

Summary

Based on KAS estimates, real GDP marked a decline of -5.6%, by September 2020. Investments and net exports were characterized with a decline, whereas consumption has marked an increase. Q4 2020 is estimated to have marked a slowdown decline compared to the previous quarters. These estimates are based on the increase of exports of goods and services in the reporting period, public consumption, the increase in remittances, etc. Conversely, public investments, the turnover of businesses, and new investment loans were characterized with a considerable decline.

On quarterly basis, assets of financial system increased by EUR 236.8 million, representing a slower annual increase of 6.6%. The trend of financial system assets mainly is attributable to the banking sector activity and insurance sector. The significant growth of assets of the banking sector in this quarter mainly reflects the deposits activity, as a result of the transfer of funds from the pension sector (the withdrawal of 10% of pension savings by the contributors) to the citizens' accounts, and the increase of the level of deposits from nonfinancial corporations.

Within assets of the banking sector, cash and balance with the CBK marked the highest growth, followed by lending activity, and investments in securities. Whereas, within liabilities, deposits as the main source of financing the banking activity, marked the most notable increase in this quarter. With an increase were characterized also the category of own resources (from the retained earnings and realized profit). The banking sector continued to be well capitalized, liquid, and with high quality of credit portfolio.

The pension sector was characterized with a contraction of assets in Q4 2020, as a result of the withdrawal of 10% of pension savings at the end of the year, a dynamic which was neutralized to some extent from the collected contributions and positive return on investments.

The insurance sector was characterized by an increase of assets during Q4 2020, higher level of written premiums and the decrease of the level of claims paid compared to Q4 2019.

Microfinance sector has marked a contraction of activity against the previous year. The credit portfolio quality continued to be high, albeit with a declining trend as a result of the increase of credit risk, caused by Covid-19 pandemic. During the fourth quarter of 2020, Kosovo's Government issued debt with a significant higher value compared to the same quarter of the previous year. The increase of the level of sovereign debt reflects the pandemic circumstances which had an impact on the decline of fiscal income, and at the same time the increase of expenditures to support the economy.

CONTENTS

Summary	i
Macroeconomic Developments	4
Financial System	5
Banking Sector	5
Assets	6
Performance of the Banking Sector	11
Box 1. Stability index of the banking sector	13
Pension sector	15
Insurance sector	17
Performance of the insurance sector	18
Microfinance sector	18
Assets	18
Performance of the microfinance sector	20
Securities market	22

CHARTS AND TABLES

Chart 1. Assets Value of Kosovo's financial system	05
Chart 2. Quarterly changes of assets of financial system constituent sectors	05
Chart 3. Banking sector assets structure in the respective quarters	06
Chart 4. Quarterly changes of loans stock	06
Chart 5. Quarterly changes of loans to nonfinancial corporations, by economic activity	07
Chart 6. New loans to nonfinancial corporations and households	07
Chart 7. Structure of liabilities and own resources	08
Chart 8. Deposits by sources	08
Chart 9. Structure of deposits by main categories	08
Chart 9-A. New collected deposits	09
Chart 10. Interest rate on loans and deposits	09
Chart 11. Interest rates on loans to nonfinancial corporations	09
Chart 12. Interest rate on loans to households	10
Chart 13. Interest rates on deposits	10
Chart 14. Interest rates on nonfinancial corporations deposits	10
Chart 15. Interest rates on household deposits	11

Chart 16. Profit and profitability indicators of the banking sector -----	11
Chart 17. Nonperforming loans and loan loss provisions -----	12
Chart 18. Solvency indicators -----	12
Chart 19. Liquidity indicators -----	12
Chart 20. Assets of the pension sector -----	15
Chart 21. Structure of KPST assets -----	16
Chart 22. Structure of SKPF assets -----	16
Chart 23. Return on investments and KPST performance-----	16
Chart 24. Assets of the insurance sector-----	17
Chart 25. Written premiums and claims paid-----	18
Chart 26. Assets of microfinance sector-----	18
Chart 27. Value of loans to households and nonfinancial corporations -----	19
Chart 28. Value of loans to nonfinancial corporations, by economic sectors -----	19
Chart 29. Value of microfinance sector leasing-----	19
Chart 30. Average interest rate on microfinance sector loans -----	20
Chart 31. Average interest rate on loans to enterprises, by economic sectors-----	20
Chart 32. Microfinance sector income and expenses-----	21
Chart 33. Profitability indicators of microfinance sector -----	21
Chart 34. Indicators of loans portfolio quality -----	21
Chart 35. Amount of issued debt -----	22
Chart 36. Bid to cover ratio -----	22
Chart 37. Government securities structure -----	22
Table 1. Macroeconomic selected indicators -----	24

Macroeconomic Developments¹

Based on KAS estimates, real GDP marked a decline of -5.6%, by September 2020. Investments and net exports were characterized with a decline, whereas consumption has marked an increase. Q4 2020 is estimated to have marked a slowdown decline compared to the previous quarters. These estimates are based on the increase in exports of goods and services in the reporting period, in public consumption, the increase of remittances, etc. Conversely, public investments, the turnover of businesses, new investment loans were characterized with a considerable decline.

Consumer prices marked a decline of -0.1% in Q4 2020, mainly as a consequence of the decline of transport prices, footwear and clothing, recreation, home furnishing, etc. The slowdown increase of prices was marked also by the prices of food and non-alcoholic beverages, thus making the core deflation reach 0.8%.

Mitigating the negative effects of the Covid-19 pandemic, has improved the performance of budget revenues compared to previous quarters. Budget revenues, in Q4 2020, decreased by -0.6% (-13.5% in Q3 2020), while budget expenditures increased by 8.6%. Consequently, Kosovo's budget recorded a primary budget deficit of EUR 280.5 million. Public debt reached EUR 1.5 billion, which is for 23.9% higher

compared to Q4 2019. As a percentage to GDP, public debt reached 21.8% from 17.5% as it was in Q4 2019.

The external sector was characterized with a reduction of the current account deficit of 56.8% in Q4 2020. The positive balance of services as well as primary and secondary income have increased significantly, while the goods deficit has improved. Trade deficit of goods was EUR 836.2 million or 2.0% lower compared to Q4 2019. This decline of goods deficit is primarily attributable to the considerable increase of exports, while also the import of goods marked an increase which was lower than the increase of exports. Within the balance of payments, remittances were characterized with an increase of 26.3%, in Q4 2020.

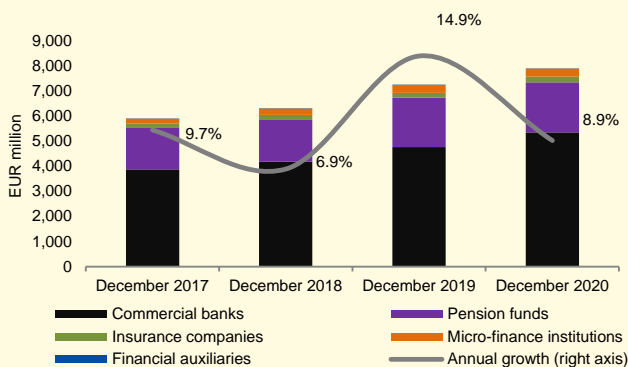
¹For more information on macroeconomic developments, please refer to: Quarterly Assessment of Macroeconomic Developments (Q4 2020) published on the CBK website.

