granted loans are refunded. The number of new generated certificates and the number of new loans reported to CRK are presented on monthly basis in the figure above.

On the other hand, the CRK serves to the certified officers of lending institutions to search credit information in order to evaluate loan applications and follow the borrowers' situation. Natural persons and businesses as individual borrowers are the subjects of information to CRK. If deemed necessary, i.e. for the verification of disputable records, each individual borrower can receive from CBK his own credit information recorded in CRK. In the figures above are presented on monthly basis the number of searches conducted by the certified officers of lending institutions and the number of detailed reports generated and distributed based on the individual borrowers' requests.

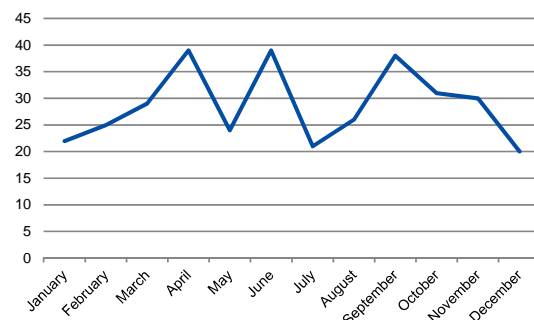
As to new developments during 2010, it is worth emphasizing the engagement in the USAID three-year program on development of business environment in Kosovo, which also includes advancing the credit information.

Figure 84. Number of searches on monthly basis in 2010



Source: CBK (2011)

Figure 85. Number of detailed individual



Source: CBK (2011)

Advancing will include implementation of changes in CRK and in functions of different relevant CBK departments. In order to facilitate the foreseen activities, CBK established a joint working group with USAID experts.

5.6. Statistics and Economic Analysis

Year 2010 is characterized by multidimensional achievements in the area of statistics as well as in that of economic analysis. Along with international recognition of compiled statistics, it was also recognized the expertise conducted by CBK Statistics Directorate staff, through its inclusion in the IMF experts' list for monetary and financial statistics. This made CBK be not only recipient but also a provider or technical assistance to other countries in the region.

A particular achievement within the CBK statistical operation in 2010 is transmission of balance of payments statistics to IMF on quarterly basis, in the framework of publications such *International Financial Statistics* and *Balance of Payments Statistical Yearbook*, along with monetary and financial statistics forwarded in 2009. This proves the internationally recognized quality of balance of payments statistics compiled by CBK.

New versions of Banking Statistics Report (BSR), Interest Rates Report (IRR) and International Transactions Reporting System (ITRS) have been implemented during 2010.

Implementation of new versions of these statistical projects was in function of following Kosovo bank market developments in compliance with international statistical standards. This has direct impact on the increase of quality of statistics variety compiled and published by the CBK.

As of January 2010, time series started to be published in a new format, including statistics under direct CBK responsibility, such as: monetary and financial statistics and those of balance of payments. During 2010, it was also continued with publication of Monthly Statistical Bulletin, where December edition represents the 113th edition, implying a constant increase both in quality and quantity of information presented in the bulletin.

In accordance with IMF "Stand-By" agreement, as of August 2010, the selected monetary, financial and the balance of payments statements have been reported to IMF. Also, in the framework of this program it is envisaged that CBK will be the promoter in relation to General Data Dissemination Standard (GDDS), the issue of which is expected to be successfully finalized in the beginning of 2011.

Economic Analysis Directorate (EAD) activity during 2010 was characterized by advancing and expanding periodical and non-periodical CBK publications. In this context, the most important development was the first edition of the Financial Stability Report, which represents the continuity of the Financial Sector Bulletin, but with extended content, which enables presentation of a more completed picture in terms of the financial sector stability in the country. In addition to parts where developments in global and national economy are described (with focus on banking sector), the Financial Stability Sector also includes a number of specific analyses, which have treated specific segments relating to financial sector operation in the country. In 2010, EAD has also started the compilation of the macroeconomic sample for Kosovo economy. A significant progress was marked on 'stress-test' compilation for Kosovo banking sector, where in cooperation with the IMF mission, it

With his survey "Determinants of Foreign Direct Investment in South East European Countries (SEEC)", **Bejtush Kiqmari**, surveyor in the CBK Statistical Office was awarded the prestigious price "Olga Radzyner", which is awarded each year by the National Bank of Austria for the best scientific surveys in the area of economy.

Previously (in 2008), a winner of this price was also Sokol Havolli from the CBK Analysis

was managed to incorporate forecasts of the economic growth in assessment of credit risk and there has been a promotion to a rather advanced level of liquidity risk assessment.

During this year, EAD kept compiling the quarterly assessment on regular basis, which is published in the Monthly Statistical Bulletin on quarterly basis. An economic statement on economic development for each quarter is given through this publication. Within the quarterly assessment, a specific analysis on developments in specific economic sectors was initiated in 2010.

Balance of Payments Bulletin represents another periodical publication within the EAD activity, providing a statement on Kosovo balance of payment, including also developments in global economy and the macroeconomic developments in the country.

Transformation of Swift Economic Indicators into Early Warning Indicators (EWI) was done in 2010. EWI represent an internal report which is compiled on monthly basis with purpose of informing CBK decision making authorities of new developments in the country, emphasizing the identification of possible risk for country's economy.

The Economic Analysis Directorate staff took part during 2010 in various local and international meetings and conferences, including some of the conferences organized by CBK. From the international conferences, it is worth mentioning the attendance of EAD staff in the European Economic Integration conference organized by Central Bank of Austria, attendance in IMF, Eurostat meetings, etc.

6. Internal Developments

6.1. Internal Control

Head of Internal Audit

Duties and responsibilities of the Head of Internal Audit (HIA) are regulated under Law on CBK (Articles 60 and 61). HIA also continued to be focused on the area of Internal Audit, control and implementation of budget and operational analyses during 2010.

Internal Audit

The Internal Audit also in 2009 has acted on the basis of the annual plan proposed by the HIA with the preliminary approval by the Audit Committee as well as by the Governing Board.

Annual Audit Plan for 2010 is drafted taking for granted the professional background and experience of the staff engaged in auditing as well as the audit outcomes from the previous years. In this context, a particular emphasis was laid on the International Audit Standards, then on preparation of a manual on audit of information technology and auditor's training on audit of financial supervision.

Audits in CBK are conducted based on the Annual Action Plan preceded by Annual Assessment of risk in compliance with International Standards of Professional Practices of Internal Audit of the Internal Auditors' Institute-IIA (Institute of Internal Auditors) as well as in compliance with section 11 of the Internal Audit Statute. Specifically, in the course of preparation of the Annual Plan, the Internal Audit is based on the following standards: Standard 1110.A1; Standard 2010; Standard 2010.A1; Standard 2010.C1. The approval of the Annual Audit Plan is also prepared according to Standard 2020, i.e. it has initially been approved by the Audit Committee as an independent body, where the final approval was done by the CBK Board. The Annual Audit Plan was also in compliance with dynamics of developments, objectives and CBK Strategic Plan for the period 2010-2015.

Risk-based audits made audits focus more on the areas where the material loss and reputation damage are more significant, which implies that the risk in central bank serves as a benchmark to the auditor. Consequently, audits were conducted monthly, quarterly, biannually, and annually. The following areas are considered to have more evident risk, which can be seen in tabular and graphical presentation.

Except audits according to the Annual Audit Plan, some "ad hoc" audits were conducted during 2010 upon the request of the Board and of the Management. During 2010, the Internal Audit examined, evaluated and reported on the inadequacy of internal control systems installed by the management.

Following examinations and evaluations of internal control systems, transaction assessment, and verification of compliance with applicable laws, rules, and regulations, the Internal Audit prepares reports in writing, which include the management responses on findings and recommendations. Reports are initially considered as draft reports, while after being discussed with the management of the relevant field and having included written comments by the management, the report becomes final and is signed by the Head of Internal and is forwarded to the CBK decision making authorities, whereas on quarterly basis, findings, recommendations, comments by management and follow-up of implementation of recommendations are forwarded to the Audit Committee, which is composed of two CBK Board non-executive members.

Table 23. Determination of auditing fields based on the risk for the three last year

Directorate	2010	2009	2008
Cashier and Treasury	17.80%	16.48%	14.00%
Asset Management	11.00%	16.87%	14.00%
Information Technology	10.04%	4.22%	
Accountancy	9.90%	15.60%	18.00%
Procurements	9.20%	10.40%	10.00%
General Services	9.10%	8.34%	
Human Resources	8.80%	9.42%	
Financial Supervision	6.40%		

Source: CBK 2011

Afterwards, the Central Bank Board is notified through the Audit Committee of the status of implementation of recommendations given by the internal Audit.

In addition to the Annual Plan and “ad hoc” audits, the operations of investments in securities and time deposits have been audited on a weekly basis during 2010. For this purpose, 52 special reports have been prepared in 2010, followed by all investments both in the money market and securities. A particular importance was given to this area, especially as of 2008 due to the global financial crisis.

During 2010, the internal Audit was focused on Information Technology activities since, according to the “risk-based” methodology, it has been estimated that the risk is more evident there, taking into consideration that CBK operates with a range of systems requiring an overall audit, in monitoring the accounting process of cash for remittances abroad, the Audit was activated only during the first quarter of 2010.

With Kosovo entering into the IMF “Stand-By” program, the Internal Audit was entrusted with the independent audit duty on the adequacy of Kosovo Government accounts.

According to the IMF program, CBK reports twice a month on all Government accounts, whereas the Department of Treasury reports on a quarterly basis, while the CBK Internal Audit reports 45 days after each testing day, which represents the last date of each year quarter. Consequently, this type of audit is empowering during each year quarter, respectively, during 2010, 2 audits of this scope have been performed and the reports have been forwarded to IMF, which included the IIIrd quarter July-September 2010 and the IVth quarter October-December 2010. With the purpose of such audit performance, it is also drafted the Procedure pursuant to IMF recommendations.

In the course of 2010, attention has been paid to the continual professional development of the Internal Audit staff, through trainings, international and local seminars, postgraduate studies and continual cooperation with the Central Banks in the region, and professional institutions such as the Institute of Internal Auditors (IIA) and the Information Systems Audit and Control Association (ISACA).

6.1.1. Control and Budget Implementation and Operational Analyses

Also, during 2010, the control and budget implementation contributed in such a way that it makes the utilization of available resources more rational and effective and in compliance with the budget approved by the CBK Board.

Budget implementation and control during 2010 contributed in implementation of CBK strategic objectives through monitoring and control of rational and effective utilization of available resources and in compliance with the budget approved by the CBK Board.

Control and budget implementation reports and operational analyzes were prepared and elaborated each month, and no substantial deviation from budget lines has been notices. Significant achievements have been reached in terms of controls and implementation of the CBK budget lines in the area of income generated from the interest in time placements in foreign banks and from securities, and the maintenance and monthly evidence on clients deposits and CBK placements in foreign banks (income and expenditures interests).

6.2. Human Resources

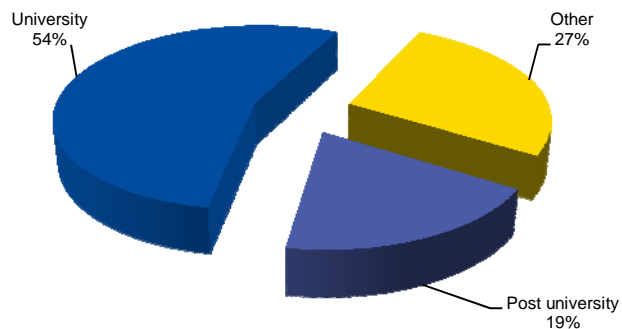
The purpose of human resources continued to remain the staff development in compliance with objectives of CBK, through development of policies on labor relation in CBK and Code of Ethics and Conduct, relevant policies and procedures focused on staff training and development, leadership and performance success process/employees' performance, analysis of competences and planning of individual business objectives and individual needs of employees' education, in order to orient the whole human potential towards achieving the CBK aims, goals and objectives.

In order to enhance the performance efficiency through efficient administration, better service, information quality, communication, decision making, and *on-line* recruitment, the human resources implemented during 2010 the human resources software by a functional database.

During 2010, the average number of CBK employees was 165, which is by 2.4% higher than in the previous year; out of them 54% are have university degree 19% with post-university degree and 27% with high, secondary and primary school.

From the employees with post-graduate degree, three of them are attending doctorate studies (PhD), two of them aboard and one in the country.

Figure 86. Structure of qualification of CBK employees



Source: CBK (2011)

Table 24. Trainings attended during 2010

Trainings organized by:	Number of participants
Central European Bank, Frankfurt- Germany	24
Financial Stability, Battenberg, Switzerland	1
Center of Excellence in Finance, Ljubljana, Slovenia	4
Joint Vienna Institute- Austria	10
Financial Stability Institute-FSI	1
Bank of Luxembourg	1
National Bank of Poland	5
Bank of France	7
Eurostat	1
Federal Reserve Ban, New York	4
Deutsche Bundesbank, Germany	2
Kosovo Bank Association	2
Bank of Netherlands	7
National Bank of Austria	2
National Bank of Czech Republic	4
Financial Supervision Authority-Poland	1
Information Systems Audit and Control Association-ISACA	1
Kosovo Public Relations Institute-IMP	2
Central Bank of Macedonia	1
Central Bank of Turkey	2
International Organization on Pension Supervision - IOPS	1
Oracle- London	1
International Training Centre-Malta	1
International Monetary Fund	1
Turkish Capital Market Board and USA Securities Market Commission	1
Solvency II-Switzerland	1
World Bank -Zagreb	1
Swiss Actuary Association	1
European Actuary Academy-Zagreb	1
WB Centre on Financial Reporting Reforms	2
Training Initiative for Financial Supervision - TIFS	1
CBK	32
Bank Association of Turkey	1

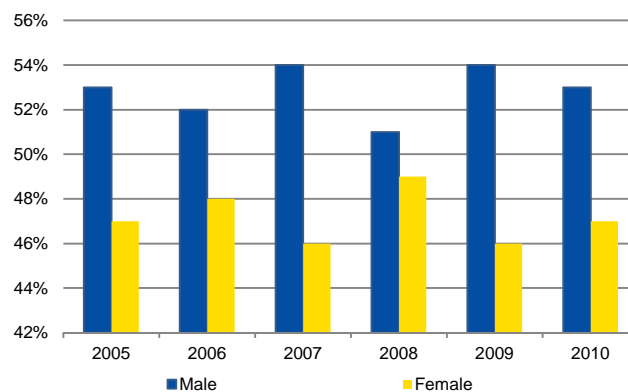
Source: CBK 2011

Out of total 165 employees in 2010, 47% of them were female staff.

