

## Summary

According to Kosovo Agency of Statistics (KAS) data, real GDP marked a decline of 9.3 per cent in Q2 2020. With a decline were mainly characterized new loans, export of services and also capital expenditures of the government, while, despite the pandemic crisis, remittances, FDI and also export of goods have marked an increase.

On quarterly basis, assets of financial system expanded by EUR 238.2 million, mainly reflecting the increase of the banking sector and pension sector assets. Assets expansion of the banking sector is mainly attributable to the high level of deposits collected in this quarter, which at the same time presents the main financing source of the banking activity. While, the expansion of assets of the pension sector came as a result of the collected contributions and return on investments during this period. Banking sector marked a slowdown increase of its lending activity in this quarter, which was more reflected on households. Also, the level of new loans was significantly lower compared to the trend marked in the previous periods, as a result of COVID-19 effects. The banking sector marked a net profit of EUR 17.9 million in this quarter, representing a lower level for EUR 3.4 million compared to Q2 2019. This came as a result of the higher increase of expenditures against the slower increase of the sector income. Financial soundness indicators of the sector continued to stand at satisfactory values. Banking sector continued to be characterized with high credit portfolio quality, thus having low level of nonperforming loans (2.6 per cent at the end of Q2 2020 from 2.5 per cent as it was at the end of Q2 2019), and optimal coverage with provisions (of 134.8 per cent compared to 161.2 per cent as it was at the end of Q2 2019). Solvency indicators (with a level of 16.7 per cent) and liquidity (with a level of 36.1 per cent) continue to be above the regulatory recommended minimal level (of 12.0 per cent and 25.0 per cent, respectively).

Pension sector was characterized with an activity expansion being impacted by positive return on investments, thus recovering to some extent from losses incurred during Q1 2020, and by collected contributions.

Insurance sector during the second quarter of 2020 was characterized with an activity expansion, albeit at a lower level. The level of the collected premiums and claims incurred, during this period, marked a decline, which reflects the COVID-19 pandemic effects. Compared to the negative financial results marked in the second quarter of the previous year, in this quarter the sector resulted to have marked a profit, which came as result of the sharper decline of expenditures compared to the slower decline of the collected premiums. Expenditures decline was primarily impacted by the COVID-19 containment measures.

Microfinance sector marked an activity increase in Q2 2020, albeit the increase was significantly slower than in the previous periods, being impacted by containment measures against COVID-19 pandemic (closure of the economy). However, the microfinance sector continued to have satisfactory performance and good credit portfolio quality, albeit compared to the trend of the previous periods these indicators have shown a declining tendency. In Q2 2020, Kosovo's Government issued a debt with a quite high value compared to the same period of the previous year. The high issuances of sovereign debt was necessary since the Kosovo's Government during Q2 2020 marked a decline of budget revenues (as a consequence of COVID-19 pandemic), and the necessity to support the domestic economy through economic fiscal package. The value of debt issued by Kosovo's Government during Q2 2020 amounted to EUR 162.4 million. All of the primary dealers at the securities auctions of Kosovo's Government, pension sector, banking sector and insurance sector have increased the investments level in this instrument during this period (March 2020 - June 2020).

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## ABBREVIATIONS

CAR	Capital Adequacy Ratio
CBK	Central Bank of the Republic of Kosovo
CHF	Swiss Franc
EUR	Euro currency
FDI	Foreign Direct Investments
GBP	British Pound
GDP	Gross Domestic Product
IMF	International Monetary Fund
KAS	Kosovo Agency of Statistics
MF	Ministry of Finance of the Republic of Kosovo
NPL	Nonperforming loans
REER	Real Effective Exchange Rate
ROAA	Return on Average Assets
ROAE	Return on Average Equity
RWA	Risk-Weighted assets
SEE	Southeastern Europe
USD	American Dollar
WEO	World Economic Outlook

## Macroeconomic Developments<sup>1</sup>

According to Kosovo Agency of Statistics (KAS) data, real GDP for Q1 2020 marked a slowdown annual growth of 1.3 per cent. The dynamics of macroeconomic developments changed direction diametrically in the following months of April and May, with the announcement of the pandemic situation and taking restrictive measures by the Government to prevent the spread of the virus. According to KAS, the economic activity was characterized with a decline of 9.3 per cent in Q2 2020. With a decline were mainly characterized new loans, export of services and also capital expenditures of the government, while, despite the pandemic crisis, remittances, FDI and also export of goods have marked an increase.

Consumer prices marked a slowdown increase of 0.6 per cent until June 2020, mainly as a result of the price decline of transport, recreation, footwear and clothing, and also due to the slowdown increase of food prices. Core inflation marked a decline of 0.2 per cent.

Fiscal sector, until June 2020, was characterized with a decline of budget revenues of 10.9 per cent and an increase of budget expenditures of 2.2 per cent. Consequently, Kosovo's budget recorded a primary budget deficit of EUR 111.5 million. Public debt reached EUR 1.3 billion, which is for 16.2 per cent higher compared to Q2 2019. As a percentage to GDP, public debt reached 18.2 per cent, from 16.5 per cent as it was in Q2 2019.

External sector was characterized with a decline of the current account deficit of 19.0 per cent, which is mainly attributable to the deficit decline of goods and the increase of the positive balance of primary and secondary income. Conversely, the positive balance of services was significantly lower. Within the balance of payments, remittances marked an annual increase of 7.2 per cent, while Foreign Direct Investments (FDI) marked an increase of 48.7 per cent, until June 2020.

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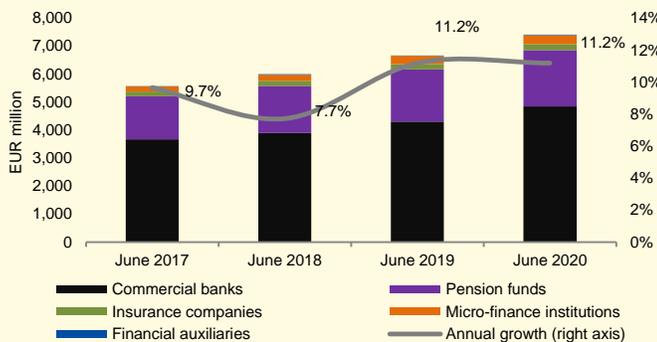
<sup>1</sup> For more information on macroeconomic developments, please refer to: Quarterly Assessment of Macroeconomic Developments (Q2 2020) published on the CBK website.

## Financial System

*Despite the health and economic crisis caused by COVID-19 pandemic, the financial system in the country retained the increasing pace from the previous period. Assets of the financial system in Kosovo, at the end of June 2020, reached a value of EUR 7.41 billion, representing an annual increase of 11.2 per cent (figure 1).*

Assets expansion of financial system against the previous period (June 2019), came as a result of the activity increase of the banking sector (mainly being supported by collected deposits) and pension sector (of collected contributions and return on investments).

Figure 1. Assets value of Kosovo's financial system



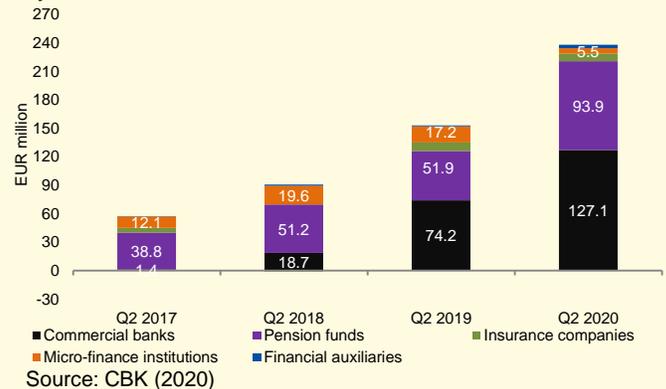
Note: The data are as at end of the noted quarter  
Source: CBK (2020)

On quarterly basis, financial system assets expanded by EUR 238.2 million, primarily being affected by the assets of the banking sector (EUR +127.1 million) and assets of the pension sector (EUR +93.9 million), and to lower extent from other sectors (EUR +17.2 million) (figure 2).

The expansion of the banking sector activity mainly came as a result of the high deposits level collected during this quarter, after the decline they suffered in

Q1 2020, which were mainly affected by the COVID-19 pandemic.

Figure 2. Quarterly change of assets of financial system constituent sectors



While, the expansion of assets of the pension sector came as a result of the collected contributions and return on investments during this period. Therefore, pension sector recovered to a significant extent from investment losses caused during Q1 2020, as a consequence of the effects generated in the foreign markets from the spread of COVID-19 pandemic.

