



CENTRAL BANKING AUTHORITY OF KOSOVO
AUTORITETI QENDROR BANKAR I KOSOVËS
CENTRALNI BANKARSKI AUTORITET KOSOVA

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LIST OF ABBREVIATIONS

ATM	Automated Teller Machine
CBAK	Central Banking Authority of Kosovo
CBP	Credit Bank of Pristina
CCIU	Currency Counterfeit Investigation Unit
CEFTA	Central Europe Free Trade Agreements
CPI	Consumer Price Index
CRK	Credit Registry of Kosovo
DC	Depository Corporations
EAR	European Agency for Reconstruction
EBRD	European Bank for Reconstruction and Development
ECB	European Central Bank
EU	European Union
EUR	Euro
FC	Financial Corporations
FDI	Foreign Direct Investments
FTA	Free Trade Agreement
FYROM	Former Yugoslav Republic Of Macedonia
HHI	Herfindalf – Hirschman Index
HICP	Harmonized Index of Consumer Prices
ICS	Interbank Clearing System
IMF	International Monetary Fund
IOPS	International Organization of Pension Supervisions
KCB	Kosovo Consolidated Budget

LIST OF ABBREVIATIONS

KEK	Energetic Corporation of Kosovo
KPST	Kosovo Pension Saving Trust
KTA	Kosovo Trust Agency
MFE	Ministry of Economy and Finance
MOU	Memorandum of Understanding
NewCos	New Companies
NPISH	Nonprofit Institutions Serving Households
ODC	Other Depository Corporations
OFC	Other Financial Corporations
OFI	Other Financial Intermediaries
PISG	Provisional Institutions of Self Government
POE	Publicly Owned Enterprises
POS	Point of Sales
PTK	Post and Telecommunication of Kosovo, J.S.C.
SEE	South – East Europe
SOE	Socially Owned Enterprises
SOK	Statistical Office of Kosovo
SRSG	Special Representative of Secretary General
TPL	Third Party Liability
UNMIK	United Nations Mission in Kosovo

Dear Mr. Special Representative of the Secretary General of the United Nations,
Dear Mr. President of Kosovo,

Once again, the financial sector of Kosovo achieved real progress in providing financial services, thereby supporting continued economic development and the drive toward a market economy. In 2006, as in the previous years, the financial sector increased the quality and the volume of its supply towards economic actors, elevating Kosovo to the relative level of its neighbouring countries. Although economic development is insufficient to address the challenges Kosovo is facing, its financial sector provides to households and companies the basic supply to support their projects.

In that regard, the financial sector must be considered as one of Kosovo's assets.

Following a low growth rate of GDP in 2005 (finally estimated at 0,3%), economic activity improved in 2006, with a real GDP growth presently estimated at 3%. Of course, the level of economic growth should be boosted in order to overcome demographic increases and the difficult challenges ahead for Kosovo; nevertheless, it is positive that, in 2006, GDP grew thanks to the contribution of the private sector, and despite the negative impact of both a contraction of donors' assistance and unspent investment credit lines from Kosovo's budget.

Lending activity from commercial banks was still high in 2006, with an increase of total loans by 24%, bringing the ratio of total loans to GDP to 27 %, a higher level than in many neighbouring countries. Credit demand is showing a slow shift from import financing towards equipment funding.

Nevertheless, though, there is still little supply for long-term needs and a relatively high cost of credit, it should be stressed that good bankable projects, as well as initiatives from entrepreneurs in sectors with value added, are still too few. Moreover, it is illusive to rely mainly on the settlement of Kosovo's status to attract foreign investors, while Kosovo's infrastructures and international image need to be improved.

In other words, an upgrade of the different components of the business environment should go hand in hand with the present overall efficiency of the financial system.

In its capacities as a central banking and supervisory authority, the CBAK has been determined to contribute positively to economic development, by strengthening the financial sector and offering the best services to its different partners, as well as to the general public. A regulation, issued on August 24 2006, provided the CBAK with a new status, enlarging its competencies and paving the way to institutional changes. Prudential rules applicable to the financial sector have been amended to upgrade the regulatory framework and to move towards risk-based supervision.

On a practical side, the CBAK has shown its readiness to use all the scope of its powers to enforce the regulation and to upgrade professional and management practices. This led the CBAK Board to revoke, in March 2006, the license of one commercial bank, for which liquidation is still ongoing. Due to a quick coverage of small deposits, limited knock-on effects were noticeable on the banking sector.

On the side of pension funds, a comprehensive restructuring of the specialized institutions has been performed, mostly in full cooperation with the institutions themselves, which will bring the entire six in-house pensions fund to be closed, and most of them to have their funds transferred to general pension providers.

Last, the CBAK has developed a pro-active approach towards foreign investors, in order to bring strong and experienced actors, mainly from the region, to invest in the Kosovo financial sector. In that respect, for example, a large Slovene banking institution took over the two largest domestically owned banks in the first months of 2007.

Regarding its central banking activities, the CBAK has undertaken several initiatives to improve its services to economic actors and public authorities. Namely, the economic analysis and statistics functions have been strengthened and the first balance of payments as well as other studies on the Kosovo financial sector have been issued; the new credit register has been made fully operational; information on payments cleared by the CBAK have been extended and made available to the Treasury in real time; a comprehensive upgrade of the security of the CBAK building has been carried out.

Internationally, the CBAK has already succeeded in being involved in the major international and regional professional organizations and circles. Then, in the context of the institutional changes of the Territory which are expected for the months to come, the CBAK will devote its means to finish Kosovo's integration with the outside world, in particular in the field of mutual recognition of insurance policies, and appropriate connections with the major payments systems.

The expected changes of the international status of Kosovo could be seen as assets and challenges for the financial sector, as well as for the CBAK itself. Assets, since regional integration could be speeded up for the best of the economy; challenges, since independence and professionalism of the CBAK –built thanks to the huge financial and technical assistance of international community- shall be, not only maintained, but also strengthened. Once more, it must be stressed that foreign companies and financial actors will invest in Kosovo only if the business environment is assessed as being secure and friendly, and if financial supervision as well as central banking activities are performed in a neutral, independent and professional way.

In that context, I am pleased to submit to you the 2006 Annual Report of the CBAK.



Michel Svetchine

As of 31 December 2006 the Governing Board of the Central Banking Authority of Kosovo was composed of following members:

Governing Board of the CBAK:

Mr. Ajri Begu, Chairman of the Governing Board,
Mr. Michel Svetchine, Managing Director of the CBAK,
Mr. Gazmend Luboteni, Professor, Faculty of Economics - University of Prishtina
Mrs. Chiara Bronchi, Head of Fiscal Affairs Office – EU pillar of UNMIK
Mr. Lulzim Ismaili, Director of the Treasury

Audit Committee of the Governing Board of the CBAK:

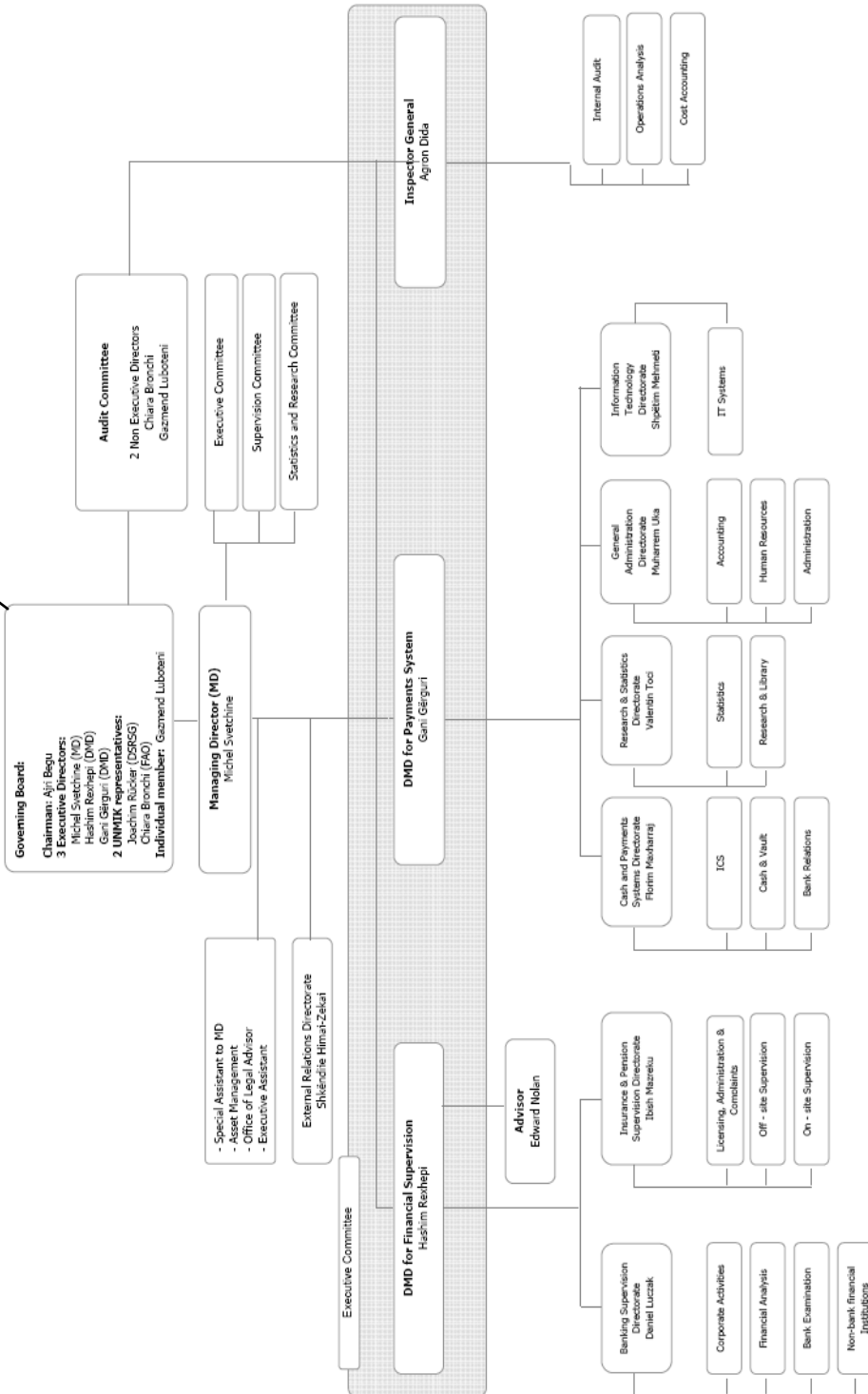
Mr. Gazmend Luboteni, Professor, Faculty of Economics - University of Prishtina
Mrs. Chiara Bronchi, Head of Fiscal Affairs Office - EU pillar of UNMIK
Mr. Agron Dida, Inspector General

Executive Committee of the CBAK:

Mr. Michel Svetchine, Managing Director of the CBAK
Mr. Hashim Rexhepi, Deputy Managing Director for Financial Sector Supervision
Mr. Gani Gërguri, Deputy Managing Director for Payments System
Mr. Agron Dida, Inspector General

Organizational Structure of the CBAK (as of 31 December 2006)

Mr. Rücker, Mr. Gerguri and Mr. Rexhepi were members of the GB until 23 August 2006. Effective from 24 August 2006, Mr. Lulzim Ismajli has been appointed ex officio as a member of the GB.



1. Executive Summary

1. Executive Summary

The new UNMIK Regulation 2006/47 on the Central Banking Authority of Kosovo (CBAK) lists the principal objectives of the CBAK: To foster the soundness, solvency and efficient functioning of a stable market-based financial system, encouraging market emergence of safe financial instruments; and without prejudice to this, to support the general economic policies in Kosovo with a view to contributing to an efficient allocation of resources in accordance with the principle of an open market economy. One of the special powers accorded to the CBAK by the new regulation is to conduct regular economic and monetary analysis of the Kosovo economy, make public the results, and submit proposals and measures to the UN Interim Administration in Kosovo and the Provisional Institutions of Self Government on the basis of such analysis. In these terms, CBAK regularly publishes its Annual Report that describes the developments in the Kosovo economy, with a special focus in the financial sector, as well as developments in the world and regional economies. The CBAK Annual Report also addresses issues concerning the internal developments in the CBAK including the audited financial statements.

The global economy during 2006 was characterized by an output expansion of 5.1% that was mainly due to the increase in investments. Countries that drove the output expansion were the USA, Japan, China, and India. The global economy during 2006 was subject to inflationary pressures deriving from, on one hand, the strong global demand for oil and, on the other hand, tight oil supply that led to a higher oil price internationally and hence to higher headline inflation.

The countries of South-Eastern Europe are keeping the momentum in terms of economic growth, recording an average GDP growth of 5.7%. The economic growth in these countries was mainly driven by strong domestic demand, favourable environment for investments, and rising exports. The country that had the best economic performance was Romania, followed by Bulgaria, Bosnia and Herzegovina, and Serbia. Despite the favourable economic performance, high unemployment and external imbalances remain a concern for the countries of South-Eastern Europe.

The Kosovo economy recovered from the previous year's stagnation, recording an estimated real GDP growth of 3.0% in 2006. The GDP growth was exclusively driven by private sector investments that were mainly supported by banking sector loans and foreign direct investments. However, the high unemployment rate and high current account deficit remain a concern for policymakers. The current account deficit continued to be financed primarily by remittances from the Kosovo diaspora and donors.

Following deficits in 2004 and 2005, the Kosovo consolidated budget in 2006 recorded a surplus of 3.4% of nominal GDP (euro 76.5 million). The budget surplus resulted from, on one hand, the over performance in revenue collection and, on the other hand, substantial under-spending of budgeted capital expenditures which were mainly due to inadequate internal planning of budgetary proceedings in some spending agencies.

In general, the price levels in Kosovo remain stable. The inflation rate in 2006 stood at 0.7%, which is lower than the average in the Western Balkans. One of the reasons for the price stability is the use of the Euro as currency. However, to some extent the price levels in Kosovo are affected by the evolution of international presence and donors assistance, which impacts both tradable and non-

tradable prices. Consequently, the anticipated decline of the international presence affects price levels over the medium term.

During 2006, the Kosovo Trust Agency (KTA) continued to decisively accomplish the privatization of the Socially Owned Enterprises (SOEs). This privatization process was initiated with the intention to enhance both the value and the governance of SOEs and POEs. 213 companies were tendered during the year and, if successfully privatized, the revenue generated would attain a value of euro 154 million. Taking stock as of year-end 2006, the total number of privatized companies stood at 216 and the accumulated privatization revenues reached euro 275 million.

The financial sector in Kosovo remained stable and profitable in 2006. The structure of the financial system continues to be dominated by commercial banks that, in 2006, held 89% of total financial sector assets. Kosovo's banking sector is comprised of six privately-owned commercial banks, operating through 220 banking units throughout Kosovo. The Kosovo banking sector displayed an increased level of activity and increased confidence in the domestic market during 2006 by introducing new products, such as loans with maturities up to ten years and home mortgage loans. The intermediation role of the banks in Kosovo can be considered as continuously improving as reflected by the continuing increase in loans and deposits. Banking sector loans increased by 24% in 2006, attaining a level of euro 636.6 million, or 26.1% of GDP.

With regard to financial services, CBAK continued to supply the Kosovo economy with Euro coins and banknotes for the settlement of cash transactions. CBAK also continued to provide account maintenance and payment services for entities such as Treasury, PISG, KTA and major public utility companies. With a view toward fostering an efficient and safe payment system, the CBAK continued to manage and operate the Inter-Bank Clearing System (ICS). The volume and value of transactions in 2006 continued a steadily increasing trend. In addition, the Kos-giro project launched in 2005 continues to facilitate bill payments through standardization and automation of an efficient scheme for all the participants involved: the CBAK, commercial banks, large billers and large remitters. In accordance with the CBAK Regulation and Investment Policy, conservative risk management that prioritizes safety and liquidity over income, continued to guide the asset management that represents another function of CBAK.

At the beginning of 2006, CBAK launched the Credit Registry of Kosovo (CRK) with the aim of facilitating the exchange of credit information among credit-providing institutions. The CRK provides credit information on potential borrowers to the credit-providing institutions. This enhancement of the information exchange process should provide faster and more accurate information on a potential borrower's creditworthiness, presumably improving access to credit and enabling sounder lending decisions.

The supervisory and regulatory oversight of financial institutions in a way that fosters a sound, accessible, and competitive financial system is one of the key responsibilities of the CBAK. The primary objectives of banking supervision are to protect depositor funds and maintain a stable financial system. In conjunction with these objectives, the CBAK revoked the license of Credit Bank of Pristina (CBP) after determining that the CBP no longer fulfilled the necessary solvency and liquidity standards to protect its depositors. The liquidation process of CBP is ongoing. All depositors received an immediate refunding of up to euro 3,500, which fully paid 97% of depositors. Further payments are made as CBP assets are liquidated. Despite the closure of this

bank, other banks continued to operate effectively, with industry deposits first remaining stable and then steadily growing during the period.

2. External Economic Environment

2. External Economic Environment¹

2.1. World Economy

Despite a slight moderation of the growth pace in 2005, world output increased sharply in the first half of 2006. Although moderated slightly in the second half, global growth has been estimated at 5.1%. Increased investments (industry based) and export growth of countries recording the highest output growth have been an important driver of the world economic performance. In terms of sector performance, manufacturing and service sector have grown persistently. The expansion in the world economy was driven by the strong growth in US, Japan, China, India and some other large emerging countries. China is one of the countries that exceeded the projected growth rate, where output is estimated to have increased by 10.4%. However, apart from China, other developing countries marked an increase of 5.5%. Investment growth and the significant increase in net exports has contributed in the China's growth, while in Japan, financial sector reform, strong exports and steady business investment have brought about the sound economic performance. Strong economic performance was also shown in the Middle East countries as well as in the euro area.

Strong global demand for oil and tight supply has caused an increase of oil prices internationally. This has increased the production cost, boosted domestic prices and led to higher headline inflation in many countries, while the core inflation was mainly under control. The recorded inflation rate in many cases was higher than the central banks' inflationary target. According to Federal Reserve estimates, the US Consumer Price Index (CPI) in 2006 stood at 2.3 percent, while their comfort zone for core inflation was 1.5 percent. The main tool used to adjust to the high inflation by most central banks, particularly US Federal Reserve, was the increase of short-term interest rates. The same instrument was used by the European Central Bank, while Bank of Japan ended its policy of zero interest rate in July 2006.

The US current account (CA) deficit that is still considered as the main source of the global imbalance, exceeded \$800 billion. Despite the export growth, the strong demand for imports maintained the large CA deficit. In addition, investment demand was considered to have moderated, leading to further CA deficits. However, large CA surpluses encountered by East Asia and oil-exporting countries continue to offset the deficit of US. For example, China recorded a large surplus in 2006 that accounted for around 4.5% of its GDP. The US dollar depreciated slightly against euro, pound and yen over the past two years. On the other hand, in most Asian countries (especially China), and oil producing countries, exchange rate appreciated. At the end of 2006, euro stood at USD 1.33, which is 6.9% above its 2005 average. As for Yen, euro was traded at 153 JPY, which is 11.5% above its 2005 average. Euro appreciated against British pound in 2006 and was traded at 0.68 GBP, a half percentage point below its 2005 average.

2.2 European Union

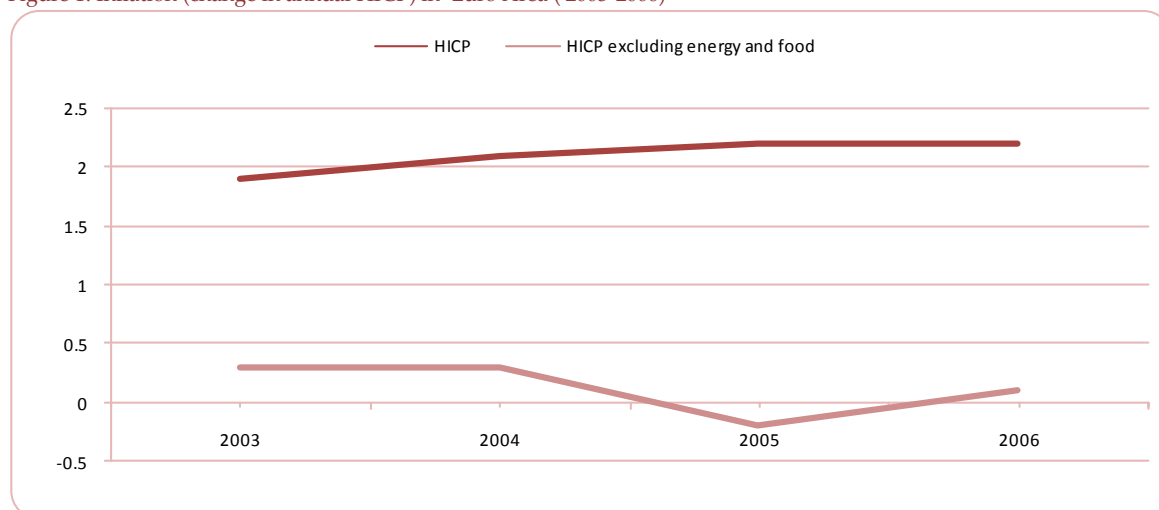
The European Union has been successful in accomplishing its goal of bringing economic benefits through developing and maintaining an effective single market. According to Eurostat estimates, annual real GDP growth in EU countries averaged between 2.5% and 2.9% in 2006, indicating an

¹ The section on developments in the external economic environment is based on various publications: IMF (2006), EBRD (2006), Business Monitor International (2007), European Commission (2006), ECB (2007) and Eurostat (2007).

improvement compared to the growth of 1.3% in 2005, while GDP *per capita* stood at US\$ 25,913. Domestic demand is considered the main driver of the economic growth. The financing conditions were favorable in 2006 and enabled an increase in consumption and investments, which in turn contributed to the economic growth.

According to the ECB, the average annual Harmonized Index of Consumer Prices (HICP) stood at 2.2% in 2006, indicating a similar level with the year before. Developments in energy prices and particularly in oil prices are the cause of the slight increase in inflation. During 2006, the inflation rate was volatile mainly due to short-term changes in energy and food prices. However, as figure 2 shows, excluding unprocessed food and energy, HICP remained fairly stable in 2006.

Figure 1. Inflation (change in annual HICP) in Euro Area (2003-2006)



Source: Eurostat (2007).

Balance of payments indicates a strong growth in both, exports and imports of goods in the euro area. Due to rising trade deficit, cumulative CA registered a deficit of €28.8 billion, compared to a surplus of €23.6 billion in 2005. The shift from surplus to deficit is mostly due to a more significant increase in imports that resulted from the increased cost of oil and energy-related imports. Imports of goods experienced a sharp rise in 2006 mainly due to growth in domestic demand.

Regarding the developments in individual euro area countries, Ireland was an outlier in terms of real GDP growth with an annual increase of 5.8%, followed by Greece and Finland that recorded a real GDP growth of 3.7% and 3.5%, respectively. Italy on the other side recorded the lowest GDP growth of 1.5%. While in non-euro area countries, United Kingdom recorded a real GDP growth of 2.7% in 2006. The moderation in GDP performance of the EU was mainly due to the slowdown in private consumption. However, domestic demand continued to be the main driver of the economy. Annual HICP was estimated at 2.4% (compared to 2.0% in 2005) and the increase is explained by rising energy prices. Denmark recorded a real GDP growth of 2.7% in 2006, while Sweden at 4.0%. The driving force of the economic activity of both countries was a strong domestic demand. Annual HICP inflation eased further to 1.4% in Denmark, while it remained unchanged at 1.2% in Sweden.

Mentioning a few transition countries, now members of the EU, Czech Republic, Poland and Hungary, recorded GDP growth of 6.2%, 5.0% and 3.5%, respectively. Output growth in Czech

Republic and Poland was mainly driven by domestic demand, while Hungary's growth was driven by net exports. Due to the tax increases and administered price rises, HICP rose significantly in Hungary (6.3%), and declined in Czech Republic and Poland. Slovenia's real GDP has been robust since 2001, averaging at 3.4% (compared with 1.4% in the euro area for the same time period).

2.3 South East Europe

Although the South-East European (SEE) countries are experiencing a favorable growth in recent years, there is still a long way to go. In terms of GDP level, only Albania, Croatia, and Romania achieved the pre-transition GDP level; while the unemployment and high foreign imbalances remain a concern for policymakers in the region. The average real GDP growth for the region is keeping the momentum achieving 5.7% in 2006 compared to 4.9% in 2005. Romania had the strongest real GDP growth rate followed by Bulgaria, Bosnia and Herzegovina and Serbia (Table 1). As shown in Table 1, in terms of GDP *per capita*, Croatia accounting for US\$ 9540 is an outlier compared to other countries in the region that achieved an average GDP *per capita* US\$ 4,439. Romania is the second, by attaining the GDP *per capita* level of US\$ 5793. Except Bulgaria that achieved a GDP *per capita* of US\$ 3,981, other countries in the region are considered poor with a recorded average GDP *per capita* of only US\$ 2,952, which is slightly above the threshold for low-income countries of US\$ 2,500.

Table 1. Main macroeconomic indicators in SEE (2005-2006)

Country	Real GDP growth		GDP per capita		Inflation, % y-o-y		Unemployment	
	2005	2006	2005	2006	2005	2006	2005	2006
Albania	5.5	5.5	2,710.0	2,955.0	2.3	2.5	14.7	na
B&H	5.5	6.0	2,612.0	2,992.0	2.4	7.8	44.5	na
Bulgaria	5.5	6.4	3,465.0	3,931.0	6.6	6.5	10.7	9.2
Croatia	4.3	4.6	8,568.0	9,540.0	3.6	2.0	12.3	na
FYROM	3.8	4.1	2,797.0	2,967.0	1.2	2.9	36.5	na
Montenegro	4.1	5.5	2,383.9	na	2.6	3.5	27.3	na
Romania	4.1	7.7	4,577.0	5,793.0	8.6	4.9	5.9	5.2
Serbia	6.2	5.7	2,469.0	2,893.0	17.7	6.6	31.7	na
Average	4.9	5.7	3,697.7	4,438.7	5.6	4.6	23.0	7.2

Source: Business Monitor International (2007), EBRD (2006).

However, despite the favorable developments in the region, a concerning issue remains the high level of unemployment. Bosnia and Herzegovina is an outlier with a recorded unemployment level of 44.5% as of end-2005. The FYROM is the second country with the highest unemployment rate that stood at 36.5%. The lowest level of unemployment (5.9%) has been recorded in Romania.

Inflation can be alleged as being under control during 2006 in the region (see Table 1). The strong domestic demand and high energy and food prices put pressure on inflation. The average inflation rate in the region in 2006 was at around 5.5%. Most countries relied on exchange rate policies during 2006, as an instrument to accommodate to inflationary pressures. In addition, a stable nominal regime was evident in most countries through the currency boards (the case of Bosnia and Herzegovina and Bulgaria), euroisation (Montenegro and Kosovo) and a fixed peg exchange rate (in FYROM).

Strong domestic demand, supported by credit growth and rising wages in some countries, was the main driver of the economic growth. In addition, the economic growth was also supported by favorable investment conditions that encouraged foreign direct investments (FDI), as well as export increase. The enforcement of new free trade agreements by joining CEFTA (Central Europe Free Trade Agreements) stimulated a recovery of export markets, thus widening the export opportunities for the countries in the region. However, the strong domestic demand reflected a higher demand for imports in the region offsetting to some extent the strong export growth.

The region encountered an industrial revival from considerable FDI inflows primarily attracted by the improved investment climate, mainly achieved by the reforms undertaken to join the EU, the economic stability measures in terms of maintaining the sound monetary and fiscal stance. The recorded net FDI rose from US\$ 13 billion in 2005 to US\$ 19.3 billion in 2006, which shows an increase of 48.5% for the region. Inflows were mainly related to the privatization programs still undergoing in some countries and greenfield investment. The highest level of net FDI was recorded in Romania where the net FDI amounted to US\$ 8.65 billion, Serbia US\$ 3.5 billion and Bulgaria US\$ 3 billion. The lowest level of FDI was recorded in Montenegro, where net FDI amounted at US\$ 150.2 million (Table 2).

Table 2. Foreign Direct Investment, net (millions of US\$), 2001-2006

Years	Albania	B&H	Bulgaria	Croatia	FYROM	Montenegro	Romania	Serbia
2001	204.0	130.0	803.3	1,178.5	440.7	10.0	1,154.0	165.0
2002	135.0	266.0	876.3	585.6	77.7	84.0	1,080.0	475.0
2003	178.0	382.0	2,070.3	1,932.0	96.0	44.0	2,156.2	1,360.0
2004	332.2	490.0	2,777.1	870.9	155.9	63.3	6,368.0	966.0
2005	264.8	300.0	2,297.9	1,509.1	97.0	474.3	6,587.3	1,481.0
2006	350.0	570.0	3,000.0	2,824.8	300.0	150.2	8,652.0	3,500.0
Average	244.0	356.3	1,970.8	1,483.5	194.5	137.6	4,332.9	1,324.5

Source: EBRD (2006).

The average CA deficit in SEE countries stood at 8.3% of GDP in 2006 (Table 3). The main contributors to large foreign imbalances are Bulgaria, Bosnia and Herzegovina, and Romania, accounting for an estimated 13.4% of GDP, on average. Croatia and Montenegro remain the countries in the region with the most sustainable source of external revenues, namely with increasing tourism revenues and substantial FDI inflows as the financing items for the CA deficit. Large CA deficits remain the challenge for governments in the years to come which will necessitate further structural reforms. Structural reforms will assist in keeping the current pace of FDI, considering that they represent the main financing item of the external imbalance. Remittances and the donor sector, on the other side, have been an important factor in financing the CA deficits in some other countries in the region.

In general, the SEE countries performed sound fiscal policies in 2006. The contributing factor to this may be considered the IMF programs and other International Financial Institutions conditionalities. Despite a well maintained fiscal discipline in the region, yet, government spending is still large relative to GDP in several countries (for example, Bosnia and Herzegovina, Croatia, Montenegro and Serbia). Budget balance was relatively under control in the region during 2006, averaging at

0.3% of GDP (Table 3). Croatia represents the country with the highest budget deficit, recorded at 3.0% of GDP, whereas Bulgaria recorded the highest budget surplus, estimated at 3.6% of GDP.

Table 3. Yearly Budget balance and Current Account balance (2005-2006)

Country	Budget balance (% of GDP)		CA balance (% of GDP)	
	2005	2006	2005	2006
Albania	-3.3	-0.6	-6.6	-6.4
Bulgaria	2.3	3.6	-11.3	-16.0
B & H	2.6	2.1	-21.8	-11.8
Croatia	-4.1	-3.0	-6.4	-7.5
FYROM	0.2	0.4	-1.4	0.8
Montenegro	-1.7	-0.3	-8.6	-5.0
Romania	-0.8	-1.6	-8.7	-10.7
Serbia	1.4	1.5	-9.7	-9.7
Average	-0.4	0.3	-9.3	-8.3

Source: Business Monitor International (2007), EBRD (2007).

Albanian economy maintained its good performance in 2006 recording a GDP growth of 5.5% that is similar to 2005. The main contributor to the real GDP growth remains private consumption and investment, financed mainly by strong remittance inflows and increasing bank credit. Inflation has been maintained under control generally, being under Bank of Albania targeted range of 2% to 4%. Average annual inflation stood at 2.5% in 2006, indicating a slight increase compared to 2.3% in 2005. The Albanian Lek remained relatively stable during 2006, compared with the appreciation against the euro by approximately 3% in nominal terms during 2005. CA deficit was estimated at 6.4% of GDP in 2006 and was mainly financed by strong remittance inflows as well as increased tourism revenues. FDI is estimated at 3.1% of GDP in 2006 that is well behind other countries in region. Budget balance situation improved considerably. The estimates show that budget deficit decreased to 0.6% of GDP in 2006 compared to 3.3% of GDP in 2005. Credit to private sector recorded a significant expansion, growing by 74% during 2006.

Bosnia and Herzegovina recorded a relatively strong growth in 2006 estimated at 6.0%, compared to 5.5% in the previous year. The strong economic growth has resulted from substantial investments as well as strong export growth. Inflation reached 7.8% in 2006 and the main reason for the increase was the introduction of the VAT in January 2006 and high oil prices. The CA deficit is still considered high, although decreased significantly in 2006 at around 11.8% of GDP (from 21.8% in 2005). Deficit has been financed mainly by capital transfers, FDI and other capital inflows. Net FDI inflows rose slightly in 2006 and amounted to US\$ 570.0 million (US\$ 300 million in 2005). Due to the strict currency board regime with the euro, the BAM - BiH currency (Convertible Marka) remained stable during 2006.

The Bulgaria's real GDP grew from 5.5% in 2005 to 6.4% in 2006. Rapid credit growth stimulated investments and consumption, being the driving force of the economic growth. The annual inflation decreased slightly from 6.6% in 2005 to 6.5% in 2006, mainly due to a drop in food prices. The CA deficit increased substantially to 16.0% of GDP, and has been financed by strong flows of FDI and bank lending. Net FDI is still considered high, recorded at US\$ 3 billion, although rose

only slightly compared to 2005. On the other side, budget balance recorded a surplus of 3.6% of GDP.

Real GDP in Croatia grew by 4.6% in 2006 compared to 4.3% in 2005. Domestic demand was the main driver of economic growth. Investments, exports and tourism remain an important factor of the good performance of the economy. Average annual CPI marked a decrease to 2.0% from 3.3% in 2005. The CA deficit increased slightly to 7.5% of GDP, compared to 6.4% in 2005. Net FDI rose from US\$ 1.5 billion in 2005 to US\$ 2.8 billion in 2006 and, apart from tourism revenues, continues to be an important financing item of the CA deficit. The recorded budget deficit in 2006 was 3.0% of GDP, signifying a decrease compared to 2005 when the estimated budget deficit was 4.1% of GDP. Real GDP growth in FYROM increased to 4.1% in 2006 from 3.8% in 2005. Although the private consumption and investments increased, the economic growth was above all driven by exports. CPI increased by 2.9% during 2006, compared to 1.2% during 2005. The external balance improved in the 2006, mainly due to higher exports and an increase in net current transfers. The annual CA balance shifted to a surplus of 0.8% of GDP in 2006 from a deficit of 1.4% in 2005. Net FDI although increased comparing to 2005 is still considered low, recording US\$ 300.0 million. The exchange rate of denar remained stable against the euro on a level of 61.3 MKD/EUR.

Montenegro achieved real GDP growth of 5.5% (4.1% in 2005) mainly due to strong performance in services and tourism sector. However, investments are an important factor in the economic growth of Montenegro. In the first half of 2006, industrial production rose by 2.9% y-o-y. Annual CPI increased from 2.6% in 2005, to 3.5% in 2006. The CA deficit further declined at 5.0% of GDP compared to 8.6% of GDP in 2005 mostly due to an increase in exports and services (tourism related). Following the privatization process, net FDI amounted to approximately US\$ 150.2 million compared to US\$ 474.3 million in 2005, indicating a decrease of US\$ 324.1 million. The budget deficit in 2006 declined from 1.7% of GDP in 2005 to 0.3% of GDP in 2006.

Romania continued to show strong economic performance. The real GDP growth was recorded at 7.7%, compared to 4.1% in 2005. Strong growth of private consumption and investments were the main drivers of the good performance. The annual inflation rate decreased to 4.9% in 2006 from 8.6% in 2005. Currency appreciation, the postponement of administered prices increases and drop in agricultural prices were the reasons of the reduction in the average annual inflation. Budget deficit grew from 0.8% of GDP in 2005 to 1.6% of GDP in 2006. In addition, the CA deficit worsened to 10.7% of GDP in 2006, compared to 8.7% of GDP in 2005. The net FDI inflows continued to be the main financing source for the external imbalances, recorded at US\$ 8.65 billion.

Real GDP growth in Serbia was estimated at 6.2% in 2006 compared to 6.3% in 2005. Credit growth stimulated domestic consumption which in turn boosted the economic growth. Export growth on the other hand contributed considerably to the increase of real GDP. Inflation decelerated at 6.6% y-o-y in 2006 compared to 17.7% y-o-y in 2005. CA deficit is still high, amounting at 9.7% of GDP in 2006 and is partially financed by strong remittance inflows and export growth. FDI rose in 2006, recording US\$ 3.5 billion compared to US\$ 1.5 billion in 2005 and the increase is mainly due to the privatization process.

To summarize, the regional economic environment in 2006 was generally favorable, with high levels of economic growth, stable inflation and exchange rates, and improved investment climate.

The challenge for the region remains the downsizing of the CA deficit as well as the unemployment rate.

3. Kosovo Economy

3. Kosovo economy

In 2006, Kosovo economy recovered from the previous year stagnation recording an estimated real GDP growth of 3.0%.² Unlike the government-fuelled growth recorded in 2004, the growth in 2006 was supported exclusively from the private sector investments. The private sector investments were mainly supported by the banking sector loans and foreign direct investment. Apart from the decline of the donor sector, the 'local content' of GDP marked an increase of around 5%, which is comparable with the average real GDP growth in SEE.

Even if it is obvious that Kosovo needs a higher rate of economic growth to address the challenges it is facing - and namely the financing of public infrastructure, as well as the reduction of unemployment - the level of economic growth recorded in 2006 is to be considered as encouraging, because it has been obtained despite the restrictive effects resulting from a reduction of donor assistance (from euro 426 million to euro 343 million), and a reduction of the government capital expenditures.