Female participation in managerial positions reaches at 33% in total in 2010, which represents a growing trend of female participation in decision making compared to the previous years of the CBK functioning.

The average age of total employees in 2010 was around 40 years.

With purpose of better implementation of its objective, CBK continually invests on its staff training and development through participation in courses, trainings, seminars, workshops and academic programs relevant to CBK.

Figure 87. Gender structure in CBK

Source: CBK (2011)

In addition to its own resources, CBK in 2010, enjoyed financial support for trainings by the World Bank, namely by the Financial Sector Technical Assistance Project (FSTA) and by the Central European Bank.

Central Bank of the Republic of Kosovo continually offers opportunity for students from universities/colleges, from the country and from abroad, to attend the practice program called “internship” During 2010, eleven (11) students completed also their practice work successfully at different CBK directorates.

6.3. Legal Activity of the CBK

Significant successes have been recorded in 2010 towards strengthening and modernization of legal infrastructure. Thus, the Law on Central Bank of the Republic of Kosovo was adopted during this year, which law clearly established the Central Bank objectives and duties, in compliance with international standards and practices. The new Law on Central Bank establishes the legal framework for a modern bank with all necessary attributes for achieving the objectives and performance of duties established under this law. The Law on Establishment of Deposit Insurance System for Financial Institutions in Kosovo was also adopted this year. The objective of this law is to protect small depositors, while the Fund is expected to become operational during 2011.

With purpose of modernization of legislation in the financial sector area and its harmonization with the core principles of the European Union directives and the international standards, during 2010 it was also proceeded with drafting the other laws in the financial sector area. This group of laws includes: draft law on banks, draft law on pension funds, draft law on compulsory motor liability insurance and the draft law on payments. These laws which are envisaged to be adopted during 2011 will supersede the relevant existing regulations.

In the course of application of the new Law on CBK and other relevant laws, it was also continued with adoption of a wider range of sublegal acts which aim at practical functionality of provisions of applicable legislation. Also, the legal activity also continued in reaching cooperation agreements with other local and international institutions, with purpose of efficient exercise of duties relating to issues within the mutual competency scope of relevant institutions.

In general, the entire legal activity during this year was oriented in further development of the legal framework which enabled the continuation of safe and effective function of financial sector in Kosovo.

6.4. Finance and Information Technology Management

In the area of financial management and information technology, the CBK made a great step ahead towards the implementation of technical and functional advancement of its basic banking system – *Oracle Flexcube* during 2011. Implementation of two new software components on securities and online banking were also included within this project. This project was initiated in 2009 (necessary researches were conducted in the second half of 2009, while the final approval was done in November 2009) and started to be implemented in July 2010. Through these project objectives, an advancement of the previous version functionality (5.1) was done and the new functionalities of new version (11.0) have been implemented, as required by CBK. An emphasis should be laid in relation to preparation of financial information and reports, expenditure processing, management of core assets, management of clients’ accounts, execution of local and international payments, etc. The

new component in securities enabled automation and standardization of securities management purchased by CBK, whereas the new component on online banking achieved a further advancement of services to the CBK clients. This project continued during the second half of 2010, and the system became officially operational on 1 January 2011. It is worth mentioning that this was the largest project ever implemented in CBK, and which included, in addition to relevant finance directorate and information technology directorate, the cash operation and payment directorate and asset management directorate as well.

The CBK finance management is done within the Financial Planning and Reporting Directorate. This directorate is responsible for accountancy services, financial administrative and supporting services, budgeting process, preparation of financial reports and conduct of financial analyses. During 2010, the regular duties were successfully performed and advancements in several aspects have been achieved. In addition to engagement in advancing the CBK basic banking system, it is worth mentioning the preparation of CBK Budgeting Policy and supplementation and update of several operation instructions. With the IMF technical assistance, it was drafted the Accountancy Manual, which will be adopted in 2011. Periodical financial reports and budget analysis have also been increased and refined. In the course of CBK role as a fiscal agent, in 2010, it was recorded an additional engagement in coordinating relations with IMF on behalf of the State of Kosovo, as well as in managing the CBK special financial arrangements with Treasury. The CBK information technology is managed through the relevant directorate. The main duty of the Information Technology and Systems Directorate is to provide efficient support-oriented services to users for different CBK function areas. This directorate is responsible for administration and maintenance of all CBK information systems. During 2010, some new developments have been recorded. Apart from the advancement of the CBK basic banking system, a number of software and hardware components of other information systems have been advanced, and several relevant operation guidelines and instructions have been issued. It is worth mentioning that introduction and use of optical fiber connections in external communications, led to the increase of efficiency and security in this area. Also, activation of automation of reserve arrangements outside CBK building for information systems represents another important event in operation modernization.

7. Regional and International Cooperation

7.1. International Agreements

Also in 2010, CBK continued its engagements towards signing international memorandums of understanding with similar institutions and agencies from different countries. The following memorandums of understanding have been signed during the year:

Memorandum of Understanding between CBK and Insurance Supervision Agency of Montenegro.

Memorandum of Understanding between CBK and Insurance Supervision Agency of the Republic of Macedonia.

Memorandum of Understanding on mutual assistance and information exchange on the issue of securities and insurance supervision between CBK and Bulgarian Financial Supervision Commission.

These mutual agreements will certainly increase the quantity and quality of the necessary information to ensure an effective and efficient supervision of financial institutions by the signatory parties and will enable exchange of mutual experience and staff training in relevant fields.

7.2. International Promotion and Representation

CBK continued to be in 2010 an organizer and co-organizer of important events in Kosovo financial sector and economy. Thus, it organized the following important events during last year:

The conference on the occasion of publication of the first edition of the Financial Stability Report in Kosovo, where among the guests were the Governor of Central Bank of Turkey and the Governor of Bank of Albania;

The conference on the topic "*Study Promotion of Remittances in Kosovo 2010*", prepared in close cooperation between CBK and USAID-it, IMF, Ministry of Economy and Finance, Kosovo Statistical Office. This Study and the conference organized therein, raised a better awareness on understanding of flow, utilization and effect of the migrant remittances have on people's life, as well as their impact of Kosovo economy in general;

The conference on the topic "*Insurance perspective in the light of future developments*", organized in cooperation with the Kosovo Association of Insurance Companies. Keynote speakers in this conference were representatives from Kosovo institutions, regional regulatory authorities (Slovenia, Montenegro, Macedonia and Albania) and insurance companies, including representatives from the Executive Committee of International Insurance Supervision Association;

The conference on the topic "*Finance resources for economic growth: Has Kosovo sufficient money*" organized in cooperation with the International Civilian Office (ICO). In addition to CBK, the speakers in this conference were representatives from ICO, Liaison Office of the European Commission, IMF, Ministry of Economy and Finance, representatives from Kosovo financial sector and from the institutions dealing with macroeconomic analyses.

The seminar on the topic "*A step closer to liberalization of compulsory motor liability insurance*", organized by CBK in cooperation with the World Bank.

This seminar brought together well-known world experts in the insurance area, where among the participants were representatives from the World Bank, Turkey, Italy, Great Britain, representatives from the Financial Supervision Authority of Albania, representatives from Kosovo Insurance Association and insurance companies operating in Kosovo.

The CBK representatives attended all IMF and World Bank regular (spring and autumn) meetings held during 2010. In this context, obligations deriving from the membership in these two institutions kept being fulfilled with full efficiency, including the necessary reporting, voting procedures on certain issues up to active participation in meetings of Belgian-Austrian Constituency, which in 2010 was also joined by the Republic of Kosovo. Also, the senior CBK management took active part in annual meetings and round tables of the European Fund for Southeastern Europe (EFSE), respectively in the work of EFSBE Board, then in the work of Advisory Board and round tables organized by the Center of Excellence in Finance (CEF), with its headquarters in Ljubljana.

In the framework of participation in conferences of particular international importance, it is worth underlining the CBK representation in the 5th two-year Conference on risk management and financial supervision, organized by the Financial Stability Institute of *the Bank for International Settlements (BIS)*, in Basel (Switzerland), wherein in the context of meetings for strengthening the international cooperation, a meeting was held with the President of Federal Financial Supervision Authority of Germany (BaFin). Also, it is worth mentioning the CBK representation in the 6th European Central Bank (ECB) Conference on central banking on the topic "Review of the approach against monetary policy – lessons learnt from the crisis", which, except the governors and world eminent experts, it was also attended by the IMF Managing Director, President of ECB and the President of the USA Federal Reserves.

Among the important visits to CBK, it is worth mentioning the visit by a delegation of young businessmen from Chicago of the USA and the visit of CBK delegation to Regulatory and Supervision Authority (BRSA), Central Bank of Turkey, Bank Association of Turkey and Capital and Market Board of Turkey.

In accordance with challenges and priorities set for 2010, official visits have been paid to the Central Bank of Macedonia and the Central Bank of Bulgaria, where it was discussed about the possibilities of finding new ways of cooperation, and it was also discussed the possibility of concluding memorandums of understandings on information and experience exchange between the relevant authorities. A visit of similar character was also paid to the Financial Supervision Commission of Bulgaria (with which it was signed a Memorandum of Understanding). It is also worth mentioning that during the previous year, the cooperation dynamics significantly increased (mainly in the staff training area) with Central Bank of Albania, Central Bank of Poland and Central Bank of Slovenia, with which we signed an agreement on technical assistance which gives the CBK staff an opportunity to attend a practical teaching in the Bank of Slovenia pursuant to the needs to be identified by the CBK.

In the course of attempts to increase the international cooperation in the scope of its responsibilities, the CBK conducted during 2011 a wide range of activities to find acceptable modalities for ensuring access to the SWIFT System (Society for Worldwide Interbank Financial Telecommunication System) and the Green Card System.

8. Financial Statements of the CBK



Central Bank of the Republic of Kosovo

Financial statements

as at and for the year ended 31 December 2010

Central Bank of the Republic of Kosovo

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Independent Auditors' Report

To the Governing Board of
the Central Bank of the Republic of Kosovo

Pristina, 27 May 2011

Report on the Financial Statements

We have audited the accompanying financial statements of Central Bank of the Republic of Kosovo ("the Bank"), which comprise the statement of financial position as at 31 December 2010, the statements of comprehensive income, changes in equity and cash flows for the year then ended, and notes, comprising a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with International Financial Reporting Standards, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.



We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements give a true and fair view of the financial position of the Bank as at 31 December 2010, and of its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

KPMG Albania Shpk Kosovo Branch

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Central Bank of the Republic of Kosovo

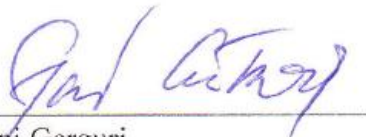
Statement of financial position


As at 31 December

<i>In thousands of EUR</i>	Note	2010	2009
Assets			
Cash on hand	7	60,194	21,806
Current accounts with non-resident banks	8	25,621	34,899
Treasury bills	9	199,275	529,652
Deposit accounts with non-resident banks	10	807,332	487,529
Assets related with International Monetary Fund	11	154,554	124,482
Property and equipment	12	1,736	2,115
Intangible assets	13	898	174
Other assets	14	429	351
Total assets		1,250,039	1,201,008
Liabilities			
Due to domestic banks	15	203,572	233,246
Due to IMF related accounts	16	153,868	124,786
Due to governmental institutions	17	798,721	665,187
Due to public and commercial entities	18	43,228	130,847
Other domestic liabilities	19	2,670	2,019
Total liabilities		1,202,059	1,156,085
Capital and reserves			
Statutory fund	20	30,000	30,000
Reserve fund	21	14,923	11,203
Retained Earnings		3,057	3,720
Total capital and reserves		47,980	44,923
Total liabilities, capital and reserves		1,250,039	1,201,008

The notes on pages 5 to 37 are an integral part of these financial statements.

These financial statements set out on pages 5 to 37 were approved by the management of CBK on 5 April 2011 and signed on its behalf by:


Gani Gerguri
Acting Governor


Faton Ahmetaj
Director of Financial Planning and
Reporting

Central Bank of the Republic of Kosovo

Statement of comprehensive income

For the year ended 31 December 2010

<i>In thousands of EUR</i>	Note	2010	2009
Interest income		4,574	6,629
Interest expense		(2,852)	(2,500)
Net interest income	22	1,722	4,129
Fee and commission income		2,575	2462
Fee and commission expense		(248)	(269)
Net fee and commission income	23	2,327	2,193
Grant revenue	24	57	24
Other operating income	25	1,522	1,340
Foreign exchange net gain/(loss)	28	1,408	(303)
Operating income		7,036	7,383
Personnel expenses	26	(2,395)	(2,160)
Depreciation and amortization	12,13	(564)	(505)
General and administrative expenses	27	(1,020)	(998)
Operating expenses		(3,979)	(3,663)
Profit for the year		3,057	3,720
Other comprehensive income		-	-
Total comprehensive income for the year		3,057	3,720

The notes on pages 5 to 37 are an integral part of these financial statements.

Central Bank of the Republic of Kosovo

Statement of changes in equity

As at 31 December

<i>In thousands of euro</i>	Statutory fund	Reserve fund	Retained Earnings	Total
Balance at 1 January 2009	30,000	3,736	7,467	41,203
Total comprehensive income for the year				
Other comprehensive income	-	-	-	-
Profit	-	-	3,720	3,720
Total comprehensive income for the year	-	-	3,720	3,720
Transactions required by law, recorded directly in equity	-	-	-	-
Transfer to statutory fund	-	7,467	(7,467)	-
Total transfers to statutory fund	-	7,467	(7,467)	-
Balance at 31 December 2009	30,000	11,203	3,720	44,923
Balance at 1 January 2010	30,000	11,203	3,720	44,923
Total comprehensive income for the year				
Other comprehensive income	-	-	-	-
Profit	-	-	3,057	3,057
Total comprehensive income for the year	-	-	3,057	3,057
Transactions required by law, recorded	-	3,720	(3,720)	-
Transfer to reserve fund	-	-	-	-
Total transfer to reserve fund	-	3,720	(3,720)	-
Balance at 31 December 2010	30,000	14,923	3,057	47,980

The notes on pages 5 to 37 are an integral part of these financial statements.