Financial System

Assets of financial system reached a value of EUR 7.91 billion, by the end of December 2020. Compared to the previous year, financial system expanded with slower trend (chart 1), mainly being impacted by developments in the pension sector. Withdrawal of 10% of pension savings by the contributors² in December, and the lower return on investments during the year have had an impact on the trend of the pension sector.

Banking sector had the main contribution to assets growth of the financial system, marking an annual increase of 12.4% in 2020 (13.7% in the previous period). Insurance and microfinance sector, had positive contribution to the increase, albeit their impact remains low due to the low weight they have to total assets of the sector.

Chart 1. Assets value of Kosovo's financial system



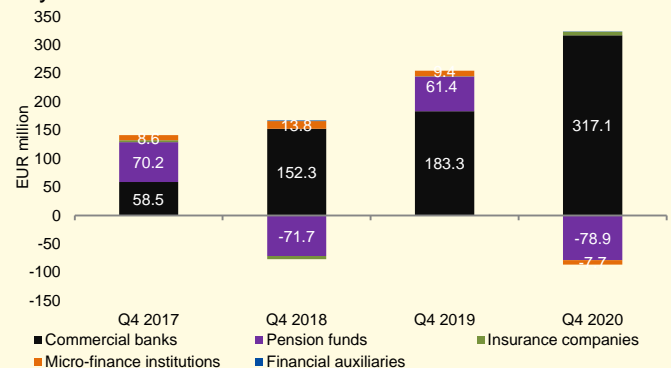
Note: The data are as at end of the noted quarter
Source: CBK (2021)

Meanwhile, on quarterly basis, financial system assets increased by EUR 236.8 million, primarily being affected by the banking sector activity (EUR +317.1 million) and the insurances sector (EUR +6.2 million).

Pension sector assets contracted by EUR 78.9 million, while microfinance sector marked a contraction of assets by EUR 7.7 million.

The significant growth of assets of the banking sector in this quarter mainly reflects the deposits activity, as a result of the transfer of funds from the trust pension sector funds (10%) to the citizens' accounts, and the increase of the level of deposits from nonfinancial corporations. Pension sector marked a contraction of assets due to the withdrawal of pension savings, which was neutralized to some extent by the positive return on investments during this period.

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



Source: CBK (2021)

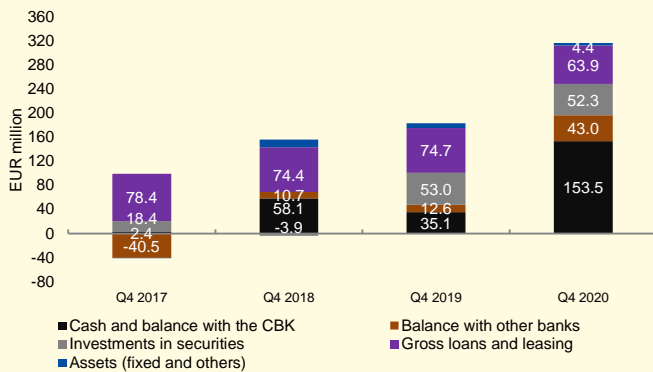
Banking Sector

Within assets of the banking sector, cash and balance with the CBK marked the highest growth, followed by lending activity, and investments in securities. Whereas, within liabilities, deposits as the main source of financing the banking activity, marked the most significant increase in this quarter. With an increase was characterized also the category of own resources (from the retained

² The Law 07/L-016 for economic recovery – Covid-19

earnings and realized profit). The banking sector continued to be well capitalized, liquid, and with high quality of credit portfolio.

Chart 3. Banking sector assets structure in the respective quarters



Source: CBK (2021)

Assets

The value of total assets of the banking sector at the end of Q4 2020, reached EUR 5.35 billion, representing an annual growth of 12.4%. On quarterly basis, assets of the insurance sector increased by EUR 317.1 million, in Q4 2020. Lending activity of the banking sector (which has the largest share within the assets of the sector, with 60.6%) increased by EUR 63.9 million in this quarter, EUR 10.8 million less compared to the previous year (chart 3). The category of balance sheet with commercial banks, which is mainly comprised of deposits and the like, invested in banks abroad, marked an increase of EUR 43.0 million. The category of investments in securities has marked an increase of EUR 52.3 million in this quarter, thus maintaining almost the same increased level as in the previous year. The category of cash held at treasury and at the CBK marked a more significant increase of EUR 153.5 million during this quarter, reflecting the notable

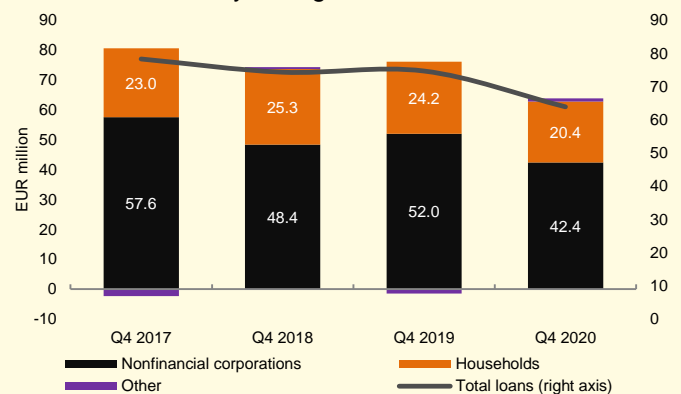
increase of deposits at the end of 2020 (primarily the transfer of funds of the pension saving trust to the citizens' accounts within the law of the economic recovery).

Loans

The value of total loans at the end of Q4 2020, reached EUR 3.25 billion, representing an annual increase of 7.1% (an increase of 10.0% marked at the end of Q4 2019). For the first time in the recent five years, the lending activity was characterized with slowdown of double digit increase into a single digit increase, which was impacted by the crises of the pandemic conditions. Loans to nonfinancial corporations, which have a share of 63.3% to total loans, slowed down the increase at 7.2% from 9.8% as at end-December 2019.

Similarly, loans to households slowed down the annual increase at 7.1% from 10.4% as it was a year earlier.

Chart 4. Quarterly change of loans stock

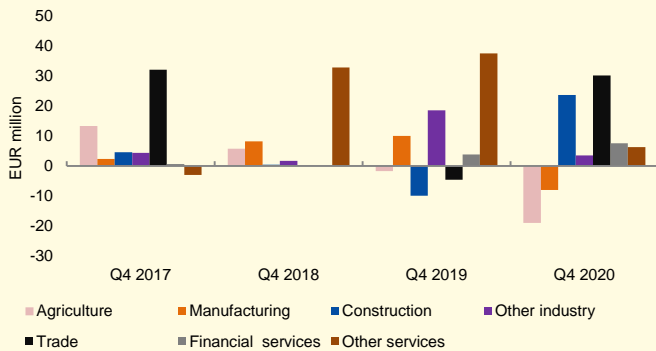


Source: CBK (2021)

Loans to households increased by EUR 20.4 million only during Q4 2020 (EUR 24.2 million during Q4 2019), while loans to nonfinancial corporations increased by EUR 42.4 million (EUR 52.0 million during Q4 2019) (chart 4).