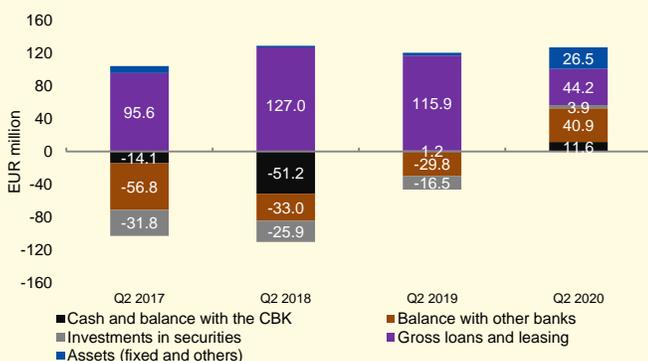
## Banking Sector

*Within the assets of the banking sector, loans were characterized by slower growth during this quarter, while investments in securities marked a recovery. Deposits, as the main financing source of the banking activity, increased in this quarter, followed by the equity of the banks and borrowings issued by the external sector. Despite the increased risks as a result of the economic and social crisis stimulated by the COVID-19 pandemic, the banking sector continued to be sustainable, with a high credit portfolio quality, satisfactory level of liquidity and well capitalized.*

## Assets

The value of total assets of the banking sector at the end of Q2 2020, reached EUR 4.85 billion, representing an annual growth of 12.7 per cent. Whereas, on quarterly basis, banking sector assets expanded by EUR 127.1 million, in Q2 2020. Due to the COVID-19 pandemic spread, lending activity of the banking sector (which covers the largest weight within the sector's assets with a share of 64.5 per cent) was characterized with slowdown pace (figure 3). Due to the lack of placement of assets in the form of loans, banks have diversified assets in other balance sheet items as deposits in other banks, cash and balance with the CBK, and investments in securities. The category of the balance sheet with commercial banks marked a significant increase of EUR 40.9 million in this quarter, mainly as a result of the withdrawal of funds deposited at other banks, both in the country and abroad. With an increase was characterized also the category of cash and balance with the CBK (for EUR 11.6 million), which primarily reflects the level of collecting the deposits in this quarter.

Figure 3. Banking sector assets structure in the respective quarters



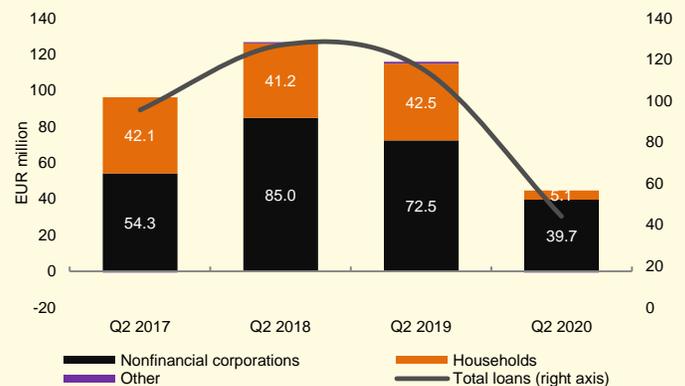
Source: CBK (2020)

In this quarter, investments in securities, marked an increase of EUR 3.9 million compared to the decline of EUR 16.5 million that had been marked in the same period of the previous year.

## Loans

The value of total loans at the end of Q2 2020, reached EUR 3.13 billion, representing an annual increase of 6.4 per cent (an increase of 10.5 per cent marked at the end of Q2 2019). For the first time in the recent four years, the lending activity was characterized with slowdown of dynamics of increase from a double digit into a single digit increase. This dynamic of double digit increase of lending has been interrupted since March 2020, when the first containment measures against COVID-19 pandemic had started. Loans to nonfinancial corporations, which comprise 63.6 per cent of total loans, marked a slowdown increase of 6.3 per cent (10.7 per cent in the previous period). Similarly, loans to households almost halved down the lending pace compared to the previous period, falling at 6.8 per cent (annual increase of 10.3 per cent marked at the end of Q2 2019).

Figure 4. Quarterly change of loans stock

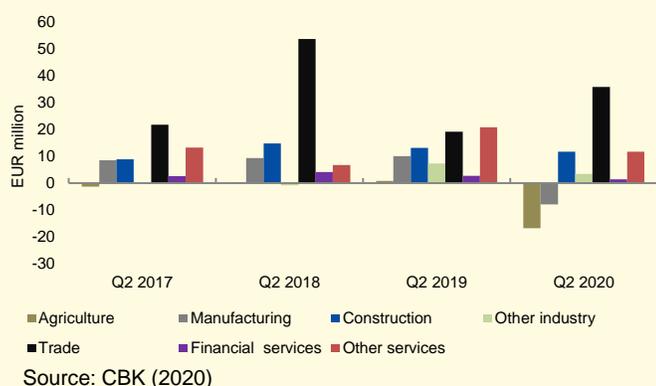


Source: CBK (2020)

The significant slowdown of lending was mainly driven by the decline of new loans.

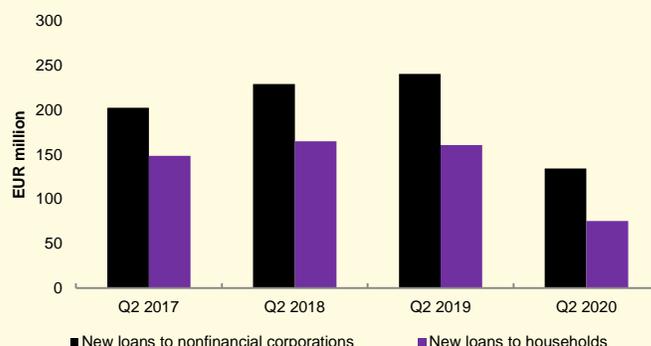
In Q2 2020, total loans marked an increase of EUR 44.2 million, against the increase of EUR 115.9 million in Q2 2019. Loans to households marked a more significant slowdown increase, with only EUR 5.1 million (EUR 37.4 million less compared to Q2 2019). Whereas, loans to nonfinancial corporations increased by EUR 39.7 million, in Q2 2020, or EUR 32.8 million less compared to Q2 2019. (figure 4).

Figure 5. Credit structure by economic activity



As regards to economic activities, on quarterly basis, lending only to the trade sector marked an increase compared to the previous quarter, reaching the value of EUR 35.9 million (EUR 19.1 million in Q2 2019). The increase of lending to trade sector, is interlinked to the fact that trade was the sector less affected by the restrictive measures against the spread of COVID-19 pandemic (figure 5). Lending to construction sector, financial services, and other services marked an annual slowdown increase. While, lending to agriculture sector and manufacturing, in Q2 2020 decreased by EUR 16.9 million and EUR 8.0 million, respectively, compared to the increase of EUR 0.8 million and EUR 10.0 million, respectively, in Q2 2019.

Figure 6. New loans to nonfinancial corporations and households in Q2



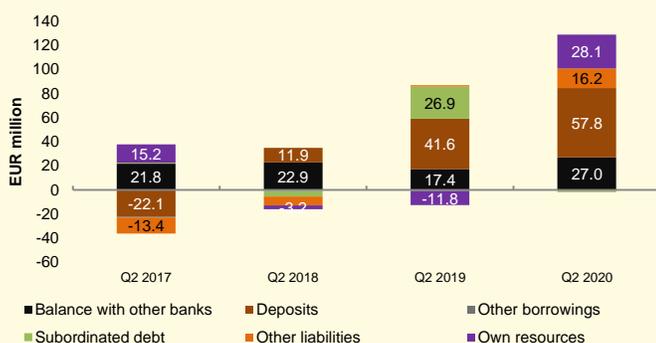
New loans in Q2 2020 marked a value of EUR 209.4 million, which nearly halved (an annual decline of 47.8 per cent) compared to Q2 2019. The decline of new loans was more significant in April and May, while during the month of June there were marked possible signs of recuperation of lending. New loans to nonfinancial corporations, in Q2 2020, marked a value of EUR 134.2 million, representing an annual decline of 44.2 per cent (figure 6). A more significant annual decline was marked on loans with investment purposes of 63.1 per cent, whose value reached EUR 36.1 million in Q2 2020. Whereas, new loans with investments purposes marked a value of EUR 95.3 million in Q2 2020, marking an annual decline of 31.8 per cent, compared to Q2 2019. Based on sectoral basis, the only sector that was characterized with an annual increase was the agriculture sector, whose new loans increased by 1.6 per cent in Q2 2020, reaching a value of EUR 5.4 million. Whereas, with a sharp decline were characterized new loans to industry sector and services sector, which contracted for EUR 49.6 million and EUR 48.6 million, respectively, marking the value of EUR 36.3 million and EUR 81.7 million, respectively, in Q2 2020.