Central Bank of the Republic of Kosovo

Statement of cash flows

For the year ended 31 December 2010

<i>In thousands of EUR</i>	Note	2010	2009
Cash flows from operating activities			
Profit for the year		3,056	3,720
<i>Adjustments for:</i>			
Depreciation	12	478	444
Amortization	13	86	61
Grant revenue	24	(57)	(24)
Gain on sale of equipment		-	(11)
Interest income	22	(4,574)	(6,629)
Interest expense	22	2,852	2,500
		1,841	61
Change in treasury bills		250,380	(15,959)
Change in deposit accounts with nonresident banks		(163,904)	(61,824)
Change in assets with IMF		(22,477)	(124,458)
Change in other assets		(85)	31
Change in due to domestic banks		(29,672)	96,088
Change in due to IMF related accounts		21,490	124,761
Change in due to governmental institutions		132,947	(243,129)
Change in due to public and commercial entities		(87,619)	106,648
Change in other domestic liabilities		(654)	32
		103,554	(117,749)
Interest received		4,119	9,160
Interest paid		(2,347)	(2,574)
Net cash used in / (generated from) operating activities		105,326	(111,163)
Cash flows from investing activities			
Proceeds from sale of equipment		-	11
Purchase of equipment	12	(99)	(472)
Purchase of intangible assets	13	(810)	(149)
Net cash used in investing activities		(909)	(610)
Cash flows from financing activities			
Proceeds from grants		53	33
Net cash generated from financing activities		53	33
Net increase/(decrease) in cash and cash equivalents		104,470	(111,740)
Effect of exchange rate		-	(303)
Cash and cash equivalents at 1 January		618,835	730,878
Cash and cash equivalents at 31 December	29	723,305	618,835

The notes on pages 5 to 37 are an integral part of these financial statements.

Central Bank of the Republic of Kosovo

Notes to the financial Statement

(in thousands of EUR, unless otherwise stated)

1. Reporting entity

The Central Bank of the Republic of Kosovo (hereinafter "CBK" or "the Bank"), the successor to the Central Banking Authority of Kosovo, is an independent juridical entity with full capacity as a legal person under the law applicable in the Republic of Kosovo. CBK is a distinct public entity with the authority to license, supervise and regulate financial institutions in the Republic of Kosovo. The Bank acts in accordance with Law No.03/L-209 "Law on Central Bank of the Republic of Kosovo", hereafter referred to as ("the CBK Law"). As per this law, the principal objectives of CBK are to:

- foster and maintain a stable financial system, including a safe, sound and efficient payment system.
- contribute to achieving and maintaining domestic price stability.
- support the general economic policies of the Government.

As prescribed in the Law, CBK shall act in accordance with the principles of an open market economy with free competition, favoring an efficient allocation of resources.

CBK operates from its premises located in Pristina. The address of the registered office of CBK is as follows:

33 Garibaldi Street

Pristina, Kosovo.

Central Bank Board, Executive Board and Governor

The decision-making bodies of CBK are the Central Bank Board, the Executive Board, and the Governor. As per Article 79, paragraph 2 of the CBK Law, the Central Bank Board comprises of the Governor, the General Director of Treasury and three non-executive members and is charged with the supervision of the implementation of the policies, and the supervision of the administration and the operations of CBK.

As at 31 December 2010, the Central Bank Board of CBK comprised the following members:

- Gazmend Luboteni – Chairman
- Gani Gerguri – Acting Governor
- Lulzim Ismajli – Member, Director of Treasury of Ministry of Finance
- Sejdi Rexhepi – Member
- Mejd Bektashi – Member

2. Basis of preparation

a) Statement of compliance

The financial statements have been prepared in accordance with International Financial Reporting Standards (IFRSs).

b) Basis of measurement

The financial statements have been prepared on the historical cost basis.

Central Bank of the Republic of Kosovo

Notes to the financial Statement

(in thousands of EUR, unless otherwise stated)

2. Basis of preparation (Continued)

c) Functional and presentation currency

These financial statements are presented in Euro (“EUR”), which is CBK’s functional currency. Except as indicated, financial information presented in Euro has been rounded to the nearest thousand.

d) Use of estimates and judgments

The preparation of the financial statements requires management to make judgments, estimates and assumptions that affect the application of policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimate is revised and in any future periods affected. In particular, information about significant areas of estimation uncertainty and critical judgments in applying accounting policies that have the most significant effect on the amounts recognized in the financial statements are described in note 5.

The accounting policies set out below have been applied consistently to all the periods presented in these financial statements.

3. Significant accounting policies

a) Foreign currency transactions

Transactions in foreign currencies are translated to the functional currency at exchange rates at the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies at the reporting date are retranslated to the functional currency at the exchange rate at that date. The foreign currency gain or loss on monetary items is the difference between the amortised cost in the functional currency at the beginning of the period, adjusted for effective interest and payments during the period, and the amortised cost in foreign currency translated at the exchange rate at the end of the period. Non-monetary assets and liabilities denominated in foreign currencies that are measured at fair value are retranslated to the functional currency at the exchange rate at the date that the fair value was determined. Foreign currency differences arising on retranslation are recognised in profit or loss.

b) Interest

Interest income and expense are recognised in profit or loss using the effective interest method. The effective interest rate is the rate that exactly discounts the estimated future cash payments and receipts through the expected life of the financial asset or liability (or where appropriate, a shorter period) to the carrying amount of the financial asset or liability. The effective interest rate is established on initial recognition of the financial asset and liability and is not revised subsequently.

Central Bank of the Republic of Kosovo

Notes to the financial Statement

(in thousands of EUR, unless otherwise stated)

3. Significant accounting policies (continued)

b) Interest (continued)

The calculation of the effective interest rate includes all fees and points paid or received transaction costs, and discounts or premiums that are an integral part of the effective interest rate.

Transaction costs are incremental costs that are directly attributable to the acquisition, issue or disposal of a financial asset or liability.

Interest income and expense presented in the profit or loss includes interest on financial assets and liabilities at amortised cost on an effective interest rate basis.

c) Fees and commission

Fees and commission income and expenses that are integral to the effective interest rate on a financial asset or liability are included in the measurement of the effective interest rate.

Other fees and commission income, including transaction fees for operating accounts, fund transfers and licensing fees are recognized as the related services are performed.

Other fees and commission expenses relate mainly to transaction and service fees, which are expensed as the services are received.

d) Employee benefits

i. Defined contribution plans

CBK makes compulsory social security contributions that provide pension benefits for employees upon retirement. These contributions are classified under defined contribution plans based on Kosovo legislation. CBK's contributions are charged to profit or loss as incurred.

CBK makes pension contributions as permitted by the Kosovo law, whereby the State provides pension benefits for employees upon retirement. CBK's contributions to the pension plan are charged to profit or loss as incurred.

e) Taxation and profit allocation

CBK is exempt from income tax according to Law No. 03/L-209 issued on 22 July 2010. See note 4 (f) on how CBK allocates its profit.

Central Bank of the Republic of Kosovo

Notes to the financial Statement

(in thousands of EUR, unless otherwise stated)

3. Significant accounting policies (continued)

f) Financial assets and liabilities

i. Recognition

CBK initially recognizes deposits on the date they originate. All other financial assets and liabilities are initially recognized on the trade date at which CBK becomes a party to the contractual provisions of the instrument.

A financial asset or financial liability is measured initially at fair value plus, for an item not at fair value through profit or loss, transaction costs that are directly attributable to its acquisition or issue.

ii. Derecognition

CBK derecognizes a financial asset when the contractual rights to the cash flows from the asset expire, or it transfers the rights to receive the contractual cash flows on the financial asset in a transaction in which substantially all the risks and rewards of ownership of the financial asset are transferred. Any interest in transferred financial assets that is created or retained by CBK is recognized as a separate asset or liability. On derecognition of a financial asset, the difference between the carrying amount of the asset (or the carrying amount allocated to the portion of the asset transferred), and the sum of (i) the consideration received (including any new asset obtained less any new liability assumed) and (ii) any cumulative gain or loss that had been recognized in other comprehensive income is recognized in profit or loss.

CBK derecognises a financial liability when its contractual obligations are discharged or cancelled or expire.

iii. Offsetting

Financial assets and liabilities are offset and the net amount is presented in the statement of financial position when, and only when, CBK has a legal right to set off the amounts and intends either to settle on a net basis or to realise the asset and settle the liability simultaneously.

Income and expenses are presented on a net basis only when permitted by the accounting standards, or for gains and losses arising from a group of similar transactions.

iv. Amortized cost measurement

The amortised cost of a financial asset or liability is the amount at which the financial asset or liability is measured at initial recognition, minus principal repayments, plus or minus the cumulative amortisation using the effective interest method of any difference between the initial amount recognised and the maturity amount, minus any reduction of impairment.

v. Fair value measurement

Fair value is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction on the measurement date.

When available, CBK measures the fair value of an instrument using quoted prices in an active market for that instrument. A market is regarded as active if quoted prices are readily and regularly available and represent actual and regularly occurring market transactions on an arm's length basis.

Central Bank of the Republic of Kosovo

Notes to the financial Statement

(in thousands of EUR, unless otherwise stated)

3. Significant accounting policies (continued)

v. Fair value measurement

If a market for a financial instrument is not active, CBK establishes fair value using a valuation technique. Valuation techniques include using recent arm's length transactions between knowledgeable, willing parties (if available), reference to the current fair value of other instruments that are substantially the same, discounted cash flow analyses and option pricing models. The chosen valuation technique makes maximum use of market inputs, relies as little as possible on estimates specific to CBK, incorporates all factors that market participants would consider in setting a price, and is consistent with accepted economic methodologies for pricing financial instruments. Inputs to valuation techniques reasonably represent market expectations and measures of the risk-return factors inherent in the financial instrument. CBK calibrates valuation techniques and tests them for validity using prices from observable current market transactions in the same instrument or based on other available observable market data.

iv. Identification and measurement of impairment

At each reporting date CBK assesses whether there is objective evidence that financial assets not carried at fair value through profit or loss are impaired. Financial assets are impaired when objective evidence demonstrates that a loss event has occurred after the initial recognition of the asset, and that the loss event has an impact on the future cash flows on the asset that can be estimated reliably.

Objective evidence that financial assets are impaired can include default or delinquency by a borrower, restructuring of a placement or advance by CBK on terms that CBK would not otherwise consider, indications that a borrower or issuer will enter bankruptcy, the disappearance of an active market for a security, or other observable data relating to a group of assets such as adverse changes in the payment status of borrowers or issuers in CBK, or economic conditions that correlate with defaults in CBK.

Impairment losses on assets carried at amortised cost are measured as the difference between the carrying amount of the financial assets and the present value of estimated cash flows discounted at the assets' original effective interest rate. Losses are recognised in profit or loss and reflected in an allowance account against loans and advances. Interest on the impaired asset if applicable, continues to be recognised through the unwinding of the discount. When a subsequent event causes the amount of impairment loss to decrease, the impairment loss is reversed through profit or loss.

g) Cash and cash equivalents

Cash and cash equivalents include cash balance on hand, demand deposits with banks and highly liquid financial assets with original maturities of less than three months, which are subject to insignificant risk of changes in their fair value, and are used by CBK in the management of its short-term commitments.

Cash and cash equivalents are carried at amortised cost in the statement of financial position.

h) Investment securities

Investment securities, consisting of Treasury Bills, are initially measured at fair value plus incremental direct transaction costs and subsequently accounted for as held-to-maturity.

Central Bank of the Republic of Kosovo

Notes to the financial Statement

(in thousands of EUR, unless otherwise stated)

3. Significant accounting policies (continued)

h) Investment securities (continued)

Held-to-maturity investments are non-derivative assets with fixed or determinable payments and fixed maturity that CBK has the positive intent and ability to hold to maturity, and which are not designated at fair value through profit or loss. Held-to-maturity investments include treasury bills.

Held-to-maturity investments are carried at amortised cost using the effective interest method. Any sale or reclassification of a significant amount of held-to-maturity investments not close to their maturity would result in the reclassification of all held-to-maturity investments as available-for-sale, and prevent CBK from classifying investment securities as held-to-maturity for the current and the following two financial years.

i) Property and equipment

i. Recognition and measurement

Items of property and equipment are measured at cost less accumulated depreciation and impairment losses.

Cost includes expenditures that are directly attributable to the acquisition of the asset. The cost of self-constructed assets includes the cost of materials and direct labour, any other costs directly attributable to bringing the asset to a working condition for its intended use, and the costs of dismantling and removing the items and restoring the site on which they are located. Purchased software that is integral to the functionality of the related equipment is capitalised as part of that equipment.

When parts of an item of property or equipment have different useful lives, they are accounted for as separate items (major components) of property and equipment.

ii. Subsequent costs

The cost of replacing part of an item of property or equipment is recognised in the carrying amount of the item if it is probable that the future economic benefits embodied within the part will flow to CBK and its cost can be measured reliably. The costs of the day-to-day servicing of property and equipment are recognised in profit and loss as incurred.

iii. Depreciation

Depreciation is recognised in profit or loss on a straight-line basis over the estimated useful lives of each part of an item of property and equipment.

The estimated useful lives for the current and comparative periods are as follows:

	2010	2009
Leasehold improvements	20 years	20 years
Equipment	5 years	5 years
Computers	3 years	3 years
Vehicles	5 years	5 years

Depreciation methods, useful lives and residual values are reassessed at the reporting date.

Central Bank of the Republic of Kosovo

Notes to the financial Statement

(in thousands of EUR, unless otherwise stated)

3. Significant accounting policies (continued)

j) Intangible assets

Software acquired by CBK is stated at cost less accumulated amortisation and accumulated impairment losses.

Subsequent expenditure on software is capitalised only when it increases the future economic benefits embodied in the specific asset to which it relates. All other expenditure is expensed as incurred.