In terms of economic activities, on quarterly basis, only lending to agriculture and manufacturing sector, marked an annual decline. With a significant increase of lending was characterized trade sector, construction and financial services sector (chart 5).

Chart 5. Quarterly change of loans to nonfinancial corporations, by economic activity



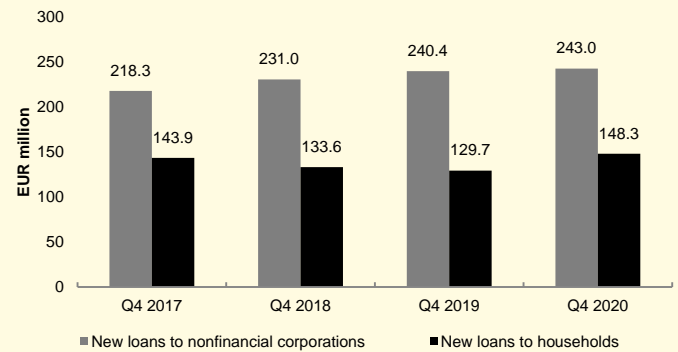
Source: CBK (2021)

New loans, in Q4 2020 marked a value of EUR 391.3 million, representing an annual increase of 5.7% compared to Q4 2019. New loans designated to nonfinancial corporations increased by 1.1%, amounting to EUR 243.0, in Q4 2020 (chart 6). A significant increase was marked by loans with non-investment purposes with 34.7%, whose value reached EUR 122.8 million in this quarter. While, new investment loans were characterized with an annual decline of 21.0%, falling at the value of EUR 113.9 million in Q4 2020. By sectoral terms, new loans to services sector marked an increase, whereas other sectors were characterized with a decline in Q4 2019 (agriculture, industry and other sectors).

Meanwhile, new loans to households were characterized with a significant increase. The value of total new loans was for EUR 18.7 million higher against Q4 2019, reaching the value of EUR 148.3 million in Q4 2020. Of which, new consumer credit

marked an increase with EUR 10.5 million, amounting to EUR 98.4 million during Q4 2020. New mortgage loans were also characterized by a more notable increase of 44.3%, reaching the value of EUR 39.8 million during Q4 2020.

Chart 6. New loans to nonfinancial corporations and households, in Q4



Source: CBK (2021)

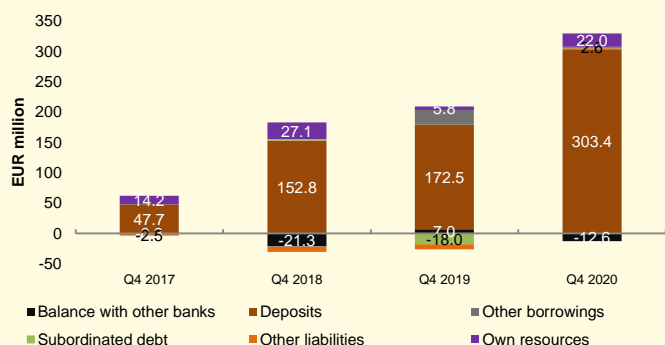
The dynamics recorded in the new loans issued during the fourth quarter and in the previous quarters of 2020 reflect also the reprogrammed loans by the banking sector. During this period, the CBK enabled the restructuring of loans as an easing measure for clients / borrowers affected by the crisis caused by the Covid-19 pandemic. As a consequence, during the period of March - December 2020, at an average, around 38.0% of total loans stock were comprised of re-programmed loans, whereas their historic level was of an average of 1.0%.

Liabilities and Own Resources

The structure of liabilities and own resources is mainly comprised by deposits (81.4%), whose stock, at the end of December 2020, reached EUR 4.36 billion marking an annual growth of 11.5% (16.2% in December 2019). While, on quarterly basis, deposits marked an accelerated increase in Q4 2019 (chart 7). Conversely,

the category of own resources of the sector increased by EUR 22.0 million in Q4 2020 (EUR 5.8 million in Q4 2019), as a consequence of the profit realized and retained earnings during this period. At the end of December 2020, the stock of total equity reached the value of EUR 611.0 million, marking an annual increase of 17.5%.

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



Source: CBK (2021)

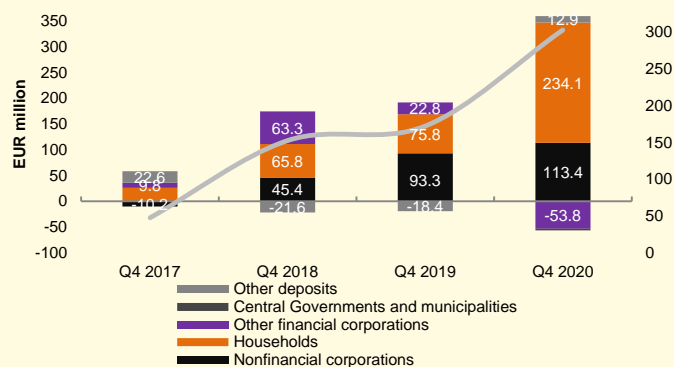
Deposits

The double-digit increase of deposits stock compared to the previous year, despite the negative effects caused by the Covid-19 pandemic, was mainly due to the transfer of 10% of pension funds to contributors' accounts, as well as the increase of non-financial corporations deposits. Withdrawal of contributions from pension accounts was reflected in an increase of the banking sector deposits, in Q4 2020.

During this period, deposits marked an increase of EUR 303.4 million, against the increase of EUR 172.5 million in Q4 2019. Household deposits increased by EUR 234.1 million in Q4 2020, reaching the value of EUR 2.94 billion at the end of the period (December 2020) (chart 8). Whereas, nonfinancial corporation deposits increased by EUR 113.4 million in this

quarter, reaching the value of EUR 825.7 million at the end of the period (December 2020).

Chart 8. Deposits by sources, quarterly change

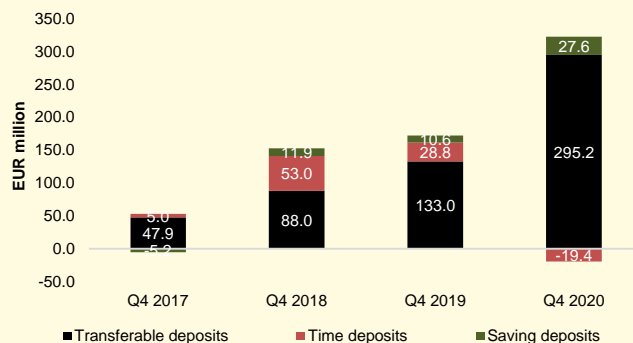


Source: CBK (2021)

Deposits from other financial corporations in this quarter decreased by EUR 53.8 million (EUR +22.8 million in Q4 2019), which mainly reflects the developments in the pension sector.

At the end of period, the stock of this category amounted to EUR 263.3 million. According to the categories of deposits, transferable deposits expanded with a value of EUR 295.2 million (EUR +133.0 million in Q4 2019) on quarterly basis, while their stock reached the value of EUR 2.79 billion at the end of the period (December 2020) (chart 9).