With a significant decline were characterized also new loans to households. The value of total new loans was EUR 85.5 million lower compared to Q2 2019, reaching the value of EUR 75.2 million in Q2 2020. Of which, new consumer credit marked a sharper contraction with EUR 71.7 million compared to Q2 2019, reaching the value of EUR 49.2 million in Q2 2020. New mortgage loans shrank for EUR 6.3 million compared to Q2 2019, reaching the value of EUR 21.3 million at the end of Q2 2020.

### Liabilities and Own Resources

The structure of liabilities and own resources is mainly comprised by deposits (80.5 per cent), whose stock, at the end June 2020 reached EUR 3.90 billion and marked an annual growth of 14.0 per cent. Also on quarterly basis, during Q2 2020, total deposits expanded by EUR 57.8 million (figure 7). The category of own resources increased by EUR 28.1 million in Q2 2020 (EUR -11.8 million in Q2 2019), as a consequence of the profit realized during the second quarter of 2020, and due to nondividend distribution, as it occurred in Q2 2019.

Figure 7. Structure of liabilities and own resources, quarterly change



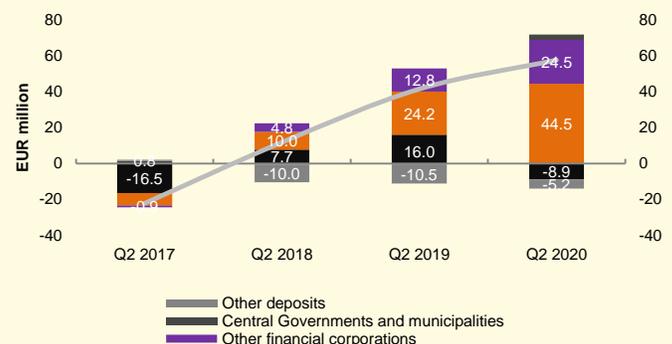
Source: CBK (2020)

Nondividend distribution is one of the preventive measures taken by the CBK in order for the banking sector to be well capitalized at this time when the country and the world is facing COVID-19 pandemic. At the end of the June 2020, the stock of total equity reached the value of EUR 570.0 million, marking an annual increase of 12.6 per cent. Within the category of other liabilities, subordinated debt declined by EUR 1.1 million (EUR +26.9 million in Q2 2019), while savings from commercial banks increased by EUR 27.0 million (EUR +17.4 million in Q2 2019).

### Deposits

The stock of deposits marked an annual increase of 14.0 per cent in June 2020, representing the highest annual increase in the last ten years. This growth came as a result of the increased level of collected deposits from households and other financial corporations (mainly pension funds). A significant increase during this period was also marked by collected deposits from public corporations.

Figure 8. Total deposits value and main categories in Q2

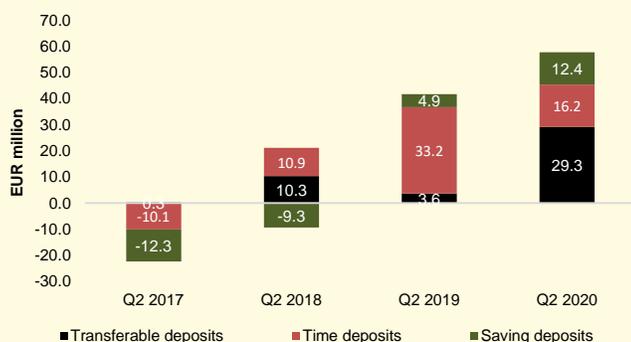


Source: CBK (2020)

Whereas, collected deposits from financial corporations, despite having had positive contribution, marked a slowdown annual increase.

Compared to the trend of deposits in the previous quarter (Q1 2020), when they were characterized with a sharp decline (EUR -62.7 million), in this quarter deposits marked a significant increase. During Q2 2020, total deposits increased by EUR 57.8 million, compared to the increase of EUR 41.6 million marked in Q2 2019. Household deposits increased by EUR 44.5 million in Q2 2020, reaching the value of EUR 2.65 billion at the end of the period (June 2020) (figure 8). Whereas, nonfinancial corporation deposits declined by EUR 8.9 million in Q2 2020, marking the value of EUR 650.2 million at the end of the period (June 2020). According to the categories of deposits, transferable deposits marked a more significant increase with a value of EUR 29.3 million (EUR 3.6 million in Q2 2019) on quarterly basis, while their stock reached the value of EUR 2.34 billion at the end of the period (June 2020) (figure 9).

Figure 9. Deposits structure by main categories, quarterly change



Source: CBK (2020)

Whereas, time deposits and saving deposits expanded during this quarter, albeit compared to the same period of the previous year these deposits were at lower levels. The value of time deposits on quarterly basis expanded

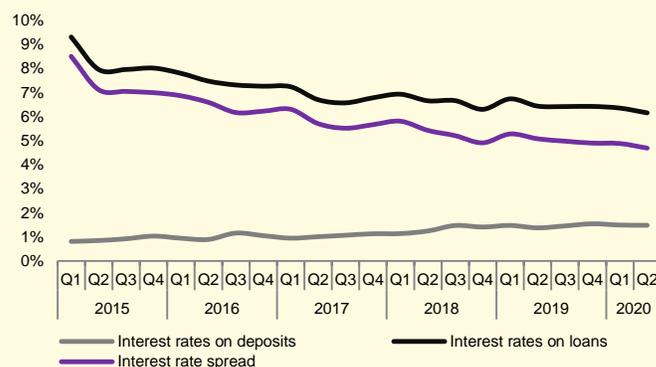
by EUR 16.2 million, while saving deposits increased by EUR 12.4 million (EUR 33.2 million and EUR 4.9 million, respectively, in the previous period). Transferable deposits continued to have the highest share to total deposits of the sector (60.0 per cent), followed by time deposits (26.8 per cent) and saving deposits (13.2 per cent).

The value of new collected deposits in Q2 2020 was EUR 67.8 million, of which EUR 18.4 million were deposits collected from nonfinancial corporations, whereas EUR 49.3 million belonged to household deposits. While, compared to Q2 2019, it was observed a sharp decline of deposits collected from households (EUR -24.0 million) and from nonfinancial corporations (EUR -22.0 million).

### Interest Rates<sup>2</sup>

The average interest rate on loans was 6.2 per cent, in Q2 2020, or 0.3 percentage points lower against the same period of the previous year.

Figure 10. Interest rate on loans and deposits



Source: CBK (2020)

Whereas, interest rates on deposits remained at the same level as in the previous periods, standing at 1.5

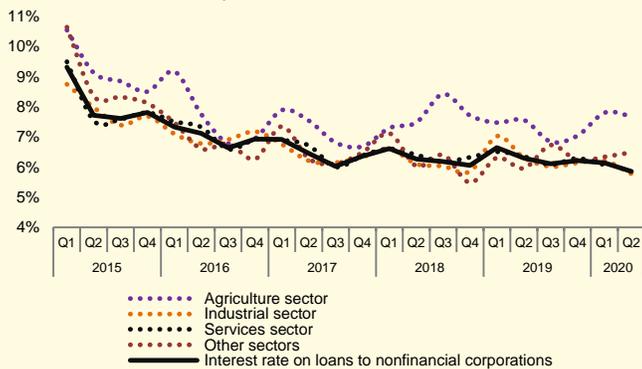
<sup>2</sup> The calculation of interest rates: quarter average of interest rates on loans and deposits. In the text it is referred as "the interest rates".

per cent in Q2 2020. Consequently, the interest rate spread of loans and deposits narrowed down to 4.7 percentage points (figure 10).

### Interest rates on loans

The average interest rate on loans in Q2 2020, for nonfinancial corporations was 5.9 per cent, or 0.5 percentage points lower against the previous year (figure 11).

Figure 11. Interest rates on loans to nonfinancial corporations

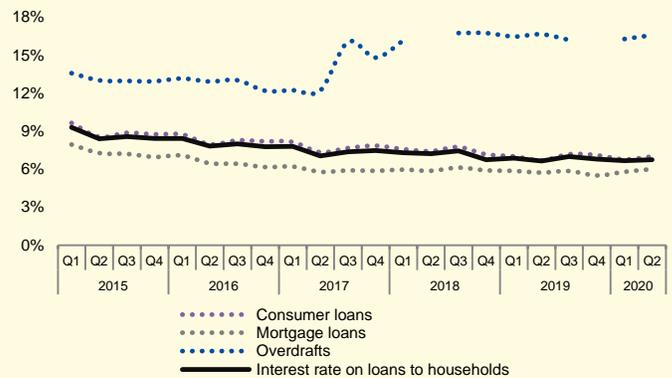


Source: CBK (2020)

As regards to categories of loans, the interest rates on investment loans was lower (5.7 per cent) compared to interest rate on non-investment loans (6.1 per cent). Alongside with the same period as in the previous year, it was observed a more significant decline of interest rates of investment loans (for 0.5 percentage points) compared to the decline for non-investment loans (for 0.3 percentage points).