Amortisation is recognised in profit or loss on a straight-line basis over the estimated useful life of the software, from the date that it is available for use. The estimate useful life of software is three years (2009: 3 years).

k) Impairment non-financial assets

The carrying amounts of CBK's non-financial assets are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists then the asset's recoverable amount is estimated.

An impairment loss is recognised if the carrying amount of an asset or its cash-generating unit exceeds its recoverable amount. A cash-generating unit is the smallest identifiable asset group that generates cash flows that largely are independent from other assets and groups. Impairment losses are recognised in profit or loss. Impairment losses in respect of cash-generating units are allocated to reduce the carrying amount of the other assets in the unit (group of units) on a pro rata basis.

The recoverable amount of an asset or cash-generating unit is the greater of its value in use and its fair value less costs to sell. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset.

Impairment losses recognised in prior periods are assessed at each reporting date for any indications that the loss has decreased or no longer exists. An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

l) Financial liabilities

CBK's sources of funding are from international, governmental, public, banking and other financial institutions. Financial liabilities are measured at their amortised cost using the effective interest rate method.

m) Grant revenue

Government grants are recognised initially as deferred income when there is reasonable assurance that they will be received and that CBK will comply with the conditions associated with the grant. Grants that compensate CBK for expenses incurred are recognised in profit or loss on a systematic basis in the same periods in which the expenses are recognised. Grants that compensate CBK for the cost of an asset are recognised in profit or loss on a systematic basis over the useful life of the asset.

Central Bank of the Republic of Kosovo

Notes to the financial Statement

(in thousands of EUR, unless otherwise stated)

3. Significant accounting policies (continued)

n) Donor financed salaries

Certain individuals engaged at CBK are international experts appointed and funded for a short term by international organisations. The funding from these international organisations includes, but it is not limited to, the payment of salaries to these international experts. As this assistance is paid by the international organisations directly to the appointee, the extent of the payments are not known nor are they included in these financial statements.

o) Provisions

A provision is recognised if, as a result of a past event, CBK has a present legal or constructive obligation that can be estimated reliably, and it is probable that an outflow of economic benefits will be required to settle the obligation. Provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and, where appropriate, the risks specific to the liability.

A provision for onerous contracts is recognised when the expected benefits to be derived by CBK from a contract are lower than the unavoidable cost of meeting its obligations under the contract. The provision is measured at the present value of the lower of the expected cost of terminating the contract and the expected net cost of continuing with the contract. Before a provision is established, CBK recognises any impairment loss on the assets associated with that contract.

p) New standards and interpretations

A number of new standards, amendments to standards and interpretations are not yet effective for the year ended 31 December 2010, and have not been applied in preparing these financial statements. None is expected to have an effect on the financial statements of the Bank with the exception of:

- IFRS 9 Financial Instruments (effective for annual periods beginning on or after 1 January 2013, earlier application is permitted). This Standard replaces the guidance in IAS 39, Financial Instruments: Recognition and Measurement, about classification and measurement of financial assets. The Standard eliminates the existing IAS 39 categories of held to maturity, available for sale and loans and receivable.
- Financial assets will be classified into one of two categories on initial recognition:
- Financial assets measured at amortized cost or financial assets measured at fair value.

A financial asset is measured at amortized cost if the following two conditions are met: the assets is held within a business model whose objective is to hold assets in order to collect contractual cash flows; and, its contractual terms give rise on specified dates to cash flows that are solely payments of principal and interest on the principal outstanding.

Gains and losses on remeasurement of financial assets measured at fair value are recognised in profit or loss, except that for an investment in an equity instrument which is not held for trading, IFRS 9 provides, on initial recognition, an irrevocable election to present all fair value changes from the investment in other comprehensive income (OCI). The election is available on an individual share-by-share basis. No amount recognised in OCI is ever reclassified to profit or loss at a later date. CBK is in the process of determining the effect, if any, on the financial statements, of the introduction of IFRS 9.

Central Bank of the Republic of Kosovo

Notes to the financial Statement

(in thousands of EUR, unless otherwise stated)

3. Significant accounting policies (continued)

p) New standards and interpretations

- Revised IAS 24 Related Party Disclosure (effective for annual periods beginning on or after 1 January 2011) The amendment exempts government-related entity from the disclosure requirements in relation to related party transactions and outstanding balances, including commitments, with (a) a government that has control, joint control or significant influence over the reporting entity; and (b) another entity that is a related party because the same government has control, joint control or significant influence over both the reporting entity and the other entity. The revised Standard requires specific disclosures to be provided if a reporting entity takes advantage of this exemption. The revised Standard also amends the definition of a related party, which resulted in new relations being included in the definition, such as, associates of the controlling shareholder and entities controlled, or jointly controlled, by key management personnel. The Bank is in the process of assessing the impact of the revised IAS 24 on its financial statements.

4. Financial risk management

a) Introduction and overview

CBK has exposure to the following risks from its use of financial instruments:

- Credit risk
- Operational risk
- Liquidity risk
- Market risk

This note presents information about CBK's exposure to each of the above risks, CBK's objectives, policies and processes for measuring and managing risk, and CBK's management of capital. Further quantitative disclosures are included throughout these financial statements.

Risk management framework

The Central Bank Board has overall responsibility for the establishment and oversight of CBK's risk management framework. CBK management reports regularly to the Central Bank Board on risk management practices. The Executive Committee and Investment Committee have obligations for developing and monitoring CBK risk management policies. These policies are implemented by the respective organisational units.

Central Bank of the Republic of Kosovo

Notes to the financial Statement

(in thousands of EUR, unless otherwise stated)

4. Financial risk management (continued)

Risk management framework (continued)

CBK's risk management policies are established to identify and analyze the risks faced by CBK, to set appropriate risk limits and controls, and to monitor risks and adherence to limits. Risk management policies and systems are reviewed regularly to reflect changes in market conditions, products and services offered. CBK, through its training and management standards and procedures, aims to develop a disciplined and constructive control environment, in which all employees understand their roles and obligations.

CBK's Audit Committee is responsible for monitoring compliance with CBK's risk management policies and procedures, and for reviewing the adequacy of the risk management framework in relation to the risks faced by CBK. CBK's Audit Committee is assisted in these functions by the Internal Audit Directorate. Internal audit undertakes both regular and ad-hoc reviews of risk management controls and procedures, the results of which are reported through the Inspector General to the Audit Committee.

b) Credit risk

Credit risk is the risk of financial loss to CBK if a counterparty to a financial instrument fails to meet its contractual obligations, and arises principally from CBK's investments in debt securities and deposits in other banks.

Management of credit risk

i. Investments and exposure to other banks

CBK limits its exposure to credit risk by investing only in debt securities issued by the governments of EU countries and having deposits with foreign banks whose short term liabilities are rated in one of the two highest categories by internationally recognized credit rating agencies. Given the high credit ratings, management does not expect any counterparty to fail to meet its obligations.

ii. Exposure to credit risk

The maximum exposure to credit risk as at 31 December 2010 and 31 December 2009 is presented by the carrying amount of its cash on hand, current accounts with non-resident banks, treasury bills and deposit accounts with non-resident banks. For details on the exposures see Notes 7, 8, 9 and 10.

None of CBK's exposures are past due or impaired. There are no changes in the credit risk management policies from previous years. CBK does not hold any collateral or other credit enhancements against its exposure to credit risk.

c) Liquidity risk

Liquidity risk is the risk that CBK will encounter difficulty in meeting obligations from its financial liabilities.

Central Bank of the Republic of Kosovo

Notes to the financial Statement

(in thousands of EUR, unless otherwise stated)

4. Financial risk management (continued)

c) Liquidity risk (continued)

Management of liquidity risk

CBK's approach to managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to CBK's reputation.

Policies to monitor and address liquidity risk are set by the Central Bank Board. CBK manages its liquidity risk by investing in short term deposits with nonresident banks and holding adequate quantity of cash in its vaults. Liquidity management policies are set to ensure that even under adverse conditions, CBK is in a position to meet its obligations.

The daily liquidity position is monitored and regular liquidity stress testing is conducted under a variety of scenarios covering both normal and more severe market conditions. All liquidity policies and procedures are subject to review and approval by CBK management. Monthly reports covering the liquidity position of CBK are regularly submitted to the Investment Committee members by the Asset Management Directorate.

Exposure to liquidity risk

Residual contractual maturities of financial liabilities, excluding future interest payments

31 December 2010		Carrying	Less than	1-3	3 Months
<i>Non-derivative liabilities</i>	Note	amount	1 month	months	to 1 year
Due to domestic banks	15	203,572	203,574	-	-
Due to IMF related accounts	16	153,868	131,776	-	22,093
Due to governmental institutions	17	798,721	497,146	226,351	75,225
Due to public and commercial entities	18	43,228	43,228	-	-
Other domestic liabilities	19	2,419	2,419	-	-
		1,201,808	878,393	226,351	97,318

31 December 2009

<i>Non-derivative liabilities</i>					
Due to domestic banks	15	233,246	233,246	-	-
Due to IMF related accounts	16	124,786	124,786	-	-
Due to governmental institutions	17	665,187	540,084	50,024	75,079
Due to public and commercial entities	18	130,847	130,847	-	-
Other domestic liabilities	19	2,019	2,019	-	-
		1,156,085	1,030,982	50,024	75,079

Central Bank of the Republic of Kosovo

Notes to the financial Statement

(in thousands of EUR, unless otherwise stated)

4. Financial risk management (continued)

c) Liquidity risk (continued)

The previous table shows the undiscounted cash flows of CBK's financial liabilities on the basis of their earliest possible contractual maturity. To manage the liquidity risk arising from financial liabilities, CBK holds liquid assets comprising cash and cash equivalents, current accounts, deposit accounts and treasury bills for which there is an active and liquid market.

Volatility in the global and Kosovo financial markets

The global financial and economic crisis has resulted in, among other things, a lower level of capital market funding, and lower liquidity levels across the banking sector, central bank interest rate cuts to help borrowers, government capital injection, higher interbank saving rates and volatility in stock markets. Further adverse developments resulting from the crisis might result in negative implications on the financial and liquidity position of CBK.

d) Market risks

Market risk is the risk that changes in market prices, such as interest rate, equity prices, foreign exchange rates and credit spreads (not relating to changes in the obligor's / issuer's credit standing) will affect CBK's income or the value of its holdings of financial instruments. The objective of market risk management is to manage and control market risk exposures within acceptable parameters, while optimizing the return on risk.

Management of market risks

CBK's operations are subject to the risk of interest rate fluctuations to the extent that interest-earning assets and interest-bearing liabilities mature or reprice at different times or in differing amounts. In the case of floating rate assets and liabilities, there is exposure to basis risk, which is the difference in repricing characteristics of the various floating rate indices.

Risk management activities are aimed at optimising net interest income, given market interest rate levels consistent with CBK's operations strategies. CBK's exposure to market risk is related only to non-trading portfolios.

Exposure to interest rate risk non-trading portfolios

One of the principal risks to which non-trading portfolios are exposed is a change in market interest rates causing a reduction in future cash flows for variable-rate financial assets or a decline in the fair values of fixed-rate financial assets. Interest rate risk is managed principally through monitoring interest rate gaps and by having pre-approved limits for repricing bands. The Investment Committee is the monitoring body for compliance with these limits. A summary of CBK's interest rate gap position on non-trading portfolios is as follows:

Central Bank of the Republic of Kosovo

Notes to the financial Statement

(in thousands of EUR, unless otherwise stated)

4. Financial risk management (continued)

(d) Market risks (continued)

Exposure to interest rate risk-non-trading portfolios

	Note	Carrying amount	Less than 3 months	3-6 months	6-12 months	1-5 years
31 December 2010						
Current accounts with non-resident banks	8	25,621	25,621	-	-	-
Treasury bills	9	199,275	69,902	94,665	34,708	-
Deposit accounts with non-resident banks	10	807,332	567,765	103,143	136,424	-
Assets with IMF	11	154,554	132,461	-	-	22,093
Total		1,186,782	795,749	197,808	171,132	22,093
Due to domestic banks	15	(203,572)	(203,572)	-	-	-
Due to IMF related accounts	16	(153,868)	(131,775)	-	-	(22,093)
Due to governmental institutions	17	(798,721)	(527,101)	(100,222)	(171,398)	-
Due to public and commercial entities	18	(43,228)	(43,228)	-	-	-
Due to domestic liability	19	(2,419)	(2,419)	-	-	-
Total		(1,201,808)	(908,095)	(100,222)	(171,398)	(22,093)
Gap		(15,026)	(112,346)	97,586	(266)	-
31 December 2009						
Current accounts with non-resident banks	8	34,899	34,899	-	-	-
Treasury bills	9	529,652	149,940	379,712	-	-
Deposit accounts with non-resident banks	10	487,529	412,270	50,208	25,051	-
Assets with IMF	11	124,482	124,482	-	-	-
Total		1,176,562	721,591	429,920	25,051	-
Due to domestic banks	15	(233,246)	(233,246)	-	-	-
	16	(124,786)	(124,786)	-	-	-
Due to governmental institutions	17	(665,187)	(590,108)	(50,028)	(25,051)	-
Due to public and commercial entities	18	(130,847)	(130,847)	-	-	-
Due to domestic liability	19	2,019	2,019	-	-	-
Total		(1,156,085)	(1,081,006)	(50,028)	(25,051)	-
Gap		20,477	(359,415)	379,892	-	-

Central Bank of the Republic of Kosovo

Notes to the financial Statement

(in thousands of EUR, unless otherwise stated)

Non-interest bearing financial assets and liabilities have not been included in the table above.

4. Financial risk management (continued)

(d) Market risks (continued)

Overall non-trading interest rate risk positions are managed by the Asset Management Directorate, which uses investment securities and placements with banks to manage the overall position arising from CBK's non-trading activities.