In general, the price level in Kosovo remains stable. The inflation rate in 2006 stood at 0.7%, which is lower than the average in SEE. One of the reasons for the price stability is the use of euro currency. However, to some extent the price level in Kosovo is affected by the evolution of international presence and donors assistance, which impacts both tradable and non-tradable prices. Consequently, the envisaged decline of international presence affected the price level over medium term.

Due to the absence of borrowing capacities, both domestically and internationally, as well as the lack of instruments to finance the budget deficit, the Government shall pursue tight fiscal policies, in order to maintain a budget deficit which could be financed with the fiscal surpluses accumulated in the early 2000s. The execution of the 2006 budget shows a surplus of 3.4% of GDP, due to additional fiscal revenues and to unspent budget lines, while the 2004-2005 deficits were financed by the budget surpluses incurred in previous years. Further reforms are needed in terms of broadening the tax base and adjustments in expenditures in order to accommodate the investment needs to address many structural problems of the economy.

With the lack of adequate infrastructure, the level of unemployment in Kosovo is one of the most concerning issues of the economy. The figure on unemployment varies from around 30% (IMF, 2004) to 40% (SOK, 2006). Kosovo has a relatively young population and much investment is needed in order to bring the unemployment rate down. The resolution of the Kosovo's political status, but above all, the upgrade of the legal business framework based on the rule of law as well as structural reforms, a substantial effort to improve education and training, modernization of the public infrastructure, with appropriate connections with main trading partners, etc. would facilitate the creation of favorable environment for investments. In addition, the revival of the agriculture, mining and energy sector which were the driving force of the Kosovo economy, and even more the development of services and subcontracting, is important for the medium term economic performance.

² Due to a recurrent lack of appropriate economic data, to evaluate precisely the evolutions of GDP in Kosovo is not an easy task. For instance, in the CBAK annual report for 2005, and based on the figures available on April 2006, it was assessed that, in 2005, Kosovo GDP had declined from 0,2% compared to 2004, while in the course of year 2006, this figure has been revised and show a growth of 0.3%.

Table 4. Kosovo Main Macroeconomic Indicators (2001-2006)

Description	2001	2002	2003	2004	2005	2006
Real GDP growth, in %	36.00%	0.40%	2.60%	2.10%	0.30%	3.00%
GDP per capita (in EUR)	1,187	1,182	1,164	1,161	1,120	1,117
Prices(CPI), annual average in %	11.7	3.6	1.1	-1.1	-1.5	0.7
Kosovo Consolidated Budget, in % of GDP						
Revenues	16.4%	23.2%	28.0%	27.5%	28.5%	31.4%
Expenditures	12.1%	19.1%	25.3%	33.3%	31.1%	28.0%
Balance	4.3%	4.0%	2.8%	-5.8%	-2.6%	3.4%
Financial Corporations (FC), in EUR thousand						
FC net claims on external sector	-	-	-	642,608	685,096	965,246
FC net claims on fiscal sector	-	-	-	-221,347	-229,676	-482,499
Claims on real sector	-	-	-	-253,463	-259,123	-184,288
Claims	-	-	-	417,993	527,226	704,299
Liabilities	-	-	-	671,457	831,349	888,587
Current account (CA) balance, in % of GDP						
CA before foreign assistance	-	-	-	-35.0%	-37.9%	-44.2%
CA after foreign assistance	-	-	-	-8.8%	-11.9%	-17.3%
Goods and services	-	-	-	-45.9%	-50.1%	-54.5%
Remittances	-	-	-	15.0%	17.2%	18.7%

Source: IMF (2006, 2007), SOK (2006), MFE (2006), CBAK (2006).

Financial sector has continued increasing credit provided to the private sector supporting consumption and especially investments in 2006. Financial sector claims amounted at euro 704.3 million, representing an annual growth of 23.1%. Financial sector in Kosovo remains stable and profitable. Mainly due to the CBAK placements, the financial sector net foreign assets in 2006 over 2005 grew with 40.9%, amounting at euro 965.2 million. Apart from the CBAK impact to the financial sector NFA, the commercial banks net foreign assets grew with 11.9% over the same time-scale amounting at euro 336.6 million.

High external imbalances remain a concern for the Kosovo economy. The current account deficit after foreign assistance, estimated at 17.3% of GDP, remains one of the highest in the region. Before foreign assistance, the current account deficit amounting at 44.2% of GDP in 2006 is more worrying. This implies the importance of the donor sector, albeit declining, in Kosovo economy. The main source of the deficit remains a huge level of imports. The export to import coverage is still very low, standing at around 8%. Transfers from Kosovans working abroad are one of the most important financing item of the current account deficit. The remittances in 2006 are estimated to amount euro 424 million, compared to euro 386 million in 2005. Apart from remittances, another source of financing is the donor sector and foreign direct investments.

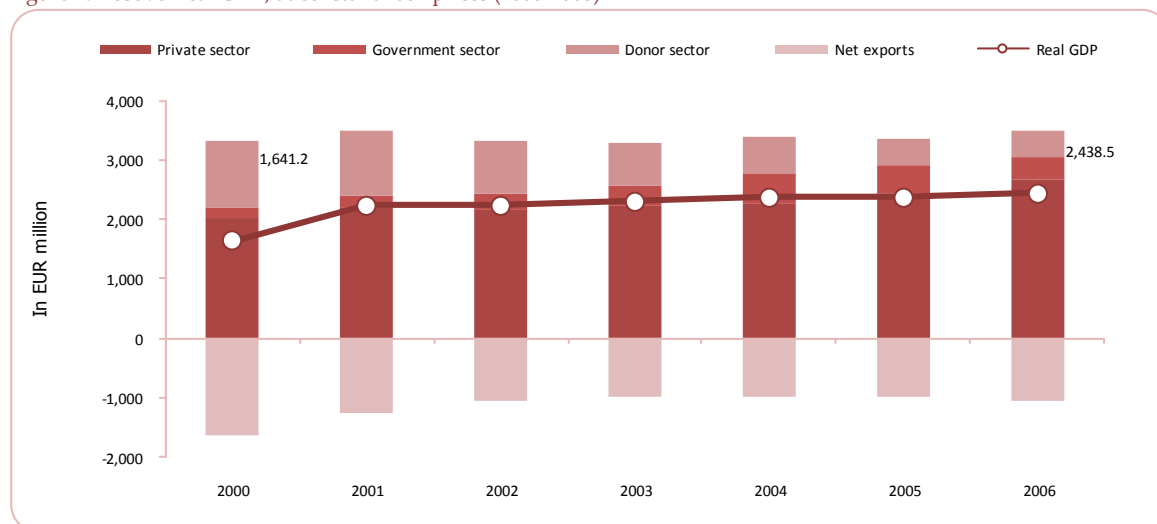
3.1. Real Sector

3.1.1 Gross Domestic Product

After a stagnation in 2005, Kosovo real GDP for the year 2006 is estimated to have increased by 3% amounting at around euro 2.4 billion (Figure 2). This makes the GDP *per capita* amounting at euro 1.118, which is below the SEE average. The GDP growth in 2006 is supported from the boost in the

private sector investments, despite the decline in the donor and government sector, which had a negative impact in the Kosovo economy.

Figure 2. Kosovo Real GDP, at constant 2002 prices (2000-2006)

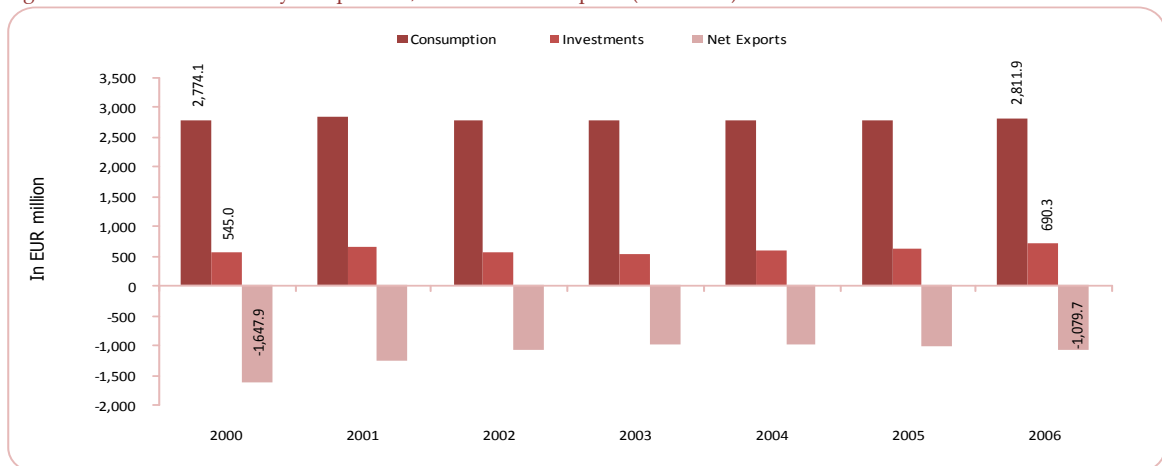


Source: IMF (2006).

Based on a sectorial approach, private sector demand (consumption and investments) in 2006 totaled at around euro 2.7 billion, growing with 8.9% against 7.7% in 2005. The increase in the private sector is supported from both, consumption and investments. While consumption grew at a slower pace by 4.1%, the private investments in 2006 boosted with 32.9%. With this increase, the private sector investments increased their share to GDP at 22.4%, representing historical peak. Regarding the government sector demand, amounting at around euro 400 million, it declined with 12.1% in 2006, which is broadly the same as the decline in 2005. The source of the decline resides with the government capital expenditures. The donor sector in 2006 declined to euro 448 million from euro 1.143 million in 2000.³ In 2000, donor sector composed 70% of Kosovo GDP, while in 2006 less than 20% of GDP. The decrease can be attributed to the sharp decline in both, consumption (from euro 871 million in 2000 to euro 405 million in 2006) and investments (from euro 272 million in 2000 to euro 43 million).

³ Donor sector includes UNMIK, KFOR, and other donor spending under the umbrella of "public investment program", and spending financed by designated donor grants. This presentation excludes wages of KFOR personnel as well as consumption of goods imported directly by KFOR.

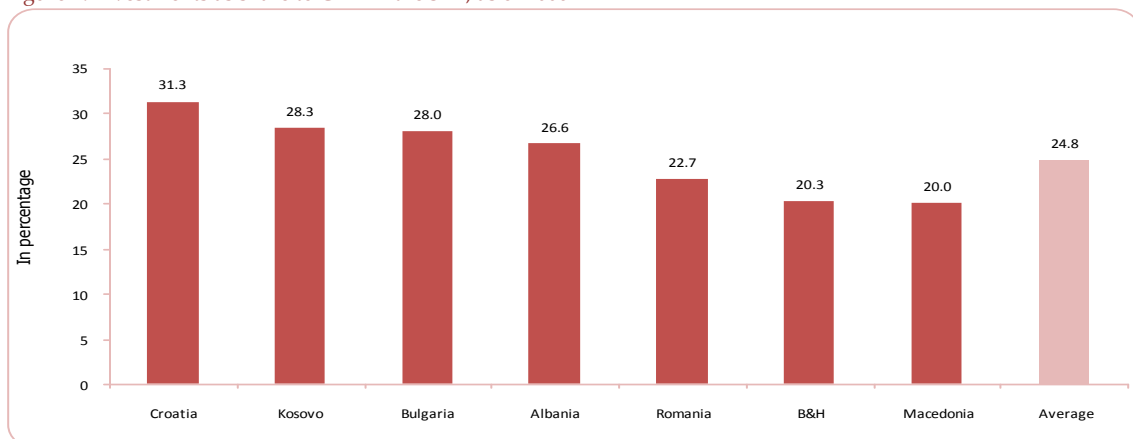
Figure 3. Kosovo Real GDP by components, at constant 2002 price (2000-2006)



Source: IMF (2006).

Based on the GDP components, consumption representing an annual growth of 2.0% stood at euro 2.8 billion in 2006. As share to GDP, consumption shows a continuous decline from its peak at 169% in 2000 to 115.3% of GDP in 2006 (Figure 3). Due to higher consumption over GDP, the domestic savings in Kosovo are negative accounting for 15.3% of GDP. Standing at euro 690 million in 2006, overall investments boosted with 14.0% against 1.3% in 2005. Apart from the increase in terms of volume, the investments increased also as a share to GDP at 28.3% in 2006, which is among the highest in the region (Figure 4). The sources of investments in Kosovo are the banking sector loans and foreign direct investments. On average, each year since 2002 the flow of the banking sector loans extended to the domestic economy accounted for around euro 140 million and the majority is directed to the private companies. The foreign direct investments in 2006 are estimated at 266 million compared with euro 59 million in 2005. With exports and imports of goods and services amounting at euro 244 million and 1.324 million, respectively, Kosovo net exports in 2006 amounted at euro -1.080 million. The high Kosovo trade deficit had the largest negative contribution to GDP.

Figure 4. Investments as share to GDP in the SEE, as of 2006



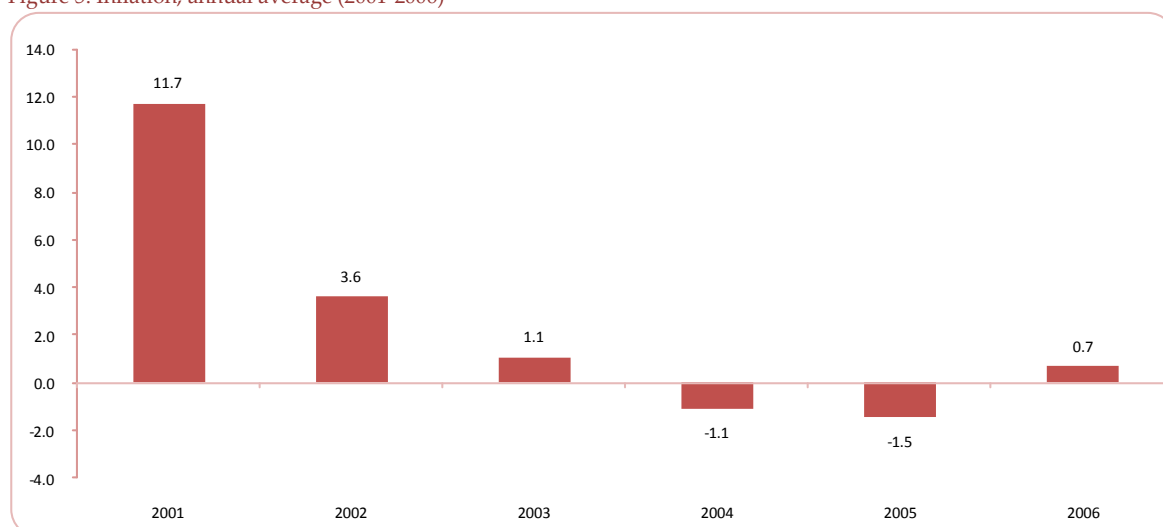
Source: EBRD (2006), CBAK (2006).

Note: The data for B&H are as of 2004, for Kosovo as of 2006, and for other countries as of 2005.

3.1.2. Prices

Downsizing of the international community presence in Kosovo, bringing the decline in the aggregate demand has pressured downwards the overall level of prices, possibly depreciating the real effective exchange rate. This may be considered as a positive sign with possible implications in terms of increasing the competitiveness and export promotion. Additional reason that supports price stability is the fact that Kosovo economy is fully euroized. As figure 5 depicts, the price level since 2002 accounted to be broadly stable. After the deflation of 1.5% in 2005, the annual average inflation in Kosovo for the year 2006 stood at 0.7%. In terms of categories composing the CPI, the pace of the prices at a large scale is affected from the food and nonalcoholic beverages which in 2006 grew with 0.7%, against -3.9% in 2005. The considerable impact of food prices in the CPI can be explained with high participation of food in the consumer basket.

Figure 5. Inflation, annual average (2001-2006)



Source: IMF (2006), SOK (2007).

Regarding the oil prices, which affected price stability globally, they grew with 10.0% in 2006. The increase was lower than in 2005 (13.9%). Having into consideration the high international presence in Kosovo, the rental prices in 2000-2003 period boosted, by attaining double digit figures. While, since 2004, with the reduction of the international staff and partially due to increase of supply, these prices declined substantially. Explicitly, the rental prices still continue to decline, easing with 0.4% in 2006, but sizeable lower than in the previous years (-7.4% in 2004, and -1.7% in 2005).

3.1.3. Unemployment

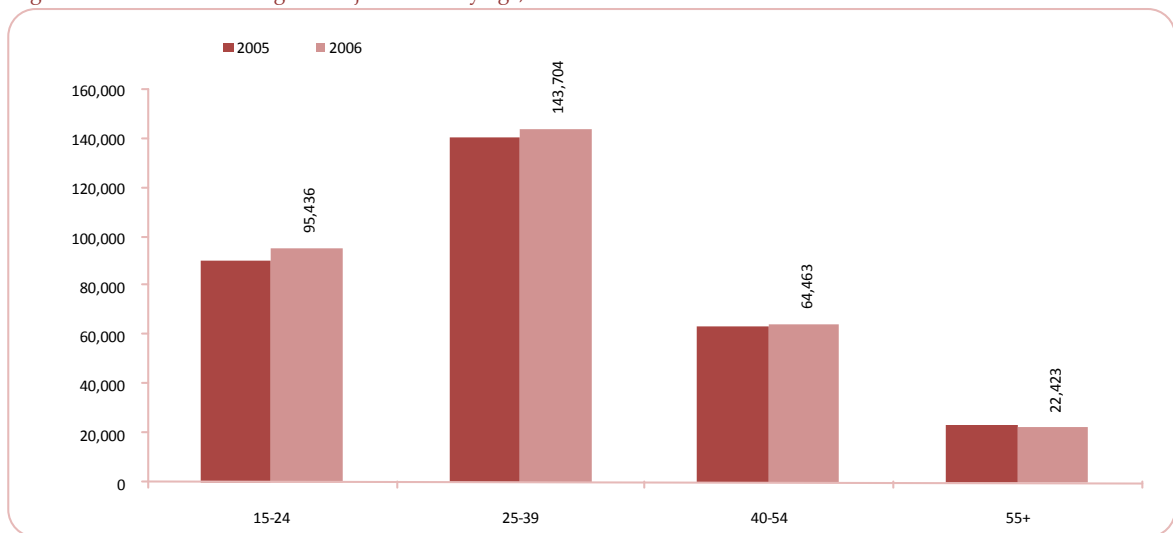
Unemployment in Kosovo remains high. Nevertheless, there are different estimates concerning the rate of unemployment. According to the IMF, the unemployment rate stands at around 30%, while according to the Labour Market Statistics, the unemployment rate accounts for 41.4%, which is

among the highest in the region.⁴ While according to the same survey, the labour force participation rate in Kosovo in 2005 is around 50.0% of the working age population.⁵

One of the factors hampering the private sector competitiveness in Kosovo is high relative cost of production (e.g., labour costs).⁶ However, with the exception of some companies in the public sector, having into consideration flexible labour market policies, the absence of social programs for unemployed, no strong labour unions, and at the same time high unemployment rate, may put pressure on the wage adjustments downwards which will have positive implications in increasing the competitiveness, attracting foreign direct investments and export promotion.

The outstanding number of registered jobseekers at end 2006 stood at 326 thousand persons, of which 46.7% are females. As presented in the Figure 6, the jobseekers aged between 25-39 constitute the dominant share of job seekers (44.1%). Compared to the previous year, in 2006 the total number of this category stood at around 144 thousand. Apart from the increase in above mentioned category, approximately the same increase in the number of registered jobseekers is recorded in the age categories 15-24 and 40-54.

Figure 6. Number of new registered jobseekers by age, as of 2006



Source: Ministry of Labour and Social Welfare (2006).

The outstanding number of registered jobseekers in Pristina totals 66.933, followed by Mitrovica region with 62.871. However, it should be taken into consideration high population density in Pristina. Only in these two regions are concentrated around 40% of total number of jobseekers. Excluding Prizren region, where total number of registered jobseekers amounts for 53.255, remaining Kosovo regions does not cross the level of 40 thousand jobseekers. Actually, the highest number represents Gjakova region with 37.564 and the lowest is recorded in Ferizaj/Urosevac region with total number of 33.868 registered jobseekers.

⁴ Unemployment rate is expressed as percentage of the unemployed persons in the labour force.

⁵ The labour force participation equals to sum of employed persons and unemployed persons to working age population.

⁶ IMF Aide Memoire, February 2007

3.1.4. Privatization

During 2006, the Kosovo Trust Agency (KTA) continued to decisively accomplish the privatization of the Socially Owned Enterprises (SOEs), a process initiated with the intention to enhance the value and corporate governance of SOEs and POEs. In 2006, the bid results for 11 waves were announced, that incorporate about 213 NewCos (New Companies)⁷ to be successfully privatized, of which 15 went through special spin-off method of privatization. According to the bid offers of the provisional winners, the amount to be accumulated from these proceeds is expected to be around euro 154.0 million. Among others, an important achievement during 2006 was the ratification of the contract for the NewCo Ferronikeli, as a very promising production company in the mining sector with potential impact in the Kosovo economy in terms of employment and exports.

Taking the stock of the privatization process, at end-2006, the number of the total privatization waves launched reached 22, with over 350 NewCos tendered. However, the number of the sale contracts signed was 216, which is the total number NewCos to be considered privatized completely. The amount accumulated from the privatized companies was euro 275.0 million - amount deposited at the CBAK as of end 2006. The revenues increased constantly during 2006, so the cumulative amount accounted for 11.3% of the GDP – a level comparable with countries in the region (for example, in 2005 this level was 11.4% in Albania, 17.0% in Croatia, 21.5% in Bulgaria, etc).

Among 216 contracts ratified up to end-2006, sixteen correspond to the companies privatized through special spin-off procedure, accounting for 30.0% of the total privatization proceeds. The conditions attached to the special spin-off contracts (investment and employment commitments) strengthen the importance of the privatization process. The amount of the investment commitments related to these contracts reaches euro 121.8 million, while the total number of the employment guarantee is about 6,000 in all sixteen companies. The implementation of the conditions within the time-limit set in the special spin-off contract is further monitored and examined by the KTA.

3.2. Fiscal Sector

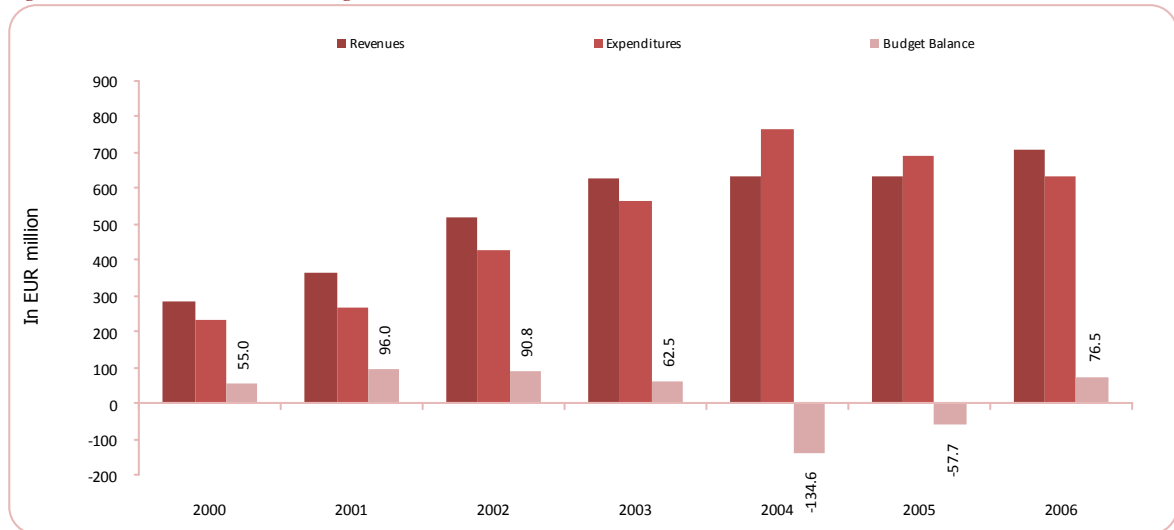
Kosovo continues to pursue fiscal policies based on a modern tax system. The budget revenues have reached at around 30% of GDP, making Kosovo to compare well with other countries in the region. Facing specific constraints the government shall pursue tight fiscal policies in order to maintain a balanced budget, or to limit the deficit to an amount compatible with previously accumulated surpluses. For example, two successive budget deficits incurred in 2004 and 2005 were financed by the budget surpluses incurred in the years prior to 2004.

Further reforms are needed in terms of broadening the tax base and adjustments in expenditures such as the wage bill, goods and services and subsidies, in order to increase capital expenditures and address the investments needs necessary to face successfully the structural problems of the economy. In addition, after the status resolution, sound fiscal policies must be implemented to safeguard the budget sustainability from the additional burdens that may arise from the cost of

⁷ The KTA can create a new company ("NewCo") in the form of a Joint Stock Company or a Limited Liability Company and transfer to these new companies part or all of the assets of the old socially owned enterprise

transfers of functions from UNMIK, not to mention the external debt that Kosovo may inherit from ex-Yugoslavia.

Figure 7. Kosovo Consolidated Budget (2000-2006)



Source: MEF.

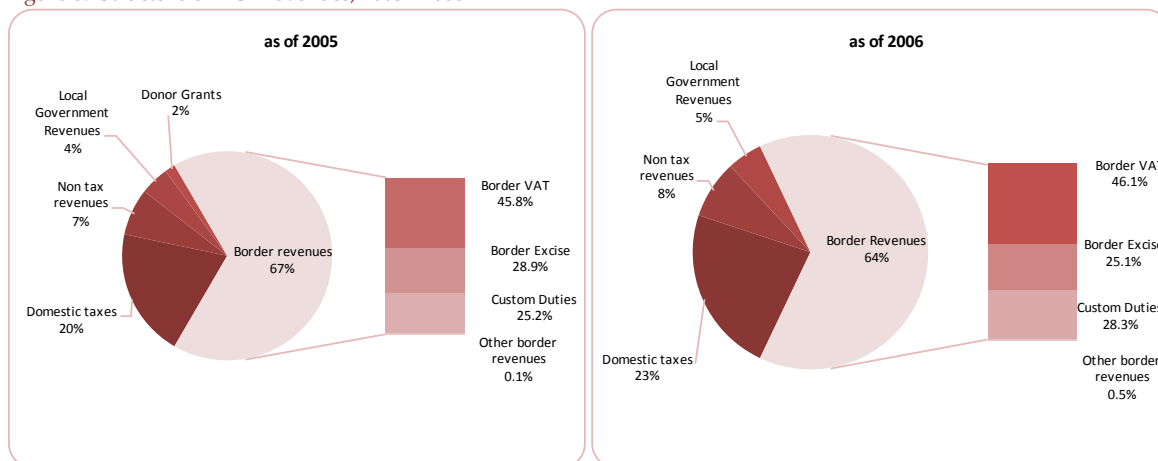
Following deficits in 2004 and 2005, Kosovo Consolidated Budget in 2006 recorded a surplus of 3.4% of nominal GDP (euro 76.5 million). The surplus was not in line with the planned budget that foresaw a deficit of 3.1% of nominal GDP (euro 71.1 million). The budget surplus resulted from, on one hand, the additional revenues (budget revenues exceeded the planned figure by 8.5% reaching euro 712 million compared to a forecast of euro 656.2 million), and on the other hand, a large under-spending of budgeted capital expenditures. Indeed, only 70% of the planned capital expenditures were actually spent.

The additional revenues were partly driven by the imposition of a special dividend scheme on the telecommunications monopoly and by a better collection of domestic taxes that recorded 30% higher than planned. The better tax collection is a favourable indication since it suggests an improvement in the administrative capacities in tax collection. On the other hand, the level of under-spent capital expenditures (euro 56.75 million) appears to be the consequence of inappropriate budgetary proceedings in some spending agencies. The negative effects of the under-spending are not to neglect, since the economy will not benefit from the multiplier effect of capital investments.

3.2.1 Budget Revenues

Budget Revenues in 2006 amounted to euro 712 million, an increase of 11.5% compared to the previous year. In nominal GDP terms, total revenues accounted for 31% of GDP, a three percentage points (pp) increase compared to 2005. The largest share of the consolidated budget revenues comes from taxes, representing 87% of total revenues, followed by non-tax revenues and municipally collected taxes with 8% and 5%, respectively.

Figure 8. Structure of KCB revenues, 2005 - 2006



Source: MEF.

Reaching euro 456.4 million, border taxes marked an increase of 7.1% compared to 2005, but as a share to total revenues, declined from 67% to 64%. A contributing factor to the increase in the volume of border taxes may be the increased volume of imports (by 11.4%) that may have been partly facilitated by the Free Trade Agreements (FTAs) with Albania and FYROM with which imports marked an increase of 28.7% and 18.4%, compared to 2005. However, the increase in the import volume was not reflected entirely in the increase in border taxes, which might partly be due to the negative impact that the FTAs may have had on border taxes through the tax exemption of 10% for goods imported from countries with FTAs in force.

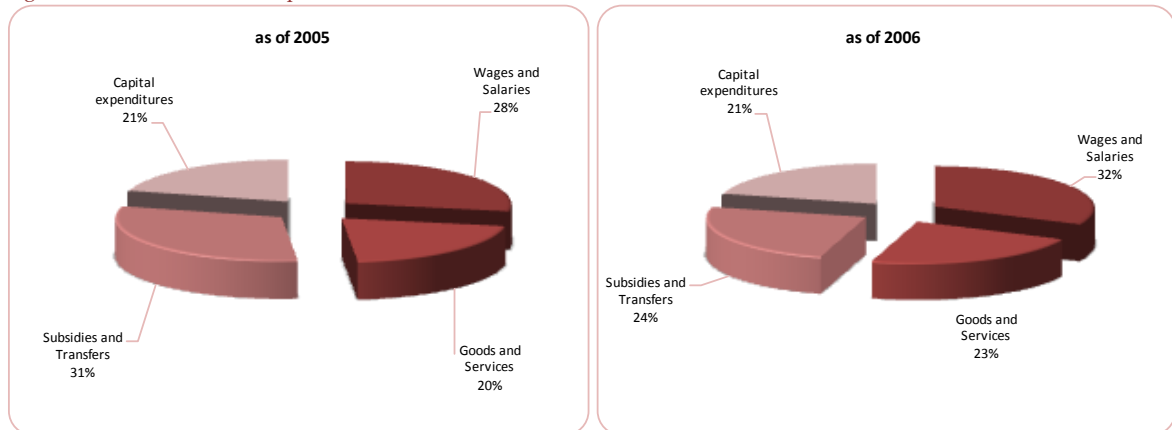
Border taxes, despite the decline as a share of total revenues, remain the category that represents the main source of budget revenues. The large share of border taxes in total budget revenues mainly results from the high reliance of the Kosovo economy on imports, and especially due to the Kosovo tax system requiring the VAT for imported goods to be paid at the border. The VAT collected in the border represents the largest category (46.1%) of border revenues.

A substantial increase was noticed in 2006 in domestic taxes collection, which rose from euro 127.2 million in 2005 to euro 164.1 million in 2006. This represents a growth of 29% in volume, while as a share to total revenues the increase was by 3 pp. The main categories in domestic taxes are the domestically collected VAT that accounted for 29% of total, followed by corporate income tax and personal income tax representing 19% and 18% of total domestic taxes, respectively.

3.2.2 Budget Expenditures

Amounting to euro 635.5 million, budget expenditures decreased by 8.7% compared to 2005, maintaining the downward trend since 2005 when budget expenditures decreased for 9.5% compared to 2004. As a share to nominal GDP, budget expenditures decreased from 31% in 2005 to 28% in 2006. The decline in the total budget expenditures in 2006 resulted from the decline in subsidies and transfers to POEs by 27.3%. Subsidies and transfers declined also as a share to total expenditures (from 30% to 24%).

Figure 9. Structure of KCB expenditures, 2005 - 2006



Source: MEF.

The structure of budget expenditures changed in favour of wages and salaries. Although the 'Medium-Term Expenditure Framework 2006-2008' foresees that the number of civil servants will decrease by 10% until 2008, the budgetary wage bill, in terms of volume, increased by 4.8% in 2006 compared to 2005.⁸ Therefore, after a sharp decline in transfers and subsidies, namely to public owned companies, that in 2005 represented the largest share of budget expenditures, wages and salaries became the largest category in budget expenditures, reaching 32% of total budget expenditures (representing an increase of 4pp in the structure of expenditures). This shows substantial difficulties to control the growth of current expenditures. Simultaneously, despite the foreseen increase of capital expenditure quoted in the 'Medium-Term Expenditure Framework 2006-2008', capital expenditures marked in 2006 a decrease of 8.1% compared to 2005, with the attached negative effects on the economy as already mentioned.

Regarding the approved budget for 2007, a deficit of euro 34.2 million or 1.5% of GDP is foreseen. The expected budget deficit results from both, the expected decrease in budget revenues and the expected increase in budget expenditures. Budget revenues are expected to account for euro 682.8 million in 2007, representing a decrease of 4.1% compared to the revenues collected in 2006, whereas, expenditures are expected to reach euro 717.4 million, implying an increase of 12.9%. The structure of budget revenues and expenditures does not appear to be subject to significant changes in 2007. The border taxes will remain the largest category in the budget revenues representing 64.1% of total, while wages and salaries will remain the largest category in the budget expenditures representing 28.4% of total.

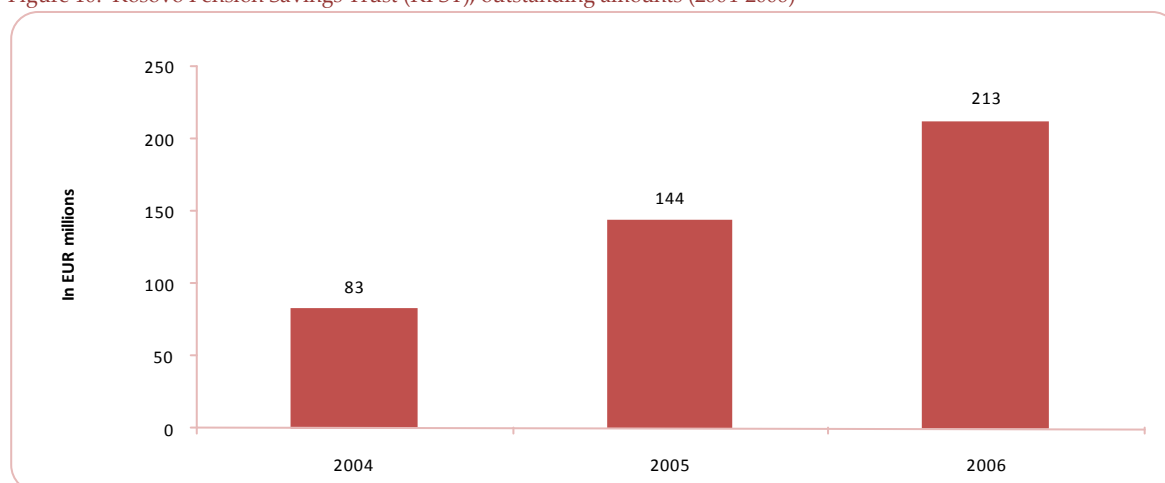
3.2.3 Pension Scheme

The social security scheme comprises of the Basic Pension Scheme and the Individual Savings Pension Scheme. The Basic Pension Scheme is financed by the Kosovo Consolidated Budget and consists of an amount of euro 40 that is paid to the inhabitants older than 65 years. The Individual Savings Pension Scheme, introduced in 2002, is managed by the Kosovo Pension Saving Trust (KPST), based on compulsory contributions from employers and employees (5% each).

⁸ MEF (2006).

The mandatory nature of the pension contributions paid in the Individual Savings Pension Scheme, in accordance with the international statistical classification standards, classifies the KPST as a “social security fund” and, as such, part of the “general government”.⁹ The outstanding amount collected through this scheme stood at euro 213 million at end-2006, representing an increase of 49% compared to 2005.

Figure 10. Kosovo Pension Savings Trust (KPST), outstanding amounts (2004-2006)



Source: KPST.

An increase was also noticed in the number of contributors that increased by 17%, reaching to around 215 thousand in 2006 (from around 183.7 thousand in 2005). The increase in the number of contributors partly results from improvements in the way that employers report their employees for pension contributions and also due to the increased number of persons employed outside the “informal economy”. The funds collected through the scheme are continuing to be invested in highly graded foreign financial market instruments, emphasizing the security principle of these assets. As such, apart from the financial sector, the government sector remains the net creditor of the external sector.