In sectoral term, the interest rate on agricultural loans marked an increase of 0.1 percentage points, reaching an average of 7.7 per cent. On the other hand, interest rate on loans to industry and loans to services marked a decline of 0.5 percentage points, reaching an average rate of 5.8 per cent and 5.9 per cent, respectively.

Figure 12. Interest rates on loans to households



Source: CBK (2020)

Concerning loans to household, the interest rate stood at 6.7 per cent, representing an increase of 0.1 percentage points compared to Q2 2019. A higher interest rate was marked by consumer credit (7.0 per cent), which marked an increase of 0.3 percentage points compared to Q2 2019. In addition, also interest rate on mortgage loans marked an increase in this quarter (of 5.7 per cent in Q2 2019 to 6.0 per cent in Q2 2020) (figure 12).

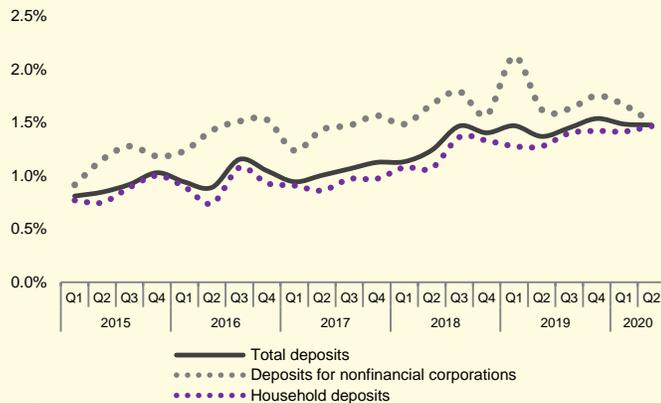
### Interest rates on deposits

The average interest rates on deposits remained at the same level as in the previous periods, standing at 1.5 per cent (figure 13).

Interest rates on deposits of nonfinancial corporations was the same as in household deposits, in Q2 2020.

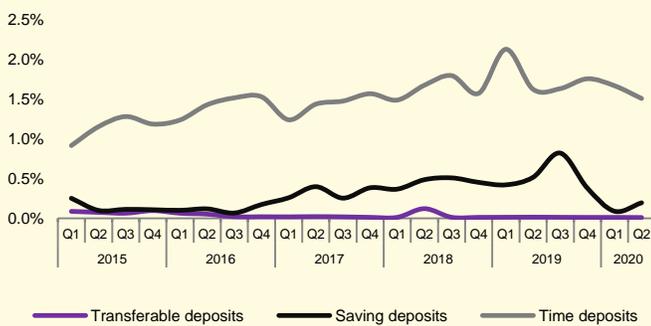
Compared to Q2 2019, the interest rate on nonfinancial corporation deposits marked a decline of 0.1 percentage points, falling at the level of 1.5 per cent. This decline came as a result of the decrease of the interest rate on time deposits (figure 14).

Figure 13. Interest rates on deposits



Source: CBK (2020)

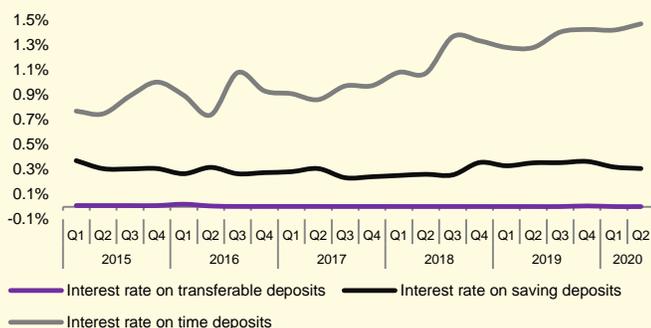
Figure 14. Interest rates on nonfinancial corporations deposits, by categories



Source: CBK (2020)

Interest rates on household deposits marked a slight increase of 0.2 percentage points compared to Q2 2019, reaching the rate of 1.5 per cent (figure 15).

Figure 15. Interest rates on household deposits, by categories



Source: CBK (2020)

This came as a result of the rate increase of time deposits of 0.2 percentage points. Interest rate on saving deposits was at the level of 0.3 per cent.

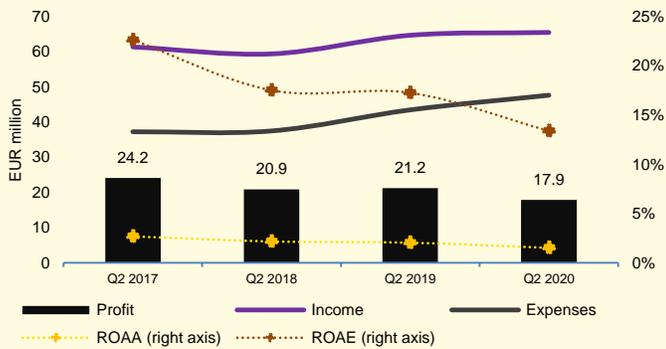
## Performance of the Banking Sector

The banking sector realized a profit with a value of EUR 17.9 million, in Q2 2020, which is for EUR 3.4 million lower compared to Q2 2019 (figure 16). The lower profit realized in Q2 2020 was a result of the higher expenditures increase (of EUR 4.2 million) compared to the increase of income (of EUR 0.8 million). The income reached EUR 65.5 million during this quarter. Interest income amounted to EUR 49.7 million (an annual decline of EUR 0.3 million), which primarily consist of interest income from loans. Meanwhile, non-interest income which is mainly comprised of fees and commissions, marked a value of EUR 13.8 million (an annual decline of EUR 0.9 million). Gains from revaluations marked a value of EUR 2.0 million in Q2 2020.

Expenditures of the banking sector marked a value of EUR 47.6 million. The largest category, the one of general and administrative expenses reached the value of EUR 26.4 million (for EUR 0.1 million higher compared to Q2 2019). The category of non-interest expenses, in Q2 2020, reached the value of EUR 13.2 million (for EUR 2.1 million higher compared to the previous period), mainly as a consequence of the higher share for expenses on loan loss provisions.

Whereas, the category of interest expenses reached the value of EUR 5.9 million (for EUR 0.8 million higher compared to the previous period).

Figure 16. Profit and profitability indicators of the banking sector



Source: CBK (2020)

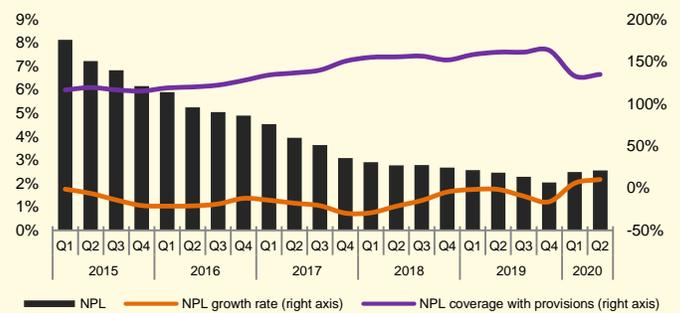
As a consequence of developments on income and expenditures of the banking sector, in Q2 2020, expenditures-to-income ratio was at the rate of 72.7 per cent, or 5.5 percentage points higher compared to the same period of the previous year. This ratio indicates that the banking sector spends EUR 0.727 for every EUR 1 earned (figure 16).

### Financial Soundness Indicators

Financial soundness indicators of the banking sector continued to remain at a satisfactory level also during the second quarter of 2020, despite the economic and health crisis caused by COVID-19 pandemic.

The indicators of credit portfolio quality, at the end of Q2 2020, stood at a satisfactory level, with low level of nonperforming loans (NPL) and a high coverage of loans with provisions. The value of nonperforming loans, after a decline of five consecutive years, in June 2020 marked an increase of 10.2 per cent. Nevertheless, the NPL rate to total loans stood at low level, at 2.6 per cent (2.5 per cent at the end of June 2019) (figure 17). Nonperforming loans continued to be well provisioned, at a level of 134.8 per cent (161.2 per cent at the end of June 2019).