Management of interest rate risk against interest rate gap limits is supplemented by monitoring the sensitivity of the Bank's financial assets and liabilities to various standard and non-standard interest rate scenarios. Standard scenarios that are considered on a regular basis include a 100 basis point ("bp") parallel fall or rise in all yield curves. An analysis of the Bank's sensitivity to an increase or decrease in market interest rates (assuming no asymmetrical movement in yield curves and a constant financial position) is as follows:

2010

	100 bp Increase	100 bp Decrease
Estimated Profit (loss) effect	141	(141)

2009

	100 bp Increase	100 bp Decrease
Estimated Profit (loss) effect	124	(124)

Exposure to other market risks/currency risks non-trading portfolios

CBK has an exposure to SDR related to its IMF assets and liabilities, which they monitor on an ongoing basis. CBK's exposure to foreign currency risk is as follows:

2010

	100 bp Increase	100 bp Decrease
Estimated Profit (loss) effect	7	(7)

2009

	100 bp Increase	100 bp Decrease
Estimated Profit (loss) effect	3	(3)

Central Bank of the Republic of Kosovo

Notes to the financial Statement

(in thousands of EUR, unless otherwise stated)

4. Financial risk management (continued)

(d) Market risks (continued)

31 December 2010	EUR	SDR	Total
Assets			
Cash on hand	60,194	-	60,194
Current accounts with non-resident banks	25,621	-	25,621
Treasury bills	199,275	-	199,275
Deposit accounts with non-resident banks	807,332	-	807,332
Assets with IMF	-	154,554	154,554
Other assets	429	-	429
Total	1,092,851	154,554	1,247,405
Liabilities			
Due to domestic banks	203,5724	-	203,574
Due to IMF related accounts	72,9823	80,886	153,869
Due to governmental institutions	798,7212	-	798,722
Due to public and commercial entities	43,228	-	43,228
Other domestic liabilities	2,419	-	2419
Total	1,121,173	80,886	1,202,062
Net foreign currency position	(28,322)	73,668	45,345

31 December 2009	EUR	SDR	Total
Assets			
Cash on hand	21,806	-	21,806
Current accounts with non-resident banks	34,899	-	34,899
Treasury bills	529,652	-	529,652
Deposit accounts with non-resident banks	487,529	-	487,529
Assets with IMF	-	124,482	124,482
Other assets	351	-	351
Total	1,074,237	124,482	1,198,719
Liabilities			
Due to domestic banks	233,246	-	233,246
Due to IMF related accounts	49,099	75,687	124,786
Due to governmental institutions	665,187	-	665,187
Due to public and commercial entities	130,847	-	130,847
Other domestic liabilities	2,019	-	2,019
Total	1,080,398	75,687	1,156,085
Net foreign currency position	(6,161)	48,795	42,634

Central Bank of the Republic of Kosovo

Notes to the financial Statement

(in thousands of EUR, unless otherwise stated)

4. Financial risk management (continued)

(d) Market risks (continued)

CBK deals predominantly in EUR, while the foreign currencies CBK deals with are predominantly Special Drawing Rights (“SDRs”). The exchange rates used for translation at 31 December 2010 and 2009 were as follows:

	2010	2009
	EUR	EUR
1 SDR	1.159	1.088

SDRs are supplementary foreign exchange reserve assets defined and maintained by the international Monetary Fund (IMF). Although SDRs are not a currency itself, they represent a potential claim on the currencies of IMF member states for which they may be exchanged. SDRs were created in 1969 to alleviate a shortage of preferred foreign exchange reserve assets, namely the US dollar and gold, the value of the SDR is defined by a weighted currency basket of four major currencies, the Euro, the US dollar, the British pound, and the Japanese yen.

(e) Operational risks

Operational risk is the risk of direct or indirect loss arising from a wide variety of causes associated with CBK’s processes, personnel, technology and infrastructure, and from external factors other than credit, market and liquidity risks such as those arising from legal and regulatory requirements and generally accepted standards of corporate behaviour. Operational risks arise from all of CBK’s operations and are faced by all of the organization’s units.

CBK’s objective is to manage operational risk so as to balance the avoidance of financial losses and damage to CBK’s reputation with overall cost effectiveness.

The primary responsibility for the development and implementation of controls to address operational risk is assigned to managerial staff within each organizational unit. This responsibility is supported by the development of overall CBK standards for the management of operational risk in the following areas:

- requirements for appropriate segregation of duties, including the independent authorisation of transactions;
- requirements for the reconciliation and monitoring of transactions;
- compliance with regulatory and other legal requirements;
- documentation of controls and procedures;
- requirements for the periodic assessment of operational risks faced and the adequacy of controls and procedures to address the risks identified;
- requirements for the reporting of operational losses and proposed remedial actions;
- development of contingency plans;
- training and professional development;
- ethical and conduct standards; and
- risk mitigation, including insurance, where this is effective.

Compliance with CBK standards is supported by a programme of periodic reviews undertaken by Internal Audit. The results of Internal Audit reviews are discussed with management of the organizational unit to which they relate, with summaries submitted to the Audit Committee and CBK management.

Central Bank of the Republic of Kosovo

Notes to the financial Statement

(in thousands of EUR, unless otherwise stated)

4. Financial risk management (continued)

(f) Capital management

Law no. 03/L-209 on the Central Bank of the Republic of Kosovo, approved on 22 July 2010 by the Assembly of the Republic of Kosovo, sets the capital requirements of CBK. According to this law, the authorized capital of CBK is EUR 30 million. The capital may be increased by such amounts as may be proposed by CBK and approved by the Government. No reduction of CBK capital shall be permitted at any time.

As per Law no. 03/L-209, the net income or the net loss of CBK is calculated in accordance with International Financial Reporting Standards (IFRS).

Net income is allocated in each year to a general reserve account until the aggregate amount of initial capital and general reserves equals five percent (5%) of the Central Bank's monetary liabilities.

50% of the net balance of realized income remaining after fulfilling the 5% criteria mentioned above is required to be transferred to the Ministry of Economy and Finance. The remaining 50% of the realized income is required to be allocated to the general reserve account of CBK.

5. Use of estimates and judgments

Management discusses with the Central Bank Board the development, selection and disclosure of CBK's critical accounting policies and estimates, and the application of these policies and estimates. Estimates and judgments are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

These disclosures supplement the commentary on financial risk management (see note 4).

Key sources of estimation uncertainty

Allowances for credit losses

Assets accounted for at amortised cost are evaluated for impairment on a basis described in accounting policy 3(f)(vi). The specific counterparty component of the total allowances for impairment applies to financial assets evaluated individually for impairment and is based upon management's best estimate of the present value of the cash flows that are expected to be received. In estimating these cash flows, management makes judgements about the counterparty's financial situation and the net realizable value of any underlying collateral. Each impaired asset is assessed on its merits, and an estimate of cash flows considered recoverable is independently approved.

Critical accounting judgments in applying CBK's accounting policies

Critical accounting judgments made in applying CBK's accounting policies include:

Financial asset and liability classification

CBK's accounting policies provide scope for assets and liabilities to be designated on inception into different accounting categories in certain circumstances.

In classifying financial assets as held-to-maturity, CBK has determined that it has both the positive intention and ability to hold the assets until their maturity date as required by accounting policy 3(h).

Central Bank of the Republic of Kosovo

Notes to the financial Statement

(in thousands of EUR, unless otherwise stated)

6. Financial assets and liabilities (Accounting classifications and fair values)

The table below sets out CBK's classification of each class of financial assets and liabilities, and their fair values.

<i>In thousands of EUR</i>	Note	Loans and receivables	Held-to-maturity	Other amortized cost	Total carrying amount	Fair value
31 December 2010						
Cash on hand	7	60,194	-	-	60,194	60,194
Current accounts with non-resident banks	8	25,621	-	-	25,621	25,621
Treasury bills	9	-	199,275	-	199,276	198,490
Deposit accounts with non-resident banks	10	807,332	-	-	807,332	807,332
Assets with IMF	11	154,554	-	-	154,554	154,554
		1,047,701	199,275	-	1,246,976	1,246,191
Due to domestic banks	15	-	-	203,572	203,572	203,572
Due to IMF related accounts	16	-	-	153,868	153,868	153,869
Due to governmental institutions	17	-	-	798,721	798,721	798,721
Due to public and commercial entities	18	-	-	43,228	43,228	43,228
Other domestic liabilities	19	-	-	2,419	2,419	2,419
		-	-	1,201,808	1,201,808	1,201,808
31 December 2009						
Cash on hand	7	21,806	-	-	21,806	21,806
Current accounts with non-resident banks	8	34,899	-	-	34,899	34,899
Treasury bills	9	-	529,652	-	529,652	529,275
Deposit accounts with non-resident banks	10	487,529	-	-	487,529	487,529
Assets with IMF	11	124,482	-	-	124,482	124,482
		668,716	529,652	-	1,198,368	1,197,991
Due to domestic banks	15	-	-	233,246	233,246	233,246
Due to IMF related accounts	16	-	-	124,786	124,786	124,786
Due to governmental institutions	17	-	-	665,187	665,187	665,187
Due to public and commercial entities	18	-	-	130,847	130,847	130,847
Other domestic liabilities	19	-	-	1,745	1,745	1,745
		-	-	1,155,811	1,155,811	1,155,811

Central Bank of the Republic of Kosovo

Notes to the financial Statement

(in thousands of EUR, unless otherwise stated)

7. Cash on hand

Cash on hand is all denominated in EUR.

8. Current accounts with non-resident banks

These accounts were held at the following banks:

	2010	2009
Deutsche Bundesbank	25,068	34,369
Raiffeisen Zentralbank	234	145
Commerzbank	315	381
Banque De France	4	4
Total	25,621	34,899

All current accounts have credit ratings of A-1/P-1 as per 2010 rankings of the above banks by Standard & Poor's/Moody's ratings at 31 December 2010.

9. Treasury bills

Treasury bills are debt securities issued by governments of European Union countries. They have maturities up to twelve months and they held until maturity. All bills are denominated in EUR and have effective interest rates ranging from 0.141% to 1.346% (2009: 0.199% to 1.490%)

Treasury bills are issued by governments of European Union countries as follows:

	2010	2009
Germany	-	99,924
France	-	164,952
The Netherlands	-	99,929
Italy	84,613	-
Portugal	34,787	-
Belgium	79,875	164,847
Total	199,275	529,652

CBK invests in treasury bills with a minimum credit rating of A-2 and P-2, as per Standard & Poor's/Moody's ratings.

Central Bank of the Republic of Kosovo

Notes to the financial Statement

(in thousands of EUR, unless otherwise stated)

9. Treasury bills (continued)

Treasury bills at 31 December 2010 include an amount of EUR 84,747 thousand (2009: EUR nil) that represents treasury bills purchased by the CBK for the Ministry of Finance and Economy (the "Ministry"). Based on a Memorandum of Understanding (MoU) signed with the Ministry, CBK acts as an Investment Manager of the funds of the Ministry. In January 2010 the parties made changes to the MoU, article III - *Allocation of Risk*. Based on this, the related credit risk is borne by the CBK and these investments are recorded in the CBK accounts. Based on the MoU, CBK also assumes responsibility for the proper operation of the Assets Management Directorate, a CBK division, and for the timely purchase, settlement, payment and accounting of all invested amounts of the Kosovo Consolidated Budget.

10. Deposit accounts with non-resident banks

Deposit accounts with non-resident banks are composed of:

	2010	2009
Time deposits		
Raiffeisen Zentralbank	94,600	56,500
ING Bank	150,088	-
KBC	20,003	48,835
Rabobank	136,064	10,003
Danske Bank	97,392	87,097
Commerzbank	53,800	4,100
Banque de France	144,387	150,824
Banque Centrale du Luxembourg	110,379	130,057
	806,713	487,416
Interest accrued on time deposits		
Raiffeisen Zentralbank	35	-
ING Bank	132	-
KBC	1	52
Rabobank	358	-
Danske Bank	2	2
Commerzbank	58	-
Banque de France	14	31
Banque Centrale du Luxembourg	19	28
	619	113
Total	807,332	487,529

Central Bank of the Republic of Kosovo

Notes to the Financial Statements

(in thousands of EUR, unless otherwise stated)

10. Deposit accounts with non-resident banks (continued)

Deposits placed with non-resident banks are denominated in EUR and earn interest at effective interest rates ranging from 0.10% to 1.20% (2009: 0.05% to 2.05%) and have original maturities from 1 to 366 days (2009: from 1 to 186 days). All deposits have credit rating A-1/P-2, as per 2010 ranking by Standard & Poors/Moody's ratings.

11. IMF related assets

	2010	2009
IMF quota	68,420	64,205
SDR Holdings	63,993	60,253
Accrued interest	48	24
IMF	132,461	124,482
Government		
Due from the Government for the use of IMF funds (SBA)	22,093	-
Total	154,554	124,482

The assets listed above are related to the admission of Kosovo to the IMF in June 2009. CBK acts as depository and fiscal agent in relation to Kosovo's membership in the IMF. This is in accordance with the Law No. 03/L-209 on the Central Bank of the Republic of Kosovo and Law No. 03-L-152 on Membership of the Republic of Kosovo in the International Monetary Fund and World Bank Group Organizations.

IMF Quota represents a subscription amount determined at the time of admission of Kosovo into IMF and is expressed in SDR and its amount is determined based on IMF rules and regulations.

SDR Holdings represents assets approved by the IMF Board of Governors as per allocations of SDRs to IMF's member countries (decisions made on 28 August 2009 and 9 September 2009). SDR holding assets bear annual interest rates in 2010 ranging from 0.25% to 0.36% (2009: 0.22% - 0.31%).

Due from the Government for the use of IMF funds, represents an amount due from the Government as per IMF and Kosovo Stand-by Arrangement signed in July 2010 through which the Government of Kosovo obtained from IMF a Stand-By Arrangement in the amount of SDR 92.6 million (EUR: 107.4 million). The interest rate of this arrangement is tied to IMF's market-related interest rate, known as the basic rate of charge, which is itself linked to the SDRs interest rate. The interest rate for the period from August 2010 until 31 December 2010 fluctuated from 1.33% to 1.36%.

Balance drawn as at 31 December 2010, SDR18.8 million (EUR 22.1 million) by the Government of Kosovo from the Stand-by Arrangement. CBK acts as depository institution for the Government of Kosovo. To regulate the Stand-By Arrangement with IMF, CBK and the Government of Kosovo entered into an agreement on July 2010 "on the Procedure for Request, Acceptance, Service and Repurchase of the Funds from the IMF in terms of the Stand -By Arrangement". Based on this arrangement CBK withdraws the SDRs from IMF, on behalf of the Government, and credit's them to the Government's account.