3.3 Financial Sector

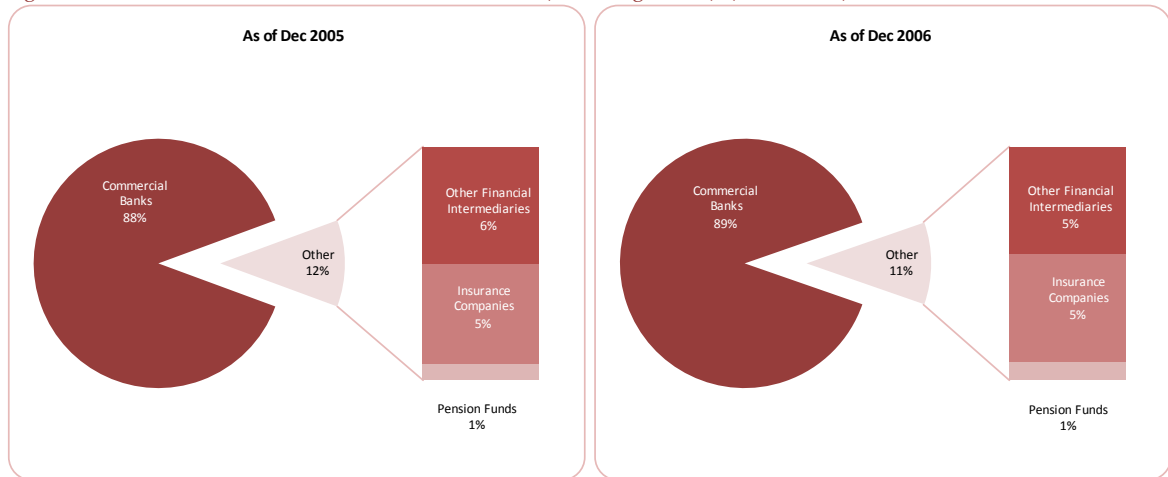
3.3.1 General Characteristics

The total financial corporations’ assets (excluding CBAK) at end 2006 reached euro 1.270,7 million, an increase of 17.8% compared to end 2005. Financial sector in Kosovo continues to be dominated by commercial banks that manage about 89.0% of the total financial sector assets and the structure did not experience any substantial change (Figure 11). The remainder of the assets is shared between insurance companies (5.0%), other financial intermediaries (5.0%), and pension funds (1.0%).¹⁰

⁹ Being considered as part of the general government, KPST is not included in the financial sector.

¹⁰ The Kosovo Pension Saving Trust (KPST) is considered to be part of General Government – defined as a social security – and consequently is not included in the financial sector.

Figure 11. The structure of the financial sector in Kosovo (excluding CBAK), (2005 – 2006)



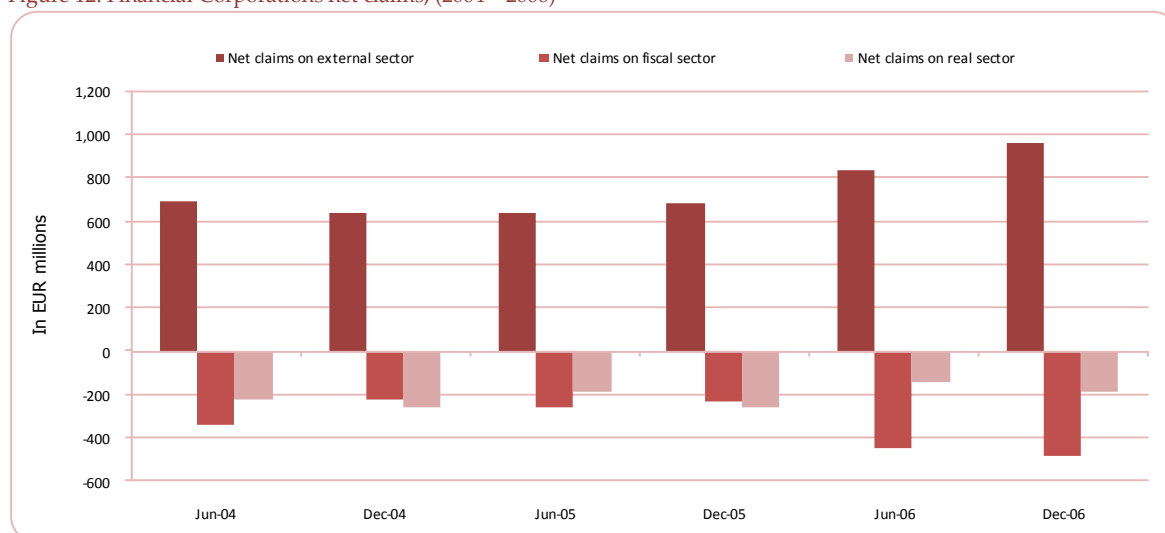
Source: CBAK (2007).

In terms of the number of financial corporations, 6 commercial banks, 9 insurance companies, 1 private pension fund, 16 other financial intermediaries (OFIs) and 23 financial auxiliaries were operating in Kosovo at the end of 2006. The other financial institutions are mainly micro-lending institutions involved exclusively in lending activity with no permission to take deposits, while the financial auxiliaries usually act as money exchange bureaus, and their share to total financial sector assets is negligible.

Supported by the increase in the government sector deposits at CBAK (mainly privatization proceeds), the net foreign assets (NFA) amounted at euro 965.2 million at end-2006. The total amount of NFA increased by 41.0% compared to 2005, reaching their historical peak, which brings the financial sector in Kosovo to remain a net creditor of the external sector. The CBAK as the main player managed about 66.3% of the total NFA of the financial corporations. In general, the observed financial capital outflow is the consequence of the necessity to keep safe large amount of funds (assets of KPST, proceeds of privatization), some of them on the short range (privatization funds), while there is few investments or placement opportunities in Kosovo.

Since the financial sector has no claims on the fiscal sector, the government deposits in financial corporations (mainly the CBAK) represent the only link between these two sectors. Namely, the net claims on the fiscal sector in 2006 amounted euro 482.5 million, compared with euro 230.0 million a year before (Figure 12). This is attributed mostly to, (i) the privatization proceeds during 2006 and, (ii) the increase of the government deposits in CBAK (due to budget surpluses for the fiscal year 2006). Indeed, the revenues from privatization as of Dec 2006 reached euro 275.0 million, accounting for 58.4% of the government sector deposits at CBAK.

Figure 12. Financial Corporations net claims, (2004 – 2006)



Source: CBAK (2007).

The financial sector linkages with the real sector (mainly nonfinancial corporations and households) consist of claims and liabilities. The claims on the real sector - mainly comprised from loans - increased by 23.3% compared to end 2005. The outstanding amount of financial sector loans in 2006 stood at euro 694.3 million, representing a yearly increase of 22.5%. Liabilities to the real sector amounting at euro 888.6 million in 2006, classify the financial sector as net debtor of the real sector (Figure 12).

3.3.2 Developments in the Banking Sector

Network and composition. Kosovo's banking sector is composed of six privately owned commercial banks, operating through 220 banking units throughout Kosovo. The banks are focused in traditional banking activities and their services are limited to the activities related to deposits and loans. However, banks have recently shown ambition to expand the variety of products and services provided to the clients.

At the end of 2006, six commercial banks were operating in Kosovo, two with full foreign ownership and the remaining four with majority domestic ownership. In March 2006, the CBAK revoked the license of Credit Bank of Pristina (CBP) after reviewing that the CBP no longer fulfilled the necessary conditions in terms of capital and liquid assets to protect its depositors. The liquidation process of CBP is ongoing. All depositors received immediate refunding up to euro 3,500, which brings about 97% of the number of depositors to be fully and quickly paid back. Further payments are made according to asset recovery process.

Despite the closure of this domestic bank, other banks continued to operate effectively and no strong contagion effect was evident during the period. The total banking deposits did not decline, but they experienced a 'freeze' during the next three months. However, after the short 'freezing' period the deposits continued to grow with the average monthly growth rate of 1.7% (same as the monthly average growth in 2005). Moreover, at end-2006 yearly increase of the total deposits was

10.7%, while the remaining deposits of the CBP since March 2006 were categorized as other liabilities in the balance sheet of the total banking sector.

The commercial banks are still expanding their branching network all over Kosovo. At the end 2006 there were 220 banking units, with about 2,416 employees. The banking network of the six operational banks at end-2006 accounted for 15 units more than at end-2005, with about 280 more employees. Evidently, about 30.0% of the branching network, including the head offices, is concentrated in Pristina, the capital of Kosovo. Follows the Gjilan region with 22.3% or 49 banking units, while other units are somehow evenly spread among three remaining main regions: Peja/Pec, Prizren and Mitrovica.

By the end of 2006 the number of Automated Teller Machines (ATMs) increased for 21 (numbering 123) and the number of Point of Sales (POS) increased for 64 numbering 1470 in total. Number of current accounts increased to 664,734 from 635,394 in 2005, what indicates that about 30% of the population in Kosovo has a bank account. The introduction of the e-banking in 2005 showed some positive results in 2006, since 3,316 accounts were using e-banking at the end of 2006, compared to only 837 at end 2005. As a result, the number and the amount of transactions carried out through e-banking increased five times compared to end-2005 (11,588 transactions totaling euro 25.8 million, as of end-2006). The e-banking service is provided by three banks only.

The increase of the banks confidence in the domestic market is shown by the introduction of new products during 2006. The four largest banks started to offer loans with maturity up to 10 years, as well as mortgage loans. In addition, during the second half of 2006, one local bank began to issue Certificates of Deposit, a new financial instrument within the Kosovo banking sector.

Regarding the ownership structure of the banking sector, there were no changes in 2006. The two foreign banks continued to be the key players in the market, increasing their dominance in the banking sector, by managing about 71.2% of total assets. In addition, almost all the yearly growth of the banking sector assets was due to foreign banks (reaching almost 27.0%), while total assets of the domestic banks (excluding the failed CBP) compared to 2005 increased for 5.4%.

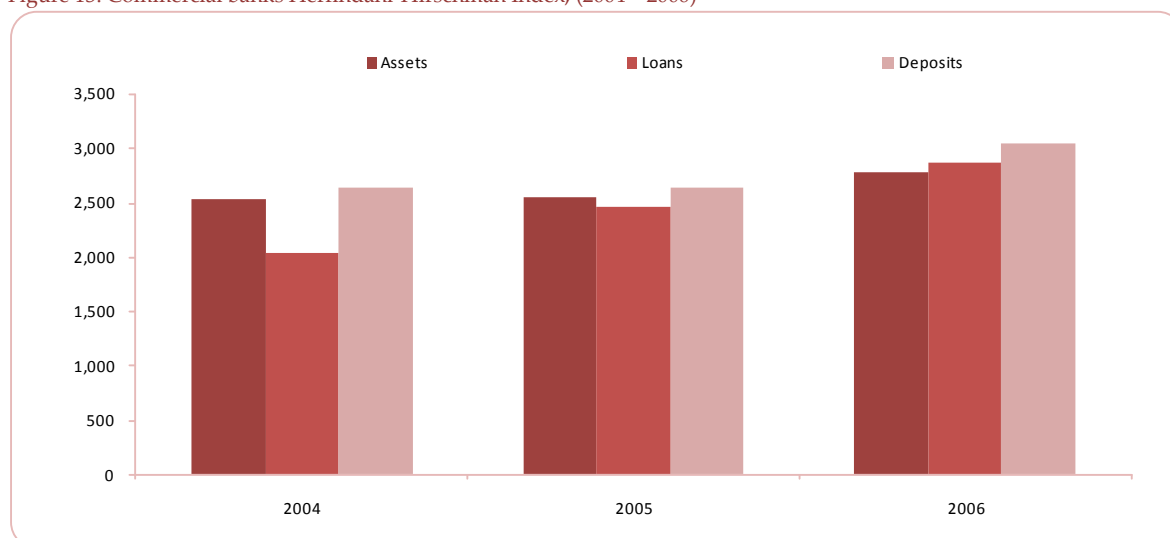
Table 5. Ownership structure of banking sector assets, in thousands of euro (2004-2006)

Description	Dec 2004		Dec 2005		Dec 2006	
	Amount	Share (%)	Amount	Share (%)	Amount	Share (%)
Foreign banks	500,832	61.6	652,866	66.3	828,604	71.2
Domestic banks	312,067	38.4	331,546	33.7	334,710	28.8
Total assets	812,899	100	984,412	100	1,163,314	100

Source: CBAK (2007).

Although the measures of concentration in the banking sector, such as the market share of the two largest banks (C2) and Herfindahl-Hirschman Index (HHI), may not conjecture the competitiveness in the market, both show that Kosovo banking sector is concentrated. The large share of the two foreign banks in the total loans (73.2%, as of end Dec 06) and deposits (75.1%, as of end Dec 06) illustrates the concentration of the Kosovo banking sector. Similar picture is shown when measuring the concentration of the sector by using HHI for assets, loans and deposits separately (Figure 13). The index shows that the market is more concentrated than in the previous periods, with a loan concentration at 2,871 points, and the deposits concentration standing at 3,047 points.

Figure 13. Commercial banks Herfindahl-Hirschman Index, (2004 – 2006)



Source: CBAK (2007).

Balance Sheet. Year 2006 recorded no significant changes regarding the structure of the banking sector assets compared to the previous year. Loans continue to represent more than half of the total banking sector assets, while deposits represent almost 80.0% of total liabilities.

With a yearly growth of 18.2%, the total banking assets at end 2006 amounted to euro 1,163.3 million. The ratio of total banking sector assets to GDP in 2006 increased to 47.7%, compared to a level of 41.7% in 2005. The ratio is higher than in some surrounding economies and is approaching the average of SEE countries - considering the Croatian case as an outlier with the ratio of 109% (See Box 1).

The banking sector increased its lending activity to the domestic market. The outstanding amount of loans represented 54.7% of total assets, showing an increase compared to 2005 (52.2%). Cash and balances with CBAK accounted for 12.3% of total assets of the banking sector, namely as a result of the mandatory liquidity reserves that banks must keep with the CBAK. Whereas, 29.4% of the banking sector assets were invested abroad (mainly placements in correspondent or parent banks abroad and liquidity placements in securities).

Table 6. Commercial banks balance sheet, in thousands of euro (2004 – 2006)

Description	Dec 2004		Dec 2005		Dec 2006	
	Amount	Share (%)	Amount	Share(%)	Amount	Share (%)
Cash and balances with BPK	116,490	14.3	131,738	13.4	143,528	12.3
Balances with commercial banks	186,009	22.8	221,936	22.5	243,105	20.9
Securities	112,281	13.8	82,946	8.4	99,428	8.5
Gross loans and lease financing	373,661	45.8	513,856	52.2	636,613	54.7
Fixed assets	15,878	1.9	16,933	1.7	22,872	2.0
Other assets	12,219	1.5	17,003	1.7	17,767	1.5
Total assets	816,538		984,412		1,163,314	
Balances from other banks	14,276	1.7	23,034	2.3	30,245	2.6
Debts to clients	695,932	85.2	843,048	85.6	930,537	80.0
<i>Deposits</i>	694,533	85.1	836,657	85.0	926,370	79.6
<i>Other borrowings</i>	1,399	0.2	6,391	0.6	4,167	0.4
Other liabilities	27,891	3.4	37,344	3.8	103,219	8.9
Subordinated debt	9,318	1.1	6,999	0.7	7,003	0.6
Own resources	69,122	8.5	73,988	7.5	92,310	7.9
Total liabilities	816,538		984,413		1,163,314	

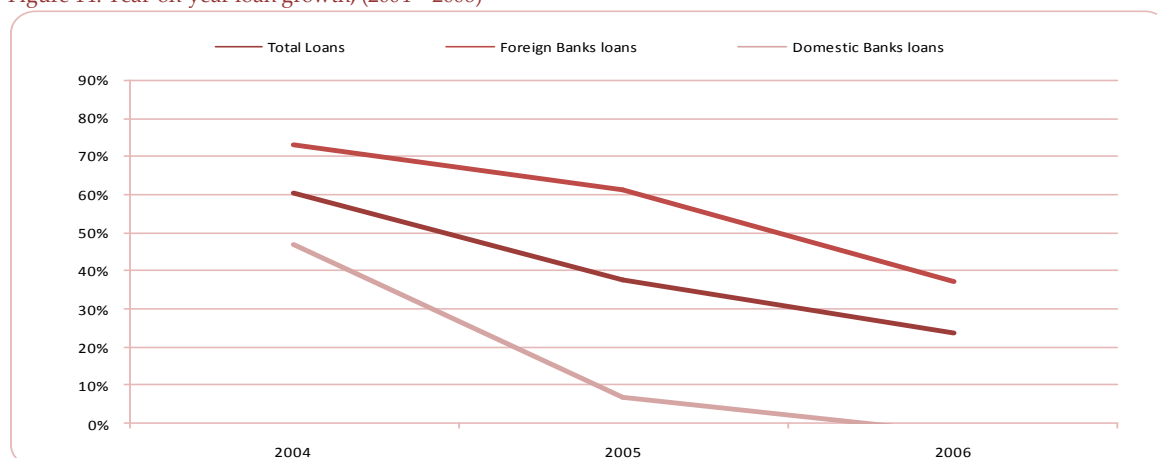
Source: CBAK (2007).

The liabilities did not experience any noticeable change in their structure (Table 6). Clients deposits remain the main component of banks' liabilities, though their share to total liabilities dropped to 79.6% at end 2006 compared to 85.0% in 2005. This decrease results from the liquidation of the CBP, since its deposits have been classified as 'other liabilities', which explains the growth of this item. The own resources of the banking sector increased by 24.8%, amounting euro 92.3 million at end-2006, following several capital increases. Nevertheless, due to the overall development of banking activities, the ratio of own funds to total liabilities remains almost unchanged.¹¹

At the end of 2006 the outstanding amount of banking sector loans reached euro 636.6 million, indicating a yearly increase of 24.0%. The ratio of banking sector loans to GDP improved too, representing 26.1% of the GDP in 2006, compared to 21.7% in 2005. This brings Kosovo to a better position compared to some of the countries in the region (See Box 1). Nevertheless, the year-on-year growth of loans, slightly above 20% in 2006, indicates that credit growth is calming down, compared to the roaring levels of more than 40% reached in the previous years (mainly because of the initial low base of the lending activity). The loan growth was mainly induced by the loan growth of the foreign banks, while in average the loan growth of domestic banks was negligible

¹¹ Own resources include: share capital, contingency reserve, profit/loss of the year and retained profit/loss.

Figure 14. Year-on-year loan growth, (2004 – 2006)



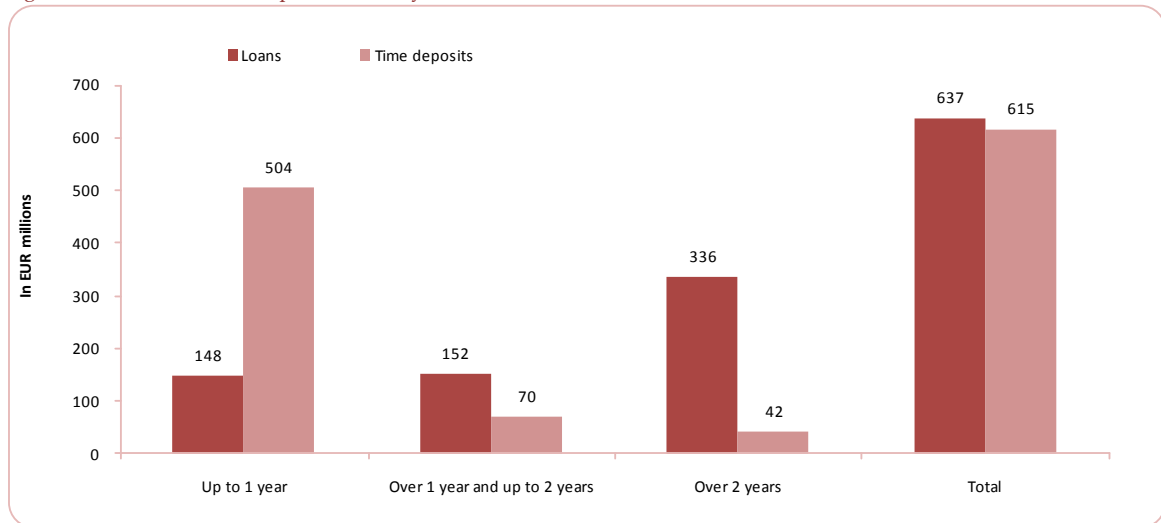
Source: CBAK (2007).

As of end-2006, non-financial corporations (NFC) still account for the largest share in total loans granted by the banking sector representing 77.1% or euro 490.5 million. In fact, majority of the lending activity targets small and medium size companies, as well as households, which represent the remaining 22.9%. With an increase of 26.5% loans to NFCs were the largest contributors to the overall loan growth. This is partly due to the involvement of some banks in the privatization of companies, while the amount of loans granted to households grew by 16%, reaching euro 146.1 million at the end 2006.

The sectorization of loans to NFCs by the economic activity remains similar compared to the previous years. Moreover, the diversification of the total loan portfolio in different industries is in line with the current situation of the economic activity in Kosovo. Trade as the main economic activity in Kosovo, continues to account for 62.7% of total outstanding granted loans, while 'other services' represent 13.8%. Credits to manufacturing firms stand at 23.4% of the total loans - with the energy and construction at 20.0%, and agriculture sector at only 3.4% (similar to 2005). In particular, a growth of 31.5% was recorded for loans granted to manufacturing sectors, which is a sign of a revival of activity in this sector.

The increase of the longer-term loans emphasizes the strengthened confidence of the banking sector towards the domestic economy. About 52.8% of the outstanding amount of loans at end 2006 had a maturity of longer than 2 years, while short-term loans up to 1 year represented only 23.3% of total loans. Loans with maturity over 2 years also increased more rapidly than short-term loans. As a result, the total increase of loans mainly occurs due to growth contribution of loans with maturity over 2 years by 20.6 percent, while the loans with a shorter maturity contributed only by 3.3 percent to the total loan growth.

Figure 15. Loans and time deposits maturity structure, as of Dec 2006

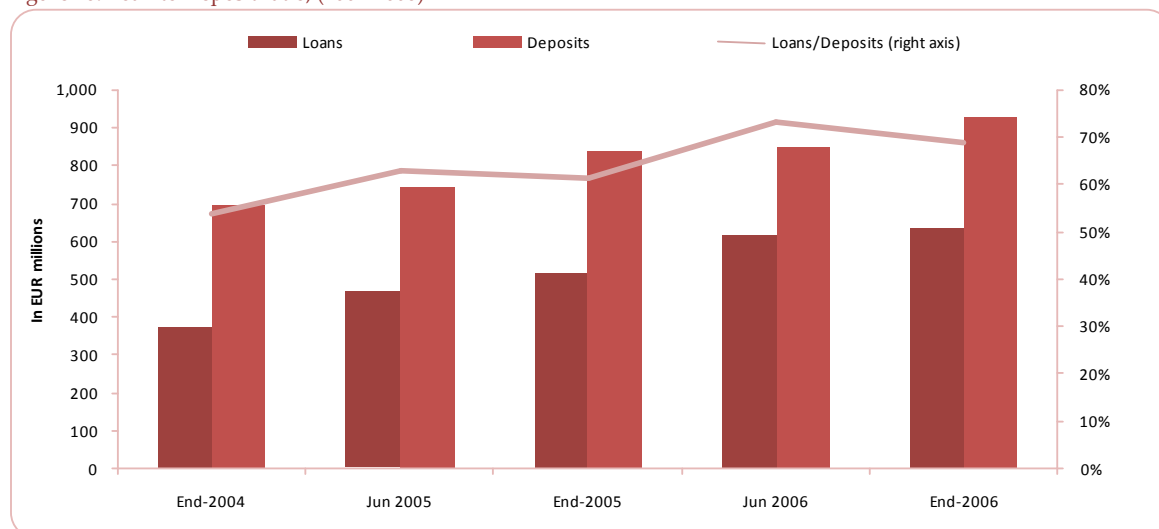


Source: CBAK (2007).

Loans are mainly financed by short-term deposits (transferable and with the maturity up to 1 year) which represent 88.0% of the total deposits. Nevertheless, term and saving deposits (deposits other than transferable) amount to euro 615.5 million covering 96.7% of the total amount of loans. Though at end of 2006 the volume of loans is slightly exceeding the volume of time deposits (Figure 6), the ratio is improving since in June 2006 time deposits accounted only for 84.0% of the total loans.

With a total amount of euro 926.4 million, the deposits grew annually by 10.7% which is a moderate increase compared to the annual growth of 20.4% and 35.2% in 2005 and 2004, respectively. However, it should be recalled that deposits collection had been initially boosted by the euro change over in 2002, while lending activity has developed step by step. In 2006, the deposit growth was slower than the loan growth, especially in the first half of the year, thus the loan to deposit ratio reached the peak of 73.0% in June 2006 (Figure 16). The opposite trend occurred during the second half of 2006 when the volume of the deposits increased faster than loans and the loan to deposit ratio fell to 68.7%. The ratio is within the regional countries interval, with Montenegro having the highest loan to deposit ratio of 89.6% and Albania the lowest at 28.3%.

Figure 16. Loan to Deposit ratio, (2004-2006)



Source: CBAK (2007).

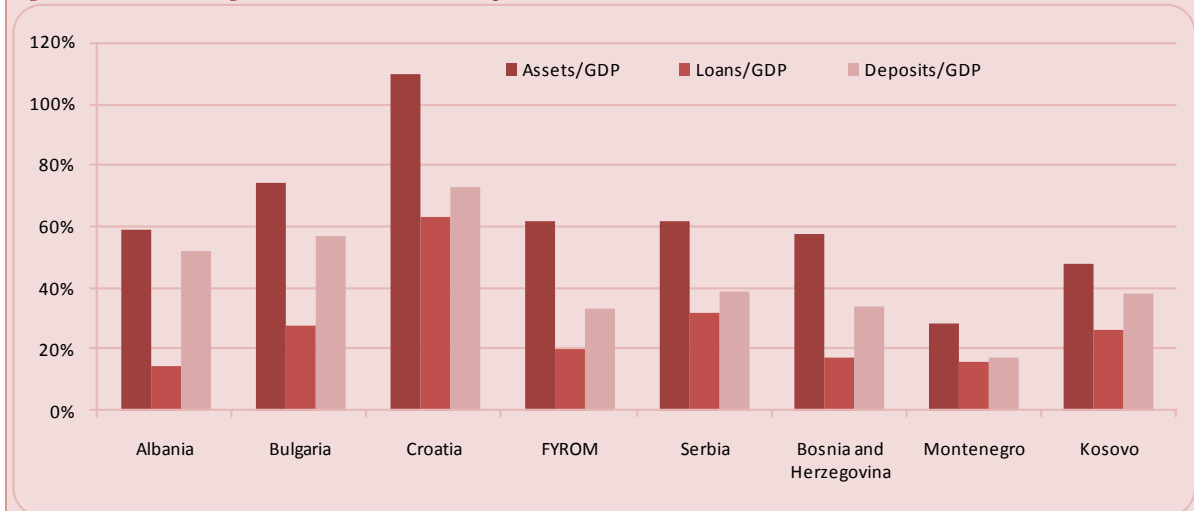
Deposits in banking sector are mainly held in euro currency, which is legal tender in Kosovo. Although the volume of non-euro deposits increased by 16.6%, they still represent only 3.7% of the total deposits. Moreover, banks do not grant loans in other currencies, so Kosovo banking system is not subject to exchange rate risk.

Deposits of the domestic sector, exclusively households, continue to be the main financing source of the banks' liabilities amounting at euro 517.1 million. Household deposits increased by 13.8% in 2006 over 2005, and sustained their positive contribution to the total deposits growth by 7.5pp. Furthermore, the household deposits increased slightly their share to total deposits to 55.8%, from 54.3% in 2005. Though the NFCs (primarily private corporations) are the main beneficiary of the banking loans, their deposits in the banking sector are growing with a slower pace. Their annual deposit increase was 6.3%, contributing with only 2.4pp to the total deposit growth. The amount of public NFC deposits stood at euro 217.6 million and were far ahead from those of the private corporations, which amounted euro 124.5 million. One public sector depositor, the Kosovo telecom company, which holds round 20% of the total deposits has acquired a systemic weight in the financial sector.

Box 1. Banking Sector assets, loans, and deposits as percent of GDP in the SEE countries

The banking system of Kosovo compares relatively well with the other countries of SEE regarding the size and the intermediation role of the banking system. The asset-to-GDP ratio of 47.7% ranks Kosovo close to the average of the SEE that stands at around 61.4%. Among the countries in the region, Croatia with 109% and Bulgaria with 74.1%, represent the countries with the highest ratio of banking sector assets to GDP, whereas the lowest ratio is recorded in Montenegro where total banking sector assets compose 28.6% of GDP.

Figure 17. Total banking sector assets, loans and deposits in SEE, as % of GDP*



Source: Business Monitor International (2006); EBRD (2005).

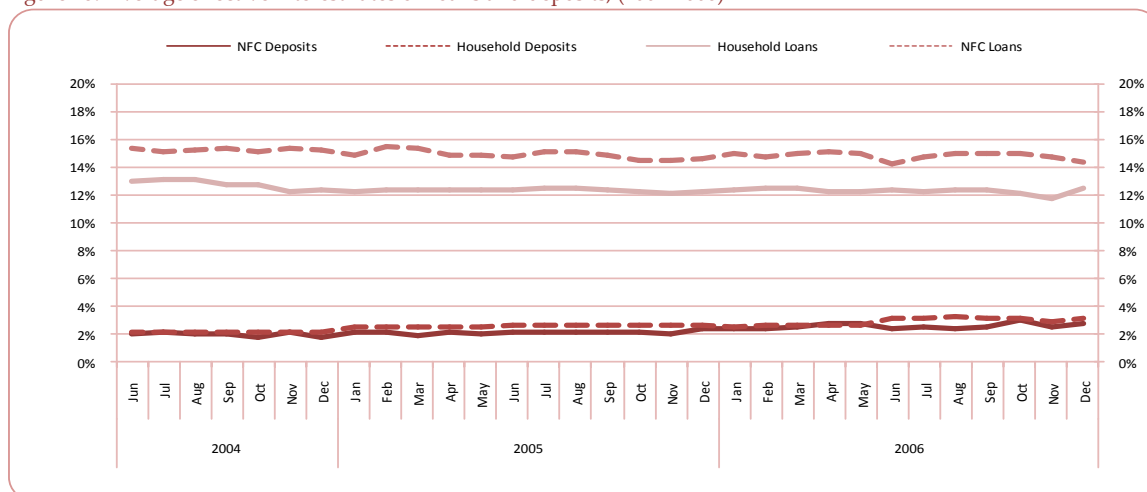
*Note: Data for SEE countries are as of 2005

Also the intermediary role of the banking system, measured by the ratio of banking sector loans and deposits to GDP, ranks the banking system of Kosovo in comparable position to other SEE countries. With the loan-to-GDP ratio of 26.1%, Kosovo ranks just below the average of the region that stands at 27.2%. The country that recorded the highest level of banking system intermediation is Croatia, where the share of loans in GDP accounted for 62.9%, whereas the lowest ratio is recorded in Albania and Montenegro where the loan-to-GDP ratio accounted for 14.7% and 15.7%, respectively.

In addition, the banking system of Kosovo compares well with other countries of the region also regarding the ratio of total banking sector deposits to GDP. In 2006, the total deposits-to-GDP ratio in Kosovo stood at 37.98%, which is just below the average of the region that accounted for 43.6%. However, taking countries on individual basis, Croatia (72.7%), Bulgaria (56.6%) and Albania (51.9%) were above Kosovo in terms of deposit-to-GDP ratio. The lowest deposit-to-GDP ratio was recorded in Montenegro where total bank deposits accounted for 17.6% of GDP.

Interest rates. At end-2006 interest rates on deposits stood at 2.97%, while lending rates at 13.37% (averaged across different products and maturities). The overall interest rate spread was continuously contracting, from 11.80% at end-2004 to 10.40% at end-2006. As Figure 18 illustrates, the interest rate spread for households is lower than for corporations. With the average of 3.18%, the household deposit interest rates were ahead of NFC deposit interest rates by 0.42 pp. While the average interest rates on household loans were for 1.90 pp lower than the interest rates on NFC loans that stood at 14.32% at end-2006.

Figure 18. Average effective interest rates on loans and deposits, (2004-2006)



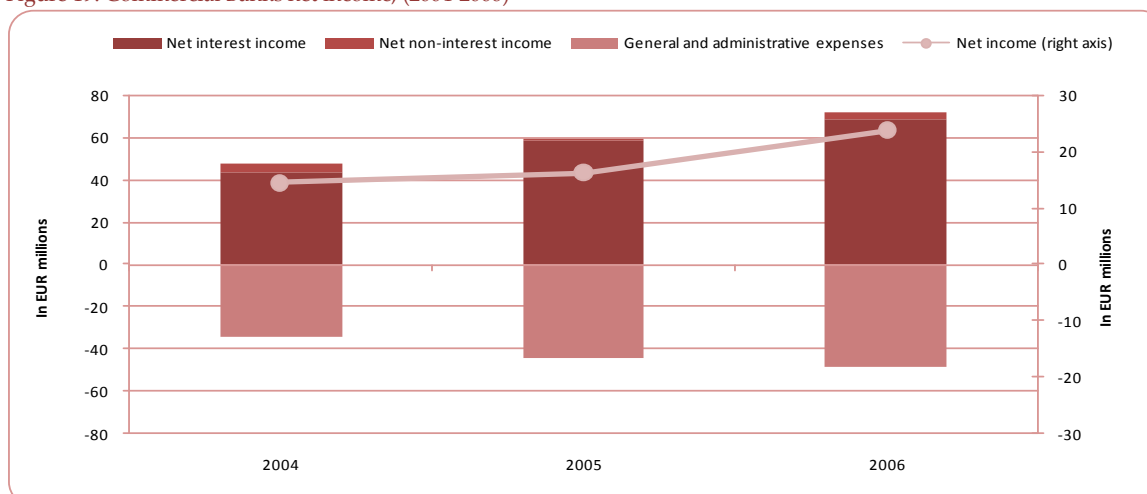
Source: CBAK (2007).

The interest rate spread of 10.40% is relatively wide and might be explained by high operational costs in the banking system, difficulties to assess credit risks, market concentration, high expectations on the return in foreign banks and uncertainty towards economic sustainability, not to mention deficiencies in the legal framework and enforcement mechanisms.

Income statement. The indicators obtained from the income statement reveal that the banking sector in Kosovo was profitable during 2006. Earning indicators maintain the level of previous years. However, there is space for improvement in lowering the administrative expenses, which continue to be high.

Banking sector in Kosovo closed the year 2006 with the net profit of euro 19.3 million. While in 2005 the profit after tax was only 4.4% higher than in 2004, in 2006 it increased by 42.6%. This was partly the result of slower growth rate of the expenditures in 2006 (15.6%) compared to income growth rate (20.8%) and of an improved credit risk management.

Figure 19. Commercial Banks net income, (2004-2006)



Source: CBAK (2007).

The total gross income of the banking sector at end-2006 reached euro 113.9 million. The banking sector profit is entirely due to interest related income on lending activities. As of Dec 2006, the interest income reached euro 88.8 million, or a yearly increase of 19.1%. The lending activity produces almost 90.0% of the banking sector interest income (or 69.7% of the total income), and 10.0% represents the income from placements in other banks and investments in securities. From the non-interest related activities, the generator of income are fees and commissions participating with 90.0% in total non-interest income (or 19.7% of the total income).

In 2006 the banking sector expenditures amounted at euro 90.1 million. While the income is generated mainly by interest related activities, the expenditures are mostly related to non-interest activities, such as provisions for loan losses and general and administrative expenses. Interest expenditures - mainly the interest paid to depositors - account for 20.0% of the total expenses. Non-interest related expenditures (other than general and administrative expenses) are mainly composed of provisions for loan losses that cumulated to euro 16.0 million at end-2006 (about 19.4% more than in 2005). Other non-interest expenditures relate to depreciation of the fixed assets amounting at euro 5.6 million. However, more than half of the total expenditures are general and administrative expenses (about 53.7%). These expenditures were higher during 2006, yet their increase was smoother than during 2005 when they accounted for 56.2% of the total expenses. This is positive development, if we take into consideration the achieved expansion of the banking sector with regard to personnel, branching network, etc.

Performance indicators. A prompt increase of after tax profit by 42.6% and a less rapid increase of the total average assets by 20.8%, slightly improved the banking sector return on average assets (ROAA) to 1.8% in 2006. Regarding the return on average equity (ROAE), it has reached an historical peak at 23.1%, which is the highest compared to the countries in the region (Box 2). This increase in ROAA and ROAE results from the profits of three banks, among which the two foreign ones.

Table 7. Bank performance indicators, in %, (2002 – 2006)

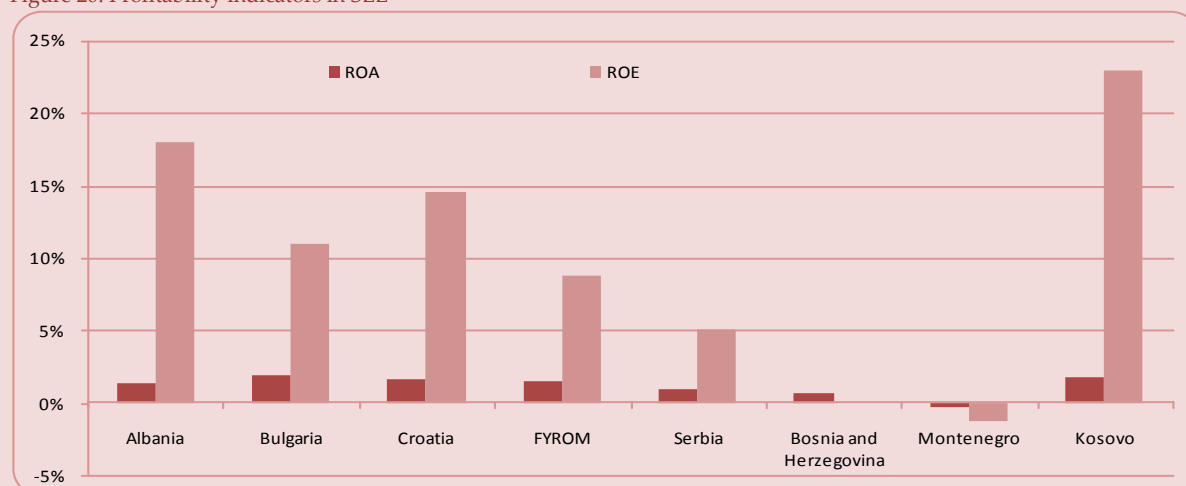
Description	2002	2003	2004	2005	2006
Return on average assets (ROAA)	0.60	1.30	1.90	1.50	1.80
Return on average equity (ROAE)	9.70	18.80	22.60	20.10	23.10
Net interest margin	3.00	4.30	5.40	6.00	5.90
Cost effectiveness	4.00	4.30	4.20	4.50	4.20

Source: CBAK (2007).