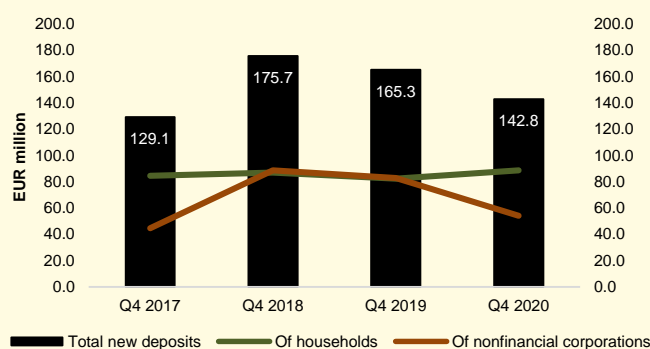
Chart 9. Deposits structure by main categories, quarterly change



Source: CBK (2021)

Whereas, time deposits during this period shrank by EUR 19.4 million (an expansion of EUR 28.8 million during Q4 2019), reaching the value of EUR 1.02 billion at the end of the period (December 2020). Saving deposits marked an expansion of the value of EUR 27.6 EUR million during this quarter (+EUR 10.6 million in Q4 2019), reaching the value of EUR 552.7 million at the end of the period (December 2020).

Chart 9-A. New collected deposits, quarterly change



Source: CBK (2021)

Transferable deposits continued to have the highest share to total deposits of the sector (64.0%), followed by time deposits (23.4%) and saving deposits (12.7%).

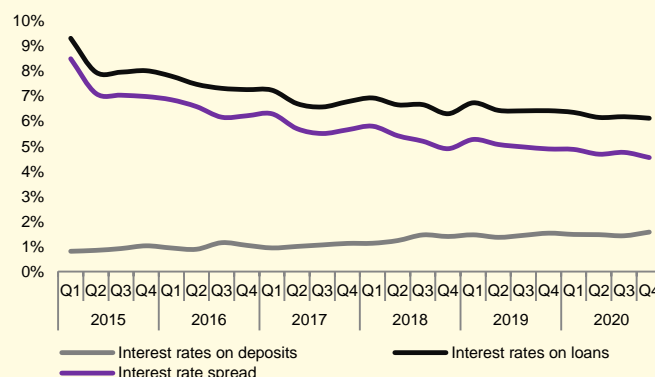
The value of new collected deposits³ in Q4 2020 was EUR 142.8 million, of which EUR 54.0 million were deposits collected from nonfinancial corporations, whereas EUR 88.7 million belonged to household deposits (chart 9A).

Interest Rates⁴

The average interest rate on loans was 6.1%, in Q4 2020, or 0.3 percentage points lower against the same period of the previous year. Whereas, interest rates on deposits remained at the same level as in the previous

periods, standing at 1.6% in Q4 2020. Consequently, the interest rate spread of loans and deposits narrowed down to 4.5 percentage points (chart 10).

Chart 10. Interest rates on loans and deposits

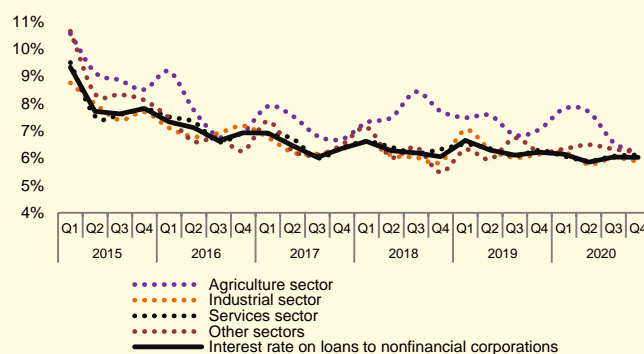


Source: CBK (2021)

Interest rates on loans

The average interest rate on loans to nonfinancial corporations stood at 6.0% during Q4 2020, or for 0.2 percentage points lower against the previous year (chart 11).

Chart 11. Interest rates on loans to nonfinancial corporations



Source: CBK (2021)

As regards to categories of loans, interest rate on investment loans was lower (6.0%) compared to interest rate on non-investment loans (6.2%).

³ New deposits include time deposits.

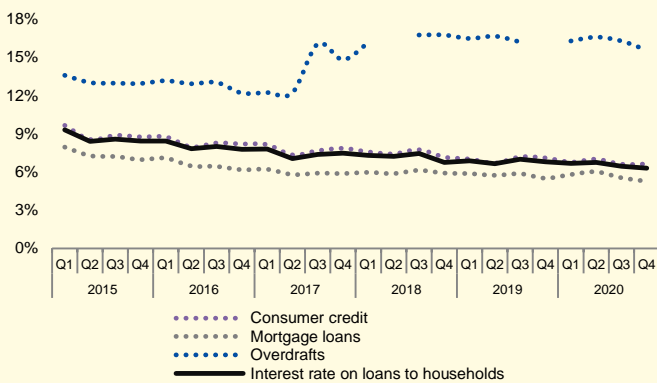
⁴ The calculation of interest rates: quarterly average of interest rates on loans and deposits. In the text it is referred as "the interest rates".

Alongside with the same period as in the previous year, it was observed a more significant decline of interest rates of non-investment loans (for 0.21 percentage points) compared to the decline for investment loans (for 0.1 percentage points).

In sectoral terms, the interest rate on agriculture loans marked a decline of 0.9 percentage points, dropping at an average of 6.2%.

Similarly, also interest rates on loans to industry and loans to services sector marked a decline of 0.3 and 0.2 percentage points, falling at 5.9% and 6.1%, respectively.

Chart 12. Interest rates on loans to households



Source: CBK (2021)

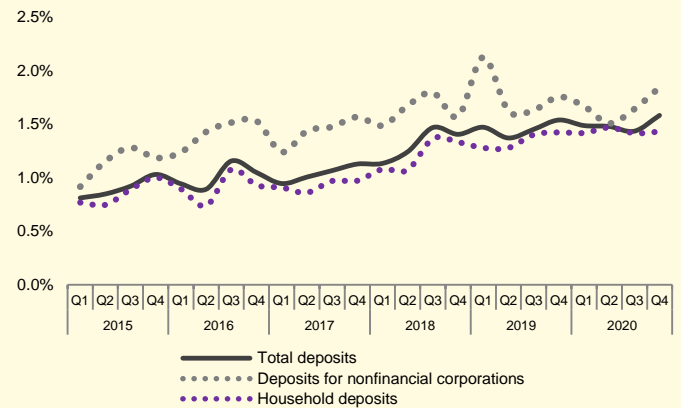
Concerning loans to households, the average interest rate stood at 6.3% , representing a decline of 0.5 percentage points compared to Q4 2019. A higher interest rate was marked by consumer credit (6.6%), which marked a decline of 0.5 percentage points compared to Q4 2019. In addition, also interest rate on mortgage loans marked a decline in this quarter (from 5.5% in Q4 2019 to 5.3% in Q4 2020) (chart 12).

Interest rates on deposits

The average interest rates on deposits remained almost at the same level as in the previous periods, standing at 1.6% (chart 13).

Interest rates on nonfinancial corporation deposits, continued to be more favorable compared to those of households, although the difference between them was marginal.