Figure 17. Indicators of credit portfolio quality and NPL growth rate

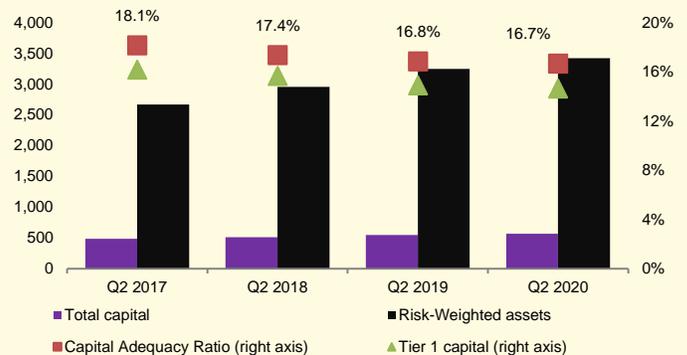


Note: The data are as at end of the noted quarter

Source: CBK (2020)

The banking sector continues to be well capitalized and sustainable. During this period, the Capital Adequacy Ratio was at the level of 16.7 per cent, representing a lower level for 1.0 percentage points than in the same period of the previous year (figure 18). The slight decline of this indicator came as a result of the lower increase of total capital compared to the higher increase of risk weighted assets.

Figure 18. Solvency indicator



Note: The data are as at end of the noted quarter

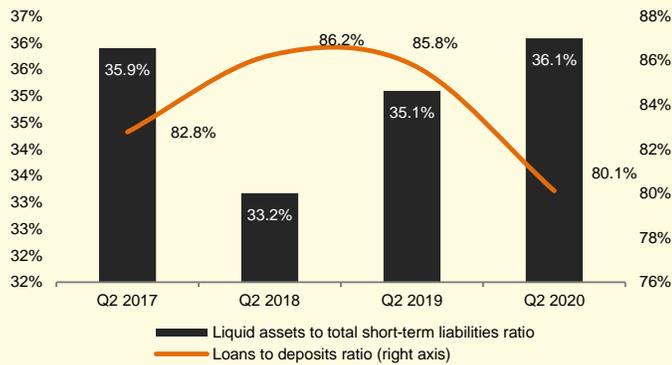
Source: CBK (2020)

Although standing at lower level, this indicator remained at satisfactory level and above the minimum required regulatory capital.

As regards to the liquidity of the banking sector, the liquid assets to short-term liabilities ratio marked a

slight growth of 1.0 percentage points compared to Q2 2019, standing at the level of 36.1 per cent.

Figure 19. Liquidity indicators



Note: The data are as at end of the noted quarter  
Source: CBK (2020)

The slight increase of this indicator, came as a result of the more accelerated increase of liquid assets (cash, the balance with the CBK and the balance with other banks) compared to the slower increase of short-term liabilities (mainly non-time deposits).

Loans-to-deposits ratio stood at the level of 80.1 per cent, which is approximate to the recommended level of 80.0 per cent.

## Pension Sector

*Pension sector was characterized with an activity expansion being impacted by positive return on investments, thus recovering to some extent from losses incurred during Q1 2020, and collected contributions during this quarter.*

Pension sector as the second sector by importance of weight in the financial sector, comprises 27.2 per cent of total assets of the financial system. Total assets of the pension sector marked an annual increase of 7.6 per cent, reaching a value of EUR 2.01 billion, at the end of Q2 2020. On quarterly basis, only in Q2 2020,

pension sector assets increased by EUR 93.9 million (a decline of EUR 56.6 million in Q1 2020), mainly as a result of the high recovery from losses from investments during Q1 2020 and collections from the contributors (figure 20).

Figure 20. Assets of the pension sector, quarterly change



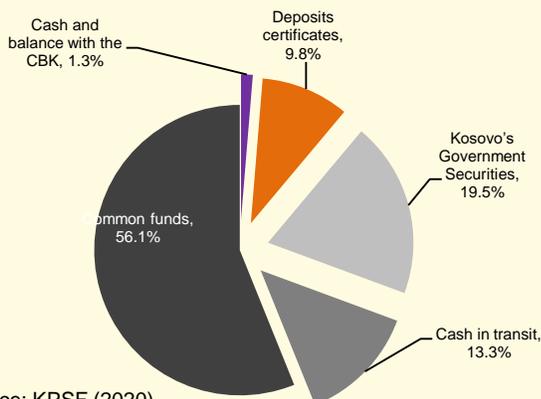
Source: CBK (2020)

Assets of the pension sector consist of 99.6 per cent which belong to Kosovo Pension Saving Trust (KPST) and 0.4 per cent of assets of Slovenian-Kosovo Pension Fund (SKPF). Assets structure of KPST is mainly comprised of assets invested abroad, albeit its weight considerably marked a decline compared to the previous period. Around 69.4 per cent of KPST assets are held abroad. Whereas, around 30.6 per cent of assets are invested in the country, representing an increase of 7.1 percentage points compared to Q2 2019. The largest portion of these assets are invested on bonds and treasury bills of Kosovo's Government, which marked a considerable increase during Q2 2020 compared to Q2 2019. This increase came as a result of the high demand to issue securities during this period and the willingness of KPST to invest in the domestic market. Also, the category of deposited assets at the banking sector continued to increase. Their share to total assets held in the country has marked a

considerable increase during the last five years, from 0.5 per cent at the end of Q2 2016 to 9.8 per cent at the end of Q2 2020 (figure 21).

During this quarter, KPST assets expanded by EUR 93.2 million, which primarily presents the investments increase in the domestic sector. Within assets invested in the country, in this quarter, the highest increase was marked by investments in securities of the Kosovo's Government (EUR +92.5 million), followed by the category of certificates of deposits (EUR +10.1 million), while the level of the cash held at the CBK marked a decline (EUR -36.6 million). Investments abroad, namely assets allocated at investments funds contracted for EUR 239.1 million, while assets on transit (which are expected to be invested abroad) marked a value of EUR 266.0 million in this quarter.

Figure 21. Structure of KPST assets (Q2 2020)



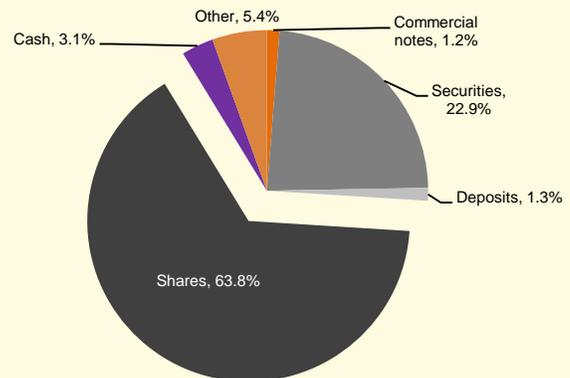
Assets structure of SKPF is mainly comprised of shares invested abroad (63.8 per cent), treasury bonds of foreign governments and of Kosovo's Government (22.9 per cent) and other assets (figure 22). Total assets of SKPF, in Q2 2020, expanded by EUR 0.8 million mainly as a result of the growth of the investments

abroad in shares, and investments in Kosovo's Government securities.

During Q2 2020, also SKPF considerably recovered from losses of investments (EUR -910.0 thousands), realizing gross profit from investments with a value of EUR 677.1 thousands (EUR 142.7 thousands in Q2 2019). Whereas, the value of new collections of contributors amounted to EUR 128.5 thousands in Q2 2020 (EUR 132.3 thousands in Q2 2019).

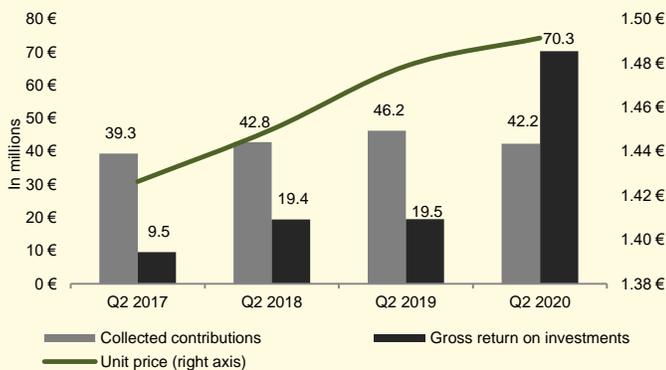
In this quarter, contributions collected by KPST increased by EUR 42.2 million, representing a decline of 8.5 per cent, compared to the same period of the previous year. This decline reflects the Kosovo Government containment measures taken to combat the spread of COVID-19 pandemic.

Figure 22. Structure of SKPF assets (Q2 2020)



The closure of certain non-essential sectors, since the second half of March until the end of May, and the gradual opening afterwards, and other restrictive measures that were into force, have had an impact on a number of employees not to receive income at all or even loose their jobs. This was reflected directly on the level of contributions collected by KPST.

Figure 23. Return on investments and KPSF performance



Source: KPSF (2020)

After considerable losses marked by KPST due to investments abroad in Q1 2020 (EUR -90.4 million), financial markets started to recover, and consequently KPST managed to realize a record profit of EUR 70.3 million in the second quarter of the year.