Box 2. Profitability of the Banking Sector in Selected SEE Countries*

In terms of profitability indicators, Kosovo ranks above the average of the region in both, Return on Assets (ROA) and Return on Equity (ROE). In 2006, Kosovo recorded a ROA of 1.8%, while the average of region stood at 0.8%. Taking countries individually, Bulgaria recorded the highest ROA at 1.8% same as in Kosovo. The lowest ROA ratio is recorded in Montenegro with a negative ROA ratio at -0.3%.

Figure 20. Profitability indicators in SEE*



Source: Business Monitor International (2006); EBRD (2005).

*Note: Data for SEE countries are as of 2005

Regarding the ROE ratio, Kosovo leads with the highest ROE ratio at 23% compared to other countries of the region that recorded an average ROE ratio of 6.5%. Within the countries of the region, Albania recorded the highest ROE ratio (17.9%), whereas the lowest ratio was recorded in Montenegro (-1.2%).

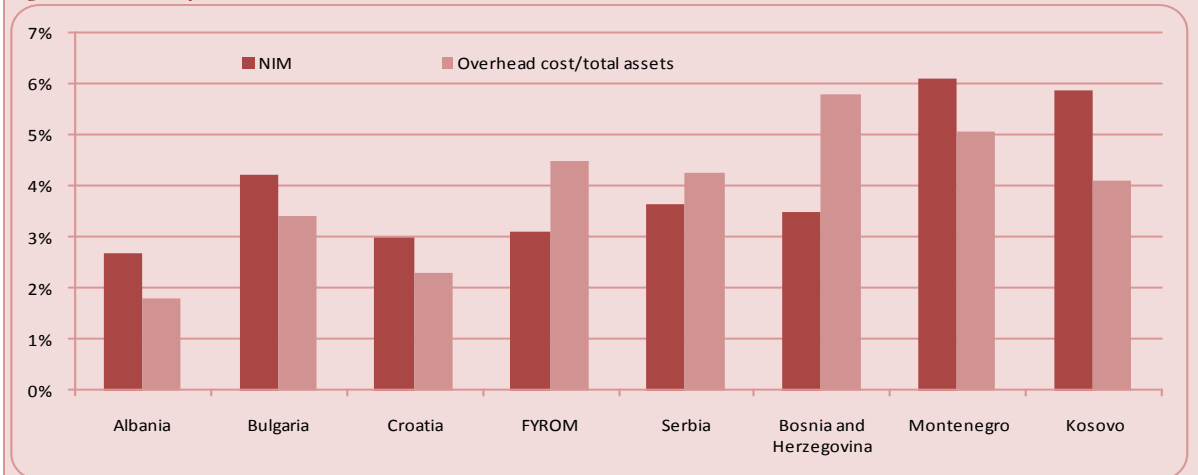
At end-2006 the net interest margin (NIM), which is the ratio of the net interest income to total assets, stood at 5.9% - comparable to 2005, and higher than in previous periods. The net interest income and total assets experienced fairly similar growth during 2006 compared to 2005 (16.5% and 18.2). The NIM is far ahead the countries in the region (Box 3), what might be the result of a fairly wide interest rate spread in Kosovo as well as the good performance of the largest banking institutions.

Cost effectiveness indicator, measured as ratio of general and administrative expenses to total assets, improved by falling from 4.5% in 2005, to 4.2% in 2006, due to the smoother increase of expenses. However, due to their present relatively high level, administrative expenses are expected to decline in the future, given the current structure of the banking sector, since administrative expenditures mainly relate to initial fixed costs and branch expansion. Furthermore, the ongoing restructuring of the domestic banks could also bring to a better control of operational costs.

Box 3. Efficiency of the Banking Sector in Selected SEE Countries

The banking sector of Kosovo recorded a NIM of 5.9% that is well above the region average that stood at 3.8%. According to this indicator, only banks in Montenegro stood at more advanced position than Kosovo, standing at 6.1%. The lowest NIM is recorded in the banking system of Albania (2.7%).

Figure 21. Efficiency indicators in SEE*



Source: Business Monitor International (2006); EBRD (2005).

*Note: Data for SEE countries are as of 2005

On the other hand, the banking system of Kosovo recorded less favourable results in terms of cost efficiency compared to the region average. The banking system of Kosovo recorded an overhead costs-to-total assets ratio of 4.2%, while the region average stood at 3.9%. The most efficient banks in terms of costs appeared to be the banks in Albania (1.8%), whereas the least efficient ones appeared to be the banks in Bosnia and Herzegovina (5.8%).

Commercial banks' loan portfolio could be assessed as being of a good quality, in general. While in 2005, past due and non-performing loans¹² accounted for 8.48% of the total loans in 2006 they represent only 7.34%. Nevertheless, the gross amount of non performing loans (which are the core of the risky assets) increased, since they accounted for 4.12% of the total loans in 2006, compared to 2.01% in 2005. This increase is partly due to the assets reclassifications required by the CBAK following its on-site inspections. After provisioning, the net amount of NPL is only euro 3.5 million. The situation of the NPLs in the Kosovo banking sector appears to be better compared to the countries in the region (Table 8). This could be the consequence of the absence of debts inherited from the former socialist economy, the cautious lending policies performed during the last couple of years, the weight of performing actors, and the prudent supervision.

¹² Past due are loans past due over 30 days and up to 90 days. While NPLs are loans past due over 90 days.

Table 8. NPLs as percentage of total loans, in SEE countries*

Country		Non-performing loans, in percent of total loans
Albania		2.3
Bulgaria		3.8
Croatia		7.2
FYROM		22.2
Serbia		23.8
Bosnia and Herzegovina		5.4
Montenegro		na
Kosovo	2005	2.0
	2006	4.1

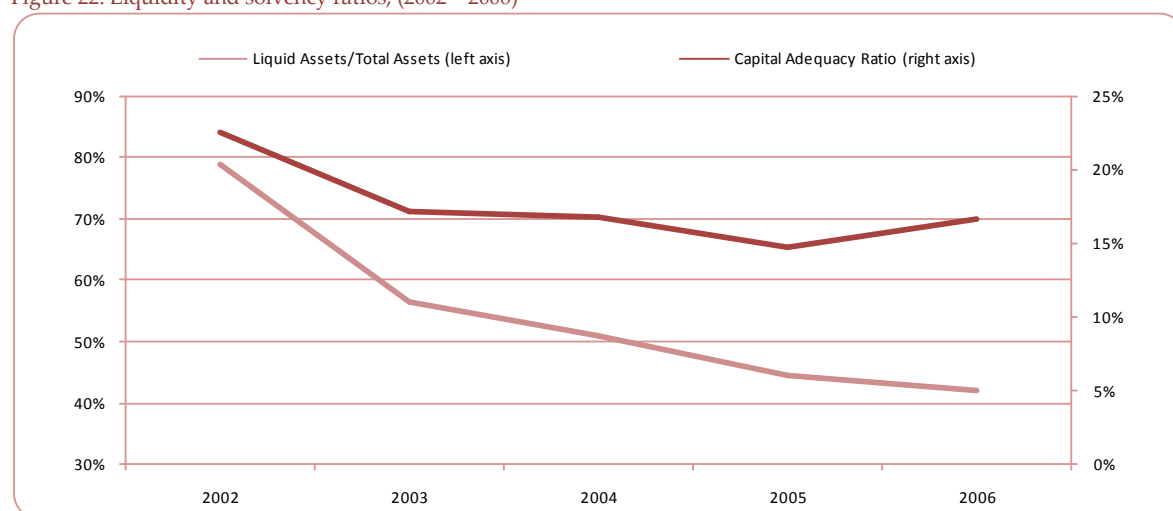
Source: EBRD Transition Report (2006) and CBAK (2007).

- Note: Data for SEE countries are as of 2005

Liquidity and capital adequacy. The selected indicators suggest that the Kosovo banking sector is liquid and solvent. The amended banking rule XXI required that by 31 December, 2006 the banks increase their minimum paid-in capital to euro 5.0 million. Thus the total banking sector capital at end-2006 accounted for 33.6% more than at end 2005.

The liquid assets of the banking sector amounted euro 486.1 million or 11.3% more than in 2005. However, the overall growth of the assets, mainly fuelled by the increase of the loans, evidently influenced the drop of the liquid assets to total assets ratio from 44.4% at end 2005, to 41.8% end of 2006. Still, the liquidity position of the banking sector remains strong. The share of the different components of liquid assets remains more or less similar. The main liquid assets is the balances with banks abroad, accounting for 50.0% of the total liquid assets, while cash and balances with CBAK account for 29.5% of the total liquid assets. As Figure 20 indicates, rapid fall of liquidity in 2002 and 2003 was followed by a lower declining trend in relation with the significant increase in the lending activity in the banking sector.

Figure 22. Liquidity and solvency ratios, (2002 – 2006)



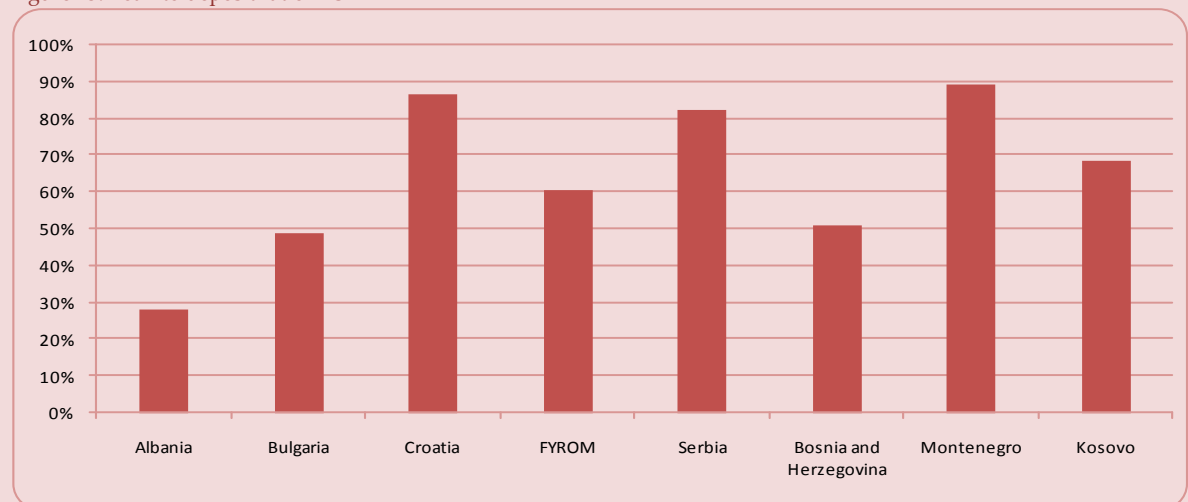
Source: CBAK (2007).

In addition to its high liquidity, the banking sector in Kosovo is solvent. At end-2006 the capital adequacy ratio (regulatory capital to risk-weighted assets) reached the level of 16.7%, compared to the ratio of 14.7% in 2005. It is above the minimum ratio of 12.0% defined in the Rule on Capital Adequacy applicable in Kosovo. This increase of ratio resulted from faster growth of the capital with respect to the risk-weighted assets (RWA) growth. Also, the regulatory Tier I capital accounts for 14.5% of the RWA, significantly higher than the minimum level of 8.0% defined in the banking rule I. The total capital (Tier I and Tier II)¹³ at end-2006 amounted to euro 117.2 million (33.6% more than in 2005), as a consequence of the increase of minimum capital of each bank to euro 5 million, set in the amended rule XXI of the CBAK banking rules, combined with regular increase of capital in line with the growing activity.

Box 4. Liquidity and CAR of the Banking Sector in Selected SEE Countries

With a level of 68.7% the loan-to-deposit ratio in Kosovo ranges slightly above the average of the region of 63.9%. The highest ratio is recorded in the banking system of Montenegro, where the loan-to-deposit ratio stood at 89.6%. Whereas, Albania recorded the lowest loan-to-deposit ratio in the region (28.3%) that is due to the low intermediation of its banking system.

Figure 23. Loan to deposit ratio in SEE*



Source: Business Monitor International (2006); EBRD (2005).

*Note: Data for SEE countries are as of 2005

Kosovo with a capital adequacy ratio of 16.7% ranges below the average of other countries in the region that stood at 23.1%. The capital adequacy ratio of Kosovo is the lowest in the region, whereas the highest is in Montenegro.

3.3.3 Insurance Companies Developments

In addition to commercial banks, in Kosovo, another important component of financial corporations are insurance companies. Though, with an amount of euro 62.9 million, insurance sector composes 5% of the total assets of the financial sector. At the end of 2006 there were nine insurance companies operating in Kosovo. Six companies are with mainly foreign ownership and three with full domestic ownership. Consequently, as in the banking sector, foreign ownership is

¹³ See the amended Rule I on Capital Adequacy for the definitions of the banks Tier I and II Capital and Risk Weighted Assets (RWA)

dominant in insurance industry with foreign held institutions managing almost 70.0% of the total assets (Table 9).

Table 9. Ownership structure of insurance sector assets, in euro thousands (2004 – 2006)

Description	Dec 2004		Dec 2005		Dec 2006	
	Amount	Share (%)	Amount	Share(%)	Amount	Share (%)
Foreign Insurance Companies	25,916	59.2	33,279	61.1	43,795	69.5
Domestic Insurance Companies	17,881	40.8	21,144	38.9	19,176	30.5
Total assets	43,797		54,423		62,971	

Source: CBAK (2007).

Deposits of the insurance sector in the depository corporations (CBAK and commercial banks) reached the amount of euro 45.3 million, or 26.6% more than in 2005. In particular, in 2006, insurance companies increased strongly their deposits in banks (by 34.8%). Consequently, the net foreign assets dropped to only euro 25,000 from euro 3.5 million at end-2005.

The core activity of insurance companies in Kosovo is the Third Party Liability (TPL) product, namely vehicles insurance policies. Received premiums are mainly accumulated from the TPL policies (about 71.2%), while the rest comes from border policies and other (non TPL) policies. The insurance activity experienced the similar trend to previous years – the amount of claims paid to the clients compared to the premiums received still remains low. Nevertheless, the ratio improved slightly to 22.4% from 19.4% in 2005. The amount of the total premiums received in 2006 was euro 48.7 million, only 3.2% more than in 2005. It is namely a sign that the TPL market is now mature, with a few numbers of non insured vehicles. Indeed, with about 408,500 policies sold in 2006, the year-to-year increase was only of 32,914.

Compared to an amount of paid gross premiums of euro 48.7 million in 2006, the claims paid to clients amounted to euro 10.9 million, showing a ratio of paid claims to premiums of 22.4%. It should be noted that in 2006 the amount of claims paid was for 19.3% higher than in 2005. About 90.0% of the total claims paid were related to the TPL policies, while the claims on border policies and other policies (non TPL) policies accounted for 10.0% of the total claims paid.

3.3.4. Pension Funds Developments

With an amount of euro 10.5 million, pension funds in Kosovo account for only 1.0% of the total financial sector assets. This amount incorporates only the assets of the supplementary schemes – pensions provided to employees from their employers, aside from the mandatory contributions to the Kosovo Pensions and Saving Trust (KPST) which is a ‘social security fund’. However, during 2006, all the six supplementary pension funds that were operating within different public corporations ceased to be active, as a consequence of voluntary and non voluntary termination. This due to either high amounts of unfunded liabilities, or to the failure (or the change of ownership) of the contributing company. At its own initiative, or under the request of each contributing company, the CBAK revoked the license, and appointed a receiver. At the end of the on-going liquidation processes, the assets collected by the different former pension funds will be transferred to other pension funds or, in certain cases, transferred to escrow accounts open in commercial banks on behalf of each pensioner. As for small pension rights, they are expected to be

paid back to their beneficiary. On the other side, in November 2006, the CBAK Governing Board granted a license to a private supplementary pension fund ‘Slovenian-Kosovar Fund’ which will also operate as an asset manager for the accumulated funds. This is the first private pension fund licensed in Kosovo.

Box 5. Pension funds operating in Kosovo, their categorization

The pension schemes in Kosovo are defined at three levels:

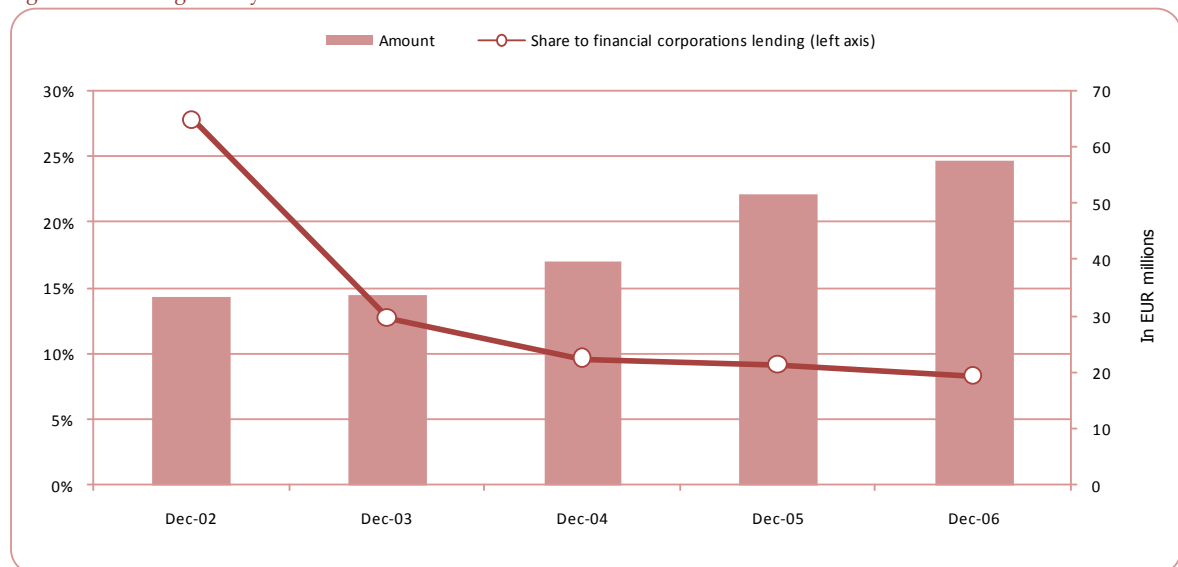
- 1) *Basic pension* (mandatory scheme) – paid by Pension Administration, and is financed by the Kosovo Consolidated Budget, which pays an amount of euro 40 to all Kosovo inhabitants older than 65 years.
- 2) *Individual savings pension* (mandatory scheme) – managed by Kosovo Pension Savings Trust (KPST) and financed by compulsory minimal contributions of employers and employees (5% each).
- 3) *Supplementary schemes* – consisting of: a. *Individual Savings Pension* (additional voluntary contribution paid by employer or the employee, or both, and managed by KPST); b. *Supplementary Employers Pensions* (provided to employees by their employers); c. *Supplementary Individual Pensions*, provided to natural persons from licensed pension provider.

3.3.5. Other Financial Intermediaries Developments

In addition to the commercial banks, other financial intermediaries (OFIs) are also involved in lending activity to the domestic economy. The OFIs are micro finance institutions not entitled to take deposits above a very limited amount. Their core business is lending activity, mainly as a support to small entrepreneurs. The main funding source of OFIs remains external donors.

At end-2006 there were sixteen OFIs operating in Kosovo, managing about 5.0% of the total financial sector assets. By end-2006, the total loan portfolio of OFIs reached the outstanding amount of euro 57.7 million, accounting for 8.3% of the total outstanding amount of loans granted by financial corporations (FC). However, in terms of the number of loans, OFI account for 25.7% of the number of loans - showing their micro-lending orientation. In 2002, while the banking sector just started its lending activity, the share of OFI loans to total loans was notably high (27.0%), then it dropped and remains quite constant (Figure 24).

Figure 24. Lending activity of other financial intermediaries



Source: CBAK (2007).

At the end 2006, OFIs held 35,541 loans in their portfolio that is about 8,418 loans more than at end-2005. The average amount per loan stood at euro 1,622 lower than in 2005 (amounting at euro 1,906).

3.4. External Sector

In 2006, the CBAK compiled and published for the first time balance of payments of Kosovo. According to the estimates (preliminary data), the current account deficit (after foreign assistance) stood at euro 393.0 million. This was mainly due to the high negative balance in the category of goods and services (euro -1.236,8 million in 2006), despite considerable inflows in the current transfers (amounting at euro 808.5 million in 2006).¹⁴ In terms of GDP, the current account deficit after foreign assistance remains high at 17.3% of GDP in 2006, compared to 11.9% in 2005. Before foreign assistance, this deficit is sizably higher (44.2% of GDP in 2006), stressing the dependence of Kosovo economy towards the donor sector.

Presently, with a growth of 10.2% compared to 2005, the goods and services balance amounting at euro -1.2 billion for the year 2006, represents a deficit of around 50% of GDP. As in the previous years, the huge current account deficit faced by Kosovo is due to the large trade deficit. With exports of goods (adjusted for coverage) amounting at around euro 100 million and imports amounting at euro 1.3 billion, the coverage of exports to imports stood at 8.1%, representing an improvement compared to the previous years. Nevertheless, having into consideration the low base, in 2006 Kosovo exports increased with 42.4% against the decline of 10% in 2005, while imports in 2006 grew with 15.2%.

¹⁴ Differences occurred among the export and import figures of goods and services showed in the section on Real Sector and section on External Sector arise due to the fact that in the Real Sector section data are in real terms and sourced by IMF, while here, in the External Sector section, data are in nominal terms and produced by CBAK.

Table 10. Balance of Payments of Kosovo (2004-2006), In EUR millions

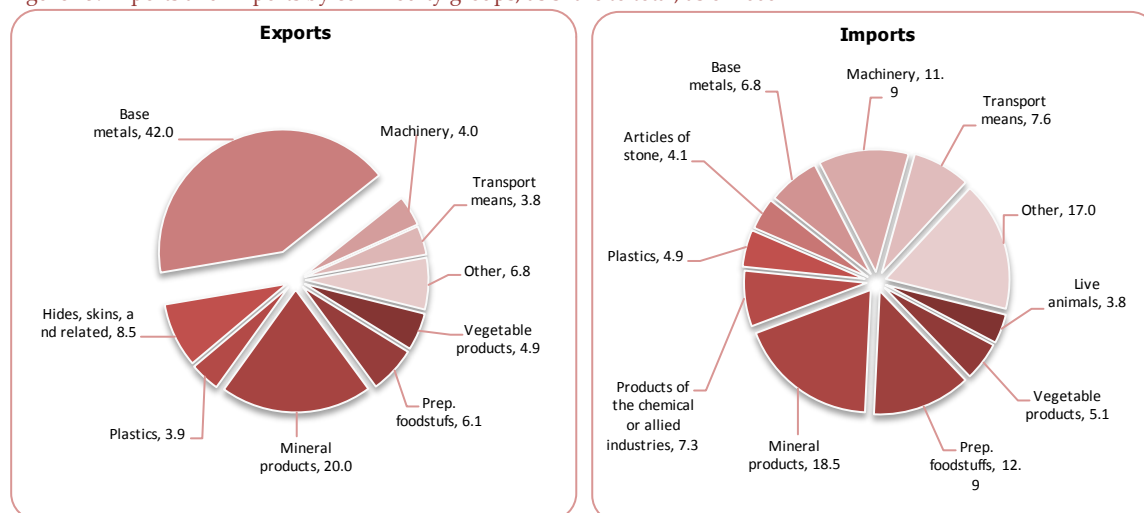
Description	2004	2005	2006
1. CURRENT ACCOUNT	-201.0	-266.7	-393.1
A. Goods and services	-1,047.3	-1,122.2	-1,236.8
Goods	-944.9	-1,021.7	-1,158.3
Credit	79.0	71.4	101.7
Debit	-1,024.0	-1,093.1	-1,260.1
Services	-102.4	-100.5	-78.5
Credit	132.0	128.6	141.1
Debit	-234.3	-229.1	-219.6
B. Income	22.7	29.7	35.2
Credit	42.3	51.5	67.1
Debit	-19.5	-21.9	-31.9
C. Current transfers	823.6	825.9	808.5
Credit 1/	987.3	980.9	931.2
Debit	-163.7	-155.0	-122.7
2. CAPITAL AND FINANCIAL ACCOUNT	146.2	78.4	42.5
A. Capital account	7.0	4.5	3.3
Credit	7.0	4.5	3.3
Debit	0.0	0.0	0.0
B. Financial account	139.3	73.9	39.2
Direct investment	21.0	59.1	266.3
Portfolio investment	-162.2	-67.8	-127.7
Other investment	282.2	110.6	-104.3
Reserve Assets	-1.8	-28.0	4.9
NET ERRORS AND OMISSIONS	54.8	188.3	350.7

Source: CBAK (2007).

1/ Remittances and donor sector figures are sourced from IMF Aide Memoire (February 2007).

Regarding the structure of exports, the highest increase is recorded in the category of mineral products, which is a positive sign and the consequence of the starting up of production in a large privatized company. Explicitly, in 2006 the export of mineral products amounted at euro 15.8 million over euro 3.2 million in 2005. As such, mineral products increased their share to total exports at 20.0% in 2006, from 6.6% in 2005 (Figure 25). Base metals although grew with euro 9 million in 2006, due to the faster increase in other categories, their share to total exports declined to 42% (from around 50% in 2005). Nevertheless, base metals and mineral products represent around 60% of Kosovo exports. Hides, skins and articles thereof represent the third largest category within the structure of Kosovo exports.

Figure 25. Exports and Imports by commodity groups, as share to total, as of 2006



Source: CBAK (2006)

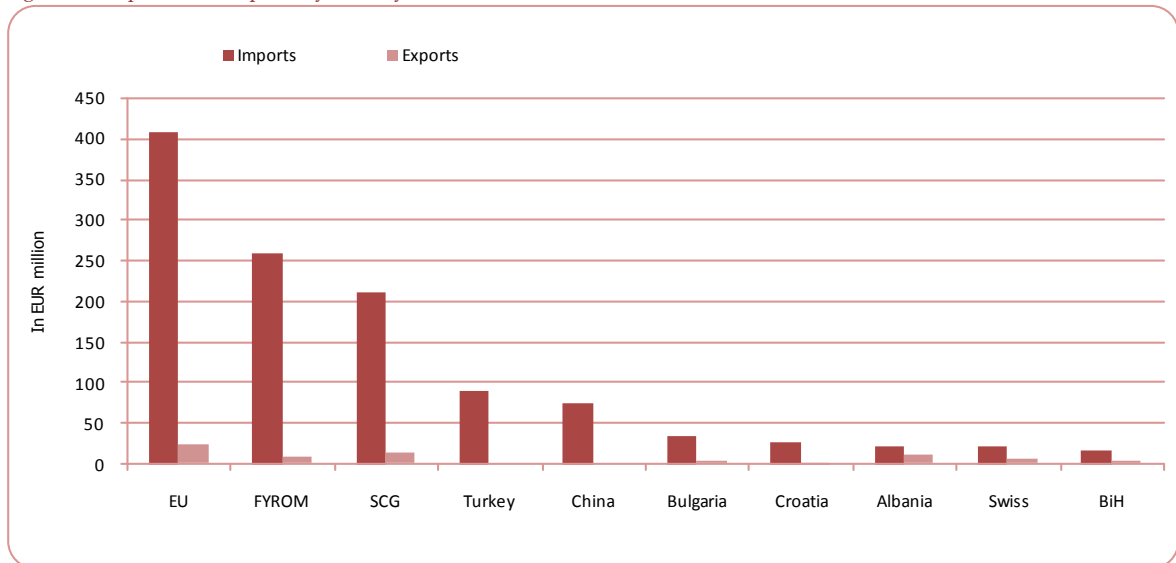
Mineral products, which account for 18.5% of total imports, grew with euro 31 million in 2006 against euro 39.5 million in 2005. What is to be noticed, is the growth of imports machinery (mainly equipments) totaling euro 156.0 million in 2006. Hence, imports of machinery and related increased their share to total imports at around 12%. Representing around 13% of imports in 2006, the imports of prepared foodstuffs increased with euro 5 million, showing a on going substitution of locally produced goods to imported ones. After the substantial increase in 2005 mainly due to the import of second-hand cars with euro 60 million (standing at euro 110.3 million), in 2006 this category declined with euro 11 million (standing at euro 99.4 million).

Countries in the region¹⁵ are Kosovo main trading partners, with exports amounting at euro 41.8 million (52.8% of exports) and imports at euro 576.7 million (43.9% of imports). Despite the light decline of exports to FYROM with euro 1.4 million, in 2006 the Kosovo exports to the countries in the region grew with euro 14.8 million, mainly from increase in the exports to Serbia and Montenegro (euro 7.0 million), Albania (euro 5.3 million) and Bulgaria (euro 3.2 million). Standing at euro 260 million, imports from FYROM in 2006 over 2005 are higher for euro 40 million, decelerating from the increase with euro 70 million in 2005 over 2004. While exports, decreasing with euro 1.4 million, stood at euro 8.2 million in 2006.

After countries in the region, EU countries representing 28.4% of exports and 34.7% of imports are the second largest trading partners. In 2006 against 2005, imports from the EU held steady, while exports grew with 29.2%, driven mostly from the increase of exports to Slovenia. Other trading partner (in terms of exports) is Switzerland. Is to be marked the fact that while exports to this country in 2005 stood at only euro 0.7 million, in 2006 grew significantly totaling euro 7.4 million. Imports from Switzerland in 2006 amounted at euro 23 million from euro 18.7 million in 2005. Apart from the above mentioned, imports from Turkey and China with the euro 90.4 million and euro 75.5 million, each, in 2006 grew with around euro 25 million, all together.

¹⁵ Albania, Bulgaria, Bosnia and Herzegovina, Croatia, FYROM, Montenegro and Serbia.

Figure 26. Exports and Imports by country, as of 2006



Source: CBAK (2006).

Income account for the year 2006 stood at euro 35.3, compared with euro 29.7 million a year before. The continuous increase is mainly due to the increase in the credit side, amounting at euro 67.1 million and the main item are earnings from investments in the financial markets abroad, dominated from the KPST investments. Another element in the credit side are wages of KFOR local staff and liaison offices in Kosovo. All together, the credit side amounts at euro 67.1 million. Regarding to the debit side, the total amount of euro 31.8 million is composed mainly from reinvested earnings from financial corporations (foreign commercial banks and insurance companies) amounting at euro 22.8 million.

Current transfers apart from the goods and services accounted to be an important element in the Kosovo balance of payments. As of 2006, the total current transfers amounted at euro 808.5 million, down from euro 825.9 million in 2005. The main item within the current transfers is worker remittances, due to the considerable number of Kosovans living in the SEE countries, mainly Germany, Switzerland, UK, etc. For year 2006, the worker remittances are estimated at around euro 424.4 million. Taking into consideration the international presence in Kosovo, and the fact that there are money outflows from expatriates, the net amount of remittances is estimated to be around to euro 300 million. Apart from the above mentioned categories, the current transfers include also donors (euro 185 million) and UNMIK budget (euro 250.8 million).

Despite considerable inflows in the direct investments, having into consideration higher outflows in the portfolio and other investments, the Kosovo capital and financial account stood at euro 42.5 million in 2006 from euro 78.4 million in 2005. As an aftermath of the privatization process, Kosovo foreign direct investments amounted at euro 266.3 million in 2006, up from euro 59.1 million in 2005. However, the economic impact of these amounts in balance of payments is limited, given that it is offset from almost the same increase of the financial sector net foreign assets.

4. Financial Supervision

4. Financial Supervision

CBAK has regulatory and enforcement powers for all financial institutions in Kosovo and participates in developing and modernizing the financial sector, which currently covers the banking industry, insurance industry, pension funds and other financial institutions (micro finance institutions, non-bank financial institutions, exchange bureaus and money transmitters).

The CBAK's goal is to have a financial supervision and regulatory process that is effective, flexible and promotes a competitive market-based financial sector, which meets the best principles of international standards in the financial sector development.

The supervisory approach of the CBAK has evolved consistent with the evolution of international best practice for supervisors, from a "rules-based" approach to a "risk-based" approach, formulated upon the Basel Core Principles and Pillar 2 of Basel II for banks, and a risk-based solvency regime that is being adopted internationally for insurance companies.

The risk based approach is intended to enable the CBAK to appropriately allocate its supervisory resources to those areas of greatest risk, within individual financial institutions and the financial sector in general. Banking supervision by risk focuses on the ability of management to identify, measure, monitor and control risk, whereas insurance supervision by risk focuses on solvency requirements and creates prudential framework that more accurately reflects the risks undertaken by insurers. The goal is to create an effective and well-balanced supervision of the insurance sector that will ensure the solvency perspective as well as other issues of importance for insurance supervision that could lead to tariff liberalization.

In accordance with legislation governing its statutory functions (UNMIK Regulations 1999/21, 2001/25, 2005/20 and 2006/47), the CBAK has set out detailed supervisory standards and requirements in order to achieve a well-regulated financial sector. In addition, the Regulations give the Governing Board of the CBAK power to adopt prudential supervision rules, which establish limits, operating guidelines, procedures and reporting requirements for financial institutions, and enforcement actions for non-compliance with legal requirements or for unsafe and unsound practices.

Financial institution regulations and prudential rules are continuously reviewed and updated to ensure that they continue to be in line with international best practices. They are also reviewed to ensure that they strike the right balance in providing a well-regulated environment while not imposing undue burdens to end-users of financial services.

4.1 Financial Sector Regulation Activity

As a regulator, CBAK participates in the enforcement of related UNMIK Regulations. The legal framework for governing these activities, according to EU standards, has been adapted to the current level of development of financial institutions in Kosovo and has been complemented by CBAK rules and decisions.

Financial supervision rules framework is created early after establishment of the CBAK, since that time the financial sector has changed, as well as has CBAK approach to supervision. Based on the above mentioned factors and as per recommendations of the technical assistance, CBAK financial supervision has been working actively to review and revise the framework of rules, and establish policies and procedures. In addition, to guide the financial industry in the implementation of "best practices", CBAK has issued "Advisory Letters" as additional supportive references. Some of these rules have been approved by the CBAK Governing Board and the remaining ones have been

finalized in consultation with the financial industry and will be presented for approval to the CBAK Governing Board during 2007.

Furthermore, as a result of this process, during 2006 CBAK Governing Board approved the following insurance supervision rules:

- o Amendment of Rule V on the ways of selling insurance products and the compulsory licensing of insurance operators, and insurance agents and brokers.

- o Rule VIII on deposit of assets as security, capital adequacy, financial reporting, risk management, investment and liquidation. Consequently rules no: VIII, IX, X, XI, XII, XIIa, XIII, XIV, XV, XVI, XIX, XX, XXIII and XXV have been abrogated

4.2 Licensing and Structure

In accordance with legislation governing its statutory function, the CBAK has the authority to set criteria for the licensing of financial institutions and to reject those which do not meet these standards.

The CBAK's vision is a stable and growing financial sector driven by market forces, but operating within a prudent regulatory and supervisory policy framework harmonized to EU/EC directives.

The CBAK's strategy in the field of financial institutions licensing is centered on attracting investors who have strong financial positions, meet the criteria of fit and proper for shareholders and management, are able to pursue a cautious approach to business to protect the interest of clients, thus helping to strengthen the financial system and increase its credibility.

Banking licensing activity of the CBAK during 2006 was primarily related to the opening of new branches and changes in banks' ownership structures. Nevertheless, during 2006 the CBAK governing board approved two (2) preliminary licenses for branches of banks with foreign capital (Banka Kombetare Tregtare –Albania and Komercijalna Banka –Serbia). The number of commercial banks in operation during 2006 was six, after license revocation of Credit Bank of Pristina-CBP. At the end of 2006, a network of six banks was operating with 220 branches and sub-branches throughout Kosovo.¹⁷

Exchange Bureaus and Money Transfer Offices. Ten exchange bureaus, one money transfer agency registered with CBAK in 2006. At the end of 2006, 16 exchange bureaus and three agencies for money transfers were operating in Kosovo. The large increase in the number of licensed exchange bureaus during 2006 is a result of a joint campaign of CBAK, UNMIK Police, KPS and FIC to legalize the dealers exchanging currency on the streets.

Micro Finance Institutions. At the end of 2006, 15 micro finance institutions and three other non-bank financial institutions were operating throughout Kosovo.

¹⁷ 2006 Addendum - Pursuant to United Nations Interim Administration Mission in Kosovo (UNMIK) Regulation No. 1999/21, the Banking and Payments Authority of Kosovo (CBAK), in its capacity of bank supervisory authority, by order dated March 13, 2006, revoked the license of Credit Bank of Pristina. CBAK appointed Mr. Michael Rouswell as Receiver for Credit Bank of Pristina and he took over the governing-managing operations of Credit Bank of Pristina at 8:00 AM on March 13, 2006.