Chart 13. Interest rates on deposits

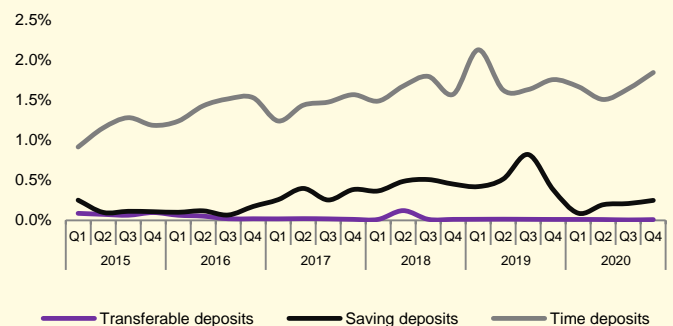


Source: CBK (2021)

Interest rates on nonfinancial corporations deposits was approximate to the previous year, standing at 1.8% (chart 14).

Similarly, also interest rates on household deposits remained approximate in this quarter compared to the previous period (Q4 2019).

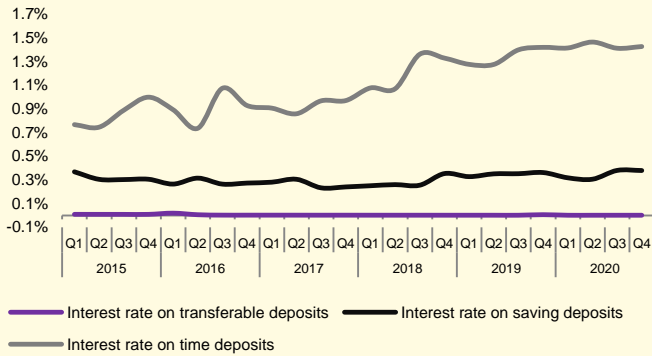
Chart 14. Interest rate on nonfinancial corporation deposits, by categories



Source: CBK (2021)

The average interest rate stood at 1.4%, similar to the rate on time deposits, while those on saving deposits stood at 0.4% (chart 15).

Chart 15. Interest rates on household deposits, by categories



Source: CBK (2021)

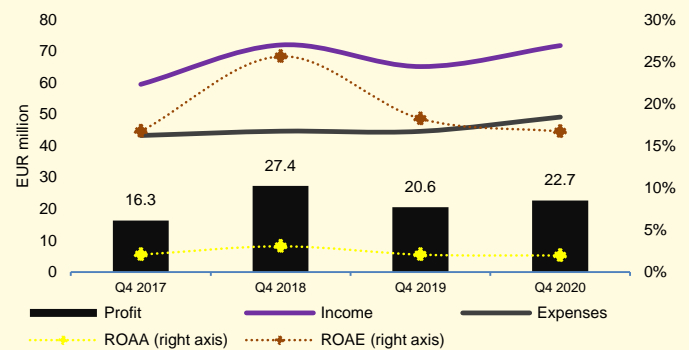
Performance of the Banking Sector

The banking sector realized a profit with a value of EUR 22.7 million, in Q4 2020, which is for EUR 2.1 million higher compared to Q4 2019 (chart 16). The profit realized in Q4 2020 was mainly a result of the higher increase of income (for EUR 6.6 million) compared to the increase of expenditures (for EUR 4.5 million). During this quarter income amounted to EUR 71.8 million, where interest income (mainly interest income on loans) amounted to EUR 47.6 million (annual decline of EUR 1.4 million). Meanwhile, non-interest income which is mainly comprised of fees and commissions, marked a value of EUR 18.8 million, marking an annual growth of EUR 5.4 million compared to Q4 2019.

Expenditures of the banking sector marked a value of EUR 49.2 million in Q4 2020. The largest category, general and administrative expenses reached the value of EUR 28.2 million, representing an approximate amount as in Q4 2019. The category of non-interest expenses, in Q4 2020, reached the value of EUR 15.3 million (for EUR 8.7 million higher compared to the

previous period), mainly as a consequence of the higher share for expenses on loan loss provisions, being impacted by the increase of credit risk caused by the pandemic situation. Whereas, the category of interest expenditures during this period decreased for EUR 3.4 million, thus standing at EUR 3.1 million, in Q4 2020.

Chart 16. Profit and profitability indicators of the banking sector



Source: CBK (2021)

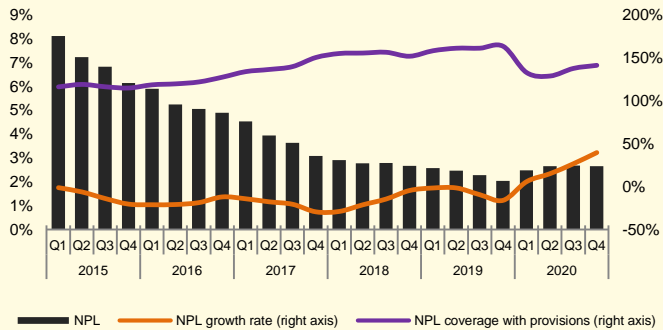
The increasing trend of income (10.2%) and expenditures (10.2%), had an impact on expenditures to income ratio to stand at the same level as in Q4 2019 at 68.4%. This ratio indicates that the banking sector spends EUR 0.684 for every EUR 1 earned (chart 16).

Financial Soundness Indicators

Financial soundness indicators of the banking sector continued to be at high level in Q4 2020, exceeding the minimum levels as required by the regulations.

Nonperforming loans, although having marked an increase compared to the previous quarters, their level to total loans continues to be low. The NPL rate to total loans ratio stood at the level of 2.7%, in December 2020 (2.0% at the end of December 2019) (chart 17). Nonperforming loans continued to be well provisioned, at the level of 141.4% (163.5% at the end of December 2019).

Chart 17. Nonperforming loans and loan loss provisions

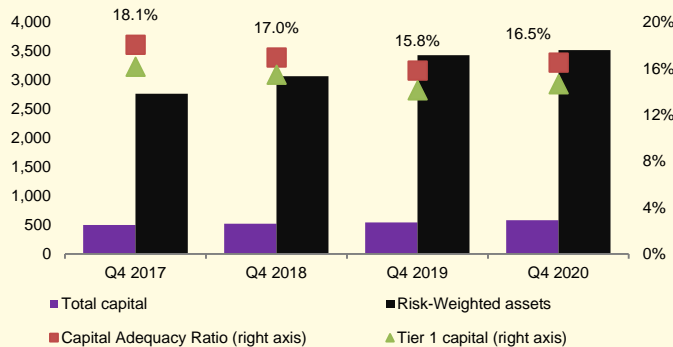


Note: The data are as at end of the noted quarter

Source: CBK (2021)

Banking sector continues to be well capitalized and sustainable as a result of the inherited capital from the previous years and the profit realized in 2020. During this period, the Capital Adequacy Ratio stood at the level of 16.5%, representing a higher level for 0.7 percentage points than in the same period of the previous year (chart 18).