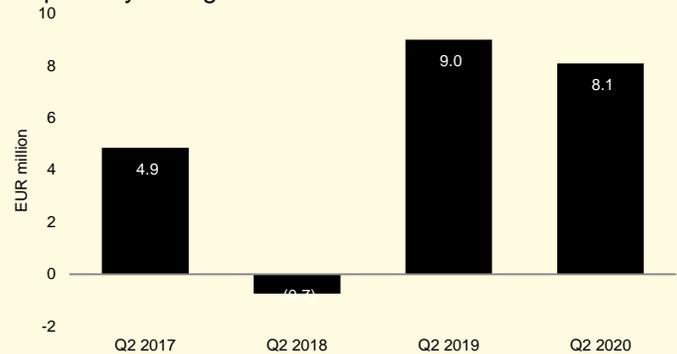
## Insurance Sector

*Insurance sector during the second quarter of 2020 was characterized with an activity expansion, albeit at a lower level. The level of collected premiums and claims incurred during this period marked a decline, which is interlinked with the COVID-19 pandemic. The insurance sector during Q2 2020 marked a high level of the profit compared to the negative financial results marked in the second quarter of the previous year.*

Assets of insurance sector by the end of June 2020, reached EUR 208.6 million, representing an annual growth of 9.8 per cent. The highest contribution to the growth of assets was given by the category of deposits held in the banking sector, followed by investments in securities, and other tangible assets. On quarterly basis, assets of the insurance sector increased by EUR

8.1 million in Q2 2020 (figure 24). Also, on quarterly basis, the increase was supported mainly by deposits held in the commercial banks, followed by other intangible asset, and the increase of investments in securities.

Figure 24. Assets of the insurance sector, quarterly change



Source: CBK (2020)

Similarly to the growth trend of assets, also the overall capitalization level of the sector was characterized with an increase. Only during this quarter, the total capital marked an increase of EUR 4.3 million, thus reaching the value of EUR 56.5 million as at end of period (June 2020). This capital increase came as a result of the increase of the paid shareholders capital and the profit realized in this period. However, the high level of losses accumulated from the previous years has had a negative impact on the further increase of the capital of insurance sector.

Regarding liabilities, they were characterized with an increase during this quarter (EUR +3.8 million in Q2 2020), while their value reached EUR 152.2 million at the end of June 2020.

The value of gross written premiums of insurance companies, in the second quarter of 2020, amounted to EUR 23.1 million, representing an annual decline of 9.4 per cent (figure 25). “Non-life” premiums account for

96.3 per cent of total written premium, whereas “life” premiums comprise 3.7 per cent. The considerable decline of collections from written premiums reflects the closure of the economy in the country during the period of March-May, with a gradual opening during the month of June, and other active containment measures to combat the spread of COVID-19 pandemic. As a consequence, only during Q2 2020, insurance sector realized sales of policies (‘non-life’) with a number of 150.2 thousands, while in the same period of the previous year the sales reached 283.0 thousands.

Similarly to the level of the written premiums, also claims paid by the insurance sector (including the Kosovo Insurance Bureau), marked a decline during this quarter, amounting to EUR 9.5 million, marking an annual decline of 23.9 per cent (figure 25). This significant decline of the level of claims collected reflects the movement restrictions of the citizens during this period, especially from the second half of March until the end of May 2020. This movement restrictions has had an impact on the lower accidents caused during this period, and consequently also a lower value of claims paid. Consequently, claims to premiums ratio in Q2 2020 improved, thus being reduced at 41.2 per cent from 49.0 per cent as it was in Q2 2019 (figure 25).

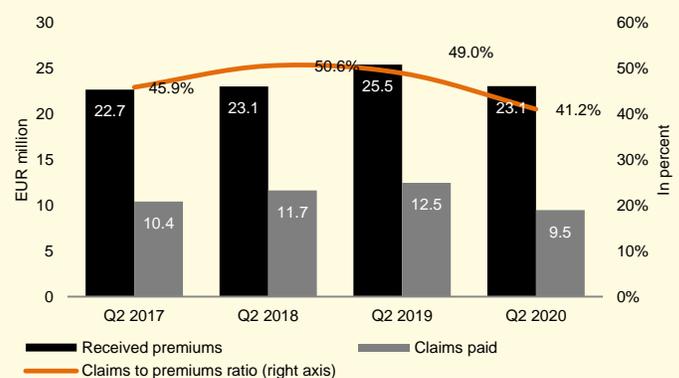
### Performance of the Insurance Sector

During Q2 2020, insurance sector performed with a net profit<sup>3</sup> of EUR 3.6 million (a loss of EUR 1.1 million in Q2 2019). The profit realized in this quarter came as a

result of the sharp decline of expenses level (claims incurred and other operating expenses of the sector) alongside with the slower decrease of collected premiums. The higher decline of expenditures is interlinked with COVID-19 pandemic, hence expenditures value is lower due to measures on movement restrictions and on other activities. Whereas, the slower decline of written premiums is a result of policies which have to be re-issued on annual basis, as the border policies, third party liabilities etc., and consequently were less affected by measures in force to combat the pandemic.

As regards to the liquidity level, insurance sector marked a significant improvement compared to the statement marked until June of the previous year.

Figure 25. Written premiums and claims paid



Source: CBK (2020)

Cash and its equivalents to technical reserves ratio shows that liquidity stood at the level of 101.8 per cent, representing a higher level of 11.2 percentage points compared to June 2019. Moreover, the other indicator of cash and its equivalent to total liabilities shows a growth of 6.4 percentage points of the level of the sector compared to the statement marked by June 2019,

<sup>3</sup> The profit/loss of the insurance company which has been revoked the license during the last year (2019), was deducted from the total net profit of the sector.

reaching 86.5 per cent at the end of June 2020. This growth was a result of the slower annual increase of cash and its equivalent (13.5 per cent) compared to liabilities (5.1 per cent).

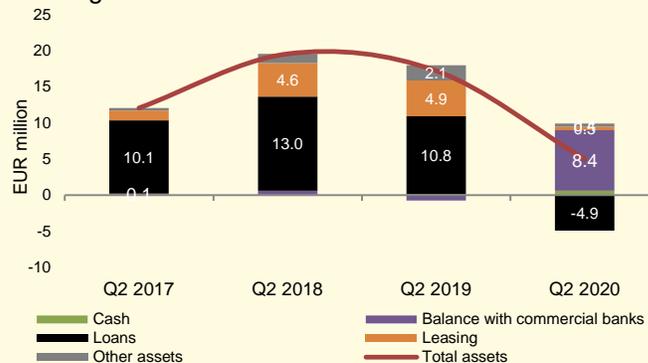
## Microfinance Sector

*Microfinance sector marked an activity increase in Q2 2020, albeit the increase was significantly slower than in the previous periods, being impacted by containment measures against COVID-19 pandemic (closure of the economy). However, microfinance sector continued to have satisfactory performance and good credit portfolio quality, albeit at lower levels compared the performance of the previous periods.*

### Assets

The assets increasing trend of the microfinance sector slowed down for the first time in five recent years. In June 2020, the total value of assets reached EUR 318.7 million, representing an annual increase of 11.8 per cent. On quarterly basis, assets increased by EUR 5.0 million, whereas compared to Q2 2019, this value was lower for EUR 12.2 million. The slower increase of assets of the sector marked in Q2 2020 compared to the same period of the previous year came as a result of the negative effects on the domestic economy caused by COVID-19 pandemic.

Figure 26. Assets of the microfinance sector, quarterly change



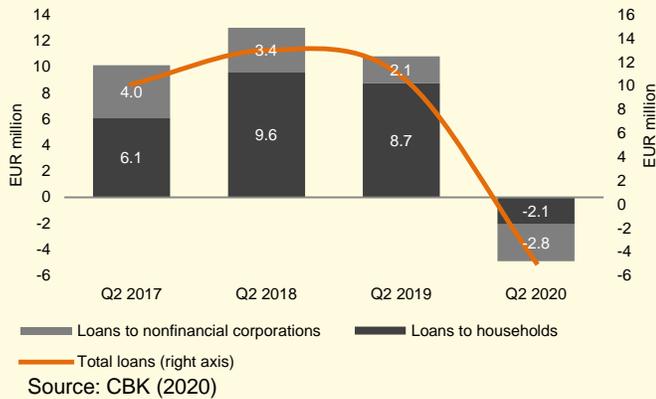
Source: CBK (2020)

This resulted in a lower value of borrowings issued by the external sector. Reluctance to place funds reflected on lending decline, and in a considerable increase of cash held at commercial banks. The activity of leasing marked a marginal increase (figure 26).