Table 11: Banks Licensing Activity, 2002 – 2006

Description	2002	2003	2004	2005	2006
Prior Licensed	7	7	7	7	6
Preliminary approval *	0	0	0	0	2
Revocation of License	0	0	0	0	-1
Total	7	7	7	7	8

Table 12: Non Bank Financial Institutions Licensing Activity, 2002 – 2006

Description	2002	2003	2004	2005	2006
Prior Registered/Licensed	14	14	15	18	19
Registered/Licensed	0	1	3	1	1
Withdraw of Registration	0	0	0	0	-2
Total	14	15	18	19	18

Table 13: Money Transfer Agencies Licensing Activity, 2002 – 2006

Description	2002	2003	2004	2005	2006
Prior Licensed	1	1	1	1	2
Licensed	0	0	0	1	1
Total	1	1	1	2	3

Table 14: Exchange Bureaus Licensing Activity, 2002 – 2006

Description	2002	2003	2004	2005	2006
Prior Licensed	3	3	4	3	6
Licensed	0	1	0	4	10
Withdraw of Registration	0	0	-1	-1	0
Total	3	4	3	6	16

Insurance Companies. As of end 2006, nine non-life insurance companies operated in Kosovo, three of which are branches of foreign companies: one from Albania) one subsidiary company from Croatia and one from Turkey. One insurance company has changed its ownership structure with a new composition of 49% domestic ownership and 51% foreign. The remaining three are insurance companies with domestic ownership including a new firm that started operations in 2006.

Insurance Intermediaries. This category includes Agents, Surplus Line Brokers, and Loss Adjusters (corporate and independent complaint adjusters). During 2006 the number of agents increased from 658 to 784, whereas the rest of the categories remained at the same levels.

Supplementary Pension Funds. No new pension funds were licenced in 2006 while five of the existing funds voluntarily ceased activities, reducing such funds from six to one. At its own initiative, or at the request of each contributing company, the CBAK revoked its license, and appointed a receiver.

Pension Fund Providers. The first private pension fund provider was licensed in Kosovo in 2006. The CBAK Governing Board granted a license to a private supplementary pension fund - 'Slovenian-Kosovar Fund' - which will also operate as an asset manager for the accumulated funds.

Table 15: Insurance Companies Licensing Activity, 2002 - 2006

Description	2002	2003	2004	2005	2006
Prior Licensed	0	8	8	8	8
Licensed	8	1	2	1	1
Canceled	0	-1	-2	-1	0
Total	8	8	8	8	9

Table 16: Insurance Intermediaries Licensing Activity, 2002 - 2006

Description	2002	2003	2004	2005	2006
Agents	231	307	446	658	784
Broker Surplus Line	0	1	3	3	3
Broker	0	0	0	2	2
Loss Adjuster Corporate	1	0	1	2	2
Independent Complaints Adjusters	0	0	2	3	3

Table 17: Pension Funds Licensing Activity, 2002 - 2006

Description	2002	2003	2004	2005	2006
Supplementary Pension Funds	5	6	5	6	1
Private Pension Fund Provider	0	0	0	0	1

4.3 Financial Supervision Activities

One of the main functions of CBAK is to provide supervisory and regulatory oversight to financial institutions in a way that fosters a sound, accessible, and competitive financial system that both inspires trust and offers a large scope of financial services. In carrying out this mission, the Banking, Insurance, and Pension Supervision Directorates are responsible for licensing, regulating and controlling financial institutions and non-bank financial institutions operating in Kosovo.

4.3.1 Banking supervision aims to protect depositors' funds and to maintain a stable financial system by fostering an efficient and competitive financial environment. The CBAK Banking Supervision Directorate promotes these goals through:

A Stable Banking and Non-Banking Financial System

The promotion of a safe, sound, and stable financial system is one of the most basic reasons for the existence of financial institution supervision and regulation. A stable financial system provides depositors with a secure place to keep their funds. It provides businesses and individuals a dependable framework for conducting monetary transactions.

A Competitive Banking and Non-Banking Financial System

Another important purpose of financial institution supervision and regulation is the maintenance of a competitive financial system. A competitive financial system provides customers with the lowest priced and most efficiently delivered financial goods and services.

A Fair Banking and Non-Banking Financial System

Another important goal of regulation is consumer protection. Appropriate rules and regulations require financial institutions to disclose information that helps consumers evaluate product options open to them, such as the cost of credit, their rights and potential liability, and the true rate of return on their deposits.

CBAK rules and UNMIK regulations govern many aspects of banks and non-bank financial institutions. Matters such as who owns, controls, and manage financial institutions; how much financial institutions can lend to a single customer or group of customers; how much capital financial institutions should have; where financial institutions can locate their offices; and what services they can provide are all addressed by banking and non-banking rules and regulations.

The main objective of the supervisory process is to evaluate the over-all safety and soundness of financial institutions. This evaluation includes an assessment of the organization's risk-management systems, financial condition, loan portfolio and compliance with applicable banking and non-banking rules and regulations.

The supervisory process entails both on-site examinations and off-site surveillance and monitoring. In general, CBAK staff performs on-site examinations of banking and non-banking financial institutions at least once every twelve months. This routine may be supported by more frequent "targeted" examinations in order to follow up the implementation of previous recommendations.

CBAK examines financial institutions' operations by:

Off-site Analysis - Collecting information (reports, information and data which banks and non-bank financial institutions submit to the CBAK) and rating the indicators of operations and comparing these with prescribed limits, previous data and accepted international standards.

On-site Examinations - Performing qualitative appraisal of banks and non-bank financial institutions activities by checking their internal data using a risk based approach.

In its off-site supervision of financial institutions, the CBAK uses ongoing screening analyses to help detect adverse trends developing in financial institutions and in the financial industry. This information enables the CBAK to better direct examiner resources to those institutions needing supervisory attention.

The on-site examination is the fact-finding phase of supervision. The facts are analyzed to determine the condition of the financial institution. These findings are summarized in the Report of Examination. Using these facts, the risk profile of the financial institution is determined, which in turn dictates the manner in which the institution will be treated by supervisors during the forthcoming supervisory cycle.

The CBAK on-site examination team conducts an in-depth evaluation of the scope of formalized policies, procedures and practices that are used by the financial institution to manage and control its loan portfolio. The purpose of this specific loan review is to identify problems in the loan area since loans usually represent the greatest source of risk in financial institutions. This risk is limited by CBAK rules and regulations.

Risk-Focused Supervision - With banking and non-banking financial institutions growing in both size and complexity, the CBAK has moved towards a risk-focused approach to supervision that is more a continuous process than a point-in-time examination. The goal of the risk-focused supervision is to identify the greatest risks to a financial institution and assess the ability of the institution's management to identify, measure, monitor, and control these risks.

CBAK uses the CAMEL approach for risk assessment. The CAMEL supervisory assessment system is a supervisory tool used by most bank supervisors in the developed countries. This supervisory system is an acronym for the five components of the assessment system: Capital adequacy, Asset quality, Management and administration, Earnings, and Liquidity. Each component of CAMEL is rated from 1 to 5, with 1 expressing the best rating and 5 expressing the lowest rating. In addition, the financial institution is assigned an overall composite rating from 1 to 5, which is derived from the individual component ratings.

Each bank and large non-bank financial institution is assigned a composite assessment rating based on the evaluation of pertinent financial and operational standards according to uniform criteria and principles including: :

- **Capital Adequacy** - The adequacy of the capital base, net worth and reserves to support present operations, the usual occurrence of a risk, and future growth of the financial institution.
- **Asset Quality** - The quality of loans, investments and other assets.
- **Quality of Management** - The ability of management to properly administer all aspects of the business of the financial institution, and plan for further needs and changing circumstances.
- **Earnings** - The ability to generate earnings to cover its costs, including adequate provisions for possible loan losses, pay interest on deposits and provide adequate security for depositors' funds.
- **Liquidity** - The maintenance of enough liquid assets to cover current needs, particularly depositors' withdrawals.

The results of an on-site examination are reported to the board of directors and management of the financial institution in a report of examination based on this CAMEL supervisory assessment system.

Table 18: Bank supervision: On-Site Examination conducted during the year 2006

Description	No. of Examinations
Banks - full scope	4
Banks - focused	6
Banks – branches – pre-opening and reallocation	32
Micro Financial Institutions - full scope	12
Money Transfer Agencies – full scope	2
Exchange Bureaus – full scope	4

4.3.2 The Insurance and Pension Supervision Directorate main objective is to maintain security, stability and efficiency of the insurance and pension sectors, to protect policyholders and to offer a proper operational environment for shareholders. Therefore, supervision and examination procedures were performed based on the annual inspection plan for 2006. Insurance companies, insurance intermediaries and pension funds are supervised through:

Off-Site Analysis is performed by collecting information (reports and other data) which insurance companies and pension funds submit to the CBAK. Based on the analysis of the information received, operational indicators such as solvency margin, financial strength, loss ratio, technical provisions, maximum risk retention, reinsurance are rated against international standards. Also, CBAK assesses compliance with its rules and regulations. Off-site analysis identifies the issues and weaknesses in an insurance company or pension fund, whereas on-site examinations verify and monitor the improvement of the weaknesses identified.

On-Site Examinations - On-site examinations are a crucial part of the supervision process. It is important to verify data and information submitted by the insurance companies and pension funds on an ongoing basis. Amongst others, it allows Insurance and Pension Supervision to assess management's decision making processes and internal controls. To make this assessment, CBAK uses a Score Card System (SCS). The SCS is a performance grading system consisting of a five-level score from 1 to 5 with 1 identifying the highest risk and 5 the lowest. The system includes five components in its grading: Fit and proper (management and shareholding structure), System and Controls (underwriting, claims processing, technical provision, compliance, etc), Quality of Reinsurance, Auditors Report and Fairness to Policy Holders.

Based on this examination system, individual scores and the overall score are based on professional judgment. The scores are analyzed to determine the condition of the institution. The condition of the company is summarized in the Report of Examination and based on the findings a supervisory strategy is developed for the institution's next supervisory cycle.

Table 19: Insurance Supervision: On-Site Examination conducted during the year 2006

Description	No. of Examinations
Insurance Company - full scope	6
Insurance Company - focused	9
Insurance Companies – agents offices	185
Broker surplus Line	3
Insurance Broker	3

During 2006, all of the six supplementary pension funds that were operating within different public corporations ceased to be active as a consequence of voluntary or non-voluntary termination. These terminations were due to high amounts of unfunded liabilities, failure, or change in the ownership of the contributing company. At its own initiative or by request of each contributing company, the CBAK revoked its license, and appointed a receiver. At the end of the still on-going liquidation process, the remaining assets former pension funds will be transferred to other pension funds or, in certain cases, transferred to escrow accounts in commercial banks opened on behalf of each pension holder; as for small pension rights, they are expected to be paid back to their beneficiaries.

Table 20: Pension Supervision: On-Site Examination conducted during the year 2006

Description	No. of Examinations
KPST	1
Supplementary Pension Funds	3

4.4. Enforcement Actions

Despite the efforts of supervisors, situations have occurred where banks failed to meet supervisory prudential requirements or used unsafe and unsound banking and insurance practices. As a result of regulatory violations or unsafe and unsound banking practice, the CBAK initiated 22 enforcement actions against banks in 2006, whereas insurance supervision initiated 16 enforcement actions against insurance companies

In 2006 enforcement actions taken under Regulation No. 1999/21 and 2001/25, range from written warnings to revocation of license and were based on the weight of violations, risk exposure, repeated violations, etc. Types of enforcement actions taken by CBAK included oral or written communication, restriction of certain activities, formal agreements between CBAK and banks, and requirements for increases of equity capital, and monetary penalties. Enforcement actions undertaken against banks have resulted in the stronger financial positions of financial institutions and reduced risks.

Box 6. Liquidation of the Credit Bank of Prishtina (CBP)

In March 13 2006, CBAK Governing Board revoked the license of the CBP, ordered the interruption of its activities as of March 13 2005, dismissed the bank's governing Board and management and appointed a receiver to manage the bank and protect the depositors' interest. Consequently:

- First tranche of repayment to depositors of up to euro 1.000 was performed immediately.
- Second tranche of repayment to depositors was increased to euro 3.500 soon after.
- Further tranches of repayment were performed in several waves, as the receiver collected sufficient funds in order to cover 70% of the deposits, with a repayment ceiling of euro 20.000 per depositor.
- At the present, euro 9 million has been repaid to depositors out of euro 32 million.
- Based on the present expectations of loan recoveries, the Receiver foresees a good possibility of collecting loans from the borrowers of the CBP. Higher and quicker repayment of deposits will depend on the collection of loans.
- The liquidation process may last several years.

5. Services provided to the Authorities, to the financial community and to the public

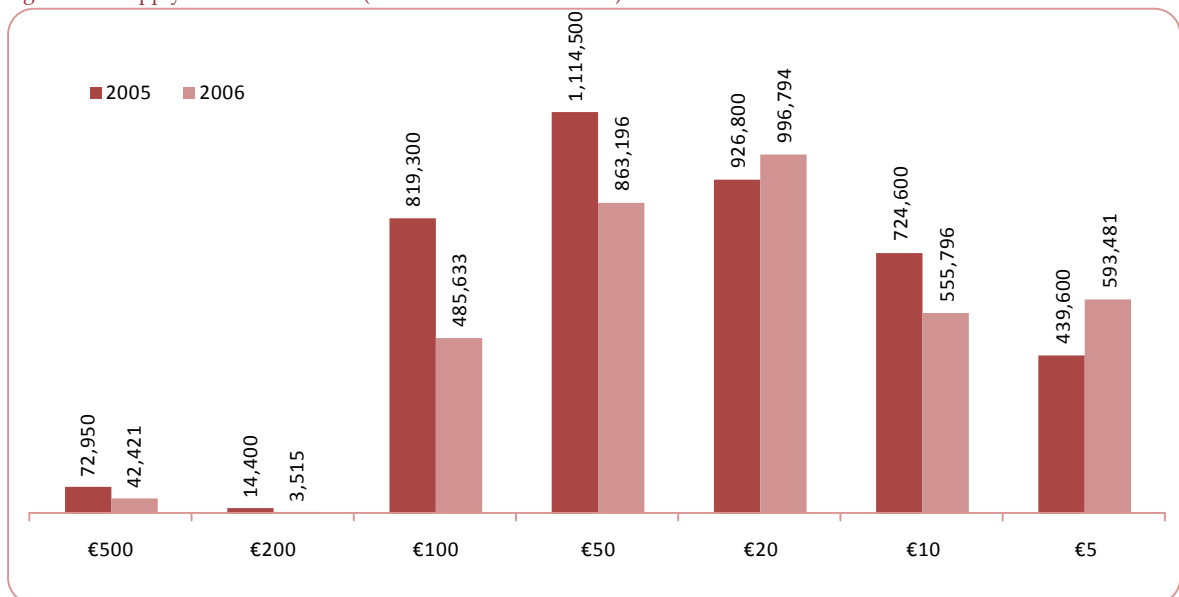
5. Services provided to the Authorities, the financial community and the public

The Central Banking Authority of Kosovo provides public institutions, the financial community, and the public with the usual financial services offered by a central bank, with the exception of any credit facility or temporary liquidity since the CBAK is not an issuing bank. As a result of decisions of the United Nations Mission in Kosovo, the currency used in Kosovo is the euro.

5.1. Cash Operations and Management

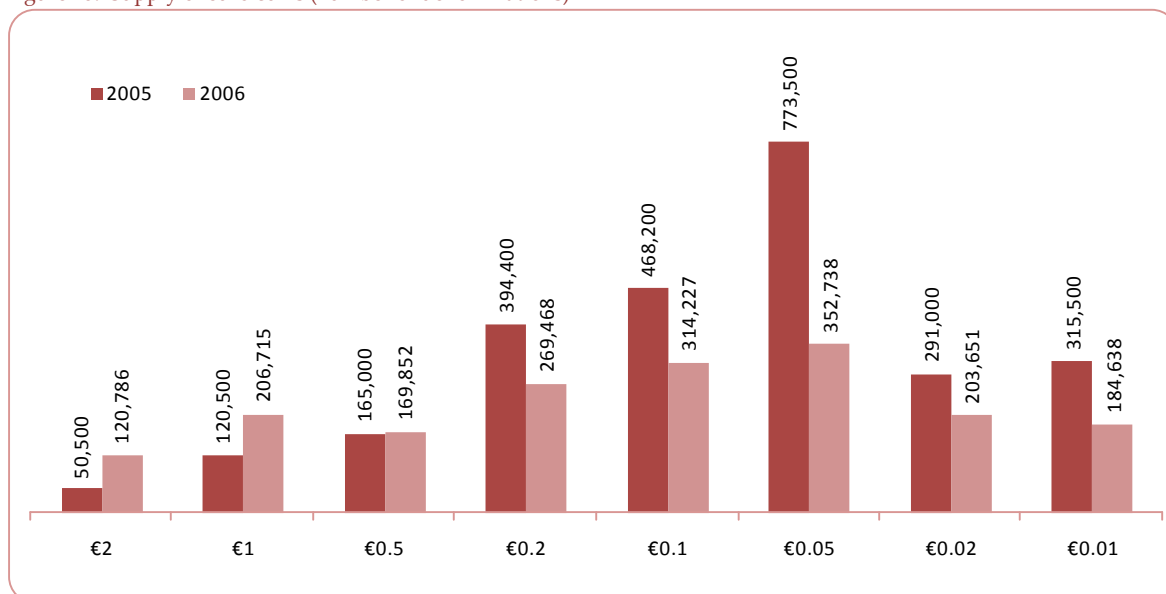
The CBAK is responsible to ensure an adequate supply of banknotes and coins for the settlement of cash transactions in the economy. As the euro is the principal currency permitted to be used in Kosovo, the CBAK's responsibilities regarding cash operations and management relate to euro.

Figure 27: Supply of euro banknotes (number of denominations)



Source: CBAK (2007)

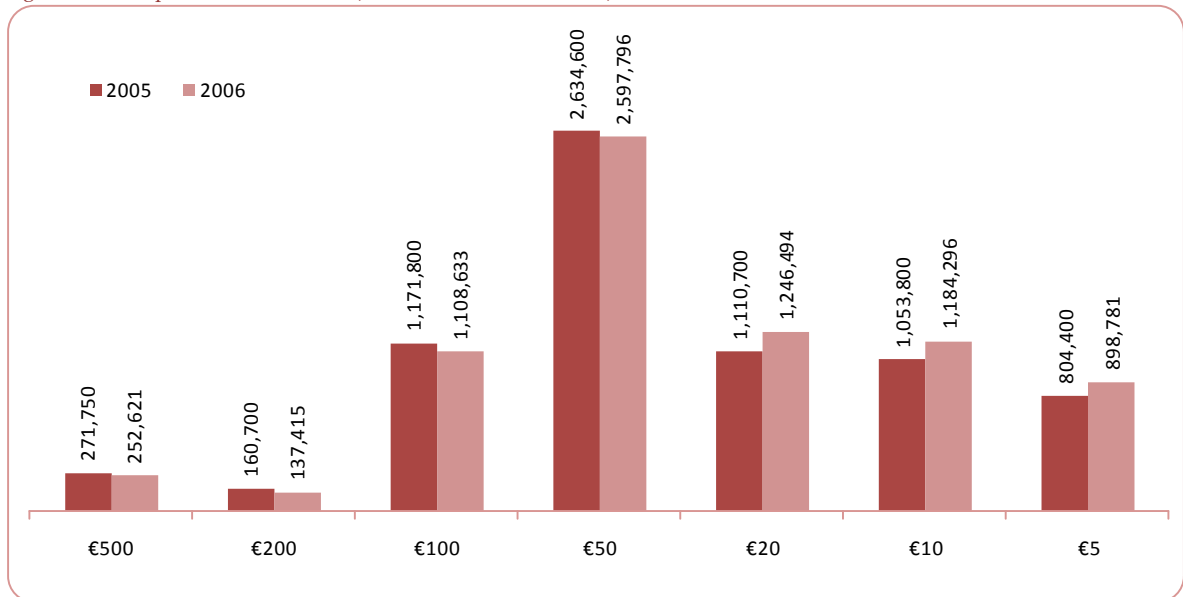
Figure 28: Supply of euro coins (number of denominations)



Source: CBAK (2007)

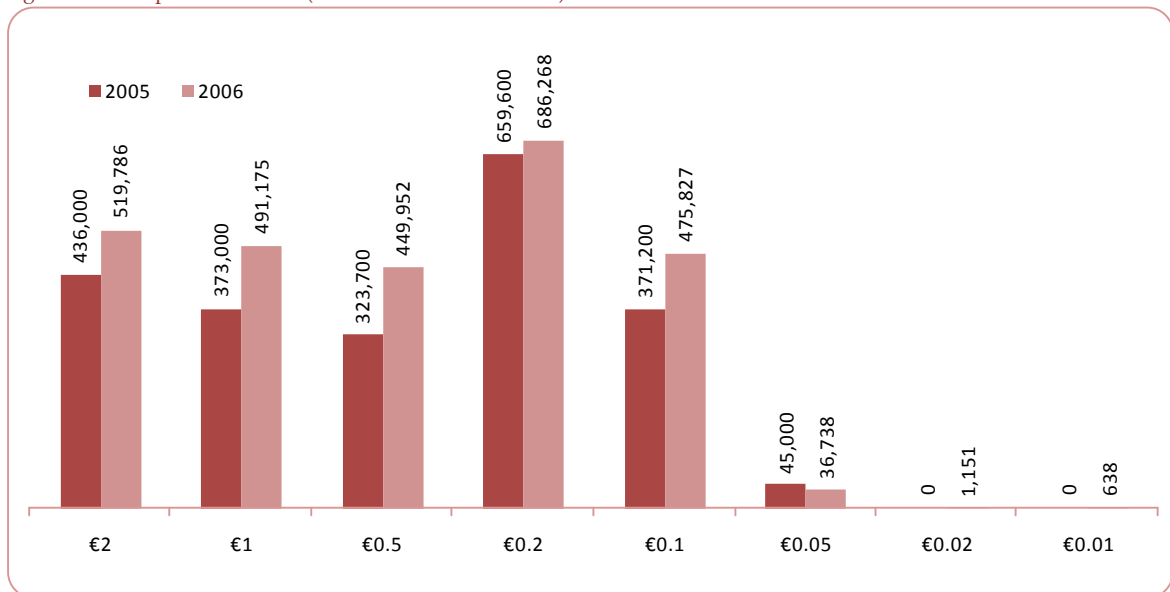
As it is shown in the figures above, during the course of 2006, the CBAK supplied commercial banks and other institutions with over 3.5 million euro banknotes amounting to nearly euro 143 million and 1.8 million euro coins amounting to nearly euro 0.65 million. In terms of total value, the cash supplied in 2006 decreased by nearly 13.2 percent compared to 2005, while the structure of cash supply according to denominations varied noticeably year-on-year. While the supply of 5 and 20 euro banknotes increased, the supply of other denominations decreased. Then, whereas the supply of highest denomination coins (0.5, 1 and 2-euro coins) increased, the supply of lowest denomination coins (1, 2, 5, 10, and 20-eurocent coins) decreased, although the CBAK continued to promote the use of red coins (1, 2, 5-eurocent coins) and made them available like the previous year. The decrease of supply of red coins reflects the decrease of need for them primarily caused by relative rounding of retail prices.

Figure 29: Accepted euro banknotes (number of denominations)



Source: CBAK (2007)

Figure 30: Accepted euro coins (number of denominations)



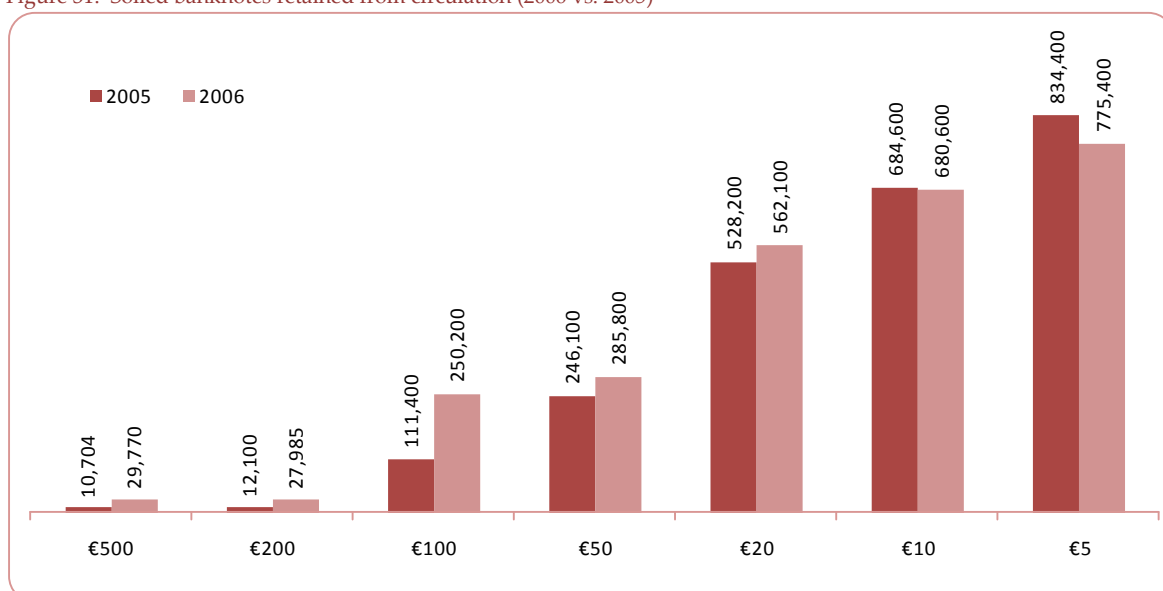
Source: CBAK (2007)

On the other hand, in 2006 the CBAK accepted more than 7.4 million euro banknotes and more than 2.6 million euro coins as cash deposits by the commercial banks and other institutions. Expressed in value, these deposits reached nearly euro 435.8 million and nearly euro 2.0 million, respectively. In contrast to the cash supplied by the CBAK, the total value of cash deposited with the CBAK shows an increase of 7.1 percent compared to the previous year.

Same as previous years, in 2006, the cash deposited with the CBAK was higher than the cash supplied by the CBAK. Actually, reaching around euro 294.7 million in 2006, the difference was

more significant than in the previous two years when it was around euro 249.8 million and euro 176.8 million, respectively. As the CBAK keeps in the vaults only the minimum required level of cash by shipping to the euro area the excess, where it is transformed into interest-earning assets, the year-on-year increase of the cash deposited over cash supplied lead also to increase of the net cash shipment abroad. The net cash shipment abroad in 2006 amounting to euro 306.8 million was considerably higher than in 2005 and 2004, when it was euro 237.5 million and euro 191 million, respectively.

Figure 31: Soiled banknotes retained from circulation (2006 vs. 2005)



Source: CBAK (2007)

Processing of banknotes and coins deposited with the CBAK continued to be carried out by modern processing equipment and according to standard rules. Indeed, in 2006, the CBAK enhanced the pool of cash processing equipment with several most up-to-date items. In the course of 2006, nearly 2.6 million euro banknotes (34.9 percent of euro banknotes deposited with the CBAK) were classified as soiled and were retained from circulation and shipped to the euro area. Such a considerable volume of soiled euro banknotes retained from circulation contributed significantly to the improvement of the quality of cash in circulation.

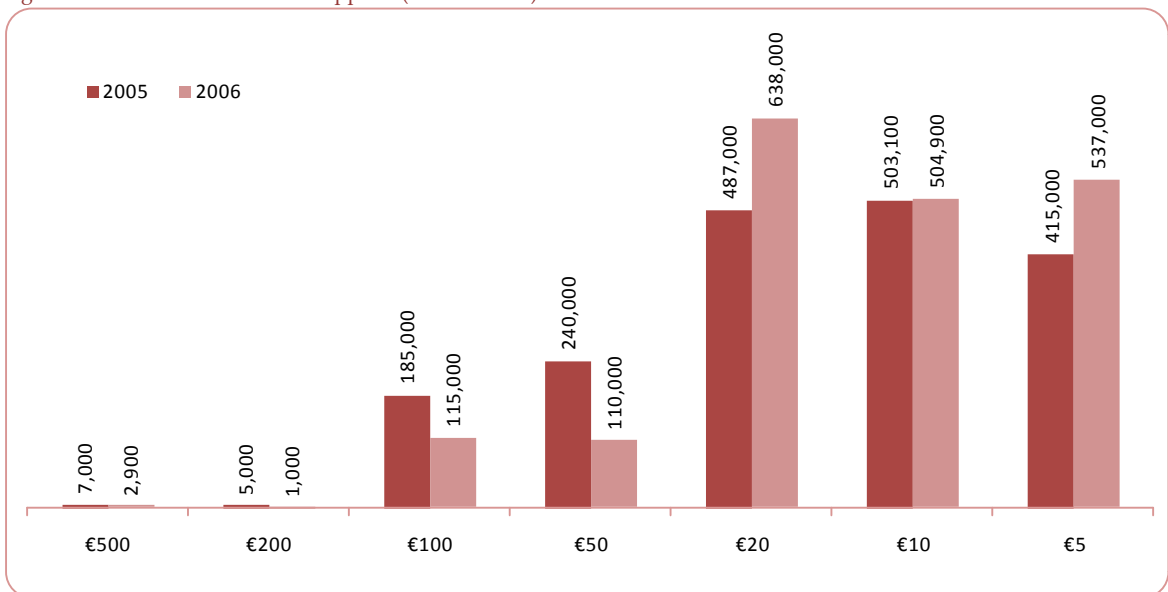
The quality of cash in circulation was also improved through supply of brand new euro banknotes, which were shipped from the euro area. During 2006, the CBAK supplied nearly 2.0 million brand new euro banknotes (54.7 percent of all euro banknotes supplied). Most of new banknotes supplied were low denomination banknotes, which were mainly supplied to the commercial banks for the purpose of furnishing their ATMs. Then, also all of the used euro banknotes supplied were of the highest standard quality.

Figure 32: Ratio of brand new banknotes supplied in 2006 to total



Source: CBAK (2007)

Figure 33: Brand new banknotes supplied (2006 vs. 2005)



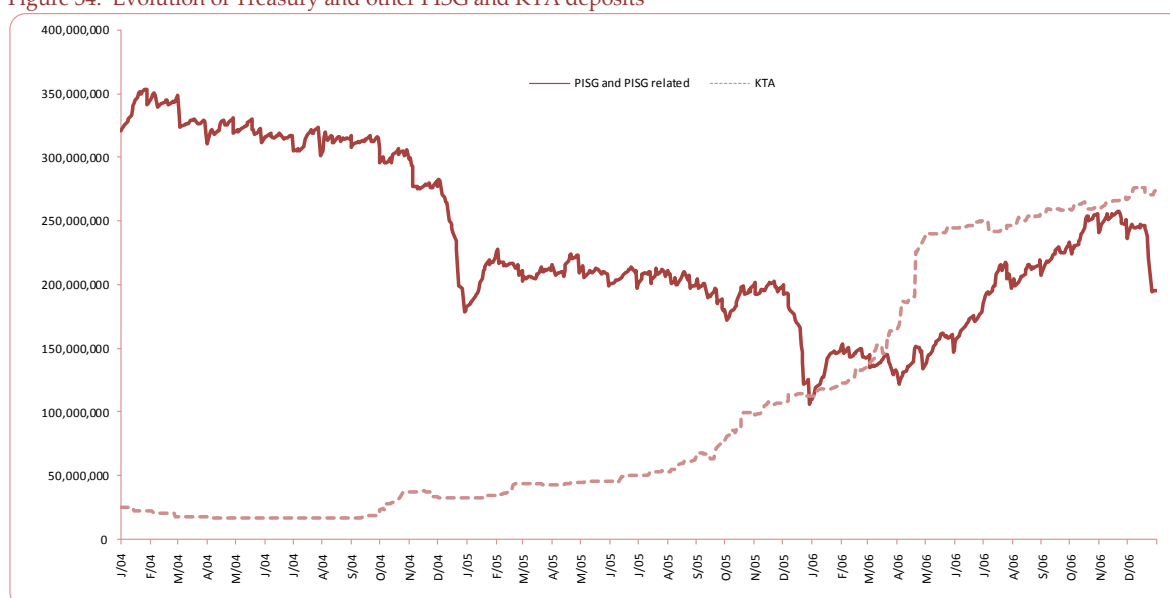
Source: CBAK (2007)

Regarding anti-counterfeit measures, the CBAK continued to analyze cases of counterfeit currency throughout 2006. In addition, it continued to cooperate with the police authorities regarding the reporting of counterfeits and training on counterfeits. In particular, the CBAK and the police authorities have cooperated on enhancing the procedures for counterfeit reporting by financial institutions. Also terms of reference of a joint counterfeit analysis committee were agreed.

5.2. Services provided to the Treasury

The function of the banker –or more appropriately of a financial services provider- to the Treasury was given to the CBAK based on the Regulation, within the section on the specific powers of the CBAK. The CBAK provides financial services on behalf of and for the account of not only the Treasury, but also the other PISG entities and the KTA. It also offers financial services to major public utility companies. In 2006, like in the previous years, these services mainly consisted of account maintenance and payment operations to the exclusion of any credit facility.

Figure 34: Evolution of Treasury and other PISG and KTA deposits



Source: CBAK (2007)

The Treasury and other PISG deposits together with KTA deposits constituted the majority of the total deposits held in accounts with the CBAK. As of 31 December 2006, the Treasury and other PISG deposits amounted to euro 195.7 million. During the year, KTA deposits became more significant due to intensification of the privatization process, reaching euro 275 million at the end of the year. The evolution of the deposits of the Treasury and other PISG entities and the KTA held in accounts with the CBAK is presented in the figure above.

Also the majority of domestic payment operations are conducted on behalf of and for the account of Treasury. As for the international payment operations of Treasury, at the end of 2006, arrangements were made for carrying them out through CBAK.

During 2006, the CBAK continued to support enhancement of Treasury and other entities transaction and reconciliation processes. Standard electronic forms of account and individual transaction information developed in 2006 were customized for Treasury and KTA to better suit their needs. Then, an application for automated generation of all Treasury account information files was developed as a complementary tool to the special telecommunication link with Treasury, which was also implemented in 2006.

5.3. Asset Management

The CBAK is in charge of managing the funds deposited by the Ministry of Finance and Economy, entities of the United Nations Interim Administration Mission in Kosovo and Provisional Institutions of Self Government (PISG), public agencies, financial institutions, and donor organizations. In practice, the deposited funds belongs namely to the Ministry of Finance (budget reserves), the Kosovo Trust Agency –KTA- (proceeds for the privatization process) and financial institutions (mandatory liquidity reserves).

As of December 31, 2006, the total managed assets was euro 630 million, out of which the deposits from the PISG and related entities was euro 196 (31 % of the total), KTA euro 275 million (44 %) and financial institutions euro 121 million (19 %).

In accordance with UNMIK Regulation 2006/47 on the Central Banking Authority of Kosovo , the Governing Board has determined the investment policy to be followed by the Management, and under its control, by the asset management unit. Since a large amount of the managed funds are public assets, or could be paid back with a short notice, a special focus is given to safety and liquidity, and then to return on investments.

All investment operations are carried out with banks which enjoy high ratings (Aaa and Aa or equivalent). Managed assets are placed in euro currency, either in bank term deposits (52% as of end of year 2006), or in governmental securities (43%), with a maturity of less than one year and a high investment grade (Aaa or Aa or equivalent) and last in current accounts. Exposures per single counterparties and per countries are strictly limited. The compliance with the approved internal investment rules is followed on a daily basis, while all operations are daily booked by an independent back office and reported to the managing director office. Analyses of counterparty risks as well as audits of the assets management functions are regularly carried out.

Deposits received by the CBAK are remunerated on the basis of the European Central Bank (ECB) deposit facility rate, while in average the return obtained by the CBAK is closed to the ECB minimum bid rate. CBAK is taking a margin which contributes to its earnings.

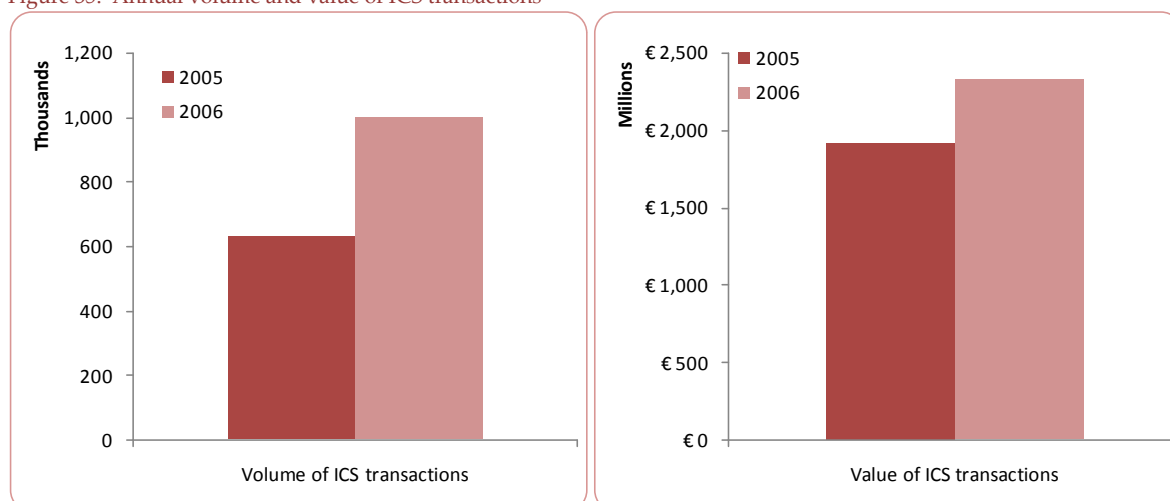
5.4. Services Provided to the Financial Community

5.4.1. Payments System

One of the objectives of the CBAK is to foster an efficient and safe system for domestic payments. Since its establishment, the CBAK has actively pursued this objective, and a major milestone was achieved in May 2001, when the Interbank Clearing System (ICS) was established in order to facilitate the domestic payment operations through the banking system. The CBAK not only operates and oversees the ICS but also participates directly in its operations along with all commercial banks.