Chart 18. Solvency indicator



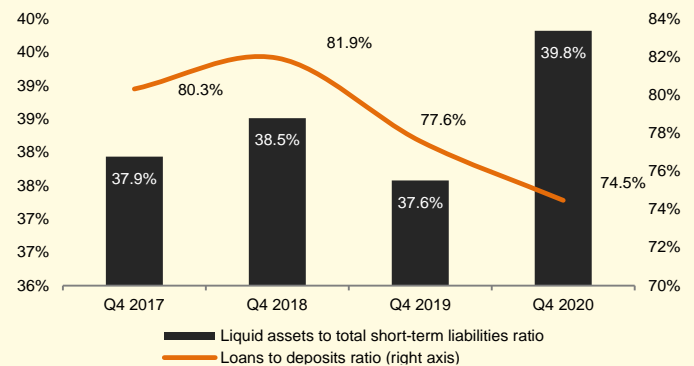
Note: The data are as at end of the noted quarter

Source: CBK (2021)

The increase of this indicator is attributable to the higher increase of the capital compared to the slower increase of risk weighted assets. The more notable increase of capital was affected also by the non-distribution of the dividend during 2020⁵. Whereas, the

slower increase of risk weighted assets reflects the slowdown growth of lending compared to the previous year.

Chart 19. Liquidity indicators



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

Source: CBK (2021)

As regards to the liquidity of the banking sector, the liquid assets to short-term liabilities ratio marked a slight improvement of 2.3 percentage points compared to Q4 2019, standing at the level of 39.8%. The 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 transferable deposits). At the end of December 2020, as a consequence of the higher increase of deposits compared to the increasing trend of loans, loans to deposits ratio declined at 74.5% from 77.6% as it was in December 2019.

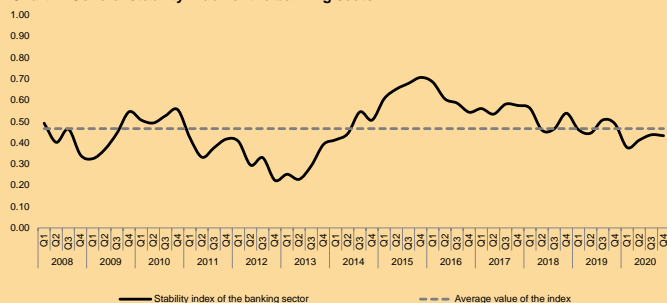
⁵ An exception is the distribution of the dividend of EUR 3.7 million by one of the banks, assets which were invested in other capital instruments out of the banking sector.

Box 1. Stability index of the banking sector

Banking sector, before the outbreak of Covid-19 pandemic, operated in an environment with low risks level. The spread of Covid-19 pandemic, as of the second half of March, and the containment measures taken continuously, have had an impact on the increase of risks to which the banking sector is exposed. In this box will be elaborated the effect of Covid-19 pandemic on the indicators with high frequency of the banking sector, summarized in the Stability Index of the Banking Sector.

The stability index of the banking sector is constructed to measure and assess the internal soundness of the banking sector which reflect the stability of the banking sector. The index has been constructed on the base of the financial indicators of the banking sector, taking the values ranging from 0 to 1, where the higher values represent a risk in decline and vice versa.⁶ The index has been calculated on quarterly basis in order to assess the increase or the decline of the risk sensitivity through this index.

Chart 1. General stability index of the banking sector



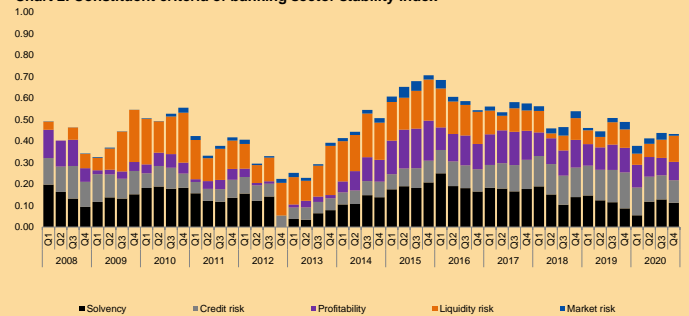
Source: CBK (2021)

Based on the general aggregated index of the sector's stability, at an average, it was marked an increase of

the risk sensitivity (read: a decline of the index) in Q4 2020 compared to Q4 2019. The overall value of the index, if it is compared to the same quarters of the previous years, it is held at the lowest level (0.43) since Q4 2013 (chart 1).

Compared to the same quarter of the previous year, a decline of the index (read: an increase of risk sensitivity) was marked by: credit risk indicator, profitability and the market. Whereas, an increase of index (a decline of risk sensitivity) was marked by the risk indicator of solvency and liquidity. It is worth mentioning that the indicator that measures the market risk, has quite low weight to the overall index, and the increase of this indicator does not present risk for the banking sector, as a result of the low level of assets held in foreign currency (chart 2).

Chart 2. Constituent criteria of banking sector stability index



Source: CBK (2021)

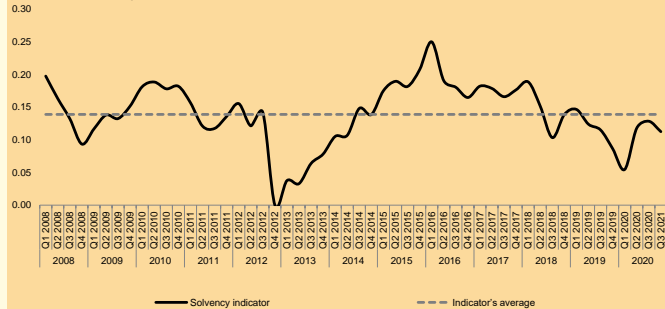
The decline of sensitivity to solvency risk, at the end of Q4 2020, compared to the statement marked in Q4 2019, is attributable to the increase of the capitalization level of the sector. The increase of the capital level has influenced the faster growth of regulatory capital against the slower growth of risk-bearing assets. The increase of the capital level is a result of the retained earnings during this period as

⁶ For further details on the methodology of construction of the stability index of the banking sector, please refer to the Financial Stability Report no. 9.

well as the profit realized until December 2020. Whereas, the slowdown increase of risk-bearing assets is a result of the slowdown of lending growth activity since the beginning of the pandemic compared to the performance of recent years (double-digit increase in the previous three years).

The increase of sensitivity to liquidity risk, in Q4 2020, compared to the level marked in the same period of the previous year, mainly is attributable to the higher increase of liquid assets compared to the slower growth of the short-term liabilities. Cash and assets held at the CBK by commercial banks marked higher growth compared to December of the previous year. This increase of liquid assets among others reflects the beginning of the withdrawal of 10% of pension savings by the citizens within the economic recovery package by the end of December 2020.

Chart 3. Solvency indicator



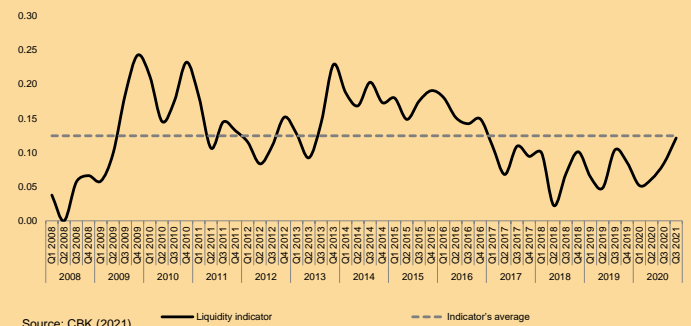
Source: CBK (2021)

Conversely, short-term liabilities marked a slower increase against the liquid assets, which mainly consist of deposits within a one year of maturity.