### Loans

On annual basis, total loans marked an increase of 7.3 per cent by the end of June 2020, whose stock reached the value of EUR 220.6 million. Compared to the previous period, loans marked a significant slowdown increase, which was reflected on lending to nonfinancial corporations and on lending to households as well. Lending to households expanded at a rate of 8.2 per cent (an annual increase of 27.9 per cent until June 2019), reaching the value of EUR 150.0 million at the end of June 2020. Loans value, on quarterly basis, decreased for EUR 4.9 million in Q2 2020, compared to the increase of EUR 10.8 million that had been marked in Q2 2019. Only in Q2 2020, loans to households marked a decrease of EUR 2.1 million (figure 27).

Figure 27. Value of loans to households and nonfinancial corporations, annual change of loans



Loans stock to nonfinancial corporations marked a value of EUR 70.6 million at the end of June 2020, representing an annual increase of 5.4 per cent (an annual growth of 15.8 per cent until June 2019). On quarterly basis, during Q2 2020, loans to nonfinancial corporations marked an increase of EUR 2.8 million (figure 27).

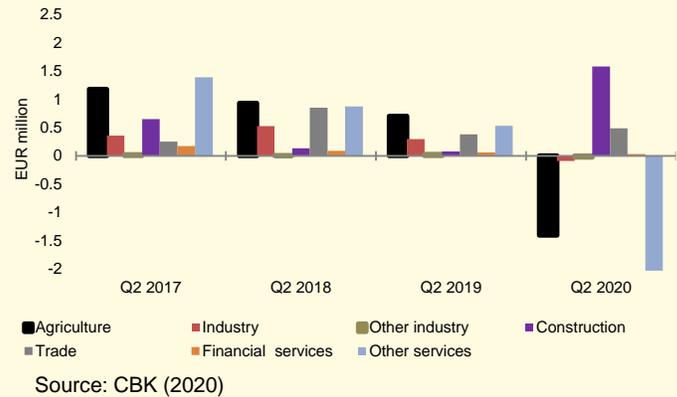
On sectoral basis, the value of loans issued to construction sector marked the highest increase of EUR 1.6 million for the period, followed by the marginal increase of loans to trade sector (EUR 0.5 million) during Q2 2020 (figure 28). Lending to agriculture sector and other services sector during this period was characterized with the highest decline of EUR 1.4 million and EUR 3.5 million, respectively.

### Leasing

The activity of leasing of the microfinance sector marked a marginal increase during Q2 2020 with a value of EUR 0.5 million, reaching the value of EUR 54.7 million at the end of the period. This increase was mainly a result of leasing to nonfinancial corporations, the value of which increased by EUR 0.3 million during

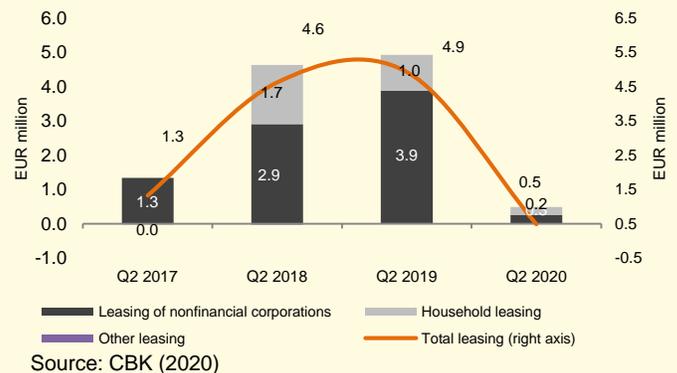
this quarter, reaching the value of EUR 29.5 million at the end of the period (figure 29).

Figure 28. Value of loans to nonfinancial corporations, by economic sectors, quarterly change



Similarly, also leasing to households increased by EUR 0.2 million in Q2 2020, reaching the total value of EUR 25.2 million at the end of the mentioned period.

Figure 29. Value of microfinance sector leasing

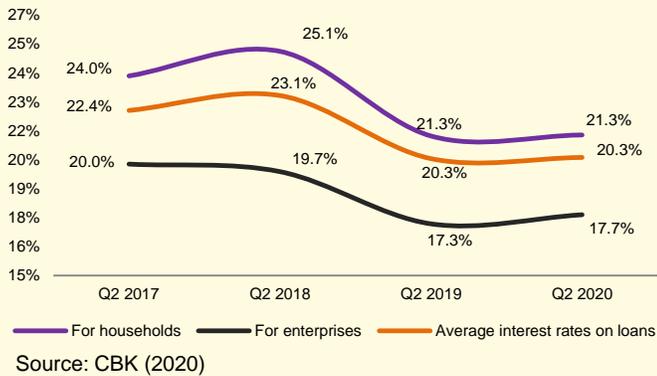


### Interest Rates

During the second quarter of 2020, the average interest rate on loans was 20.3 per cent, representing the same rate compared to the same period of the previous year (figure 30).

Concerning households, the interest rate stood at the same level as in the previous period, namely at 21.3 per cent (figure 30).

**Figure 30. Average interest rate on microfinance sector loans**



Based on the categories of loans, the average interest rate on mortgage loans increased by 0.6 percentage points, reaching 22.5 per cent in Q2 2020, compared to the previous period. Meanwhile, regarding consumer credit, interest rate remained unchanged as in the previous period, standing at 20.7 per cent in Q2 2020.

**Figure 31. Average interest rate on loans to enterprises, by economic sectors**



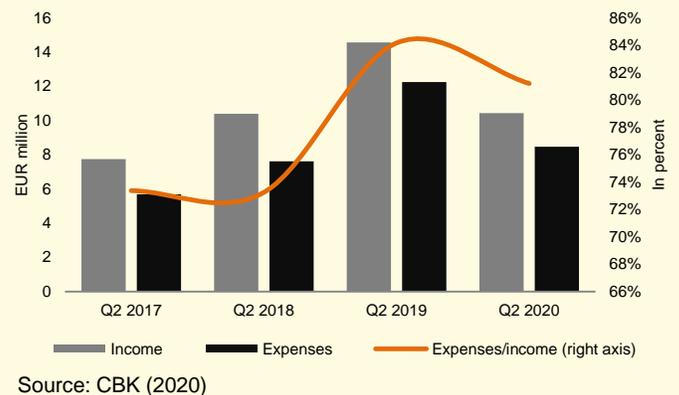
Unlike as with households, the interest rate on loans to nonfinancial corporations edged up slightly. In Q2 2020, interest rates applied to nonfinancial corporations stood at 17.7 per cent, representing an

increase of 0.4 percentage points compared to Q2 2019. On sectoral aspect, the lowest interest rate on loans remained in services sector with 17.3 per cent, albeit compared to the previous period the rate marked the highest increase for 4.2 percentage points. While, the interest rate on loans to agriculture marked the sharpest decline of 1.9 percentage points, falling at 19.3 per cent. Also, the interest rate on loans to industry sector marked a decline during this period with 1.1 percentage points, falling at 21.0 per cent during Q2 2020 (figure 31).

### Performance of the Microfinance Sector

Microfinance sector despite of marking a lower level of income collected, marked a positive financial performance in Q2 2020. During this quarter, the income of the sector amounted to EUR 10.4 million, representing a decline of EUR 4.1 million compared to the same quarter of the previous year.

**Figure 32. Microfinance sector income and expenses**



This decline came as a result of the decrease of interest income of EUR 3.7 million, falling at EUR 9.8 million during Q2 2020 (figure 32). Non-interest income declined by EUR 0.4 million during this quarter,

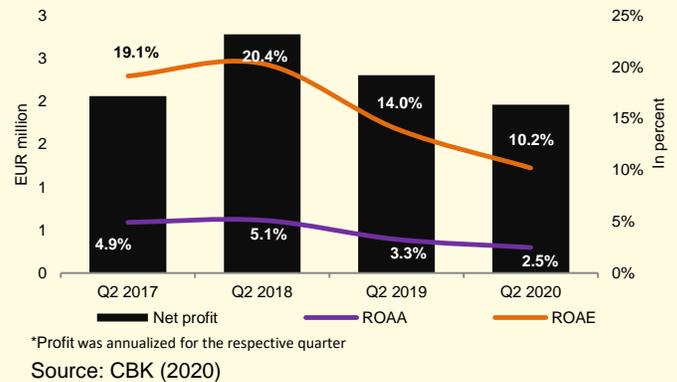
decreasing the value at 0.6 million, which primarily reflects the decline of income from services.