The volume and the value of transactions routed through the ICS have been steadily increasing, reflecting the relative increase of non-cash payments and the growth of confidence in the domestic banking system. Meanwhile, ICS has undergone continuous technological development as the means of transactions have been streamlined and enriched.

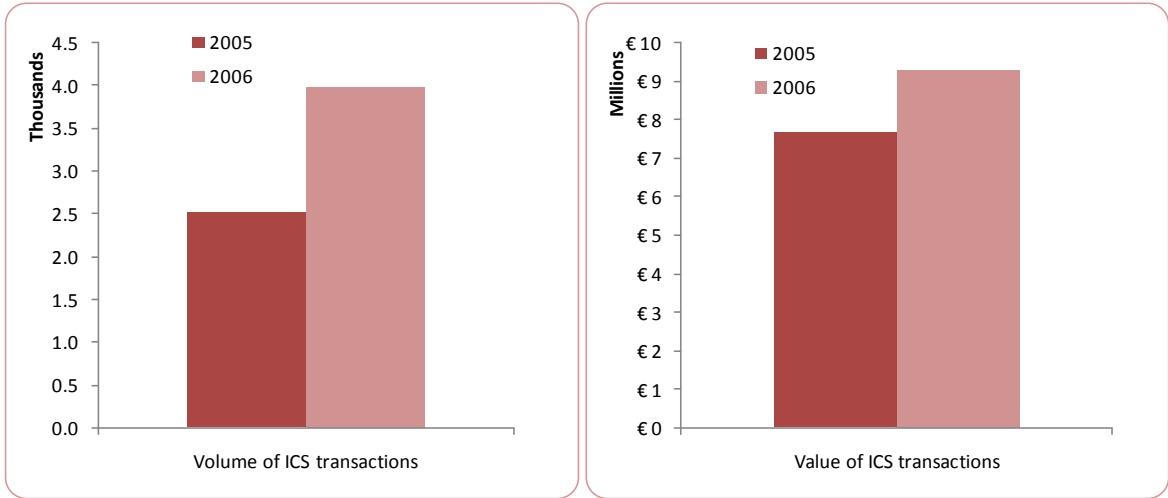
Figure 35: Annual volume and value of ICS transactions



Source: CBAK (2007)

Like previous years, in 2006, the year-on-year increase of both volume and value of ICS transactions was significant. During 2006, around 997 thousand transactions with a total value of euro 2,325 million were channeled through the ICS. Compared to the ICS transactions in the previous year, the volume of transactions increased 58 percent, and the value of transactions increased 21 percent.

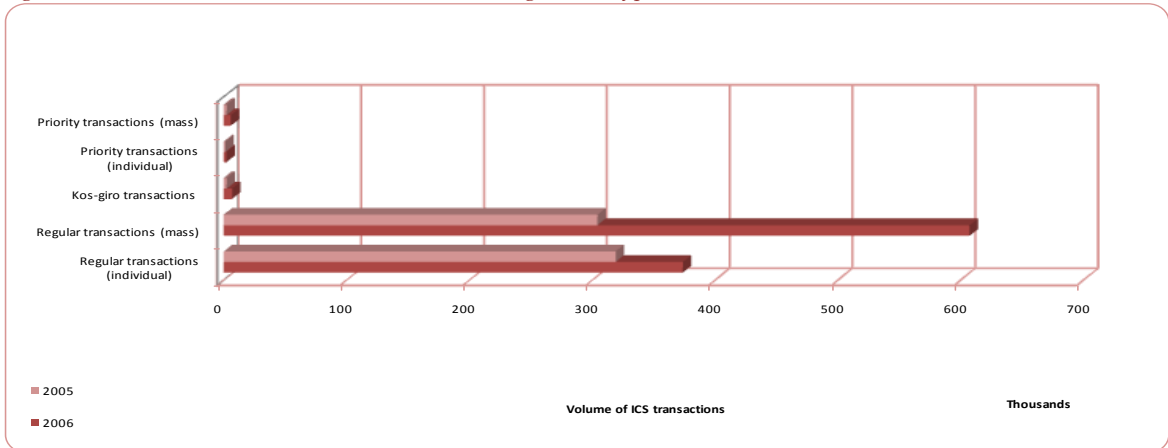
Figure 36: Daily average volume and value of ICS transactions



Source: CBAK (2007)

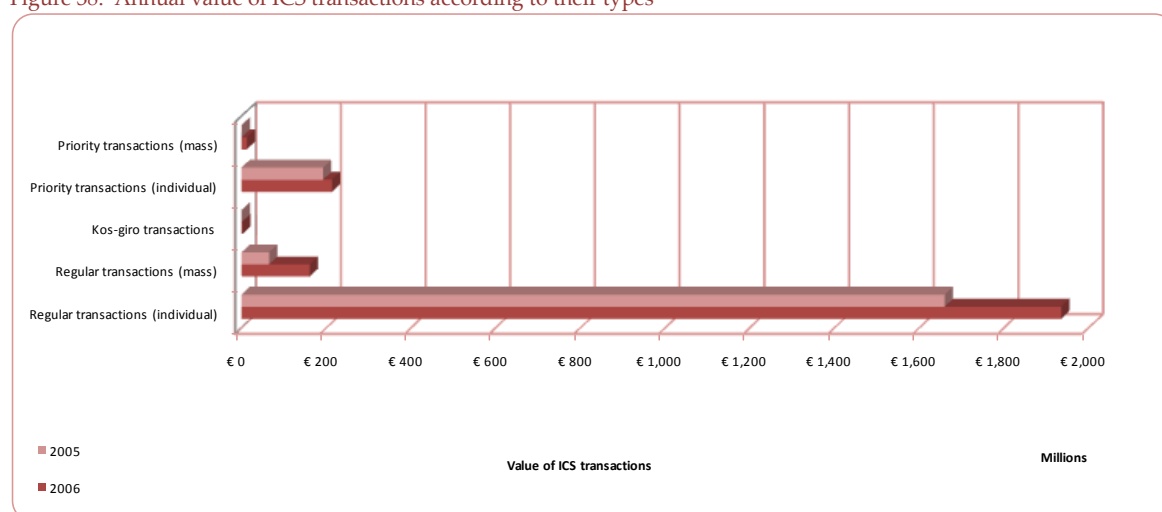
The significant growth of the ICS transactions can also be seen from the daily average data. The daily value of ICS transactions in 2006 was around euro 9.3 million, compared to around euro 7.7 million in 2005. Then, the daily volume of ICS transactions in 2006 was nearly 4.0 thousand, compared to around 2.5 thousand in 2005.

Figure 37: Annual volume of ICS transactions according to their types



Source: CBAK (2007)

Figure 38: Annual value of ICS transactions according to their types



Source: CBAK (2007)

Regular transactions constitute around 99 percent of ICS transactions, and they are channeled through ICS as either individual (one-to-one) transactions or mass (one-to-many or many-to-one) transactions. They are cleared through regular clearing sessions and settled on a net basis. It has to be mentioned that in 2006, the second daily clearing session was introduced due to the increase of the volume of regular transactions. Kos-giro transactions represent a distinct type of regular transactions that are also cleared through clearing sessions and settled on a net basis. They are channeled through ICS as mass (many-to-one) transactions. Whereas the individual regular transactions are designed for payments in general and mass regular payments are designed for payments and collections of various entities, the Kos-giro transactions are designed for standardized and automated collections of large billing institutions. The Kos-giro transactions were introduced in 2005 and had a significant relative increase in 2006.

Priority transactions still represent a small fraction of overall ICS transactions, but their volume has been increasing considerably each year. They are cleared and settled immediately on a gross basis. Similar to regular transactions, priority transactions can be channeled through ICS as either individual or mass transactions.

The five distinct types of ICS transactions can be grouped into two categories depending on whether they are settled on a net or gross basis as indicated above. Transactions settled on a net basis continue to dominate over transactions settled on a gross basis. In terms of volume, transactions settled on a gross basis, despite their annual doubling in 2006, continue to represent less than one percent of ICS transactions. In terms of value, though, transactions settled on a gross basis represent more than 10 percent of ICS transactions, and in 2006 they had an annual increase of nearly 20 percent.

Figure 39: Annual volume and value of ICS transactions: Net vs. Gross



Source: CBAK (2007)

As a direct participant in the ICS, the CBAK takes part in the channeling of domestic payment orders on behalf of and for the account of its clients. During 2006, the CBAK sent through ICS over 109.6 thousand outgoing payment orders, and it received through ICS 60.3 thousand incoming payment orders. Expressed in value, the amount of outgoing payment orders in 2006 was euro 659.6 million, and the amount of incoming payment orders was euro 913.9 million. The CBAK remained in terms of both value and volume of transactions the largest participant in the ICS.

5.4.2. Kos-giro

The Kos-giro scheme represents a major feature of the payments infrastructure. Its introduction a year earlier was a major achievement in the development of low value high volume retail payments. Kos-giro has been designed to facilitate bill payments through standardization and automation of an efficient scheme for large billers, payers and the banking sector.

The Kos-giro is based on internationally accepted standards and provides a way for the payer to pay bills to the biller through the banking system. The biller provides the payer with the bill (payment request) with a standardized payment form attached, which contains payment details in a bar code. When the form is presented to the bank, automatically the payment details are obtained through bar code reader device and the payment is initiated, i.e. the payer's account is debited or the payer pays in cash. Actually, if the biller has the account at the same bank, the payment is finalized immediately, i.e. the biller's account is credited. Alternatively, the payment is finalized after being channeled through ICS. In addition, Kos-giro also provides for a standardized and efficient way of providing necessary details to the biller for automated reconciliation.

The Kos-giro scheme underwent significant developments in 2006. Although initially, designed as scheme to enable free-of-charge processing of bills for the payer, it was adjusted to enable also the alternative processing (with charges borne by the payer) depending on the position of the biller. Regarding the original arrangement an agreement among banks was achieved in 2006 laying out

the interbank fee policy and procedure. In the course of the year, two new billing institutions joined the Kos-giro scheme KEK for electricity bills and Kosovo Property Agency for its rental scheme. Also, the UNMIK Customs Service has made the necessary preparations and is expected to join the scheme in early 2007.

5.4.3. Credit Registry of Kosovo

One of the main services that the CBAK provides to the financial community, namely credit providing institutions, is making available the credit reports on their credit applicants and borrowers through the Credit Registry of Kosovo (CRK) system that was introduced in 2006. The CRK is designed as a web-based application and is accessible online and in real time by credit providing institutions. In the CRK, credit providing institutions enter and update data on their granted credits, and they may obtain from the CRK a summary report on level and status of outstanding credits related to their individual borrowers or credit applicants. The CRK is designed also that through CBAK each interested person could obtain own credit details. Then, it also serves for the supervisory purposes of the Bank Supervision.

The CRK provides an important tool for functioning of the credit market. It enables better assessment of creditworthiness and risks of the borrower / credit applicant and, as a result, it greatly facilitates the credit granting process.

During 2006, the CRK underwent several upgrades in order to enhance its function for both the credit providing institutions and the Bank Supervision. In order to better meet needs and inquiries of credit providing institutions and Bank Supervision, a special organizational unit was established in the second half of 2006. Apart from running the system, this unit also coordinates its further development and monitors technical compliance of credit providing institutions.

5.5. Research and Statistics Activities

The greatest accomplishment of the Research and Statistics Directorate (RSD) during 2006 was the compilation of the Kosovo Balance of Payments (BOP) statistics for two consecutive years, 2004 and 2005. This is the first time that the BOP statistics were compiled and disseminated by the RSD, as published in CBAK Bulletin No. 3. Concerning the financial sector statistics, they have been improved in terms of quality and quantity, thus providing a reliable source of information for various users.

The RSD has continued to publish the Monthly Statistics Bulletin (MSB). In December of 2006, the RSD published the 64th edition of the MSB (with quarterly assessment), with the primary objective of improving the statistics in Kosovo. Also, the dissemination of the time-series on the official CBAK website and in the layout of the bulletin, including the monthly data since end-2000, seems to be appreciated by the users.

The CBAK Bulletin (Structure of the Financial Sector) was also compiled and published in 2006. It contains information on the financial sector in Kosovo, with special reference to the banking sector, and describes the main developments in the sector. In the future, this information will be included in a new publication with the title of the Financial Stability Report.

During 2006, two studies were initiated within the RSD. One study related to the intermediation costs of the banking sector and the second related to the privatization process in Kosovo. The studies are continuing and the results will be published by the CBAK.

6. Internal Developments

6. Internal Developments

6.1. New Regulation on CBAK

In August 2006, The Special Representative of the Secretary General (SRSG) has signed a new regulation on the Central Banking Authority of Kosovo. This new regulation has been drafted with the aim of increasing the role of Kosovars and Kosovo's Institutions.

The new regulation asserts the role of the CBAK in the financial sector through two principal objectives: (i) fostering the soundness, solvency and efficient functioning of a stable market-based financial system, encouraging market emergence of safe financial instruments; and (ii) supporting the general economic policies in Kosovo with a view to contribute to an efficient allocation of resources in accordance with the principles of an open market economy.

The tasks of the CBAK are clearly identified in the areas of financial supervision, payments systems, economic studies, participation and membership in international financial institutions, organizations and councils which falls within its fields of competence.

Main provisions of the newly approved CBAK Regulation No. 2006/47 are:

- General Powers have been broaden in order to ensure operational independency and neutrality- (Section 4.2). C
- Capital shall increase from 10 to 20 million Euro-(Sections 12.1)
- Composition of The Governing Board ensures majority of the member appointed by the Kosovar institutions- (Section 18) - The Governing Board shall be composed of five members appointed by the Special Representative of the Secretary-General, the Managing Director who shall be the Chief Executive Officer of the CBAK, and four non-executive Directors among which the Chairperson of the Board. In consultation with the Special Representative of the Secretary-General: (a) the Managing Director will be nominated by a proposal of the PISG which, after approval by the Assembly, shall be submitted for appointment to the SRSG1. Two non-executive Directors shall be nominated by a proposal of the PISG, one of which upon proposal to the PISG by the Ministry of Finance and Economy, and both of which after approval by the Assembly, shall be submitted to the SRSG for appointment; and (b) One non-executive Director will be the Director of the Treasury and another non-executive Director will be nominated by a proposal by UNMIK. As a transitional provision, the SRSG shall be appoint directly the first person to assume the responsibilities of Managing Director (Section 10). One of the two non-executive Directors appointed by the SRSG shall be designated by the SRSG as the Chairperson of the Governing Board, following consultations with the Board members. Governing Board members, except the Directors of the Treasury, and the two Deputy managing Directors, must be persons of recognized integrity and professional high education and experience in financial, banking, or legal matters, without any political mandate, current or having lasted less than one year. Previous governing Board was composed of 7 members, all directly appointed by The SRSG
- International Functions are enlarged –(Section 8)
- A greater role in the field of economic information – (Section 9)
- Financial independence is ensured – (Section 14)

6.2 Physical Security Upgrade Project

A very important and large Project related to the security upgrade of the CBAK building started in April 2006 and by the end of 2006 around 90% of projected works were completed.

The first and main aim of this project was to ensure the safe and secure function of the Bank, the execution of its everyday transactions and in the handling of major money transfers. Consequently, new areas for different categories of transfers have been relocated and high security devices have been installed accordingly. Subsequently, a comprehensive Access Control system has been installed and restricted areas have been provided with Biometric door Access Control, including complete new computer network (LAN), telephone network and entire electrical system. In addition, a complete new system of CCTV cameras for the whole building together with the external areas, including a new Intruder Alarm system linked to the Police, then a new Fire Alarm system was installed. There has been rational rearrangement of office space as well.

Also, significant upgrade has been done with respect to Health and Fire Safety and outside the building as well. For the particular care of disabled persons, a disabled ramp has been constructed outside the building, whereas the entire roof waterproof system has been changed.

Last but not least, it is to be highlighted that complete Project has been performed according to the best EU standards and CBAK has complied all the time with all required permissions from respective authorities.

Finally, the CBAK acknowledges great contribution and understanding shown by its staff in performing the business activities without any interruption parallel with the execution of this large and very important Project.

6.3 Governance and Internal Control

Inspector General exercises the function of head of internal control. He is appointed by the Managing Director with the approval of the Governing Board and could be removed from office only by a decision of the Special Representative of the Secretary-General. The present Inspector General has been appointed for a five years mandate starting February 2007.

Inspector General is one of the three members of the audit committee –the two others are Board members- and he reports both to the managing Director and to the Audit committee, and last through this channel to the Board.

The Office of the Inspector General comprises two units: internal audit and budget control (operations analysis and cost accounting).

6.3.1 Internal audit

Internal audit has worked according to the Annual Plan -approved by both the Audit Committee and the Governing Board- which is based on a risk approach. Depending of the foreseen risks, controls and audits are conducted from a monthly to an annual basis, generally at the initiative of the Inspector General, while the Managing Director and the Audit Committee are also at the origin of targeted audits

Numerous controls on valuable assets, namely cash, and accounts reconciliation were performed in the course of last year, showing only very little discrepancies. Regarding audits themselves, they have aimed to achieving the following goals:

- Fulfillment of objectives and aims defined by the management
- Rational and effective usage of assets
- Responsibility and integration of information
- Compliance of operations with policies, plans, procedures, regulations and laws in force.

In order to share experience and to strengthen capacities, the Inspector General has embarked in an extensive cooperation program with the central banks of the region, while internal control activities have still benefited from training and technical assistance provided by foreign institutions. In that respect, the Inspector General and his staff have joined the International Institute of Auditors.

6.3.2 Budget control

This unit controls the conformity of expenditures with the budgetary lines approved by the Governing Board; it also gives a special focus on the compliance of procurement process and documentation of expenses. It has started to perform detailed operational and cost accounting analyses; these functions will be developed in 2007 and 2008.

6.4 Human Resources Development

The Year 2006 marks an important set of milestones related to further increase of CBAK staff knowledge, skills and expertise.

During the year 2006, more than 45% of all CBAK staff participated in relevant courses organized by different international institutions (IMF - Joint Vienna Institute, European Central Bank, Deutsche Bundesbank, Banque de France, Austrian National Bank, The Federal Reserve Bank of New York, Bank of Japan etc.) and other institutions in Kosovo (Kosovo Bankers Association, SCAAK, etc.).

In addition, a special one year Professional Development Program and the three months Executive Leadership Program sponsored by USAID have been successfully completed by five senior managers of the CBAK. Also, in line with its Staff Training and Development Policy, the CBAK continued to sponsor enrollment of its most skilled staff in job related postgraduate studies.

During 2006, the average number of CBAK employees stood at 141, which is just 1% higher compare to its average during 2005. In terms of the structure, 48% was female employees, and 4,5% from Minorities, whereas in terms of qualifications around 60% of employees held university degree.

6.5 CBAK Organizational Structure Upgrade in 2006

The overall objective of organizational structure change in 2006 was to enhance the CBAK's development by strengthening its capacity to deliver its strategic agenda, thanks to a carefully designed organization structure.

Introduced in January 2006, the new Organizational Structure has highlighted the Kosovarisation process in the management of the CBAK, through appointment of two senior local staff (Chief Operations Officer and Chief Supervision Officer) as Deputy Managing Directors of the CBAK. At the same time, aimed to further increase its efficiency, accountability and transparent governance, two organizational pillars of the CBAK (Financial Supervision and Central Banking Operations) were reorganized into several directorates, two in Financial Supervision and four in the Central Banking Operations. In 2006, only one foreigner carried out executive functions (the Managing Director), while three expatriate experts held the following positions: adviser for financial supervision, senior officer in charge of financial regulation, personal assistant to the managing director.

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7. Financial Statements of the Central Banking Authority of Kosovo

Central Banking Authority of Kosovo

Financial statements

as at and for the year ended 31 December 2006

(with independent auditor's report thereon)

Central Banking Authority of Kosovo

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Independent Auditors' Report

To the Governing Board of the
Central Banking Authority of Kosovo

We have audited the accompanying financial statements of Central Banking Authority of Kosovo ("the Bank"), which comprise the balance sheet as at 31 December 2006, and the income statement, statement of changes in equity and cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes.

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. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatements, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

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 relevant ethical requirements and plan and perform the audit to obtain reasonable assurance whether the financial statements are free of 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 principles 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 opinion.

KPMG Albania Sh.p.k., an Albanian limited liability company and a member firm of the KPMG Network of independent member firms affiliated with KPMG International, a Swiss cooperative.



Opinion

In our opinion, the financial statements give a true and fair view of the financial position of the Bank as at 31 December 2006, and of its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

KPMG Albania Sh.p.k.

A handwritten signature in blue ink that reads 'KPMG Albania'.

18 May 2007
Prishtina, Kosovo

Central Banking Authority of Kosovo

Balance sheet

As at 31 December

<i>In EUR '000</i>	Note	2006	2005
Assets			
Cash on hand	6	11,136	24,464
Current accounts with non resident banks	7	22,480	23,765
Treasury bills	8	203,398	159,269
Deposit accounts with non resident banks	9	404,025	190,633
Property and equipment	10	1,262	329
Intangible assets	11	144	165
Other assets	12	177	377
Total assets		642,622	399,002
Liabilities			
Due to domestic banks	13	94,477	82,518
Due to local governmental institutions	14	475,821	229,891
Due to public and commercial entities	15	45,076	64,126
Other domestic liabilities	16	2,658	2,745
Total liabilities		618,032	379,280
Capital and reserve			
Statutory fund	17	10,000	10,000
Reserve fund	18	14,590	9,722
Total capital and reserve		24,590	19,722
Total liabilities, capital and reserves		642,622	399,002

The notes on pages 1 to 30 are an integral part of these financial statements.

These financial statements set out on pages 1 to 30 were approved by the Management of the CBAK on 18 May 2007 and signed on its behalf by:


Michel Svetchine
Managing Director


Gani Gerguri
Deputy Managing Director

Central Banking Authority of Kosovo

Income statement

For the year ended 31 December

<i>In EUR '000</i>	Note	2006	2005
Interest income		15,187	7,369
Interest expense		(8,731)	(3,432)
Net interest income	19	<u>6,456</u>	<u>3,937</u>
Fee and commission income		744	705
Fee and commission expense		(250)	(557)
Net fee and commission income	20	<u>494</u>	<u>148</u>
Grant revenue	21	317	468
Other operating income	22	<u>792</u>	<u>311</u>
Operating income		<u>8,059</u>	<u>4,864</u>
Personnel expenses	23	(1,254)	(1,085)
Depreciation and amortisation	10,11	(282)	(366)
General and administrative expenses	24	(870)	(822)
Operating expenses		<u>(2,406)</u>	<u>(2,273)</u>
Profit for the period		<u>5,653</u>	<u>2,591</u>

The notes on pages 1 to 30 are an integral part of these financial statements.

Central Banking Authority of Kosovo

Statement of changes in equity for the year ended 31 December 2006

<i>In EUR '000</i>	Statutory fund	Reserve fund	Retained Earnings	Total
Balance at 1 January 2005	10,000	7,513	-	17,513
Profit for the period	-	-	2,591	2,591
Total recognised income and expense	-	-	2,591	2,591
Payments to the Ministry of Finance and Economy	-	(382)	-	(382)
Transfer to reserve fund	-	2,591	(2,591)	-
Balance at 31 December 2005	10,000	9,722	-	19,722
Balance at 1 January 2006	10,000	9,722	-	19,722
Profit for the period	-	-	5,653	5,653
Total recognised income and expense	-	-	5,653	5,653
Payments to the Ministry of Finance and Economy	-	(785)	-	(785)
Transfer to reserve fund	-	5,653	(5,653)	-
Balance at 31 December 2006	10,000	14,590	-	24,590

The notes on pages 1 to 30 are an integral part of these financial statements.

Central Banking Authority of Kosovo

Statement of cash flows

For the year ended 31 December

<i>In EUR '000</i>	Notes	2006	2005
Cash flows from operating activities			
Net surplus for the year		5,653	2,591
Adjustments for:			
Depreciation	10	137	163
Amortisation	11	145	204
Grant revenue for the year	16	(124)	(199)
Interest income	19	(15,187)	(7,369)
Interest expense	19	8,731	3,432
<i>Operating cash flows before changes in working capital</i>		<i>(645)</i>	<i>(1,178)</i>
Decrease/(increase) in treasury bills		(57,178)	9,994
Decrease/(increase) in deposit accounts with non resident banks		(24,254)	(2,250)
Decrease/(increase) in other assets		200	(266)
Increase in due to domestic banks		11,959	9,619
Increase in due to local governmental institutions		245,930	4,682
Increase/(decrease) in due to public and commercial entities		(19,050)	31,300
Increase/(decrease) in other domestic liabilities		(5)	611
<i>Cash flows used in operating activities</i>		<i>156,937</i>	<i>52,312</i>
Interest received		13,875	7,426
Interest paid		(8,731)	(3,432)
Net cash from operating activities		162,101	56,506
Cash flows from investing activities			
Acquisition of equipment	10	(1,070)	(65)
Acquisition of intangible assets	11	(124)	(130)
Net cash used in investing activities		(1,194)	(195)
Cash flows from financing activities			
Payments to Ministry of Finance and Economy	18	(785)	(382)
Proceeds from grants	16	42	112
Net cash from financing activities		(743)	(270)
Net (decrease)/increase in cash and cash equivalents		160,164	56,041
Cash and cash equivalents at 1 January		348,834	292,793
Cash and cash equivalents at 31 December	25	508,998	348,834

The notes on pages 1 to 30 are an integral part of these financial statements

Central Banking Authority of Kosovo

Notes to the financial statements

(Amounts in EUR '000, unless otherwise stated)

1. Reporting entity

The Central Banking Authority of Kosovo (the "CBAK"), a successor to the Banking and Payments Authority of Kosovo (BPK) is a distinct public entity with the authority to license, supervise and regulate financial institutions in the territory of Kosovo. The CBAK was established in accordance with the provisions of the United Nations Interim Administration Mission in Kosovo ("UNMIK") Regulation no. 1999/20 issued on November 15, 1999 (as amended on October 1, 2001,) "On the Banking and Payments Authority of Kosovo". Furthermore, on August 24, 2006 Special Representative of the Secretary General has signed a new Regulation on Central Banking Authority of Kosovo and transformed the Banking and Payments Authority of Kosovo into Central Banking Authority of Kosovo. Under this Regulation the CBAK's principal objectives are to:

- Foster the soundness, solvency and efficient functioning of a stable market based financial system, encouraging market emergence of safe financial instruments; and
- Support the general economic policies in Kosovo with a view to contributing to an efficient allocation of resources in accordance with the principles of an open market economy.

The CBAK has, among others, the following specific powers to:

- Recommend broad policy guidelines to the Special Representative of the Secretary-General of the United Nations and Provisional Institutions of Self Government in areas under its responsibility;
- Formulate and implement measures for, and oversee and regulate, payments and settlement systems for transactions in domestic and foreign currency in Kosovo;
- Own and operate one or more payments systems;
- Act as banker and fiscal agent to the Ministry of Finance and Economy and, to provide financial advice at its request;
- Hold foreign currency deposits of banks, Ministry of Finance and Economy and other public entities;
- Ensure an adequate supply of bank notes and coins for the settlement of cash transactions;
- License, supervise and regulate financial institutions; and
- Conduct regular economic and monetary analysis of the Kosovo economy, make public the results, and submit proposals and measures to the United Nations Interim Administration Mission in Kosovo and the Provisional Institutions of Self Government on the basis of such analysis.

The CBAK operates from the premises located in Pristina.

The address of the registered office of the CBAK is as follows:

33, Garibaldi Street,
Pristina,
Kosovo.

Central Banking Authority of Kosovo

Notes to the financial statements

(Amounts in EUR '000, unless otherwise stated)

1. Reporting entity (continued)

Governing Board

The Governing Board determines policies for the operations of the CBAK and supervises their implementation. Under UNMIK regulations, the Board is composed of five members appointed the Special Representative of the Secretary General.

As at 31 December 2006 the Governing Board of CBAK comprised of the following members:

- Mr Ajri Begu, Chairperson of Governing Board, Non-executive Director
- Mr Michel Svetchine, Managing Director of CBAK
- Ms Chiara Bronchi, Non-executive Director
- Mr Lulzim Ismajli, Non-executive Director
- Mr Gazmend Luboteni, Non-executive Director

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.

(c) Functional and presentation currency

These financial statements are presented in euro ("EUR"), which is the CBAK'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 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.

Central Banking Authority of Kosovo

Notes to the financial statements

(Amounts in EUR '000, unless otherwise stated)

2. Basis of preparation (continued)

(d) Use of estimates and judgments (continued)

In particular, information about significant areas of estimation uncertainty and critical judgments in applying accounting policies that have the most significant effect on the amount recognized in the financial statements are described in note 4.

3. Significant accounting policies

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

(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 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 the income statement 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.

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 income statement include:

- interest on financial assets and liabilities at amortised cost on an effective interest rate basis.

Central Banking Authority of Kosovo

Notes to the financial statements

(Amounts in EUR '000, unless otherwise stated)

3. Significant accounting policies (continued)

(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 of transaction fees for operating accounts, fund transfers and licensing fees are recognized as the related services are performed.

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

(d) General and administrative expenses

The general and administrative expenses are recognized when incurred.

(e) Employee benefits

(i) Defined contribution plans

The CBAK makes compulsory social security contributions that provide pension benefits for employees upon retirement. The local authorities are responsible for providing the legally set minimum threshold for pensions in Kosovo under a defined contribution pension plan. The CBAK's contributions to the benefit pension plan are charged to the income statement as incurred.

Additionally the CBAK recognizes fixed contribution payable into a separate pension fund which is maintained by CBAK. CBAK has no legal or constructive obligation to pay further contributions.

(ii) Short-term benefits

Short-term employee benefit obligations are measured on an undiscounted basis and are expensed as the related service is provided.

A provision is recognised for the amount expected to be paid under short-term cash bonus or profit-sharing plans if the CBAK has a present legal or constructive obligation to pay this amount as a result of past service provided by the employee and the obligation can be estimated reliably.

(f) Taxation and profit allocation

The CBAK is exempt from income tax according to the UNMIK Regulation 1999/20 issued on 15 November 1999 (as amended on 1 October 2001) "On the Banking and Payments Authority of Kosovo" replaced with the new UNMIK Regulation 2006/47 issued on 24 August 2006 "On Central Banking Authority of Kosovo" and is required by law to pay any balance of its net income directly to the Ministry of Finance and Economy after allocation to replenish the levels of reserve funds directly by the Governing Board.

(g) Financial assets and liabilities

(i) Recognition

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

Central Banking Authority of Kosovo

Notes to the financial statements

(Amounts in EUR '000, unless otherwise stated)

3. Significant accounting policies (continued)

(g) Financial assets and liabilities (continued)

(ii) Derecognition

The CBAK 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 the CBAK is recognized as a separate asset or liability.

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

(iii) Offsetting

Financial assets and liabilities are set off and the net amount is presented in the balance sheet when, and only when, the CBAK 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 for impairment.

(v) Fair value measurement

The determination of fair values of financial assets and financial liabilities is determined by using valuation techniques. Valuation techniques include net present value techniques, the discounted cash flow method, comparison to similar instruments for which market observable prices exist, and valuation models. The CBAK uses widely recognised valuation models for determining the fair value of common and more simple financial instruments. For these financial instruments, inputs into models are market observable.

(vi) Identification and measurement of impairment

At each balance sheet date the CBAK 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.

Central Banking Authority of Kosovo

Notes to the financial statements

(Amounts in EUR '000, unless otherwise stated)

3. Significant accounting policies (continued)

(g) Financial assets and liabilities (continued)

(vi) Identification and measurement of impairment (continued)

Objective evidence that financial assets are impaired can include default or delinquency by a borrower, restructuring of a placement or advance by the CBAK on terms that the CBAK 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 the CBAK, or economic conditions that correlate with defaults in the group.

Losses are recognised in profit or loss and reflected in an allowance account against placements and advances.

When a subsequent event causes the amount of impairment loss to decrease, the impairment loss is reversed through profit or loss.

(vii) Designation at fair value through profit or loss

The CBAK has designated financial assets and liabilities at fair value through profit or loss when either:

- the assets or liabilities are managed, evaluated and reported internally on a fair value basis;
- the designation eliminates or significantly reduces an accounting mismatch which would otherwise arise; or
- the asset or liability contains an embedded derivative that significantly modifies the cash flows that would otherwise be required under the contract.

Financial assets that have been designated at fair value through profit or loss include treasury bills in the 2005 financial statements.

(h) 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 the CBAK in the management of its short-term commitments.

Cash and cash equivalents are carried at amortised cost in the balance sheet.

(i) Investment securities

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

(i) Held-to-maturity

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

Central Banking Authority of Kosovo

Notes to the financial statements

(Amounts in EUR '000, unless otherwise stated)

3. Significant accounting policies (continued)

(i) Investment securities (continued)

(i) Held-to-maturity (continued)

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 the CBAK from classifying investment securities as held-to-maturity for the current and the following two financial years.

(j) 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 the CBAK and its cost can be measured reliably. The costs of the day-to-day servicing of property and equipment are recognised in profit or 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:

	2006	2005
• Vehicles	5 years	5 years
• Office and other equipment	5 years	5 years
• Computer equipment	3 years	3 years

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

Central Banking Authority of Kosovo

Notes to the financial statements

(Amounts in EUR '000, unless otherwise stated)

3. Significant accounting policies (continued)

(k) Intangible assets

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

Subsequent expenditure on software assets 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 (2005: 3 years).

(l) Impairment of non-financial assets

The carrying amounts of the CBAK'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.

(m) Deposits and other financial liabilities

Deposits are the CBAK's sources of funding. They are initially measured at fair value plus transaction costs, and subsequently measured at their amortized cost using the effective interest method.

Central Banking Authority of Kosovo

Notes to the financial statements

(Amounts in EUR '000, unless otherwise stated)

3. Significant accounting policies (continued)

(n) Grant revenue

Grants that compensate the CBAK for expenses incurred are recognized as revenue in the income statement on a systematic basis in the same periods in which the expenses are incurred. Grants that compensate the CBAK for the cost of an asset are recognized in the income statement as revenue on a systematic basis over the useful life of the asset.

(o) Donor financed salaries

Certain members of the management of the CBAK are international experts appointed by international organisations who provide financial support to the CBAK. In addition these international organisations also appoint short term experts and consultants as the need arises. The financial support of these international organisations includes but it is not limited to the payment of the salaries to these management and consultant appointments. As this assistance is paid by international directly to the appointee the extent of the payments are not known nor are they included in these financial statements. The length of the appointment of the management personnel is not absolutely clear, though it is the objective of the international organisations to ultimately replace these appointees with local staff.

(p) Fiduciary activities

In certain specific instances the CBAK acts as fiscal agent and paying agent of the Ministry of Finance and Economy. Assets and income arising from these activities are excluded from these financial assets where the CBAK acts in fiduciary capacity such as nominee or agent.

(q) Provisions

A provision is recognised if, as a result of a past event, the CBAK 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 the CBAK 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, the CBAK recognises any impairment loss on the assets associated with that contract.

Central Banking Authority of Kosovo

Notes to the financial statements

(Amounts in EUR '000, unless otherwise stated)

3. Significant accounting policies (continued)

(r) Reserve fund

In accordance with UNMIK Regulation 1999/20 (as amended) each year the CBAK shall allocate net income to the general reserve fund until the capital and the general reserve fund amount to 5% of the aggregate amount of the credit balance of all accounts maintained on the books of the CBAK by account holders shown on the balance sheet of the CBAK for the year ended of each financial year.

(s) New standards and interpretations not yet adopted

A number of new standards, amendments to standards and interpretations are not yet effective for the year ended 31 December 2006, and have not been applied in preparing these financial statements:

- *IFRS 7 Financial Instruments: Disclosures* (effective from 1 January 2007). The Standard will require increased disclosure about the significance of financial instruments for an entity's financial position and performance, and qualitative and quantitative disclosures on the nature and extent of risks. The CBAK considers that the significant additional disclosures required will relate to its financial risk management objectives, policies and processes. The CBAK will apply IFRS 7 from annual periods beginning 1 January 2007.
- *IAS 1 Amendment to IAS 1 Presentation of Financial Statements – Capital Disclosures* (effective from 1 January 2007). As a complimentary amendment arising from IFRS 7 (see above), the Standard will require increased disclosure in respect of the CBAK's capital. This amendment will require significantly more disclosures regarding the capital structure of the CBAK. The CBAK will apply the Amendment to IAS 1 from annual periods beginning 1 January 2007.
- *IFRS 8 Operating Segments* (effective from 1 January 2009). The Standard requires segment disclosure based on the components of the entity that management monitors in making decisions about operating matters. Operating segments are components of an entity about which separate financial information is available that is evaluated regularly by the chief operating decision maker in deciding how to allocate resources and in assessing performance. The CBAK will apply IFRS 8 from annual periods beginning 1 January 2009.
- *IFRIC 7 Applying the Restatement Approach under IAS 29 Financial Reporting in Hyperinflationary Economies* (effective for annual periods beginning on or after 1 March 2006). The Interpretation contains guidance on how an entity would restate its financial statements pursuant to IAS 29 in the first year it identifies the existence of hyperinflation in the economy of its functional currency. The Interpretation is not relevant to the CBAK's operations as the CBAK does not have the currency of a hyperinflationary economy as its functional currency.
- *IFRIC 8 Scope of IFRS 2* (effective for annual periods beginning on or after 1 May 2006). The Interpretation clarifies that the accounting standard IFRS 2 Share-based Payment applies to arrangements where an entity makes share-based payments for apparently none or inadequate consideration. The Interpretation is not relevant to the CBAK's operations.