Central Bank of the Republic of Kosovo

Notes to the financial Statement

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12. Property and equipment

Property and equipment is composed as follows:

	Leasehold improvements	Equipment	Computers	Vehicles	Assets in the course of construction	Total
Cost						
At 1 January 2009	1,279	1,459	613	107	-	3,458
Acquisitions	-	84	166	222	-	472
Disposals	-	-	-	(43)	-	(43)
At 31 December 2009	1,279	1,543	779	286	-	3,887
At 1 January 2010	1,279	1,543	779	286	-	3,887
Acquisitions	-	23	67	-	9	99
At 31 December 2010	1,279	1,566	846	286	9	3,986
Depreciation						
At 1 January 2009	128	775	396	72	-	1,371
Charge for the period	64	217	127	36	-	444
Disposals	-	-	-	(43)	-	(43)
At 31 December 2009	192	992	523	65	-	1,772
At 1 January 2010	192	992	523	65	-	1,772
Charge for the period	64	215	143	56	-	478
At 31 December 2010	256	1,207	666	121	-	2,250
Carrying amounts						
At 1 January 2009	1,151	684	217	35	-	2,087
At 31 December 2009	1,087	551	256	221	-	2,115
At 31 December 2010	1,023	359	180	165	9	1,736

There are no assets pledged as collateral as at 31 December 2010 (2009: nil).

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13. Intangible assets

Intangible assets are composed as follows:

	Software under development	Software	Total
Cost			
Balance at 1 January 2009	25	1,036	1,061
Acquisitions	41	108	149
Balance at 31 December 2009	66	1,144	1,210
Balance at 1 January 2010	66	1,144	1,210
Acquisitions	760	50	810
Balance at 31 December 2010	826	1,194	2,020
Amortization			
Balance at 1 January 2009	-	975	975
Amortization for the year	-	61	61
Balance at 31 December 2009	-	1,036	1,036
Balance at 1 January 2010	-	1,036	1,036
Amortization for the year	-	86	86
Balance at 31 December 2010	-	1,122	1,122
Carrying amounts			
Balance at 1 January 2009	25	61	86
Balance at 31 December 2009	66	108	174
Balance at 31 December 2010	826	72	898

14. Other assets

Other assets are composed as follows:

	2010	2009
Accrued fee income	324	333
Accounts receivable and prepayments	105	18
Total	429	351

Accrued fee income represents the estimated license renewal fees and other fees for the fourth quarter for local financial institutions.

Central Bank of the Republic of Kosovo

Notes to the financial Statement

(in thousands of EUR, unless otherwise stated)

15. Due to domestic banks

Under CBK supervision Banking Rule XVII, commercial banks operating in Kosovo are required to maintain a liquidity reserve amounting to 10% of their qualifying customer deposits. At least half of these reserve balances must be kept in accounts at CBK.

CBK pays interest to commercial banks on the balances held by them at CBK representing up to 10% of the minimum required capital. No interest is paid by CBK to commercial banks on amounts maintained at CBK above the 10% of the minimum required capital. The annual interest rate for the year ended 31 December 2010 was 0.10% (31 December 2009: 0.10%).

15. Due to domestic banks (continued)

	2010	2009
ProCredit Bank Kosovo	28,790	27,069
Raiffeisen Bank Kosovo	25,970	26,503
NLB Prishtina	11,106	9,349
Komercijalna Banka - Mitrovica Branch	1,467	1,198
Banka Ekonomike e Prishtinës	4,029	2,957
Banka për Biznes	3,032	2,789
Banka Kombëtare Tregtare - Prishtina Branch	1,594	1,677
Turk Ekonomi Bankasi Sh.A	5,822	4,613
Total liquidity required reserves	81,810	76,154
Additional balances on current accounts		
ProCredit Bank Kosovo	36,163	69,846
Raiffeisen Bank Kosovo	25,524	29,070
NLB Prishtina	14,945	11,187
Banka Ekonomike e Prishtinës	5,526	11,052
Banka për Biznes	15,033	19,657
Banka Kreditore e Prishtinës in Receivership	7	59
Banka Kombëtare Tregtare - Prishtina Branch	7,774	4,195
Komercijalna Banka - Mitrovica Branch	1,508	1,328
Turk Ekonomi Bankasi Sh.A	15,282	10,698
Total additional balances on current accounts	121,762	157,092
Total on current accounts	203,572	233,246

Central Bank of the Republic of Kosovo

Notes to the Financial Statements

(in thousands of EUR, unless otherwise stated)

16. Due to IMF Related liabilities

	2010	2009
IMF Account No. 1	167	-
IMF Account No. 2	6	-
IMF Security Account	72,808	49,099
IMF - Paid portion of Government quota	16,630	15,409
IMF SDR Allocation	64,209	60,253
Accrued Interest	48	25
Total due to IMF	137,238	109,377
Due to Government		
IMF - Paid portion of Government quota	16,630	15,409
Total Due to Government	16,630	15,409
Total	153,868	124,786

16. Due to IMF Related liabilities (continued)

These positions are related to the admission of Kosovo to the IMF in June 2009.

Accounts No.1 and No.2 are IMF accounts with CBK opened as per IMF's request based on IMF's rules and regulations.

IMF Security Account represents a promissory note to be paid by the Kosovo Government upon IMF's request. This amount represents a liability of CBK to IMF and is matched by a corresponding claim of CBK to the Government of Kosovo.

IMF paid portion of Government quota represents the amount paid by the Government to the IMF regarding the IMF quota.

SDR Allocation represents allocations of SDRs to IMF's member countries as approved by IMF Board of Governors on 28 August 2009 and 9 September 2009.

SDR Allocations are interest-bearing with annual interest rates for 2010 ranging from 0.25% - 0.36% (2009: 0.22% - 0.31%).

Central Bank of the Republic of Kosovo

Notes to the financial Statement

(in thousands of EUR, unless otherwise stated)

17. Due to governmental institutions

Due to governmental institutions includes current accounts from the following:

Current accounts

	2010	2009
Treasury - Ministry of Finance	49,572	88,245
Privatization Agency of Kosovo	65,089	451,041
Interim administration institutions	1,678	797
Total current accounts	116,339	540,083

Time Deposits

Treasury - Ministry of Finance	140,010	125,104
Privatization Agency of Kosovo	457,680	-
Total time deposits	597,690	125,104

Securities

Treasury - Ministry of Finance	84,692	-
Total Securities	84,692	-
Total	798,721	665,187

The effective annual interest rate for current accounts for the year ended 31 December 2010 is 0.10% (for the year ended 31 December 2009: 0.10%). For time deposits the effective interest rates for the year 2010 ranged from 0.17% - 1.09% (2009: 0.20% - 1.30%).

Central Bank of the Republic of Kosovo

Notes to the Financial Statements

(in thousands of EUR, unless otherwise stated)

18. Due to public and commercial entities

	2010	2009
Current accounts		
Insurance companies	5,027	7,664
Other public institutions	38,131	123,114
Pension funds	68	67
Other	2	2
	43,228	130,847

The effective interest rate for current accounts as at 31 December 2010 is 0.10% (31 December 2009: 0.10%).

19. Other domestic liabilities

	2010	2009
Safe custody accounts	2,419	1,745
Deferred grants income	5	9
Sundry creditors	17	6
Other deferred income and liabilities	228	259
	2,670	2,019

The Safe custody balance represents these types of account and amounts.

Amounts EUR 1,130 collected by the CBK until 5 January 2004 on behalf of the Kosovo Government for the offices of the former national bank of Kosovo, which were rented out to various entities/individuals. This amount also included interest earned on these rent payments until 31 December 2010.

Included in the safe custody accounts are also certain amount of cash, in various currencies, that CBK inherited upon inception, from the former National Bank of Kosovo and the interest earned over the years.

In the safe custody accounts are also included EUR 763 thousand related to the current accounts of the Kosova Insurance Company which was liquidated on April 2010.

Central Bank of the Republic of Kosovo

Notes to the financial Statement

(in thousands of EUR, unless otherwise stated)

19. Other domestic liabilities (continued)

The movement in deferred grant revenue was as follows:

	Ministry of Finance (ICU Portfolio)	World Bank	ECB	Total
Deferred grant revenue at 1 January 2009	-	-	-	-
Grants received during the year	33	-	-	33
Grant revenue for the year	(24)	-	-	(24)
Grant reconciliation from previous years	-	-	-	-
Deferred grant revenue at 31 December 2009	9	-	-	9
Deferred grant revenue at 1 January 2010	9	-	-	9
Grants received during the year	12	10	31	53
Grant revenue for the year	(16)	(10)	(31)	(57)
Grant reconciliation from previous years	-	-	-	-
Deferred grant revenue at 31 December 2010	5	-	-	5

20. Statutory fund

The CBK statutory fund as at 31 December 2010 is EUR 30,000 thousand as per Law no. 03/L-209 approved on 22 July 2010. The CBK statutory fund as at 31 December 2009 was EUR 30,000 as per the replaced CBK Law no. 03/L-074.

CBK reports directly to the Assembly of Kosovo. CBK capital is not subject to encumbrances.

21. Reserve fund

The level of the reserve fund is regulated by Law no. 03/L-209 on the Central Bank of the Republic of Kosovo. The profit of each financial year is allocated as described in note 4 (f) in accordance with this law.

Central Bank of the Republic of Kosovo

Notes to the Financial Statements

(in thousands of EUR, unless otherwise stated)

22. Net interest income

Net interest income is composed as follows:

	2010	2009
Interest income		
From deposit accounts	2,813	2,414
From treasury bills	1,496	4,010
From current accounts	265	205
	4,574	6,629
Interest expense		
On current accounts from non-banking entities	659	1,780
On current accounts from bank entities	163	360
On time deposits	2,030	360
	2,852	2,500
Net interest income	1,722	4,129

23. Net fees and commission income

Net fee and commission income is composed as follows:

	2010	2009
Fee income		
From cash deposits	344	220
From foreign incoming transfers	61	75
From foreign outgoing transfers	247	344
From the inter-bank clearing system	260	196
From the credit registry system	131	93
From management of treasury fund	1,500	1,500
Other fees	32	34
	2,575	2,462
Fee expenses		
For cash transportation	212	203
For correspondent bank transactions	36	66
	248	269
Net fee and commission income	2,327	2,193

Income from management of treasury fund is earned from deposits that CBK holds for the Ministry of Finance, which are invested in accordance with prior approval of the Ministry of Finance. The assets and liabilities are matched and all income on the assets is paid over to the Ministry of Finance. Income from management of treasury fund consists of a fee that CBK receives for this service. CBK retains credit risk on the assets in this portfolio. Accordingly, CBK records the assets and the matching liabilities in its statement of financial position.

Central Bank of the Republic of Kosovo

Notes to the Financial Statements

(in thousands of EUR, unless otherwise stated)

24. Grant revenue

Grant revenue is composed as follows:

	2010	2009
European Central Bank ("ECB")	31	-
World Bank	10	-
Ministry of Economy and Finance	16	24
Total	57	24

25. Other operating income

Other operating income mainly comprises of fees charged to financial institutions in Kosovo as part of issuing or renewing licenses, as well as other statutory fees related to their activities. Other operating income consists of the following:

	2010	2009
Fees charged to insurance companies	922	775
Fees charged to commercial banks	546	514
Fees from non-banking financial institutions	51	40
Other fees	3	11
Total	1,522	1,340

26. Personnel expenses

Personnel expenses are composed as follows:

	2010	2009
Wages and salaries	1,578	1,495
Health insurance costs	151	135
Pension contributions	258	245
Staff training	214	147
Central Bank Board expenses	155	108
Other	39	30
Total	2,395	2,160

The average number of employees at CBK in 2010 was 164 (2009: 161).

Central Bank of the Republic of Kosovo

Notes to the Financial Statements

(in thousands of EUR, unless otherwise stated)

27. General and administrative expenses

General and administrative expenses are composed as follows:

	2010	2009
Insurance expenses	258	240
Repairs and maintenance	39	48
Software maintenance	140	111
Communication expense (telephone, telex and internet)	105	85
Utilities	81	80
Audit and consulting expense	25	24
Security and guard services	54	44
Travel and transportation	82	95
Vehicle operating expenses	31	28
Stores and stationery	28	28
Representation expenses	16	16
Computer and other consumables expense	38	41
Publication and literature expenses	52	38
Official representation expenses	39	93
Other	32	27
Total	1,020	998

28. Foreign exchange net income gain/(loss)

Foreign exchange net income gain/(loss) EUR 1,408 thousand for the year ended 31 December 2010 (2009: loss of 303 thousand) represents unrealized foreign exchange gains and losses in relation to foreign exchange differences resulting upon translation of SDR assets and liabilities on the CBK books.

29. Cash and cash equivalents

Cash and cash equivalents are composed as follows:

	Note	2010	2009
Cash on hand	7	60,194	21,806
Current accounts with non-resident banks	8	25,621	34,899
Treasury bills with maturity up to three months		69,863	149,893
Deposit accounts with non-resident banks with maturity up to three months		567,627	412,237
Total		723,305	618,835

Cash and cash equivalents are held for the purpose of meeting short-term cash commitments rather than for investment or other purposes. An investment qualifies as a cash equivalent when it has a short maturity, three months or less from the date of acquisition.

Central Bank of the Republic of Kosovo

Notes to the Financial Statements

(in thousands of EUR, unless otherwise stated)

30. Commitments and contingencies *Legal*

CBK is involved in routine legal proceedings in the ordinary course of business. It is management's opinion that the final outcome of these lawsuits will not have a material effect on CBK's financial statements as at and for the year ended 31 December 2010.

Other commitments

Other commitments are composed as follows:

	31 December 2010	31 December 2009
Purchase of computer applications	-	10
Upgrade of the core accounting system	45	765
Total	45	775

In 2009, Kosovo became member of the World Bank Group organizations - International Bank for Reconstruction and Development (IBRD), the International Development Association (IDA) and the Multilateral Investment Guarantee Agency (MIGA). In relation to this membership, CBK acts as depository. This is in accordance with the Law No. 03/L-209 on the Central Bank of the Republic of Kosovo and Law No. 03-L-152 on Membership of the Republic of Kosovo in the International Monetary Fund and World Bank Group Organizations.