Expenditures of the sector marked the value of EUR 8.5 million in Q2 2020, representing a value which is lower for EUR 3.8 million compared to the same quarter of the previous year. Expenses decline mainly reflects the decrease of non-interest expenses (administrative expenses and staff expenses and loan loss provisions), which declined by EUR 2.8 million, falling at EUR 5.1 million during Q2 2020. Also, a decline was marked by interest expenses and other operating expenses, albeit at lower levels.

Expenses-to-income ratio, as an indicator of the sector performance, marked a decline of 3.0 percentage points compared to the previous period, standing at the level of 81.2 per cent in Q2 2020. This implies that for every EUR 1 invested, the microfinance sector spends around EUR 0.812. The higher decline of income compared to expenses resulted on the net profit of this quarter to decline for EUR 300 thousands compared to Q2 2019, falling at the value of EUR 2.0 million (figure 33).

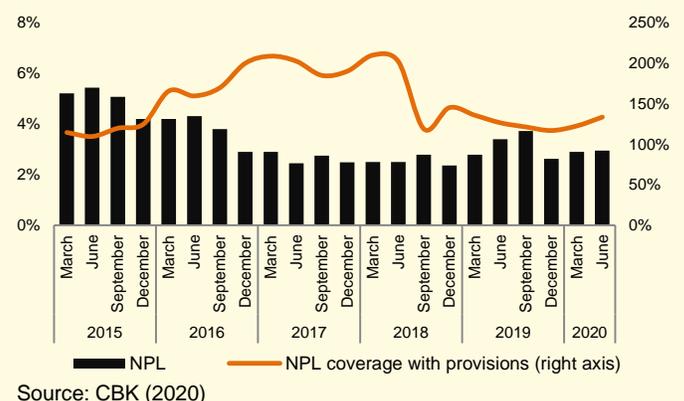
The financial performance of the sector was reflected also on two other profitability indicators, Return on Average Assets (ROAA) and Return on Average Equity (ROAE), which declined by 0.8 percentage points and 3.8 percentage points, respectively, compared to Q2 2019 (figure 33).

Figure 33. Profitability indicators of microfinance sector



Regarding the indicators of credit portfolio quality in microfinance institutions, nonperforming loans continued to stand at low levels and were characterized with good coverage of provisions. Until the end of the period, nonperforming loans stood at 3.0 per cent, representing a lower level compared to the same period of the previous year (3.4 per cent in Q2 2019). Moreover, the NPL coverage with provisions was 133.5 per cent, until the end of Q2 2020 (figure 34).

Figure 34. Indicators of credit portfolio quality

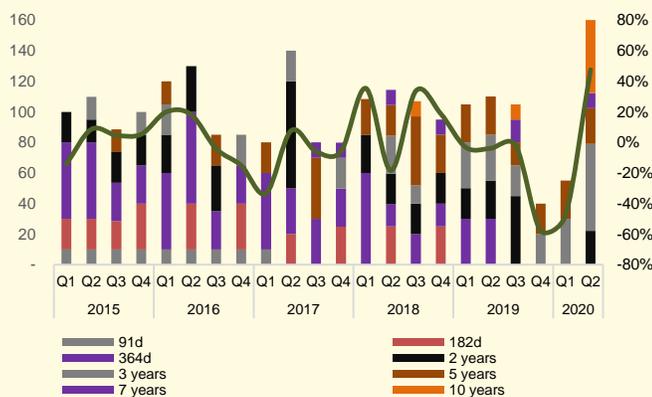


## Securities Market

In Q2 2020, Kosovo's Government issued a debt with a quite high value compared to the same period of the previous year. High issuances of sovereign debt is interlinked with the higher financing needs to support the citizens and the economy against the social and economic crises caused by COVID-19 pandemic. At the same time, budget revenues suffered a decline due to pandemic, thus increasing the financing need to come from the fiscal emergency package.

The debt issued by Kosovo's Government marked an annual growth of 47.6 per cent in Q2 2020 (figure 35). The amount of the issued debt during this period reached EUR 162.4 million, whereas total income for the Kosovo's Government reached the value of EUR 162.2 million. The demand to invest in Kosovo's Government securities continued to exceed the offer, which was for 1.16 times higher than the demanded amount, albeit compared to the previous year, it stood at lower levels. The average interest rate on securities was 2.3 per cent in Q2 2020, representing a higher rate for 0.7 percentage points than in Q2 2019 (figure 36).

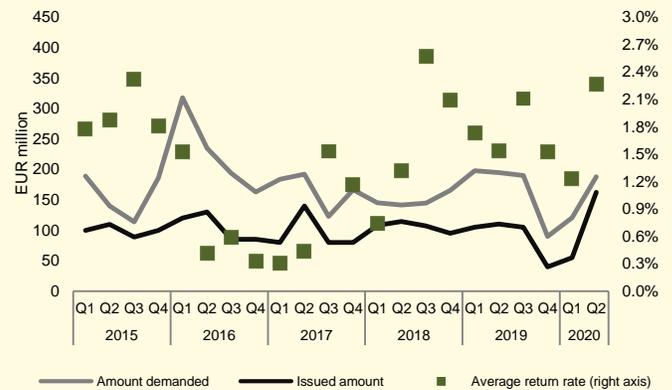
Figure 35. Amount of issued debt, annual increase



Source: Ministry of Finance (2020)

The increase of interest rate compared to the previous period reflects the trend of securities issuance towards long-term maturities. During Q2 2020, over 50.0 per cent of securities issued had a maturity over five years, while in Q2 2019 only 22.7 per cent of securities issued were with a maturity over five years.

Figure 36. Bid to cover ratio

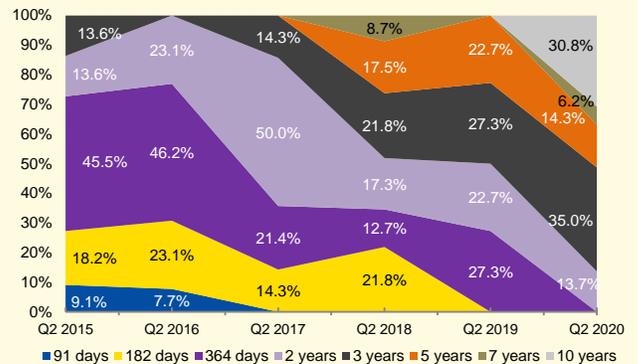


Source: Ministry of Finance (2020)

The securities structure is dominated by government bonds, with a maturity of 3 years, followed by securities with a 10-year maturity.

Compared to the second quarters of previous years, in Q2 2020 for the first time there were no issuance of treasury bills (bills with the longest maturity of up to 364 days) (figure 37). The banking sector, pension funds and insurance companies continue to be the only financial institutions in the country to invest in the primary market of Kosovo's Government securities. Until the end of Q2 2020, it was marked an increase of investments in Kosovo's Government securities of 30.8 per cent (from the pension sector), of 15.1 per cent (from the banking sector), and an increase of 8.6 per cent marked by the insurance sector, compared to the end of Q1 2020.

Figure 37. Government securities structure, in per cent



Source: Ministry of Finance (2020)

**The suggested citation of this publication:**

CBK (2020): Quarterly Assessment of Financial System No. 31 Q2 2020, Central Bank of the Republic of Kosovo, Prishtina

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## Macroeconomic selected indicators

Description	June 2019	June 2020
Real sector 1/		
Gross Domestic Product (GDP) (in millions of EUR)	3,245.3	3,073.9
Consumer prices (annual average)	3.2%	0.6%
Consumer prices (end of period)	2.9%	0.1%
Fiscal Sector 2/		
Budget Revenues (in millions of EUR)	853.5	760.3
Budget Expenditures (in millions of EUR)	853.2	871.8
Primary balance (in millions of EUR)	0.3	-111.5
Financial sector (in millions of EUR) 3/		
Assets of financial corporations	6,666.4	7,412.2
of which : Banks	4,303.4	4,849.0
Loans	2,940.0	3,127.4
Deposits	3,425.3	3,903.2
Interest Rates on Loans, end of period	6.3%	6.3%
Interest Rates on Loans, end of period	1.3%	1.5%
Interest rate gap	5.1%	4.7%
External sector,(in millions of EUR) 3/		
Balance of payments		
Current and capital account	-294.3	-227.8
of which: remittances	405.6	434.9
Financial account	-145.1	-284.1
Foreign Direct Investments in Kosovo	110.8	164.7
Portfolio investments, net	-31.7	-388.9
Other investments, net	-260.9	214.3
International Investment Position (IIP), net	-462.4	-709.7
Assets	4,912.3	5,076.3
Liabilities	5,374.7	5,786.1
External debt	2,155.0	2,273.0
Private external debt	1,663.2	1,754.4
Public external debt	491.7	518.6

Source:

1/ KAS (2020);

2/ MF (2020);

3/ CBK (2020).