Central Banking Authority of Kosovo

Notes to the financial statements

(Amounts in EUR '000, unless otherwise stated)

3. Significant accounting policies (continued)

(s) New standards and interpretations not yet adopted (continued)

- *IFRIC 9 Reassessment of Embedded Derivatives* (effective for annual periods beginning on or after 1 June 2006). The Interpretation requires that a reassessment of whether an embedded derivative should be separated from the underlying host contract should be made only when there are changes in the terms of the contract that significantly modify the cash flows that otherwise would be required under the contract. The Interpretation is not relevant to the CBAK's operations.
- *IFRIC 10 Interim Financial Reporting and Impairment* (effective for annual periods beginning on or after 1 November 2006). The Interpretation prohibits the reversal of an impairment loss recognised in a previous interim period in respect of goodwill, investments in equity instruments or financial assets carried at cost. The Interpretation is not relevant to the CBAK's operations.
- *IFRIC 11 IFRS 2 – Group and Treasury Share Transactions* (effective for annual periods beginning on or after 1 March 2007). The Interpretation requires a share-based payment arrangement in which an entity receives goods or services as consideration for its own equity-instruments to be accounted for as an equity-settled share-based payment transaction, regardless of how the equity instruments needed are obtained. It also provides guidance on whether share-based payment arrangements, in which suppliers of goods or services of an entity are provided with equity instruments of the entity's parent, should be accounted for as cash-settled or equity-settled in the entity's financial statements. The Interpretation is not relevant to the CBAK's operations.
- *IFRIC 12 Service Concession Arrangements* (effective from 1 January 2008) The Interpretation provides guidance to private sector entities on certain recognition and measurement issues that arise in accounting for public-to-private service concession arrangements. The Interpretation is not relevant to the CBAK's operations.

(t) Comparatives

For more appropriate presentation of transactions, classification of certain items in a current year financial statements differ from a prior year. Consequently presentation of prior year financial statement has been changed where necessary.

4. Use of estimates and judgments

Management discussed with the Governing Board the development, selection and disclosure of the CBAK's critical accounting policies and estimates, and the application of these policies and estimates.

These disclosures supplement the commentary on financial risk management (see note 27).

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Notes to the financial statements

(Amounts in EUR '000, unless otherwise stated)

5. Restatement of prior year financial statements

The CBAK had erroneously recorded in the previous year's financial statements additional grants to be received and related deferred grant revenue in the amount of EUR 413 thousand. As result the CBAK assets and liabilities as at 31 December 2005 were overstated by EUR 413 thousand. The financial statements as at and for the year ended 31 December 2005 were restated accordingly. In particular the amounts presented in the financial statements for other asset and other domestic liabilities are decreased by EUR 413 thousand.

6. Cash on hand

Cash on hand is denominated as follows:

	2006	2005
EUR	11,123	24,464
USD	13	-
Total	11,136	24,464

7. Current accounts with non resident banks

These accounts were held at the following banks:

	2006	2005
Deutsche Bundesbank	21,967	22,788
Raiffeisen Zentralbank Osterreich AG	237	2
Svenska Handelsbanken	211	33
Dresdner Bank	48	91
Commerzbank AG	17	851
Total	22,480	23,765

8. Treasury bills

Treasury bills are discounted debt securities issued by governments of countries part of the European Union with maturities from three to six months. All bills are denominated in EUR and are to be held to maturity with effective interest rates ranging from 3.07% to 3.59% (2005: from 2% to 2.44%). They all have highest grade credit rating graded by the three credit rating agencies – Standard & Poor's, Fitch Ratings, or Moody's.

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Notes to the financial statements

(Amounts in EUR '000, unless otherwise stated)

9. Deposit accounts with non resident banks

Deposit accounts with non resident banks are composed of:

	2006	2005
Time deposits		
Raiffeisen Zentralbank Osterreich AG	69,818	33,500
Svenska Handelsbanken	53,400	36,000
HBOS Treasury Service Plc	50,368	29,342
ING Bank	49,646	33,644
Dresdner Bank	46,300	15,400
Deutsche Bundesbank	45,000	5,000
KBC	44,612	21,486
Rabobank	21,680	8,334
Danske Bank	14,639	7,277
Commerzbank AG	7,100	500
	402,563	190,483
Interest accrued on time deposits		
Raiffeisen Zentralbank Osterreich AG	75	7
Svenska Handelsbanken	279	21
HBOS Treasury Service Plc	243	60
ING Bank	278	19
Dresdner Bank	190	11
Deutsche Bundesbank	72	2
KBC	165	12
Rabobank	146	10
Danske Bank	6	8
Commerzbank AG	8	-
	1,462	150
Total	404,025	190,633

Deposit placed with non resident banks are denominated in EUR and earn interest at effective interest rates ranging from 3.16% to 3.79% (2005: between 1.95% and 2.4%) and have original maturities from 7 to 367 days (2005: from 4 to 186 days).

Central Banking Authority of Kosovo

Notes to the financial statements

(Amounts in EUR '000, unless otherwise stated)

10. Property and equipment

	Equipment	Computers	Vehicles	Assets in course of construction	Total
Cost					
Balance at 1 January 2005	469	608	99	112	1,288
Acquisitions	-	116	-	137	253
Disposals	-	(436)	-	-	(436)
Transfers	-	-	-	(188)	(188)
Balance at 31 December 2005	469	288	99	61	917
Balance at 1 January 2006	469	288	99	61	917
Acquisitions	-	63	27	980	1,070
Disposals	-	-	(39)	-	(39)
Balance at 31 December 2006	469	351	87	1,041	1,948
Depreciation					
Balance at 1 January 2005	253	555	53	-	861
Depreciation for the period	84	60	19	-	163
Disposals	-	(436)	-	-	(436)
Balance at 31 December 2005	337	179	72	-	588
Balance at 1 January 2006	337	179	72	-	588
Depreciation for the period	68	50	19	-	137
Disposals	-	-	(39)	-	(39)
Balance at 31 December 2006	405	229	52	-	686
Carrying amounts					
Balance at 1 January 2005	216	53	46	112	427
Balance at 31 December 2005	132	109	27	61	329
Balance at 31 December 2006	64	122	35	1,041	1,262

Assets in course of construction relate to security improvements on the premises where the CBAK is exercising its activity. According to section three of UNMIK/REG/2006/47 Regulation no 2006/47 on the Central Banking Authority of Kosovo the CBAK may for its official business purpose utilize and administer on behalf of the United Nations Interim Administration Mission in Kosovo ("UNMIK") the property and facilities, including moveable and immovable property, located at Garibaldi Street 33, Pristina, Kosovo and previously used by the Public Payment Service of Kosovo. There are no assets pledged as collateral as at 31 December 2006 (2005: none).

Central Banking Authority of Kosovo

Notes to the financial statements

(Amounts in EUR '000, unless otherwise stated)

11. Intangible assets

	<u>Software</u>
Cost	
Balance at 1 January 2005	691
Acquisitions	85
Disposals	-
Transfers	45
Balance at 31 December 2005	<u>821</u>
Balance at 1 January 2006	821
Acquisitions	22
Disposals	-
Transfers	102
Balance at 31 December 2006	<u>945</u>
Amortization	
Balance at 1 January 2005	452
Amortisation for the period	204
Disposals	-
Balance at 31 December 2005	<u>656</u>
Balance at 1 January 2006	656
Amortisation for the period	145
Disposal	-
Balance at 31 December 2006	<u>801</u>
Carrying amounts	
Balance at 1 January 2005	<u>239</u>
Balance at 31 December 2005	<u>165</u>
Balance at 31 December 2006	<u>144</u>

Central Banking Authority of Kosovo

Notes to the financial statements

(Amounts in EUR '000, unless otherwise stated)

12. Other assets

	2006	2005
Accrued fee income	159	335
Accounts receivable and prepayments	18	42
Total	177	377

Accrued fee income represents estimated license renewal fee forth quarter from local financial institutions.

13. Due to domestic banks

Under the CBAK supervision regulation Rule XVII commercial banks operating in Kosovo are required to maintain liquidity reserve amounting to 10% of their respective total customer deposits. At least half of these reserve balances must be kept in accounts at the CBAK

The reserve balance in excess of 5%, up to 10%, of total customer deposits bears interest of 2.25% as at 31 December 2006 (31 December 2005: 1%). Amount under 5% and over 10% are non interest bearing.

	2006	2005
ProCredit Bank Kosovo	19,039	11,812
Raiffeisen Bank Kosovo	15,232	7,833
Kasabank	5,105	4,875
New Bank of Kosovo	2,270	2,455
Economic Bank of Pristina	2,030	1,818
Bank for Business	1,650	2,108
Credit Bank of Pristina	-	1,281
Total required liquidity reserves	45,326	32,182
ProCredit Bank Kosovo	5,354	14,627
Raiffeisen Bank Kosovo	11,225	7,864
Kasabank	12,133	12,723
New Bank of Kosovo	4,840	4,461
Economic Bank of Pristina	4,008	4,905
Bank for Business	6,487	3,362
Credit Bank of Pristina	99	2,394
National Commercial Bank of Albania	5,005	-
Total current accounts	49,151	50,336
Total	94,477	82,518

Central Banking Authority of Kosovo

Notes to the financial statements

(Amounts in EUR '000, unless otherwise stated)

14. Due to local governmental institutions

Due to local governmental institutions include current accounts from the following:

	2006	2005
Kosovo Trust Agency	275,022	113,132
Ministry of Finance and Economy	200,049	113,013
Other governmental institutions	578	647
UNMIK	172	3,099
Total	475,821	229,891

The effective interest rates for current accounts as at 31 December 2006 are 2.25% (31 December 2005: 1%).

15. Due to public and commercial entities

Due to public and commercial entities include current accounts and time deposits from the following:

	2006	2005
Current accounts		
Insurance companies	18,525	18,218
Public utility corporations	10,369	37,584
Pension funds	8,167	4,222
Other	18	2
	37,079	60,026
Time deposits		
Insurance companies	2,025	-
Pension funds	5,972	4,100
	7,997	4,100
Total	45,076	64,126

The effective interest rates for current accounts as at 31 December 2006 are 2.25% (31 December 2005: 1%) and for time deposits are between 2.56% and 3.39% as at 31 December 2006 (31 December 2005: 1.83 %).

16. Other domestic liabilities

	2006	2005
Liabilities to the Kosovo Government	1,636	1,697
Deferred grant revenue	301	383
Liabilities to the Former National Bank of Kosovo	467	450
Sundry creditors and accruals	218	180
Other domestic liabilities	36	35
Total	2,658	2,745

The balance of due to the Kosovo Government as at 31 December 2006 refers to EUR 1,038 thousand (2005: EUR 1,285 thousand) of rent collected for public buildings until establishment of ownership and EUR 598 thousand (2005: EUR 408 thousand) of supervisory penalties collected from financial institutions since 24 April 2002 and related interest remunerated as of those dates.

Central Banking Authority of Kosovo

Notes to the financial statements

(Amounts in EUR '000, unless otherwise stated)

16. Other domestic liabilities (continued)

Liabilities to the Former National Bank of Kosovo arise from the following. Upon inception, the CBAK inherited certain amounts in cash, in various currencies, from the former National Bank of Kosovo. Also in this balance are included the related interest accumulated during the years since 5 January 2004. The cash was initially converted into DEM 872 thousand on 22 December 2000 and subsequently physically transferred and deposited in the CBAK's account at the Commerzbank AG Frankfurt. Balance of the account as at 1 January 2002 was converted in EUR 446 thousand and the resulting balance as at 31 December 2006 and 31 December 2005 includes this balance and interest remunerated as of those dates.

The movement in deferred grant revenue was as follows:

	Central Fiscal Authority	United States Agency for International Development	Other	Total
Deferred grant revenue at 1 January 2005	386	26	58	470
Grants received during the year	-	-	112	112
Grant revenue for the year	(164)	(26)	(9)	(199)
Deferred grant revenue at 31 December 2005	222	-	161	383
Deferred grant revenue at 1 January 2006	222	-	161	383
Grants received during the year	-	-	42	42
Grant revenue for the year	(73)	-	(51)	(124)
Deferred grant revenue at 31 December 2006	149	-	152	301

17. Statutory fund

The initial statutory fund of the CBAK, totalling DEM 5,000 thousand (EUR 2,556 thousand) was contributed by the Central Fiscal Authority on 31 March 2000. As at 8 June 2004 based on the decision of DSRSG (Deputy of Special Representative of the Secretary General) Pillar IV the statutory fund was increased from EUR 2,556 thousand to EUR 10,000 thousand. The CBAK is reporting directly to the Special Representative of the Secretary General of the United Nations Organisation.

18. Reserve fund

The reserve fund was created during the period to 31 December 2006, in accordance with Regulation 1999/20 replaced from the Regulation 2006/47 dated 24 August 2006 and the decision of the CBAK's Governing Board. All net profit for the year in 2005 was transferred to the reserve fund. For the year 2006 the decision is not yet taken but since the reserve is under the limits determined in the regulation the whole profit of the year will be transferred to the reserve fund.

In 2006 the CBAK paid to the Ministry of Finance and Economy the amount of EUR 785 thousand (2005: EUR 382 thousand), representing the excess of its reserve fund over limits prescribed by the UNMIK Regulation 1999/20 issued on 15 November 1999 (as amended in 1 October 2001) "On the Banking and Payment Authority of Kosovo".

Central Banking Authority of Kosovo

Notes to the financial statements

(Amounts in EUR '000, unless otherwise stated)

19. Net interest income

Net interest income is composed as follows:

	2006	2005
Interest income		
From fixed term placements	9,493	3,999
From treasury bills	5,099	3,052
From current account placements (balances)	594	318
	15,186	7,369
Interest expense		
From current account deposits of non-bank entities	8,116	3,121
From eligible current account deposits of banks	491	233
From fixed term deposits	123	78
	8,730	3,432
Net interest income	6,456	3,937

20. Net fee and commission income

Net fee and commission income is composed as follows:

	2006	2005
Fee income		
From cash deposits	116	117
From foreign incoming transfers	196	165
From foreign outgoing transfers	291	282
From inter-bank clearing system	127	91
Other fees	14	50
	744	705
Fee expenses		
For cash export/import	204	544
For correspondent bank transactions	42	13
Other fees	4	-
	250	557
Net interest income	494	148

21. Grant revenue

Grant revenue is composed as follows:

	2006	2005
CFA	-	167
USAID	-	25
MEF-World bank	142	26
EU	175	250
Total	317	468

Central Banking Authority of Kosovo

Notes to the financial statements

(Amounts in EUR '000, unless otherwise stated)

22. Other operating income

Other operating income includes mainly fees charged to financial institutions in Kosovo as part of issuing or renewing of licenses as well as other statutory fees related to their activities.

23. Personnel expenses

	2006	2005
Wages and salaries	904	808
Social security and health insurance cost	224	225
Staff training	86	19
Governing Board remuneration	22	22
Other	18	11
Total	1,254	1,085

The number of employees of the CBAK as at 31 December 2006 was 143 (31 December 2005: 135).

24. General and administrative expenses

	2006	2005
Insurance expenses	240	49
Repairs and maintenance	89	23
Software maintenance	88	85
Communication expense (telephone, telex and internet)	85	94
Utilities	76	83
Audit and consulting expense	58	203
Security and cash transportation expenses (guard services)	53	48
Travel and transportation	42	102
Vehicle operating expenses	15	17
Stores and stationery	12	25
Food and restaurant expenses	11	9
Computer consumables expense	10	9
Other	91	75
Total	870	822

25. Cash and cash equivalents

Cash and cash equivalents comprise the following:

	Note	2006	2005
Cash on hand	6	11,136	24,464
Current accounts with non resident banks	7	22,480	23,765
Treasury bills	8	101,616	114,665
Deposit accounts with non resident banks	9	373,766	185,940
Total		508,998	348,834

Central Banking Authority of Kosovo

Notes to the financial statements

(Amounts in EUR '000, unless otherwise stated)

26. Commitments and contingencies

Legal

The CBAK is involved in routine legal proceedings in the ordinary course of business. It is the management's opinion that the final outcome of these lawsuits will not have a material effect on the CBAK's results.

Credit related commitments

As at 31 December 2006, the CBAK had commitments to place deposits in total amount of EUR 30,916 thousand (31 December 2005 EUR 15,315 thousand).

Other commitments

Other commitments are composed as follows:

	Not later than 1 year	Later than 1 year and not later than 5 years
Premises security upgrade (works and consulting)	941	29
Purchase of equipment	51	-
Total	992	29

27. Financial risk management

Considering the nature of the CBAK's operations, financial risk management activities are principally related to the use of financial instruments. A financial instrument is any contract that gives rise to the right to receive cash or another financial asset from another party (financial asset) or the obligation to deliver cash or another financial asset to another party (financial liability). Financial instruments result in certain risks to the CBAK. The most significant risks facing the CBAK are discussed below.

(i) Interest rate risk

The CBAK'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. The CBAK attempts to mitigate this risk by monitoring the repricing dates of its assets and liabilities. In addition, the actual effect will depend on a number of other factors, including the extent to which repayments are made earlier or later than the contracted dates and variations in interest rate sensitivity within repricing periods and among currencies.

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Notes to the financial statements

(Amounts in EUR '000, unless otherwise stated)

27. Financial risk management (continued)

(i) Interest rate risk (continued)

(a) Average yield information

The average yields of significant categories of financial assets and liabilities of the CBAK as at 31 December 2006 and 2005 were as follows:

31 December	Weighted average interest rate (in %)	
	2006	2005
Assets		
Current accounts non resident banks	2.75	1.08
Treasury bills	3.02	2.1
Deposit accounts with no resident banks	2.85	2.03
Liabilities		
Due to domestic banks	2.25	1.00
Due to governmental institutions	2.25	1.00
Due to public and commercial entities	2.43	1.00
Other domestic liabilities	1.78	1.84

(b) Interest rate repricing analysis

The following table presents the interest rate repricing dates for the CBAK's monetary assets and liabilities. Fixed-rate assets and liabilities have been reported according to their scheduled principal repayment dates.

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Notes to the financial statements

(Amounts in EUR '000, unless otherwise stated)

27. Financial risk management (continued)

(i) Interest rate risk (continued)

(b) Interest rate repricing analysis (continued)

2006	Up to 1 Month	Up to 3 month	3-12 months	1-5 years	Non interest bearing	Total
Assets						
Cash on hand	-	-	-	-	11,136	11,136
Current accounts non resident banks	22,480	-	-	-	-	22,480
Deposit accounts with non resident banks	343,035	47,807	13,183	-	-	404,025
Treasury bills	39,941	61,675	101,782	-	-	203,398
Other assets	-	-	-	-	177	177
Total Assets	405,456	109,482	114,965	-	11,313	641,216
Liabilities						
Due to domestic banks	94,477	-	-	-	-	94,477
Due to local governmental institutions	475,821	-	-	-	-	475,821
Due to public and commercial entities	45,076	-	-	-	-	45,076
Other liabilities	-	550	1,231	-	877	2,658
Total Liabilities	615,374	550	1,231	-	877	618,032
Gap at 31 December 2006	(209,918)	108,932	113,734	-	10,436	23,184
Cumulative gap	(209,918)	(100,986)	12,748	12,748	23,184	

2005	Up to 1 month	1 to 3 month	3-12 months	1-5 years	Non interest bearing	Total
Assets						
Cash on hand	-	-	-	-	24,464	24,464
Current accounts non resident banks	23,765	-	-	-	-	23,765
Deposit accounts with no resident banks	190,633	-	-	-	-	190,633
Treasury bills	44,943	69,722	44,604	-	-	159,269
Other assets	-	-	-	-	377	377
Total Assets	259,341	69,722	44,604	-	24,841	398,508
Liabilities						
Due to domestic banks	82,518	-	-	-	-	82,518
Due to local governmental institutions	229,891	-	-	-	-	229,891
Due to public and commercial entities	60,026	4,100	-	-	-	64,126
Other liabilities	2,717	-	-	-	28	2,745
Total Liabilities	375,152	4,100	-	-	28	379,280
Gap at 31 December 2006	(115,811)	65,622	44,604	-	24,813	19,228
Cumulative gap	(115,811)	(50,189)	(5,585)	(5,585)	19,228	

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Central Banking Authority of Kosovo

Notes to the financial statements

(Amounts in EUR '000, unless otherwise stated)

27. Financial risk management (continued)

(ii) Currency risk

The currency risk is the risk that the value of financial instruments will fluctuate due to changes in foreign exchange rates.

Except negligible amounts, the CBAK assets and liabilities are denominated in EUR, therefore the CBAK has no significant exposure to currency risk.

(iii) Credit risk

Credit risk is the risk of financial loss to the CBAK if counterparty to a financial instrument fails to meet its contractual obligations, and arises principally from the CBAK's current accounts and deposits with non resident banks and treasury bills. For risk management reporting purposes, the CBAK considers and consolidates all elements of credit risk exposure (such as individual obligor default risk, country and sector risk).

Credit risk is managed through the approval of transactions and placements of funds, the establishment of limits restricting risk and constant monitoring positions.

Counterparties are accepted only if have top credit ratings and are subject to regular credit review.

(iv) Liquidity risk

Liquidity risk is the risk that the CBAK will encounter difficulty in meeting obligations from its financial liabilities and it arises in the general funding of the CBAK's activities and in the management of positions.

Policies to monitor and address the liquidity risk are set by the Governing Board. The CBAK manages its liquidity risk by investing in short term deposits with non resident banks. Liquidity management policies are set to ensure that even under adverse conditions the CBAK is in a position to meet its obligations. The Asset Management Department of the CBAK monitors the liquidity risk on a continual basis by analysing liquidity ratios, gap and economic scenarios.

The following table provides an analysis of the financial assets and liabilities of the CBAK into relevant maturity groupings based on the remaining periods to repayment.

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Notes to the financial statements

(Amounts in EUR '000, unless otherwise stated)

27. Financial risk management (continued)

(iv) Liquidity risk (continued)

2006	Up to 1 month	1-3 months	3-12 months	1-5 years	Total
Assets					
Cash on hand	11,136	-	-	-	11,136
Current accounts with non resident banks	22,480	-	-	-	22,480
Deposit accounts with no resident banks	343,035	47,807	13,183	-	404,025
Treasury bills	39,941	61,675	101,782	-	203,398
Other assets	177	-	-	-	177
Total assets	416,769	109,482	114,965	-	641,216
Liabilities					
Due to domestic banks	94,477	-	-	-	94,477
Due to governmental institutions	475,821	-	-	-	475,821
Due to public and commercial entities	37,108	-	-	-	37,108
Due to public and commercial entities (time)	5,400	550	2,018	-	7,968
Other liabilities	2,658	-	-	-	2,658
Total liabilities	615,464	550	2,018	-	618,032
Gap at 31 December 2006	(198,695)	108,932	112,947	-	23,184
Cumulative gap	(198,695)	(89,763)	23,184	23,184	

2005	Up to 1 month	1 to 3 month	3-12 months	1-5 years	Total
Assets					
Cash on hand	24,464	-	-	-	24,464
Current accounts non resident banks	23,765	-	-	-	23,765
Deposit accounts with no resident banks	190,633	-	-	-	190,633
Treasury bill	44,943	69,722	44,604	-	159,269
Other assets	377	-	-	-	377
Total Assets	284,182	69,722	44,604	-	398,508
Liabilities					
Due to domestic banks	82,518	-	-	-	82,518
Due to governmental institutions	229,891	-	-	-	229,891
Due to public and commercial entities	60,026	4,100	-	-	64,126
Other liabilities	2,745	-	-	-	2,745
Total Liabilities	375,180	4,100	-	-	379,280
Gap at 31 December 2005	(90,998)	65,622	44,604	-	19,228
Cumulative gap	(90,998)	(25,376)	(19,228)	19,228	

Central Banking Authority of Kosovo

Notes to the financial statements

(Amounts in EUR '000, unless otherwise stated)

28. Estimation and disclosure of fair value

Fair value estimates are based on existing balance sheet financial instruments without attempting to estimate the value of anticipated future business and the value of assets and liabilities not considered financial instruments.

Treasury bills

The estimated fair value of treasury bills is determined using market prices or broker/dealer quotations. Where this information is not available, fair value has been estimated using discounted cash flows using prevailing interest rates for instruments with similar credit risk and remaining maturity. The fair value of treasury bills as at 31 December 2006 is EUR 203,184 thousand (31 December 2005: EUR 159,269 thousand).

Other financial instruments

The amortized cost of fixed term money market placements and deposits approximates their fair value as they have short term maturities (less than one year) and are convertible into cash and are settled without significant transaction costs. Also the value at cost of cash and current account placements and deposits is assumed to approximate their fair value due to their certain exchangeability at cost.

29. Related party transactions

As defined in IAS 24 "Related Party Disclosures", a related party is any party that has the ability to control the other party or exercise significant influence over the other party in making financial and operating decisions.

Related parties include the management and the Governing Board.

A summary of related party transactions for the years ended 31 December 2006 and 2005 are as follows:

	2006	2005
Governing Board remuneration	14	16
Management remuneration	50	30
Total	64	46

Management remuneration does not include the remuneration to the Managing Director of the CBAK, which is paid by the International Monetary Fund.

30. Subsequent events

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

8. Statistical Appendix

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Table 1.

Financial Corporations Survey

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

Description	2004	2005	2006
Net foreign assets	642,608	685,096	965,246
Claims on nonresidents	691,815	748,684	1,037,249
Currency	56,183	75,587	66,674
Deposits	383,964	422,613	660,512
Securities other than shares	236,701	242,434	303,075
Loans	11,652	4,715	6,986
Shares and other equities	3,313	3,333	...
Other	2	2	2
less : Liabilities to nonresidents	49,207	63,588	72,003
Deposits	17,862	21,466	21,413
Loans	31,345	42,122	50,589
Domestic claims	202,826	348,722	231,467
Net claims on central government	-215,167	-223,504	-472,832
Claims on central government	—	—	—
less: Liabilities to central government	215,167	223,504	472,832
Deposits	215,167	223,504	472,832
Claims on other sectors	417,993	572,226	704,299
Loans	413,517	565,552	694,336
Public nonfinancial corporations	—	—	49
Other nonfinancial corporations	329,803	439,566	548,224
Other resident sectors	83,714	125,986	146,063
Households	83,714	125,986	146,063
Other claims	4,476	6,674	9,962
Deposits	675,306	834,498	894,878
Transferable deposits	278,375	318,938	308,932
Local government	3,212	4,464	5,365
Social security fund	2,968	1,708	4,301
Public nonfinancial corporations	34,605	67,565	34,794
Other nonfinancial corporations	81,305	76,801	96,923
Other resident sectors	156,285	168,400	167,548
of which: Households	145,542	155,525	157,645
of which: NPISH	9,069	10,686	7,763
Other deposits	396,931	515,560	585,947
Public nonfinancial corporations	149,297	181,326	193,337
Other nonfinancial corporations	24,429	33,734	27,594
Other resident sectors	223,205	300,501	365,015
Households	222,496	298,884	359,482
NPISH	709	1,616	5,533
Loans	2,330	3,022	3,375
Households	2,330	3,022	3,375
Insurance technical reserves	23,605	30,817	38,039
Net equity of households in life insurance reserves	—	—	—
Net equity of households in pension funds	5,755	8,725	10,540
Prepayment of premiums and reserves against outstanding claims	17,850	22,092	27,498
Shares and other equity	145,058	165,781	198,327
Funds contributed by owners	91,201	95,319	121,193
Retained earnings	11,326	13,336	27,754
General and special reserves	10,266	13,966	15,628
Profit/loss of the year	12,683	17,571	5,415
Grants from donors	19,581	25,590	28,338
Other items (net)	-865	-300	62,093
Other liabilities	37,322	42,262	110,993
less: Other assets	37,943	43,454	54,009
plus: Consolidation adjustment	-244	892	5,109

Table 2.

Depository Corporations Survey

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

Description	2000	2001	2002	2003	2004	2005	2006
Net foreign assets	133,306	583,318	649,489	695,176	648,486	694,997	976,195
Claims on nonresidents	145,811	604,828	674,095	726,426	687,647	744,338	1,036,306
less: Liabilities to nonresidents	12,505	21,509	24,606	31,249	39,160	49,341	60,111
Deposits	9,581	16,464	17,897	20,311	17,862	21,466	21,413
Loans	2,924	5,045	6,709	10,938	21,298	27,875	38,698
Domestic claims	-2,343	-44,419	-172,094	-113,607	158,494	290,352	163,781
Net claims on central government	-5,657	-70,336	-258,592	-346,380	-215,167	-223,504	-472,832
Claims on central government	—	—	—	—	—	—	—
less: Liabilities to central gov.	5,657	70,336	258,592	346,380	215,167	223,504	472,832
Deposits	5,657	70,336	258,592	346,380	215,167	223,504	472,832
Claims on other sectors	3,314	25,916	86,498	232,773	373,661	513,856	636,613
Loans	3,314	25,916	86,498	232,773	373,661	513,856	636,613
Public nonfinancial corp.	—	—	—	198	—	—	49
Other nonfinancial corp.	3,314	25,916	80,806	193,529	289,947	387,870	490,501
Other resident sectors	—	—	5,692	39,046	83,714	125,986	146,063
Households	—	—	5,692	39,046	83,714	125,986	146,063
Broad money liabilities	115,899	486,764	413,558	499,286	717,222	867,589	917,465
Deposits included in broad money	115,899	486,764	413,558	499,286	717,222	867,589	917,465
Transferable deposits	115,899	361,534	285,278	278,681	305,169	347,751	340,563
Other financial corporations	.	.	.	.	26,795	28,813	31,631
Local government	.	.	.	.	3,212	4,464	5,365
Social security fund	.	.	.	.	2,968	1,708	4,301
Public nonfinancial corp.	22,896	6,963	3,473	5,288	34,605	67,565	34,794
Other nonfinancial corp. 1/	93,003	135,345	160,084	138,982	81,305	76,801	96,923
Other resident sectors	.	219,226	121,720	134,412	156,285	168,400	167,548
of which: Households 2/	.	219,226	121,720	134,412	145,542	155,525	157,645
of which: NPISH	.	.	.	.	9,069	10,686	7,763
Other deposits	.	125,231	128,280	220,605	412,053	519,839	576,902
Other financial corporations	.	.	.	.	19,109	24,252	31,100
Public nonfinancial corp.	.	.	.	.	149,297	181,326	193,337
Other nonfinancial corp. 1/	.	31,318	23,921	87,131	22,318	33,054	24,560
Other resident sectors	.	93,913	104,359	133,474	221,329	281,207	327,905
Households 2/	.	93,913	104,359	133,474	220,620	279,590	322,371
NPISH	.	.	.	.	709	1,616	5,533
Deposits excluded from broad money	2,984	12,913	25,113	29,169	3,987	19,974	40,144
Other nonfinancial corporations	.	.	.	.	2,111	680	3,034
Households	.	.	.	.	1,876	19,294	37,110
Shares and other equity	11,077	25,162	43,805	61,075	87,104	94,389	117,832
Funds contributed by owners	9,525	20,999	33,320	46,617	67,678	72,406	93,689
Retained earnings	.	852	4,821	-1,492	2,712	412	11,929
General and special reserves	.	821	4,601	8,037	5,273	7,244	7,742
Grants from donors	.	728	464	1,619	469	801	658
Profit/loss of the year	1,552	1,762	597	6,293	10,971	13,528	3,813
Other Items (net)	1,003	14,059	-5,080	-7,960	-1,333	3,397	64,534
Other liabilities	2,287	26,276	8,479	18,905	27,989	37,873	103,466
less: Other assets	4,352	9,328	14,041	26,908	29,078	35,368	44,041
plus: Consolidation adjustments	...	...	...	...	-244	892	5,110

Table 3.

CBAK Survey

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

Description	2000	2001	2002	2003	2004	2005	2006
Net foreign assets	52,116	293,654	345,410	453,691	344,505	394,293	639,604
Claims on nonresidents	61,697	296,235	345,773	453,990	349,684	397,399	639,712
Currency	15,828	150,843	17,474	26,590	12,064	24,464	11,136
Deposits	45,869	145,392	328,299	427,399	213,202	213,448	424,928
Securities other than shares	—	—	—	—	124,418	159,488	203,647
less: Liabilities to nonresidents	9,581	2,581	363	298	5,179	3,106	108
Deposits	9,581	2,581	363	298	5,179	3,106	108
Net claims on central government	-5,657	-70,336	-258,592	-346,380	-215,167	-223,476	-470,770
Claims on central government	—	—	—	—	—	—	—
less: Liabilities to central gov.	5,657	70,336	258,592	346,380	215,167	223,476	470,770
Deposits	5,657	70,336	258,592	346,380	215,167	223,476	470,770
Claims on other sectors	—	—	—	—	—	—	—
Monetary base	38,649	182,297	50,120	64,917	112,242	151,320	146,468
Liabilities to ODC	15,753	173,904	46,222	59,612	72,899	82,518	94,467
Transferable deposits	15,753	173,904	46,222	59,612	72,899	82,518	94,467
Deposits included in broad money	22,896	8,393	3,898	5,305	39,342	68,802	52,001
Transferable deposits	22,896	8,393	3,898	5,305	34,242	64,702	44,033
Other financial corporations	—	—	—	—	17,757	21,611	26,692
Local government	—	—	—	—	1,891	1,602	379
Social security	—	—	—	—	2,968	1,708	4,301
Public nonfinancial corp.	22,896	6,963	3,473	5,288	9,942	37,587	10,519
Other nonfinancial corp.	—	1,430	425	17	10	5	2
Other resident sectors	—	—	—	—	1,675	2,188	2,140
Other deposits	—	—	—	—	5,100	4,100	7,968
Other financial corporations	—	—	—	—	5,100	4,100	7,968
Deposits excluded from broad money	2,984	12,913	25,113	27,367	—	—	—
Shares and other equity	4,925	4,727	10,561	16,068	17,982	20,401	25,522
Funds contributed by owners	2,556	2,556	2,556	2,556	10,000	10,000	10,000
Retained earnings	.	1,133	3,599	4,512	3,045	2,970	6,390
General and special reserves	.	309	3,940	7,380	4,468	6,630	8,473
Grants from donors	.	728	464	1,619	469	801	658
Other items (net)	-99	23,381	1,025	-1,040	-885	-904	-3,157
Other liabilities	1,236	24,245	1,911	1,448	98	530	247
less: Other assets	1,335	864	886	2,488	983	1,434	3,404

Table 4.

Other Depository Corporations Survey

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

Description	2000	2001	2002	2003	2004	2005	2006
Net foreign assets	81,190	289,664	304,079	241,485	303,981	300,704	336,591
Claims on nonresidents	84,114	308,593	328,322	272,436	337,963	346,938	396,594
Currency	12,686	88,342	35,597	46,611	43,245	50,101	54,595
Deposits	71,428	212,753	292,725	106,205	170,783	209,174	235,583
Securities other than shares	—	7,498	...	119,620	112,281	82,946	99,428
Loans	.	.	.	.	11,652	4,715	6,986
Other	—	—	—	—	2	2	2
less: Liabilities to nonresidents	2,924	18,929	24,243	30,951	33,982	46,234	60,003
Deposits	—	13,884	17,534	20,013	12,684	18,360	21,305
Loans	2,924	5,045	6,709	10,938	21,298	27,875	38,698
Other	—	—	—	—	...	...	...
Claims on CBAK	12,685	176,793	45,740	59,569	73,245	81,637	88,933
Deposits	12,685	176,793	45,740	59,569	73,245	81,637	88,933
Net claims on central government 1/	—	—	—	—	—	-28	-2,062
Claims on other sectors	3,314	25,916	86,498	232,773	373,661	513,856	636,613
Loans	3,314	25,916	86,498	232,773	373,661	513,856	636,613
Public nonfinancial corporations	—	—	—	198	—	—	49
Other nonfinancial corporations	3,314	25,916	80,806	193,529	289,947	387,870	490,501
Other resident sectors	—	—	5,692	39,046	83,714	125,986	146,063
Households	—	—	5,692	39,046	83,714	125,986	146,063
Deposits included in broad money	93,003	478,372	409,660	493,981	677,880	798,787	865,464
Transferable deposits	93,003	353,141	281,380	273,376	270,927	283,048	296,530
Other financial corporations	.	.	.	.	9,037	7,202	4,939
Local government	.	.	.	.	1,321	2,861	4,986
Public nonfinancial corporations	.	.	.	.	24,663	29,978	24,275
Other nonfinancial corporations	93,003	133,915	159,660	138,964	81,295	76,796	96,921
Other resident sectors	.	219,226	121,720	134,412	154,610	166,212	165,409
Households	.	219,226	121,720	134,412	145,542	155,525	157,645
NPISH	.	.	.	.	9,069	10,686	7,763
Other deposits	.	125,231	128,280	220,605	406,953	515,739	568,934
Other financial corporations	.	.	.	.	14,009	20,152	23,132
Public nonfinancial corporations	.	.	.	.	149,297	181,326	193,337
Other nonfinancial corporations	.	31,318	23,921	87,131	22,318	33,054	24,560
Other resident sectors	.	93,913	104,359	133,474	221,329	281,207	327,905
Households	.	93,913	104,359	133,474	220,620	279,590	322,371
NPISH	.	.	.	.	709	1,616	5,533
Deposits excluded from broad money	.	.	.	1,802	3,987	19,974	40,144
Other nonfinancial corporations	.	.	.	.	2,111	680	3,034
Households	.	.	.	.	1,876	19,294	37,110
Shares and other equity	6,152	20,435	33,244	45,007	69,122	73,988	92,310
Funds contributed by owners	4,600	18,443	30,764	44,061	57,678	62,406	83,689
Retained earnings	—	-282	1,222	-6,004	-333	-2,558	5,539
General and special reserves	—	511	661	657	805	613	-731
Profit/loss of the year	1,552	1,762	597	6,293	10,971	13,528	3,813
Other items (net)	-1,966	-6,434	-6,587	-6,963	-102	3,420	62,158
Other liabilities 2/	1,051	2,030	6,568	17,457	27,891	37,344	103,219
less: Other assets	3,017	8,464	13,155	24,420	28,095	33,934	40,637
plus: Consolidation adjustment	—	—	—	—	102	11	-424

Table 5.