The increase in credit risk sensitivity came as a result of the increase of nonperforming loans in absolute value and as a ratio to total loans. The declining trend of nonperforming loans was interrupted for the first time in Q1 2020, since Q4 2014 when it had began to decrease, which among others

was affected by the methodological change with the beginning of the implementation of SNFR 9 standards.

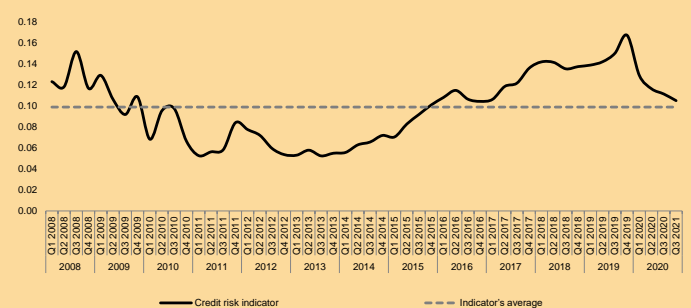
Chart 4. Liquidity indicator



Source: CBK (2021)

NPL level is expected to increase in the following period as well, where Kosovo's economy was impacted also by the Covid-19 pandemic. The increase of the sensitivity to credit risk was also influenced by the increase of the level of large credit exposures to Tier 1 capital compared to the previous period (Q3 2019).

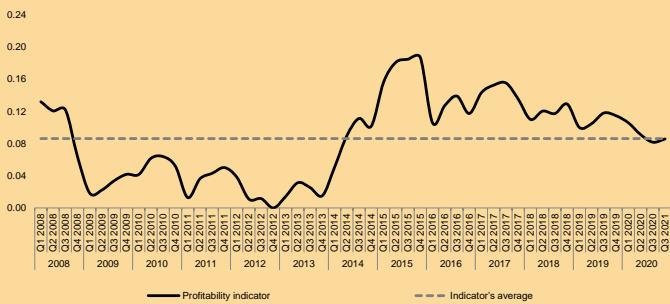
Chart 5. Credit risk indicator



Source: CBK (2021)

The increase of sensitivity to profitability risk, mainly may be attributable to the higher level of expenditures incurred in 2020, which primarily reflects the increase of expenditures for provisions on possible loan losses. The income of the sector marked an increase against the previous year, albeit were not able to maintain the profit level realized in 2019. Consequently, the lower profit has had an impact on the decline of the profitability indicators such as Return on Average Equity (ROAE), and on the expenditures to income ratio.

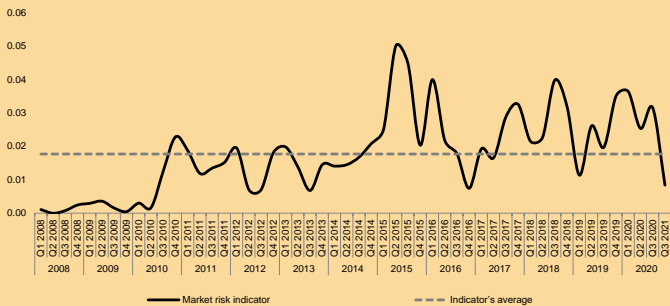
Chart 6. Profitability indicator



Source: CBK (2021)

The increase of the market risk sensitivity was mainly attributable to the growth of net position in foreign currency of the banking sector. This indicator has the lowest weight in the overall financial stability index as only 5% of assets and around 4% of liabilities are in foreign currency. Moreover, also the level of loans and deposits in foreign currency is at a quite low level. As a consequence, movements of this indicator have quite low impact in the aggregated index of the financial stability.

Chart 7. Market risk indicator



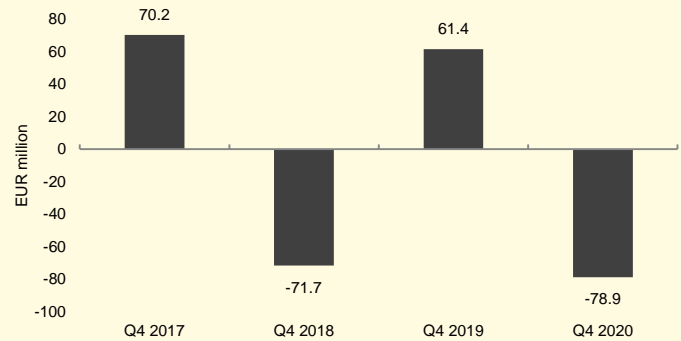
Source: CBK (2021)

Pension sector

The pension sector was characterized with a contraction of assets in Q4 2020 as a result of the withdrawal of 10% of pension savings at the end of the year, a dynamic which was neutralized to some extent from the collected contributions and positive return on investments.

Pension sector, as the second sector by importance of weight in the financial sector, comprises 25.3% of total assets of the financial system. As a consequence of the 10% withdrawal of assets by the contributors, total assets of the pension sector marked an annual increase of only 1.2%, in December 2020, reaching the value of EUR 2.0 billion. On quarterly basis, only in Q4 2020, pension sector assets increased by EUR 78.9 million (a growth of EUR 61.4 million in Q4 2019) (chart 20).

Chart 20. Assets of the pension sector, quarterly changes



Source: CBK (2021)

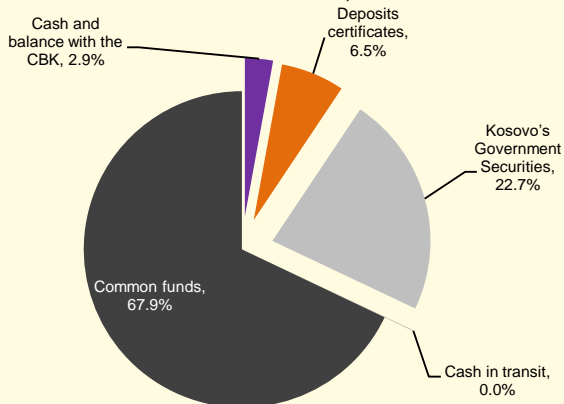
Assets of the pension sector consist of 99.6% of assets which belong to Kosovo Pension Saving Trust (KPST) and 0.4% of assets of Slovenian-Kosovo Pension Fund (SKPF).

Assets structure of KPST is mainly comprised of assets invested abroad, albeit its weight considerably marked a decline compared to the previous period. Around 68.0% of KPST assets are held abroad, or about EUR 1.35 billion allocated in common investment funds (chart 21).

The remainder of assets invested in the domestic economy (32.0%) increased by 7.2 percentage points compared to the same quarter of the previous year.

Until the end of September 2020, the value of investments in the country reached EUR 637.7 million.