In June 2009, the Government of Kosovo issued promissory notes to make payments concerning membership subscription to the above mentioned organizations upon their requests and payment instructions. The total balance at 31 December 2010 of these promissory notes was EUR 4,007 thousand.

Central Bank of the Republic of Kosovo

Notes to the Financial Statements

(in thousands of EUR, unless otherwise stated)

31. Related party transactions

Related parties include Key Management and the Central Bank Board. Their compensations are presented below:

	2010	2009
Compensation to Central Bank Board members	121	98
Compensation to Key Management Personnel	114	133
Total	235	231

32. Subsequent events

There are no events after the reporting date that would require either adjustments or additional disclosures in the financial statements.

9. Statistical Appendix

1.1. Financial corporation survey – net foreign assets and domestic claims

(Outstanding amounts, end of period, in millions of euro)

Description	Net foreign assets							Domestic claims									
	Claims on non residents						Less: liabilities to non residents	Net claims on central government			Claims on other sectors			of which:			
	Monetary gold and SDR holdings	Deposits	Securities other than shares	IMF Quota	Shares and other equities	Claims on central government		Less: Liabilities to central government	Deposits	Loans	Other non financial corporations	Households					
2004 December	722.8	772.0	---	384.0	236.7	---	83.3	49.2	202.5	-216.8	---	216.8	216.8	419.3	413.5	329.8	83.7
2005 December	827.3	890.9	---	422.6	242.4	---	145.3	63.6	348.9	-225.7	---	225.7	225.7	574.6	565.6	439.6	126.0
2006 December	1,173.6	1,245.7	---	660.0	341.3	---	170.8	72.1	231.7	-475.0	---	475.0	475.0	706.6	694.3	548.2	146.1
2007 December	1,622.4	1,704.6	---	955.0	408.9	---	175.4	82.3	124.5	-853.3	---	853.3	853.3	977.8	965.9	765.1	200.6
2008 December	1,593.1	1,726.7	---	795.1	661.6	---	128.2	133.6	419.6	-871.8	---	871.8	871.8	1,291.5	1,276.8	995.7	281.0
2009 December	1,700.5	2,036.2	60.3	910.1	724.5	64.3	144.3	335.7	573.7	-846.3	---	846.3	846.3	1,420.0	1,398.4	1,052.3	343.5
2010 December	1,995.2	2,387.7	64.0	1,257.8	525.2	68.5	269.3	392.5	765.9	-824.8	---	824.8	824.8	1,590.7	1,567.3	1,129.9	431.0

1.2. Financial corporation survey – liabilities

(Outstanding amounts, end of period, in millions of euro)

Description	Deposits					Loans				Insurance technical reserves			Shares and other equity	Other items (net)	
	Transferable deposits	of which:			Other deposits	of which:			Net equity of households in pension funds	Pre payment of premiums and reserves					
		Public non financial corporations	Other non financial corporations	Households		Public non financial corporations	Other non financial corporations	Households							
2004 December	670.7	273.7	34.6	81.3	145.5	396.9	149.3	24.4	222.5	2.3	106.5	88.7	17.9	145.1	0.7
2005 December	830.6	315.0	67.6	76.8	155.5	515.6	181.3	33.7	298.9	3.0	174.5	152.4	22.1	165.8	2.2
2006 December	886.4	300.5	34.8	96.4	156.2	586.0	193.3	27.6	359.5	3.4	251.4	223.9	27.5	209.3	54.7
2007 December	1,110.9	386.1	49.6	133.5	187.5	724.8	188.4	43.8	489.3	...	316.1	286.2	29.9	273.8	46.0
2008 December	1,351.9	390.9	15.4	176.0	186.2	961.0	250.1	51.4	656.7	...	288.6	256.3	32.3	311.1	61.1
2009 December	1,444.3	483.2	50.1	184.0	237.7	961.0	73.9	82.9	801.9	...	422.3	380.8	41.5	326.1	78.3
2010 December	1,744.2	621.2	83.8	218.6	303.5	1,123.1	42.8	83.4	995.9	...	540.5	493.7	46.8	361.7	114.8

2.1. Depository corporation survey – net foreign assets and domestic claims

(Outstanding amounts, end of period, in millions of euro)

Description	Net foreign assets							Domestic claims							
	Claims on non residents						Less: Liabilities to non residents	Net claims on central government			Claims on other sectors		of which:		
	Currency	Deposits	Securities other than shares	IMF Quota	Claims on central gov.	Less: Liabilities to central gov.		Loans	Other non financial corporations	Households					
2001 December	583.3	604.8	239.2	358.1	7.5	---	21.5	-44.2	-70.3	---	70.3	26.1	25.9	25.9	---
2002 December	649.5	674.1	53.1	621.0	...	---	24.6	-171.8	-258.6	---	258.6	86.8	86.5	80.8	5.7
2003 December	695.8	727.0	73.2	533.6	119.6	---	31.2	-112.6	-346.4	---	346.4	233.8	232.8	193.5	39.0
2004 December	648.7	687.9	55.3	384.0	236.7	---	39.2	156.9	-216.8	---	216.8	373.8	373.7	289.9	83.7
2005 December	695.1	744.5	74.6	422.6	242.4	---	49.3	289.0	-225.7	---	225.7	514.6	513.9	387.9	126.0
2006 December	975.4	1,035.6	63.4	660.0	303.1	---	60.2	162.2	-475.0	---	475.0	637.1	636.6	490.5	146.1
2007 December	1,377.5	1,426.1	145.3	955.0	308.2	---	48.6	39.1	-853.3	---	853.3	892.4	892.1	691.3	200.6
2008 December	1,436.1	1,512.0	121.1	794.9	581.8	---	75.9	311.9	-871.8	---	871.8	1,183.8	1,183.4	901.7	281.0
2009 December	1,531.6	1,782.2	111.4	910.0	626.4	64.3	250.5	442.9	-846.2	---	846.3	1,289.3	1,289.0	942.9	343.5
2010 December	1,653.1	1,957.2	164.3	1,257.8	372.7	68.5	304.0	632.8	-824.8	---	824.8	1,457.6	1,457.1	1,014.0	431.0

Table 2.2. Depository corporation survey - liabilities

(Outstanding amounts, end of period, in millions of euro)

Description	Deposits included in broad money										Deposits excluded from broad money 1/	Shares and other equity	Other items net	
	Transferable deposits	of which:					Other deposits	of which:						
		Other financial corporations	Public non financial corporations	Other non financial corporations	Households	Other financial corporations		Public non financial corporations	Other non financial corporations	Households				
2001 December	486.8	361.5	.	7.0	135.3	219.2	125.2	.	.	31.3	93.9	12.9	25.2	14.3
2002 December	413.6	285.3	.	3.5	160.1	121.7	128.3	.	.	23.9	104.4	25.1	43.8	-4.8
2003 December	499.3	278.7	.	5.3	139.0	134.4	220.6	.	.	87.1	133.5	29.2	61.1	-6.4
2004 December	719.5	303.5	29.8	34.6	81.3	145.5	416.0	19.1	149.3	24.4	222.5	—	87.1	-1.0
2005 December	865.4	345.6	30.5	67.6	76.8	155.5	519.9	24.3	181.3	33.1	279.6	19.9	94.4	4.3
2006 December	912.8	336.4	35.9	34.8	96.4	156.2	576.3	30.5	193.3	24.6	322.4	40.6	128.8	55.4
2007 December	1,126.6	413.7	27.7	49.6	133.5	187.5	712.8	40.3	188.4	41.8	439.0	53.7	186.5	49.8
2008 December	1,393.0	454.6	63.7	15.4	176.0	186.2	938.3	47.6	250.1	44.2	593.8	74.9	233.8	46.4
2009 December	1,548.5	621.4	138.2	50.1	184.0	237.7	927.0	60.7	73.9	71.7	718.5	98.1	249.0	79.0
2010 December	1,748.0	674.3	53.1	83.8	218.6	303.5	1,073.7	85.2	30.2	73.5	883.7	138.2	281.9	117.9

Table 3.1. CBK survey – net foreign assets and domestic demands

(Outstanding amounts, end of period, in millions of euro)

Description	Net foreign assets										Net claims on central government	Claims on other sectors	Liabilities to ODC
	Claims on non residents						Less: liabilities to non residents						
	Monetary gold and SDRs	Currency	Deposits	Securities other than shares	IMF Quota	IMF Account	SDR allocations	IMF Account					
2001 December	293.7	296.2	—	150.8	145.4	—	—	2.6	—	—	-70.3	0.2	173.9
2002 December	345.4	345.8	—	17.5	328.3	—	—	0.4	—	—	-258.6	0.3	46.2
2003 December	454.3	454.6	—	26.6	427.4	—	—	0.3	—	—	-346.4	1.0	59.6
2004 December	344.7	349.9	—	12.1	213.2	124.4	—	5.2	—	—	-216.8	0.1	72.9
2005 December	394.4	397.5	—	24.5	213.4	159.5	—	3.1	—	—	-225.7	0.8	82.5
2006 December	641.1	641.2	—	11.1	424.9	203.6	—	0.1	—	—	-472.9	0.5	94.5
2007 December	1,057.6	1,057.6	—	63.8	759.0	229.3	—	—	—	—	-849.4	0.3	113.6
2008 December	1,110.7	1,110.7	—	39.7	529.0	541.3	—	—	—	—	-870.5	0.3	137.2
2009 December	1,088.3	1,198.5	60.3	21.8	522.3	529.7	64.3	110.2	60.3	49.1	-681.5	0.2	233.2
2010 December	1,108.0	1,246.9	64.0	60.2	854.4	199.2	68.5	138.9	64.2	73.0	-813.1	0.5	203.6

Table 3.2. CBK survey - liabilities

(Outstanding amounts, end of period, in millions of euro)

Description	Deposits included in broad money							Deposits excluded from broad money			Shares and other equity	of which:		Other items (net)
	Transferable deposits	of which:			Other deposits		Other financial corporations	Local gov.	Funds contributed by owners	Profit/losses of the year				
		Other financial corporations	Local government	Public non financial	Other financial corporations									
2001 December	8.4	8.4	---	---	7.0	---	---	12.9	10.6	2.4	4.7	2.6	1.1	23.6
2002 December	3.9	3.9	---	---	3.5	---	---	25.1	24.6	0.5	10.6	2.6	3.6	1.3
2003 December	5.3	5.3	---	---	5.3	---	---	27.4	25.7	1.7	16.1	2.6	4.5	0.5
2004 December	37.7	32.6	20.7	1.9	9.9	5.1	5.1	---	---	---	18.0	10.0	3.0	-0.6
2005 December	66.6	62.5	23.3	1.6	37.6	4.1	4.1	---	---	---	20.4	10.0	3.0	...
2006 December	49.9	41.9	31.0	0.4	10.5	8.0	8.0	---	---	---	25.5	10.0	6.4	-1.2
2007 December	57.2	46.7	22.4	3.2	21.1	10.6	10.6	---	---	---	33.8	20.0	9.2	3.9
2008 December	63.9	56.7	49.9	5.3	1.5	7.2	7.2	---	---	---	41.4	30.0	7.5	-2.0
2009 December	130.8	130.8	129.7	...	1.1	...	...	---	---	---	44.8	30.0	3.6	-2.0
2010 December	45.6	45.6	43.9	...	...	...	...	---	---	---	47.9	30.0	3.0	-1.8

Table 4.1. Other depository corporation survey – net foreign assets and domestic claims

(Outstanding amounts, end of period, in millions of euro)

Description	Net foreign assets								Claims on CBK	Net claims on central government	Claims on other sectors				
	Claims on non residents	of which:			Less: liabilities to non-residents	of which:		Loans			Public nonfinancial corp.	Other nonfinancial corp.	Households		
		Currency	Deposits	Securities other than shares		Deposits	Loans								
2001 December	289.7	308.6	88.3	212.8	7.5	18.9	13.9	5.0	176.8	---	25.9	25.9	---	25.9	---
2002 December	304.1	328.3	35.6	292.7	...	24.2	17.5	6.7	45.7	---	86.5	86.5	---	80.8	5.7
2003 December	241.5	272.4	46.6	106.2	119.6	31.0	20.0	10.9	59.6	---	232.8	232.8	0.2	193.5	39.0
2004 December	304.0	338.0	43.2	170.8	112.3	34.0	12.7	21.3	73.2	---	373.7	373.7	---	289.9	83.7
2005 December	300.7	346.9	50.1	209.2	82.9	46.2	18.4	27.9	81.6	---	513.9	513.9	---	387.9	126.0
2006 December	334.4	394.5	52.3	235.1	99.4	60.1	21.4	38.7	88.8	-2.1	636.6	636.6	---	490.5	146.1
2007 December	319.9	368.5	81.5	196.0	78.9	48.6	17.9	30.7	107.5	-3.9	892.1	892.1	0.2	691.3	200.6
2008 December	325.4	401.3	81.4	265.9	40.5	75.9	42.0	33.7	136.8	-1.3	1,183.4	1,183.4	0.1	901.7	281.0
2009 December	443.6	583.9	89.6	387.7	97.0	140.3	65.5	74.5	233.1	-164.9	1,289.0	1,289.0	0.3	942.9	343.5
2010 December	545.1	710.3	104.1	403.3	173.4	165.2	85.5	79.4	203.4	-11.6	1,457.1	1,457.1	6.3	1,014.0	431.2

Table 4.2. Other depository corporation survey – liabilities

(Outstanding amounts, end of period, in millions of euro)