Other Financial Corporations Survey

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

Description	2004	2005	2006
Net foreign assets	-5,878	-9,901	-10,949
Claims on nonresidents	4,169	4,346	943
Currency	874	1,022	943
Securities other than shares	3	...	...
Shares and other equity	3,313	3,333	...
less : Liabilities to nonresidents	10,046	14,247	11,892
Loans	10,046	14,247	11,892
Claims on depository corporations	45,904	53,065	62,732
CBAK	22,857	25,711	34,657
Transferable deposits	17,757	21,611	26,689
Other deposits	5,100	4,100	7,968
Other depository corporations	23,046	27,354	28,074
Transferable deposits	9,037	7,202	4,942
Other deposits	14,009	20,152	23,132
Net claims on central government	—	—	—
Claims on other sectors	44,332	58,370	67,685
Loans	39,856	51,696	57,723
Other nonfinancial corporations	39,856	51,696	57,723
Other claims	4,476	6,674	9,962
Deposits	—	—	—
Loans	2,330	3,022	3,375
Other resident sectors	2,330	3,022	3,375
Households	2,330	3,022	3,375
Insurance technical reserve	23,605	30,817	38,039
Net equity of households in life insurance reserves	—	—	—
Net equity of households in pension funds	5,755	8,725	10,540
Prepayment of premiums and reserves against outstanding claims	17,850	22,092	27,498
Shares and other equity	57,955	71,391	80,495
Funds contributed by owners	23,523	22,913	27,504
Retained earnings	8,614	12,924	15,824
General and special reserves	4,993	6,722	7,885
Profit/Loss for the year	1,712	4,043	1,602
Grants from donors	19,112	24,789	27,679
Other items (net)	468	-3,697	-2,441
Other liabilities	9,333	4,388	7,527
less: Other assets	8,865	8,086	9,968
plus: Consolidation adjustment	...	...	...

Table 6.

Other Financial Intermediaries Survey

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

Description	2004	2005	2006
Net foreign assets	-9,433	-13,434	-10,867
Claims on nonresidents	613	813	891
Currency	634	822	891
less : Liabilities to nonresidents	10,046	14,247	11,758
Loans	10,046	14,247	11,758
Claims on depository corporations	3,510	5,751	2,546
Other depository corporations	3,510	5,751	2,546
Transferable deposits	2,507	3,693	1,871
Other deposits	1,003	2,058	675
Net claims on central government	—	—	—
Claims on other sectors	39,856	51,696	55,994
Gross loans	39,856	51,696	55,994
Other nonfinancial corporations	39,856	51,696	55,994
Loans	2,330	3,022	3,274
Shares and other equity	32,004	41,512	44,963
Funds contributed by owners	—	—	—
Retained earnings	7,899	10,246	11,098
General and special reserves	4,993	6,477	7,015
Grants from donors	19,112	24,789	26,850
Other items (net)	-402	-521	-564
Other liabilities	1,781	2,310	2,502
less: Other assets	2,182	2,830	3,066
plus: Consolidation adjustment	...	...	...

Table 7.

Insurance Companies and Pension Funds Survey

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

Description	2004	2005	2006
Net foreign assets	3,555	3,533	25
Claims on nonresidents	3,555	3,533	25
Currency	239	200	25
Shares and other equities	3,313	3,333	...
Claims on depository corporations	39,482	44,534	55,863
CBAK	22,857	25,711	30,636
Transferable Deposits	17,757	21,611	22,668
Other deposits	5,100	4,100	7,968
Other depository corporations	16,625	18,823	25,227
Transferable deposits	6,369	3,479	2,871
Other deposits	10,255	15,344	22,356
Net claims on central government	—	—	—
Claims on other sectors	4,476	6,674	9,962
Other claims	4,476	6,674	9,962
Insurance technical reserve	23,605	30,817	38,039
Net equity of households in life insurance reserves	—	—	—
Net equity of households in pension funds	5,755	8,725	10,540
Prepayment of premiums and reserves against outstanding claims	17,850	22,092	27,498
Shares and other equity	23,039	27,100	29,670
Funds contributed by owners	20,612	20,133	23,031
Retained earnings	715	2,678	4,384
General and special reserves	...	246	653
Profit/loss of the year	1,712	4,043	1,602
Other items (net)	870	-3,176	-1,859
Other liabilities	7,552	2,079	4,948
less: Other assets	6,683	5,255	6,807
plus: Consolidation adjustment	...	...	...

Table 8.

Insurance Companies Survey

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

Description	2004	2005	2006
Net foreign assets	3,555	3,533	25
Claims on nonresidents	3,555	3,533	25
Currency	239	200	25
Shares and other equities	3,313	3,333	...
Claims on depository corporations	33,727	35,810	45,323
CBAK	17,525	17,422	20,543
Transferable deposits	14,525	17,422	18,525
Other deposits	3,000	...	2,018
Other depository corporations	16,202	18,388	24,780
Transferable deposits	6,369	3,479	2,424
Other deposits	9,833	14,908	22,356
Claims on other sectors	4,476	6,674	9,962
Other claims	4,476	6,674	9,962
Insurance technical reserve	17,850	22,092	27,498
Net equity of households in life insurance reserves	—	—	—
Prepayment of premiums and reserves against outstanding claims	17,850	22,092	27,498
Shares and other equity	23,039	27,100	29,670
Funds contributed by owners	20,612	20,133	23,031
Retained earnings	715	2,678	4,384
General and special reserves	...	246	653
Net Profit/loss of the year	1,712	4,043	1,602
Other items (net)	870	-3,176	-1,859
Other liabilities	7,552	2,079	4,948
less: Other assets	6,683	5,255	6,807
plus: Consolidation adjustment	...	...	...

Table 9.

Pension Funds Survey

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

Description	2004	2005	2006
Net foreign assets	—	—	—
Claims on depository corporations	5,755	8,725	10,540
CBAK	5,332	8,289	10,094
Transferable Deposits	3,232	4,189	4,144
Other deposits	2,100	4,100	5,950
Other depository corporations	423	436	447
Transferable Deposits	...	...	447
Other Deposits	423	436	...
Insurance technical reserve	5,755	8,725	10,540
Net equity of households in life insurance reserves	—	—	—
Net equity of households in pension funds	5,755	8,725	10,540

Table 10.

Other Depository Corporations Balance Sheet - Assets

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

Description	2000	2001	2002	2003	2004	2005	2006
Cash and balances with BPK	25,371	265,135	81,337	106,180	116,490	131,738	143,528
Cash	12,686	88,342	35,597	46,611	43,245	50,101	54,595
Balances with BPK	12,685	176,793	45,740	59,569	73,245	81,637	88,933
Balances with commercial banks	71,428	212,753	292,725	106,205	186,009	221,936	243,105
Sight accounts	.	.	.	.	2,074	2,539	57
Time deposits	.	.	.	.	1,500	5,508	479
Nonresidents	71,428	212,753	292,725	106,205	182,435	213,889	242,569
Securities	—	7,498	...	119,620	112,281	82,946	99,428
Investment portfolio	—	—	—	—	...	...	4,500
Nonresidents	—	—	—	—	...	...	4,500
Trading portfolio	—	7,498	...	119,620	112,281	82,946	94,928
Nonresidents	—	7,498	...	119,620	112,281	82,946	94,928
Gross loans and lease financing	3,314	25,916	86,498	232,773	373,661	513,856	636,613
Public nonfinancial corporations	—	—	—	198	...	...	49
Other nonfinancial corporations	3,314	25,916	80,806	193,529	289,947	387,870	490,501
Households	—	—	5,692	39,046	83,714	125,986	146,063
NPISH	—	—	—	...	...	...	...
Fixed assets	441	4,544	9,498	12,265	15,878	16,933	22,872
Other assets	2,576	3,920	3,657	12,155	12,219	17,003	17,767
TOTAL ASSETS	103,130	519,766	473,715	589,198	816,538	984,412	1,163,314

Table 11.

Other Depository Corporations Balance Sheet - Liabilities

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

Description	2000	2001	2002	2003	2004	2005	2006
Balances from other banks	.	.	.	1,802	14,276	23,034	30,245
Debts to clients	95,927	497,300	432,612	522,887	695,932	843,048	930,537
Deposits	93,003	492,255	427,194	513,994	694,533	836,657	926,370
Transferable deposits	93,003	365,448	295,909	290,453	281,033	296,607	310,893
Central government	—	—	—	—	...	28	1,062
Local government	.	.	.	.	1,321	2,861	4,986
Other financial corp.	.	.	.	.	9,037	7,202	4,939
Public nonfin. Corp.	.	.	.	.	24,663	29,978	24,275
Other nonfin. Corp.	93,003	133,915	159,660	138,964	81,295	76,796	96,921
Households	.	219,226	121,720	134,412	145,542	155,525	157,645
NPISH	.	.	.	.	9,069	10,686	7,763
Nonresidents	.	12,307	14,529	17,077	10,106	13,530	13,302
Other deposits	.	126,807	131,285	223,541	413,499	540,050	615,478
Central government	.	—	—	—	—	—	1,000
Other financial corp.	.	.	.	.	14,009	20,152	23,132
Public nonfin. Corp.	.	.	.	.	149,297	181,326	193,337
Other nonfin. Corp.	.	31,318	23,921	87,131	24,429	33,734	27,594
Households	.	93,913	104,359	133,474	222,496	298,884	359,482
NPISH	.	.	.	.	709	1,616	5,533
Nonresidents	.	1,577	3,005	2,936	2,559	4,338	5,399
Other borrowings (incl non-neg. CD)	2,924	5,045	5,418	8,893	1,399	6,391	4,167
Nonresidents	2,924	5,045	5,418	8,893	1,399	6,391	4,167
Other liabilities	1,051	2,030	6,568	17,457	27,891	37,344	103,219
Subordinated debt	—	...	1,291	2,045	9,318	6,999	7,003
Own resources	6,152	20,435	33,244	45,007	69,122	73,988	92,310
In EUR currency	6,152	20,435	33,244	45,007	69,122	73,988	92,310
Share capital	4,600	18,443	30,764	44,061	57,678	62,406	83,689
Contingency reserve	—	511	511	511	613	613	-731
General and other reserves	.	...	150	146	192	...	...
Profit/loss of the year	1,552	1,762	597	6,293	10,971	13,528	3,813
Retained profit/loss	.	-282	1,222	-6,004	-333	-2,558	5,539
TOTAL LIABILITIES	103,130	519,765	473,715	589,198	816,538	984,413	1,163,314

1/ Untill May '04 Includes all currencies.

2/ Till May 2004 figure for all nonfinancial corporations;

3/ Till May 2004 figure for households includes NPISH;

Table 12.

EUR - Deposits at ODC, by Original Maturity

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

Description	2004	2005	2006
Government	1,321	2,889	7,048
Transferable deposits	1,321	2,889	6,048
Other deposits	...	...	1,000
Financial corporations	25,621	35,408	28,182
Other depository corporations	3,675	8,054	112
Transferable deposits	2,175	1,054	112
Other deposits	1,500	7,000	...
Other financial intermediaries	3,510	5,751	2,395
Transferable deposits	2,507	3,693	1,869
Other deposits	1,003	2,058	526
Insurance companies 1/	15,524	18,823	24,780
Transferable deposits	5,268	3,479	2,424
Other deposits	10,255	15,344	22,356
Pension funds	.	.	443
Transferable deposits	.	.	443
Other deposits	.	.	...
Financial auxiliaries	2,912	2,780	452
Transferable deposits	162	30	202
Other deposits	2,750	2,750	250
Nonfinancial corporations	275,260	318,994	338,413
Public nonfinancial corporations	173,499	211,256	217,357
Transferable deposits	24,202	29,930	24,020
Other deposits	149,297	181,326	193,337
up to 1 month	34,000	23,851	19,873
over 1 month and up to 3 months	4	12,763	19,442
over 3 months and up to 1 year	115,293	119,461	114,320
over 1 year and up to 2 years	...	25,251	39,701
Other nonfinancial corporations	101,760	107,739	121,056
Transferable deposits	78,171	74,369	94,190
Other deposits	23,589	33,369	26,866
up to 1 month	9,037	6,292	6,187
over 1 month and up to 3 months	6,028	8,294	6,816
over 3 months and up to 1 year	6,254	13,027	9,103
over 1 year and up to 2 years	169	5,090	1,738
over 2 years	2,101	667	3,023
Other domestic sectors	360,325	440,714	500,373
Households	350,694	428,727	487,282
Transferable deposits	136,862	144,734	144,986
Other deposits	213,832	283,993	342,295
up to 1 month	63,817	87,179	111,209
over 1 month and up to 3 months	42,152	41,726	39,573
over 3 months and up to 1 year	91,778	109,269	127,919
over 1 year and up to 2 years	14,229	26,544	26,486
over 2 years	1,857	19,275	37,107
NPISH	9,631	11,987	13,091
Transferable deposits	8,922	10,371	7,558
Other deposits	709	1,616	5,533
Nonresidents	12,324	17,326	18,192
TOTAL	674,850	815,332	892,208

Table 13.

Non-EUR - Deposits at ODC, by Original Maturity

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

Description	2004	2005	2006
Government	—	—	—
Financial corporations	1,102	4	1
Other depository corporations	1	3	...
Transferable deposits	1	3	...
Other financial intermediaries	...	1	1
Transferable deposits	...	1	1
Insurance companies	1,101	...	...
Transferable deposits	1,101	...	...
Nonfinancial corporations	4,425	2,839	3,714
Public nonfinancial corporations	461	48	255
Transferable deposits	461	48	255
Other deposits	—	—	...
Other nonfinancial corporations	3,964	2,791	3,459
Transferable deposits	3,124	2,426	2,731
Other deposits	840	365	728
up to 1 month	340	17	250
over 1 month and up to 3 months	188	131	208
over 3 months and up to 1 year	302	204	185
over 1 year and up to 2 years	—	—	74
over 2 years	10	13	11
Other domestic sectors	17,490	25,998	30,051
Households	17,344	25,683	29,846
Transferable deposits	8,679	10,791	12,659
Other deposits	8,664	14,891	17,186
up to 1 month	2,791	3,925	6,754
over 1 month and up to 3 months	2,190	2,466	1,815
over 3 months and up to 1 year	3,001	7,978	8,534
over 1 year and up to 2 years	664	503	80
over 2 years	19	19	3
NPISH	146	315	206
Transferable deposits	146	315	206
Nonresidents	341	542	509
TOTAL	23,358	29,383	34,275

Table 14.

ODC Loans, by Original Maturity 1/

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

Description	2004	2005	2006
Government	—	—	—
Financial corporations	—	—	—
Nonfinancial corporations	289,947	387,870	490,550
Public nonfinancial corporations	...	...	49
Over 2 years	...	...	49
Other nonfinancial corporations	289,947	387,870	490,501
Up to 1 year	111,491	117,924	128,736
Over 1 year and up to 2 years	111,259	125,220	127,654
Over 2 years	67,198	144,727	234,111
Other domestic sectors	83,714	125,986	146,063
Households	83,714	125,986	146,063
Up to 1 year	15,906	19,549	19,691
Over 1 year and up to 2 years	15,244	21,046	24,689
Over 2 years	52,563	85,392	101,684
TOTAL	373,661	513,856	636,613

1/ All loans are in EUR currency.

Table 15.

ODC Loans, by Industry

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

Description	2004	2005	2006
Agriculture	7,931	12,492	16,443
Up to 1 year	3,851	4,061	3,419
Over 1 year	4,079	8,431	13,024
Industry, energy and construction	47,773	74,230	97,667
Mining	6	512	480
Up to 1 year	...	512	480
Over 1 year	6	...	...
Industry	35,562	48,142	61,861
Up to 1 year	16,070	11,565	12,152
Over 1 year	19,492	36,578	49,708
Manufacturing (Food, Textile, etc)	29,769	44,005	54,910
Up to 1 year	12,623	10,448	10,696
Over 1 year	17,146	33,557	44,214
Manufacturing (Oil,Chem., etc)	5,724	3,544	6,259
Up to 1 year	3,441	925	1,137
Over 1 year	2,283	2,619	5,122
Electricity, gas and water	69	594	691
Up to 1 year	5	192	319
Over 1 year	64	403	372
Construction	12,205	25,575	35,327
Up to 1 year	6,401	12,459	15,315
Over 1 year	5,804	13,116	20,012
Services	234,243	301,147	376,440
Trade	197,234	249,659	307,380
Up to 1 year	78,537	81,070	92,404
Over 1 year	118,697	168,589	214,977
Wholesale and retail trade	172,843	209,575	259,511
Up to 1 year	66,328	64,038	74,515
Over 1 year	106,507	145,537	184,997
Hotel and restaurants	18,949	27,978	29,542
Up to 1 year	9,379	12,198	10,537
Over 1 year	9,571	15,780	19,006
Other trade	5,450	12,107	18,327
Up to 1 year	2,830	4,834	7,353
Over 1 year	2,619	7,272	10,974
Fin. Services	3,209	2,742	1,073
Up to 1 year	69	117	166
Over 1 year	3,141	2,626	907
Other services	33,800	48,745	67,987
Up to 1 year	10,870	11,207	28,092
Over 1 year	22,931	37,538	39,895
TOTAL	289,947	387,868	490,550

Table 16.

ODC Effective Interest Rates

Description	2004	2005	2006
DEPOSITS			
Nonfinancial corporations			
Other deposits 1/			
Up to 250.000 EUR			
<= 1 month			
Interest rate	1.71	2.10	2.12
Standardized variance	0.14	0.03	0.06
> 1 month and <= 3 months			
Interest rate	2.19	2.39	2.65
standardized variance	0.06	0.01	0.04
> 3 months and <= 1 year			
Interest rate	2.95	3.39	. *
standardized variance	0.10	0.17	. *
Equal or more than 250.000 EUR			
<= 1 month			
Interest rate	. *	2.42	3.13
Standardized variance	. *	0.08	0.19
> 3 months and <= 1 year			
Interest rate	. *	3.73	4.30
standardized variance	. *	0.05	0.08
Households			
Other deposits 1/			
<= 1 month			
Interest rate	1.70	2.02	2.12
standardized variance	0.10	0.05	0.04
> 1 month and <= to 3 months			
Interest rate	2.25	2.36	2.50
standardized variance	0.04	0.03	0.03
> 3 months and <= 1 year			
Interest rate	3.00	3.27	3.65
standardized variance	0.06	0.09	0.06
> 1 year and <= 2 years			
Interest rate	3.82	3.89	4.34
standardized variance	0.02	0.04	0.05
> 2 years			
Interest rate	. *	4.57	4.77
standardized variance	. *	0.10	0.11
LOANS			
Nonfinancial corporations			
Investment business loans			
> 1 year and <= 3 years			
Interest rate	14.31	13.82	. *
standardized variance	0.18	0.36	. *
Other business loans			
> 3 months and <= 1 year			
Interest rate	15.89	15.52	13.71
standardized variance	0.30	0.32	0.29
> 1 year			
Interest rate	14.85	14.24	14.34
standardized variance	0.19	0.13	0.18
Credit lines			
Interest rate	15.61	15.20	15.71
standardized variance	0.08	0.00	0.05
Households			
Consumer Loans			
Interest rate	12.31	12.17	12.06
standardized variance	0.19	0.12	0.14

* At least one of the conditions for publication (i.e. minimum 3 answers with new business and a standardized variance of 1/ Nontransferable (time) deposits.

Table 17.

ODC Income Statement

(Cumulative within the calendar year, in thousands of EUR)

Description	2000	2001	2002	2003	2004	2005	2006
INCOME							
Interest income	—	393	2,035	6,183	53,999	74,612	88,842
Loans	—	393	1,646	4,836	48,110	67,963	79,406
Placement with banks	—	—	389	1,347	2,452	3,969	6,613
Securities	955	8,437	8,290	29,243	3,437	2,681	2,823
Non-Interest income	—	—	—	—	19,449	19,697	25,102
Fees and commissions	—	—	—	—	17,522	17,380	22,474
Other operating income	—	—	—	—	1,927	2,317	2,628
TOTAL INCOME	955	8,437	8,233	24,355	73,448	94,309	113,944
EXPENDITURES							
Interest expenditures	—	—	996	12,027	9,978	15,389	19,846
Deposits	—	—	—	4,939	9,237	13,894	17,465
Borrowings	—	—	—	2,964	741	1,495	2,381
Non-Interest expenditures	—	—	—	1,975	14,939	18,743	21,877
Provisions for loan losses	955	8,437	8,233	19,406	11,071	13,419	16,024
Depreciation on fixed assets	955	8,437	7,237	9,362	3,868	5,324	5,853
General and administrative expenses	—	—	996	10,044	33,952	43,851	48,410
TOTAL EXPENDITURES	—	—	—	10	58,869	77,983	90,132
NET INCOME	—	—	57	4,888	14,579	16,327	23,811
Net gains/losses from dealing securities	—	—	57	2,582	-441	-362	-114
Net gains/losses from dealing in foreign ex.	—	—	—	2,306	328	990	551
Net gains/losses from exchange rate variat.	4,004	38,725	105,436	232,637	593	-39	612
Net income from ban. activ.before tax	4,004	31,228	87,401	179,556	15,059	16,916	24,861
less : Provision for taxes	4,004	31,228	74,966	116,813	2,104	3,389	5,565
Net profit / loss for period	—	—	12,435	62,743	12,955	13,527	19,296
less: dividend paid	3,240	22,351	68,475	...	...	...	...
Retained profit	3,240	22,351	62,289	84,960	12,955	13,527	19,296

Table 18.

CBAK - Interbank Clearing System

(Cumulative within the calendar year, in thousands of EUR)

Description	2001	2002	2003	2004	2005	2006
Transactions						
Amount	79,535	840,605	1,416,109	1,715,646	1,919,149	2,325,050
Number	4,888	75,763	164,207	266,743	321,669	990,858

Table 19.

International Money Transfers among Financial Corporations

(Cumulative within the calendar year, in thousands of EUR)

Description	2000	2001	2002	2003	2004	2005	2006
OUTGOING							
CBAK	8,553	77,295	241,718	277,674	369,087	309,844	304,796
Commercial banks	173,463	500,522	722,415	1,014,779	1,282,860	1,277,402	1,324,634
Financial auxiliaries	1,746	10,094	14,486	13,167	15,358	14,715	16,999
TOTAL	183,762	587,911	978,619	1,305,620	1,667,305	1,601,961	1,646,429
INCOMING							
CBAK	117,213	226,980	239,706	232,020	92,607	92,747	261,066
Commercial banks	286,096	588,229	747,932	916,723	1,154,931	943,087	1,042,330
Financial auxiliaries	6,370	41,841	106,471	137,385	162,258	167,172	184,690
TOTAL	409,679	857,050	1,094,109	1,286,128	1,409,796	1,203,006	1,488,086

Table 20.

Insurance Companies Activity

(Cumulative within the calendar year, in thousands of EUR)

Description	2001	2002	2003	2004	2005	2006
Amount of premiums received						
TPL	31,161	27,231	29,163	28,739	33,341	34,705
Border policies	.	3,686	6,557	8,604	7,061	9,429
Other (non TPL)	.	66	1,340	1,747	6,811	4,594
TOTAL	31,161	30,983	37,060	39,090	47,213	48,728
Number of policies sold						
TPL	179,864	175,008	199,223	241,901	223,770	251,641
Border policies	.	72,358	62,073	120,609	134,596	136,182
Other (non TPL)	.	67	3,827	8,423	14,520	17,977
TOTAL	179,864	247,433	265,123	370,933	372,886	405,800
Amount of claims paid						
TPL 1/	2,655	3,540	5,295	5,746	7,945	9,825
Border policies	.	.	278	580	332	481
Other (non TPL)	.	.	11	417	889	627
TOTAL	2,655	3,540	5,584	6,743	9,166	10,933

1/ Included the claims paid by the Kosovo Guarantee Fund.

Table 21.

Other Financial Intermediaries Activity

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

Description	2000	2001	2002	2003	2004	2005	2006
Amount of loans	2,661	19,718	33,437	33,874	39,856	51,696	57,723
Number of loans	2,722	11,423	16,431	19,037	22,286	27,123	35,541

Table 22.

Kosovo Consolidated Budget

(Cumulative within the calendar year, in millions of EUR)

Description	2000	2001	2002	2003	2004	2005	2006
Tax Revenues	121.7	249.7	444.4	536.4	550.1	553.3	620.5
Border taxes	115.2	208.7	364.5	428.3	436.0	426.1	456.4
Domestic taxes	6.6	41.0	79.9	108.2	114.2	127.2	164.1
	0.0	0.0	0.0				
Non tax revenues	6.0	22.7	35.3	44.7	43.8	46.3	57.0
of which: Interest	1.1	2.0	3.7	3.0	3.3	2.6	3.5
Local Government revenues	-	8.5	1.3	23.6	23.7	28.6	34.6
Donor grants	160.9	83.4	38.9	26.0	17.2	10.2	.
TOTAL	288.6	364.4	520.0	630.7	634.8	638.4	712.0
Wages and salaries	92.1	109.2	131.4	145.7	184.2	194.6	203.8
Goods and services	73.5	97.6	148.2	194.4	203.0	142.8	143.0
Subsidies and transfers	68.0	61.6	87.5	127.9	186.3	213.9	155.4
Capital outlays	...	...	62.0	97.8	192.0	144.9	133.2
	0.0	0.0	0.0				
Reserves	...	...	...	2.4	3.9	...	...
TOTAL	233.6	268.4	429.2	568.2	769.4	696.1	635.5
BALANCE (Rev-Exp)	55.0	96.0	90.8	62.5	-134.6	-57.7	76.5

Source: Ministry of Finance and Economy.

Table 23.

Depository Corporations Network and number of employees

Description	2000	2001	2002	2003	2004	2005	2006
Prishtina region	6	11	28	40	61	69	69
CBAK 1/	4	4	4	1	1	1	1
Other Depository Corporations	2	7	24	39	60	68	68
Head office	2	6	7	7	7	7	6
Branches	—	—	1	1	1	1	1
Sub-branches	—	1	16	31	52	60	61
Prizreni region							
Other Depository Corporations	2	5	18	24	37	39	37
Head office	—	—	—	—	—	—	—
Branches	2	3	8	8	9	8	6
Sub-branches	—	2	10	16	28	31	31
Peja region							
Other Depository Corporations	2	7	23	27	41	44	40
Head office	—	—	—	—	—	—	—
Branches	2	5	13	13	13	13	12
Sub-branches	—	2	10	14	28	31	28
Gjilani region							
Other Depository Corporations	2	5	34	39	50	54	49
Head office	—	—	—	—	—	—	—
Branches	2	5	14	14	14	14	12
Sub-branches	—	—	20	25	36	40	37
Mitrovica region							
Other Depository Corporations	—	3	16	22	30	32	26
Head office	—	—	—	—	—	—	—
Branches	—	2	5	6	6	6	6
Sub-branches	—	1	11	16	24	26	20
Total Network Units	29	48	136	152	219	238	221
CBAK 1/	21	21	21	1	1	1	1
Other Depository Corporations	8	27	115	151	218	237	220
Head office	1	1	1	1	7	7	6
Branches	6	15	41	42	43	42	37
Sub-branches	0	6	67	102	168	188	177
Total numbers of employees	477	976	1,525	1,781	2,199	2,479	2,557
CBAK 1/	338	339	132	124	133	138	141
Other Depository Corporations	139	637	1,393	1,657	2,066	2,341	2,416

Region in Prishtina (Gllgovc, Fushë Kosova, Lipjan, Obiliq, Podujeva, Shtime)

Region in Prizren (Dragash, Rahovec, Suharekë, Malisheva, Mamusha)

Region in Peja (Deqan, Gjakova, Istog, Klinë, Junik)

Region in Mitrovica (Leposaviq, Mitrovica, Skenderaj, Vushtrri, Zubin Potok, Zveqan)

Region in Gjilan (Kaçaniku, Kamenica, Novo Berd, Shterpc, Ferizaj, Vitia)

1/ Head Office.

Table 24.

Exports and Imports, by Trading Partners

(Cumulative within the calendar year, in millions of EUR)

Description		2001	2002	2003	2004	2005	2006
Export		10.6	27.6	35.6	56.6	48.9	79.2
Import		684.5	854.8	973.1	1,063.3	1,180.0	1,314.6
Trade balance		-673.9	-827.2	-937.5	-1,006.7	-1,131.1	-1,235.3
Albania	Export	.	.	1.88	1.8	5.2	10.5
	Import	.	.	6.11	20.2	18.1	23.3
Bulgaria	Export	.	.	0.18	0.4	1.0	4.1
	Import	.	.	30.72	42.1	37.7	36.3
Bosnia and Herzegovina	Export	.	.	0.84	1.5	3.4	4.4
	Import	.	.	11.46	12.8	19.0	18.7
Croatia	Export	.	.	1.84	0.5	0.9	0.7
	Import	.	.	23.04	25.1	25.0	28.2
European Union	Export	.	.	14.68	16.4	17.4	22.5
	Import	.	.	242.53	377.4	408.8	407.4
EU 15	Export	.	.	13.69	15.0	16.1	17.9
	Import	.	.	174.02	284.0	309.7	301.5
	of which:						
	Austria	Export	.	1.35	0.9	0.9	1.1
		Import	.	21.51	27.6	20.9	23.7
	France	Export	.	...	0.2	0.5	0.2
		Import	.	12.46	23.1	20.5	15.2
	Germany	Export	.	3.79	3.3	3.2	3.4
		Import	.	38.49	78.2	129.9	125.6
	Greece	Export	.	1.78	4.3	5.4	3.9
		Import	.	52.18	68.5	47.6	44.4
	Italy	Export	.	6.25	5.5	5.6	9.0
		Import	.	26.31	44.5	50.4	58.3
	Netherlands	Export	.	0.18	0.1	0.1	0.2
		Import	.	6.00	10.1	7.9	6.5
	United Kingdom	Export	.	0.15	0.6	...	...
		Import	.	3.80	11.1	8.0	6.8
EU new 10	Export	.	.	1.00	1.2	1.3	4.6
	Import	.	.	68.51	93.4	99.0	105.9
	of which:						
	Hungary	Export	.	0.05	0.1	0.1	...
		Import	.	17.74	19.7	16.2	20.1
	Slovenia	Export	.	0.66	1.0	1.2	4.3
		Import	.	40.70	56.9	55.5	57.2
Switzerland	Export	.	.	0.09	0.1	0.7	6.4
	Import	.	.	10.52	16.2	18.7	23.0
Macedonia	Export	.	.	6.94	9.6	9.6	8.2
	Import	.	.	290.87	149.2	219.7	260.2
Serbia	Export	.	.	.	10.1	6.9	11.9
	Import	.	.	.	161.3	163.6	192.2
Montenegro	Export	.	.	6.75	—	—	2.0
	Import	.	.	112.01	—	—	17.8
Turkey	Export	—	—	—	...	...	...
	Import	—	—	—	86.8	85.4	90.4
China	Export	.	.	1.72	...	...	...
	Import	.	.	66.35	34.3	55.8	75.5
Ukraine	Export	.	.	...	...	...	...
	Import	.	.	12.47	10.9	11.4	11.6
Brazil	Export	.	.	...	...	...	...
	Import	.	.	6.88	21.5	16.8	18.6
United States	Export	.	.	...	...	0.2	...
	Import	.	.	5.16	17.0	18.5	11.7
Other	Export	.	.	...	13.3	2.6	11.5
	Import	.	.	10.24	88.5	81.6	94.1

NOTE: Exports data are by destination country. Imports data are by country of origin of goods.

Table 25.

Exports, by Commodity Group

(Cumulative within the calendar year, in millions of EUR)

Description	2001	2002	2003	2004	2005	2006
Total	10.6	27.6	35.6	56.5	48.9	79.2
I Live animals and animal products	.	0.1	...	...	0.5	0.3
II Vegetable products	.	2.4	2.4	2.6	2.8	3.9
III Animal or vegetable fats and oils - edible	.	0.1	...	...	...	0.1
IV Prepared foodstuffs, beverages and tobac.	.	1.3	4.1	3.8	4.6	4.9
V Mineral products	.	0.3	0.5	2.4	3.2	15.8
VI Products of the chemical or allied industries	.	0.3	0.5	1.0	1.0	1.0
VII Plastics, rubber and articles thereof	.	2.7	2.7	3.7	0.9	3.1
VIII Hides, skins, leather and articles thereof	.	6.0	4.5	5.9	6.1	6.7
IX Wood and articles of wood	.	0.3	0.6	0.4	0.4	0.6
X Cellulosic material, paper and articles thereof	0.4	0.4	0.4	0.6
XI Textiles and textile articles	.	0.6	1.1	1.4	0.6	0.5
XII Footwear	.	0.1	0.1	0.1	0.1	0.7
XIII Articles of stone, plaster, ceramic and glass	.	0.6	0.8	1.8	0.4	0.6
XIV Pearls, precious, stones, metals, jewelry, etc.	0.1	0.2	0.2
XV Base metals and articles of base metal	.	6.6	12.0	19.7	23.8	33.2
XVI Machinery, appliances, electrical equip. etc	.	3.4	3.0	9.2	2.7	3.2
XVII Transport means	.	1.9	1.2	2.0	0.9	3.0
XVIII Optical, medical and musical instruments	.	0.1	0.1	1.1	0.2	0.1
XIX Arms and ammunition	0.1
XX Miscellaneous manufactured articles	.	0.7	1.4	0.7	0.3	0.6
XXI Other	.	0.1	0.1	0.1	...	...

Source: Customs and Statistical Office of Kosovo. Data for 2003 and 2004 are processed by BPK.

Table 26.

Imports, by Commodity Group

(Cumulative within the calendar year, in millions of EUR)

Description	2001	2002	2003	2004	2005	2006
Total	684.5	854.7	973.1	1,063.2	1,180.0	1,314.6
I Live animals and animal products	.	51.0	50.4	52.4	54.2	50.4
II Vegetable products	.	47.1	66.7	68.1	57.5	67.2
III Animal or vegetable fats and oils - edible	.	7.9	8.3	7.3	11.1	19.4
IV Prepared foodstuffs, beverages and tobacco	.	174.9	203.5	165.4	164.8	169.8
V Mineral products	.	123.5	138.6	173.1	212.3	243.3
VI Products of the chemical or allied industries	.	52.7	70.9	98.0	91.4	96.5
VII Plastics, rubber and articles thereof	.	25.3	32.7	42.5	51.0	64.3
VIII Hides, skins, leather and articles thereof	.	1.3	0.4	1.0	1.5	16.9
IX Wood and articles of wood	.	29.9	33.2	29.9	30.7	33.9
X Cellulosic material, paper and articles thereof	.	9.9	16.6	33.4	25.0	27.3
XI Textiles and textile articles	.	16.4	28.8	31.2	36.7	39.1
XII Footwear	.	6.2	7.5	10.4	11.3	20.5
XIII Articles of stone, plaster, ceramic and glass	.	72.5	60.5	54.9	51.5	54.5
XIV Pearls, precious stones, metals, jewelry, etc.	0.1	0.3	0.3	0.3
XV Base metals and articles of base metal	.	53.6	58.0	77.5	90.7	89.5
XVI Machinery, appliances, electrical equipment, etc	.	97.5	105.5	116.8	133.9	156.0
XVII Transport means	.	10.3	27.8	50.2	110.3	99.4
XVIII Optical, medical and musical instruments	.	8.1	8.5	15.1	16.1	24.4
XIX Arms and ammunition	0.4	0.5	0.2	11.0
XX Miscellaneous manufactured articles	.	66.5	54.6	35.4	29.6	27.1
XXI Other	0.1	...	...	3.6

Source: Customs and Statistical Office of Kosovo. Data for 2003 and 2004 are processed by BPK.