Description	Deposits included in broad money										Deposits excluded from broad money	of which:		Shares and other equity	Other items (net)	
	Transferable deposits	of which:				Other deposits	of which:					Other nonfinancial corporations	Households			
		Other financial corpor.	Public nonfinancial corp. 1/	Other nonfinancial corp.	Households 2/		Other financial corporations	Public nonfinancial corp. 1/	Other nonfinancial corp.	Households 2/						
2001 December	478.4	353.1	.	.	133.9	219.2	125.2	.	.	31.3	93.9	.	.	.	20.4	-6.4
2002 December	409.7	281.4	.	.	159.7	121.7	128.3	.	.	23.9	104.4	.	.	.	33.2	-6.6
2003 December	494.0	273.4	.	.	139.0	134.4	220.6	.	.	87.1	133.5	1.8	1.8	.	45.0	-7.0
2004 December	681.9	270.9	9.0	24.7	81.3	145.5	410.9	14.0	149.3	24.4	222.5	0.0	0.0	0.0	69.1	-0.1
2005 December	798.8	283.0	7.2	30.0	76.8	155.5	515.8	20.2	181.3	33.1	279.6	19.9	0.7	19.3	74.0	3.4
2006 December	862.9	294.5	4.9	24.3	96.4	156.2	568.4	22.5	193.3	24.6	322.4	40.6	3.0	37.1	103.3	50.9
2007 December	1069.3	367.1	5.3	28.5	133.5	187.5	702.3	29.8	188.4	41.8	439.0	53.7	2.0	50.3	152.7	39.8
2008 December	1329.0	397.9	13.8	13.8	176.0	186.2	931.1	40.4	250.1	44.2	593.8	74.9	7.3	63.0	192.3	48.1
2009 December	1417.8	490.6	8.5	48.9	184.0	237.7	927.2	60.8	73.9	71.7	718.5	97.9	11.2	83.5	204.2	81.0
2010 December	1702.3	628.7	9.2	83.8	218.6	303.5	1,073.7	85.2	30.2	73.5	883.7	138.2	9.9	112.2	234.0	119.5

Table 5.1. Other depository corporation – net foreign assets

(Outstanding amounts, end of period, in millions of euro)

Description	Net foreign assets						Claims on depository corporations						Claims on other sectors		
	Claims on non-residents	of which:			Less: liabilities to non-residents	Loans	CBK			Other depository corporations			Loans		
		Securities other than shares	Shares and other equity				Transferable depositst	Other deposits		Transferable depositst	Other deposits				
2004 December	74.1	84.2	—	83.3	10.1	10.1	48.9	25.8	20.7	5.1	23.0	9.0	14.0	45.6	39.9
2005 December	132.1	146.4	—	145.3	14.3	14.3	54.8	27.4	23.3	4.1	27.4	7.2	20.2	60.0	51.7
2006 December	198.1	210.0	38.3	170.8	11.9	11.9	66.9	39.0	31.0	8.0	28.0	4.9	23.0	69.5	57.7
2007 December	244.9	278.5	100.7	175.4	33.6	33.6	72.8	32.9	22.4	10.6	39.8	6.2	33.6	85.4	73.8
2008 December	157.0	214.7	79.8	128.2	57.7	57.7	113.0	57.1	49.9	7.2	55.9	7.9	48.0	108.3	94.0
2009 December	168.6	253.7	97.9	144.3	84.8	84.8	200.0	129.7	129.7	...	70.3	7.4	62.9	130.8	109.4
2010 December	342.1	430.5	152.5	269.3	88.5	88.5	144.8	43.9	43.9	...	100.9	9.0	91.9	138.7	115.9

Table 5.2. Other depository corporation – liabilities, excluding foreign and fiscal sector

(Outstanding amounts, end of period, in millions of euro)

Description	Loans	Insurance technical reserves				Shares and other equity					Other items			
		Net equity of households in ins.	Net equity for households in pension funds	Prepayment of premiums and reserves		Funds contributed by owners	Retained earnings	General and special reserves	Profit/Loss for the year	Other liabilities	Less: other assets	Plus: consolidation adjustment		
2004 December	2.3	106.5	...	88.7	17.9	58.0	42.6	8.6	5.0	1.7	1.7	9.3	7.6	...
2005 Dhjetor	3.0	174.5	...	152.4	22.1	71.4	47.7	12.9	6.7	4.0	-2.1	4.4	6.5	...
2006 December	3.4	251.4	...	223.9	27.5	80.5	55.2	15.8	7.9	1.6	-0.7	7.4	8.2	...
2007 December	...	316.1	...	286.2	29.9	87.4	62.1	20.1	1.7	3.5	-0.4	9.6	10.0	...
2008 December	1.0	288.6	...	256.3	32.3	77.4	54.0	12.7	7.4	3.4	11.3	24.2	12.9	...
2009 December	2.9	422.3	...	380.8	41.5	77.0	53.4	19.4	7.2	-3.1	-2.7	13.1	15.8	...
2010 December	2.9	540.4	...	493.7	46.8	79.8	56.7	14.0	7.2	2.0	2.3	22.8	20.4	...

Table 6.1. Euro deposits at other depository corporations – by initial maturity, main sectors

(Outstanding amounts, end of period, in millions of euro)

Description	Total deposits in euro													
	Government	Financial corporations					Non financial corporations		Other domestic sectors			Nonresidents		
		Other depository corporations	Other financial intermediaries	Insurance companies	Pension funds	Financial auxiliaries	Public nonfinancial corporations	Other nonfinancial corporations	Households	NPISH				
2001 December	492.3	...	...	...	...	...	165.2	...	165.2	313.1	313.1	...	13.9	
2002 December	427.2	...	...	...	...	...	183.6	...	183.6	226.1	226.1	...	17.5	
2003 December	515.8	1.8	1.8	...	...	...	226.1	...	226.1	267.9	267.9	...	20.0	
2004 December	674.9	1.3	25.6	3.7	3.5	15.5	2.9	275.3	173.5	10.18	360.3	350.7	9.6	12.3
2005 December	815.3	2.9	35.4	8.1	5.8	18.8	2.8	319.0	211.3	107.7	440.7	428.7	12.0	17.3
2006 December	890.4	7.0	28.1	0.1	2.4	24.7	0.4	337.8	217.4	120.5	499.2	486.1	13.1	18.2
2007 December	1,092.0	4.1	39.1	3.1	5.6	28.3	0.4	386.2	215.5	170.7	647.0	631.9	15.2	15.6
2008 December	1,366.9	1.4	62.9	5.0	6.5	31.5	19.4	479.7	263.8	215.9	785.0	774.5	10.5	37.9
2009 December	1,640.1	165.0	78.2	6.1	5.9	43.1	22.6	371.5	121.6	249.9	962.2	948.8	13.4	63.2
2010 December	1,830.9	12.0	104.7	7.0	7.9	47.6	41.6	415.0	122.3	292.6	1,220.1	1,206.1	14.0	79.2

Table 6.2. Non-euro deposits at other depository corporations – by initial maturity

(Outstanding amounts, end of period, in millions of euro)

Description	Non-euro deposits															
	Financial corporations	of which:					Nonfinancial corporations	Other domestic sectors					Non residents			
		CBK	Other depository corporations	Other financial intermediaries	Insurance companies	Public nonfinancial corporations		Other nonfinancial corporations	Households			NPISH				
									Transferable deposits	Saving account	Other deposits					
2004 December	23.4	1.1	...	...	...	1.1	4.4	0.5	4.0	17.5	17.3	8.7	...	8.7	0.1	0.3
2005 December	29.4	...	...	...	...	...	2.8	...	2.8	26.0	25.7	10.8	...	14.9	0.3	0.5
2006 December	34.3	...	...	...	...	...	3.7	0.3	3.5	29.8	29.6	12.4	...	17.2	0.2	0.5
2007 December	53.3	0.5	...	...	0.1	0.4	8.1	1.5	6.6	44.3	44.2	16.2	...	28.0	0.1	0.4
2008 December	81.9	0.9	...	...	...	0.9	11.6	0.1	11.5	68.4	68.2	22.9	...	45.2	0.3	1.0
2009 December	112.1	2.1	...	1.2	...	0.9	18.3	1.3	17.0	91.1	90.9	29.7	...	61.1	0.2	0.7
2010 December	113.8	3.1	...	2.9	...	...	13.7	4.3	9.4	93.8	93.3	33.1	25.9	34.3	0.5	3.1

Table 6.3. Other depository corporation loans – by initial maturity

(Outstanding amounts, end of period, in millions of euro)

Description	Total														
	Financial corporations	of which:			Nonfinancial corporations of which:	of which:			Other domestic corporations	of which:			Loans in Non Euro Currency		
		Other financial intermediaries	Insurance companies	Public nonfinancial corporations		Other nonfinancial corporations				Households					
						Up to 1 year	Over 1 year and up to 2 years	Over 2 years		Up to 1 year	Over 1 year and up to 2 years	Over 2 years			
2001 December	25.9	---	---	---	25.9	---	25.9	24.6	1.3	---	---	---	---	---	---
2002 December	86.5	---	---	---	80.8	---	80.8	67.3	13.5	---	5.7	5.7	1.4	4.3	---
2003 December	232.8	---	---	---	193.7	0.2	193.5	124.7	68.7	0.2	39.0	39.0	11.4	16.0	11.6
2004 December	373.7	---	---	---	289.9	---	289.9	111.5	111.3	67.2	83.7	83.7	15.9	15.2	52.6
2005 December	513.9	---	---	---	387.9	---	387.9	117.9	125.2	144.7	126.0	126.0	19.5	21.0	85.4
2006 December	636.6	---	---	---	490.5	---	490.5	128.7	127.7	234.1	146.1	146.1	19.7	24.7	101.7
2007 December	892.1	---	---	---	691.5	0.2	691.3	174.0	122.6	394.6	200.6	200.6	24.0	29.6	147.1
2008 December	1,183.4	0.6	---	0.6	901.8	0.1	901.7	191.0	132.3	578.4	281.0	281.0	20.9	30.9	229.2
2009 December	1,289.0	2.3	1.2	1.1	943.2	0.3	942.9	215.7	113.0	614.2	343.5	343.5	27.0	32.1	284.5
2010 December	1,458.7	5.7	2.6	3.0	1,020.3	6.3	1,013.0	266.5	61.9	684.6	431.1	431.0	25.0	29.1	377.0

Table 6.4. Other depository corporation loan – by industry

(Outstanding amounts, end of period, in millions of euro)

Description	Total									
	Agriculture			Industry, energy and construction				Services		
		Up to 1 year	Over 1 year		Up to 1 year	Over 1 year		Up to 1 year	Over 1 year	
2001 December	25.9	---	---	---	3.8	3.8	---	22.2	22.2	---
2002 December	86.5	1.5	1.5	---	13.6	13.6	---	71.4	71.4	---
2003 December	232.8	4.7	3.9	0.8	22.2	12.6	9.7	205.8	119.7	86.1
2004 December	289.9	7.9	3.9	4.1	47.8	22.5	25.3	234.2	89.5	144.8
2005 December	387.9	12.5	4.1	8.4	74.2	24.5	49.7	301.1	92.4	208.8
2006 December	490.5	16.4	3.4	13.0	97.7	28.0	69.7	376.4	120.6	255.8
2007 December	691.5	29.0	4.1	24.9	144.5	32.8	111.7	518.0	149.5	368.5
2008 December	902.4	37.4	4.1	33.3	160.2	28.9	131.2	704.8	126.4	578.4
2009 December	945.5	38.2	3.8	34.4	236.7	54.8	181.9	670.5	113.2	557.3
2010 December	1,027.0	38.3	0.4	37.9	268.5	77.4	191.1	720.2	193.1	527.1

Table 6.5. Other depository corporation effective interest rates

(New businesses, unless otherwise indicated)

Description	Deposit rates	Nonfinancial corporations									Households						
		Transferable deposits	Other deposits						Saving deposits	Transferable deposits	Other deposits				Saving deposits		
			Less than 250,000 euro			More than 250,000 euro					Up to 1 month	Over 1 month and up to 3 months	Over 6 months and up to 1 year	Over 1 year and up to 2 years		Over 2 years	
			Up to 1 month	Over 1 month and up to 3 months	Over 6 months and up to 1 year	Up to 1 month	Over 1 month and up to 3 months	Over 6 months and up to 1 year									
2004 December	2.8	0.1	1.8	2.3	3.0	*	3.3	*	*	2.0	0.0	1.7	2.1	2.9	3.8	*	1.6
2005 December	3.1	0.3	2.1	2.4	3.4	*	2.9	*	*	1.7	0.0	1.8	2.2	3.3	3.9	4.0	1.7
2006 December	3.1	0.4	2.1	2.9	4.3	*	3.1	*	*	1.5	0.0	1.9	2.3	3.4	4.2	4.5	1.7
2007 December	4.0	0.5	2.7	2.9	4.4	*	4.3	4.1	*	2.4	0.0	2.6	2.7	3.6	4.7	5.3	2.3
2008 December	4.4	0.5	3.1	4.0	5.3	*	3.6	4.9	*	2.9	0.1	3.2	4.6	4.5	5.0	3.9	2.7
2009 December	4.0	0.7	3.4	3.4	5.0	*	3.9	4.9	*	2.6	0.3	3.1	3.3	4.4	5.0	5.5	2.5
2010 December	3.4	0.6	2.4	3.1	5.0	5.1	*	3.7	*	2.1	0.6	2.6	2.6	4.5	4.8	5.1	2.2

Table 6.6. Other depository corporation effective interest rates - deposit rates

(New businesses, unless otherwise indicated)

Description	Loan rates		Non financial corporations						Households				
			Investment business loans		Kredi tjera biznesi (jo-investive)		Overdrafts	Credit lines	Loans covered by deposits	Overdrafts	Consumer loans	Mortgage loans	
	Up to 1 year	Over 1 year up to 5 years	Up to 1 year	Over 1 year up to 5 years	Up to 5 years	Over 5 years up to 10 years						Over 10 years	
2004 December	15.7	15.16	14.47	15.04	15.32	15.06	12.53	...	...	12.53	*	*	*
2005 December	14.5	17.34	13.29	15.18	14.38	15.11	11.51	...	...	11.51	*	*	*
2006 December	14.7	*	14.50	13.60	15.18	15.72	12.36	...	...	12.36	*	13.36	*
2007 December	14.1	*	13.76	*	14.64	15.09	13.72	...	...	13.72	12.92	12.36	*
2008 December	13.8	*	13.92	14.20	13.45	15.03	13.50	...	...	13.50	9.81	10.82	8.13
2009 December	14.1	*	14.34	*		*	*	13.31	*	10.67	*
2010 December	14.3	16.13	13.95	18.66	14.44	12.65	13.27	7.69	6.55	14.56	*	11.67	10.26

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