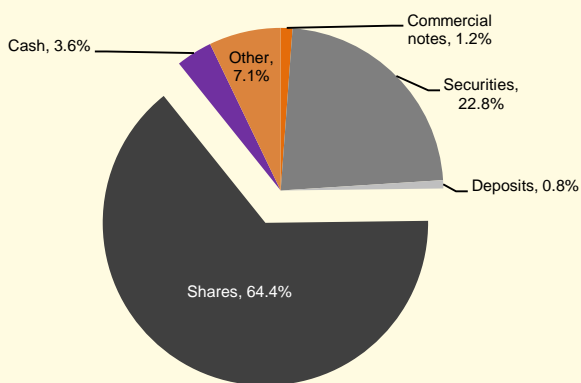
Chart 21. Structure of KPST assets, Q4 2020



Source: KPSF (2021)

The largest portion of these assets are invested on bonds and treasury bills of Kosovo's Government, which only in Q4 2020 marked an increase of EUR 18.5 million. The category of assets deposited in the banking sector shrank by EUR 54.5 million in this quarter, which among others reflects the 10% withdrawal of pension saving trust by the contributors. Whereas, cash held at the Central Bank of Kosovo marked an increase of EUR 12.2 million in Q4 2020.

Chart 22. Structure of SKPF assets, Q4 2020

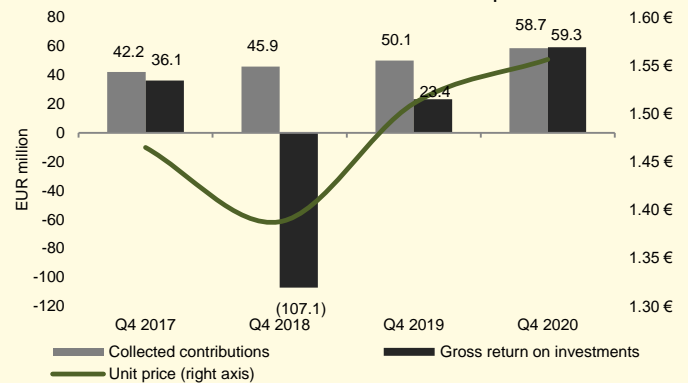


Source: SKPF (2021)

Assets structure of SKPF is mainly comprised of shares invested abroad (64.4%), treasury bonds of foreign

governments and of Kosovo's Government (22.8%) and other assets (chart 22). Total assets of SKPF increased by EUR 352.9 thousands in Q4 2020, of which the majority were invested in the domestic sector.

Chart 23. Return on investments and KPST performance



Source: KPSF (2021)

During Q2 and Q3 2020, SKPF marked a significant recovery from losses from investments recorded in Q1 2020 (EUR -910.0 thousands). Whereas, by the end of December 2020, the sector was able to realize gross return on investments with a value of EUR 388.8 thousands. Only during Q4 2020, the sector realized a gross profit from investments with a value of EUR 449.8 thousands (EUR 269.0 thousands in Q4 2019). Whereas, the value of new collections of contributors amounted to EUR 162.0 thousands in Q4 2020 (EUR 153.0 thousands in Q4 2019).

In this quarter, contributions collected by KPST increased by EUR 58.7 million, representing an increase of 17.1%, compared to the same period of the previous year. 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 only in Q2 2020, and EUR 32.7 million in Q3 and EUR 59.3 million in Q4. Therefore,

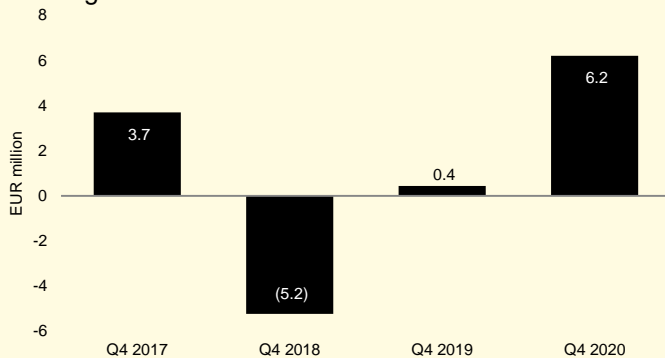
KPST closed the year 2020 with a considerable positive result, namely with a gross return on investments with a value of EUR 71.9 million.

Insurance sector

The insurance sector was characterized by an increase of assets during Q4 2020, higher level of written premiums and the decrease of the level of claims paid compared to Q4 2019.

Assets of insurance sector by the end of December 2020, reached the value of EUR 220.5 million, representing an annual growth of 12.2%. Deposits held at commercial banks and as investments in of Kosovo's Government securities were the items with the highest growth. Only in Q4 2020, assets of the insurance sector increased by EUR 6.2 million (chart 24). Also on a quarterly basis, the increase was mainly reflected in deposits held at commercial banks, followed by investments in Kosovo's Government securities, borrowings and receivables, as well as the category of re-insurer for technical reserves.

Chart 24. Assets of the insurance sector, quarterly change



Source: CBK (2021)

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 2.4 million, thus reaching the value of EUR 59.7 million as at end of period (December 2020). This capital increase came as a result of the growth of the paid shareholders capital and the category of revaluation reserves. Whereas, the realized losses and those retained from the previous years (especially in 2016) prevented a further increase of the capital of the sector in the reporting period.

Also liabilities of the sector marked an increase during this period (EUR +3.8 million), which mainly consist of technical reserves. The value of total liabilities, by end-December 2020, amounted to EUR 160.7 million.

The value of gross written premiums of insurance companies, in Q4 2020, amounted to EUR 27.0 million, representing an annual growth of 7.0% (an annual growth of 9.7% in Q4 2019) (chart 25). "Non-life" premiums account for 96.6% of total written premium, whereas "life" premiums comprise 3.4%. The slowdown increase of written premiums, to some extent, reflects the effect of the Covid-19 pandemic on the economy. During Q4 2020, the number of sold non-life policies was 256.8 thousands, compared to 286.8 thousands sold in Q4 2019.

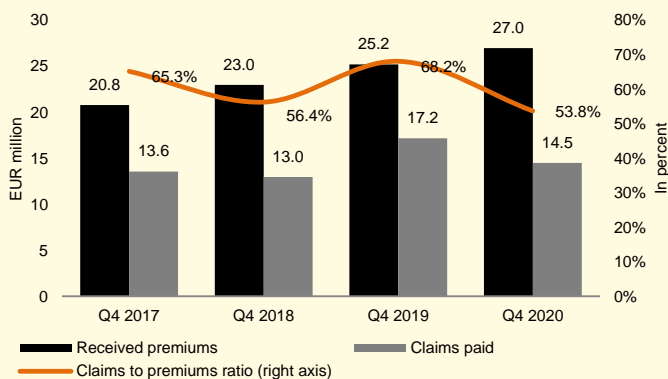
The value of claims paid by the insurance sector (including Kosovo Insurance Bureau) marked a decline in Q4 2020 against the same period of the previous year. In Q4 2020, claims paid marked a value of EUR 14.5 million (EUR 17.2 million in Q4 2019) (chart 25). As a consequence of the increased level of written premiums against the decline of the level of the claims paid, the level of claims to premiums ratio, in Q4 2020,

marked an improvement, thus declining for 14.4 percentage points, standing at 53.8% (chart 25).

Performance of the insurance sector

During Q4 2020, insurance sector performed with a net loss of EUR 820.8 thousands (a loss of EUR 4.5 million in Q4 2019).

Chart 25. Written premiums and claims paid



Source: CBK (2021)

The significant reduction of losses compared to the previous period is a result of the level decline of claims paid and operating expenses. Conversely, also the increased level of written premiums has had an impact on the significant decline of financial negative results compared to the previous period.

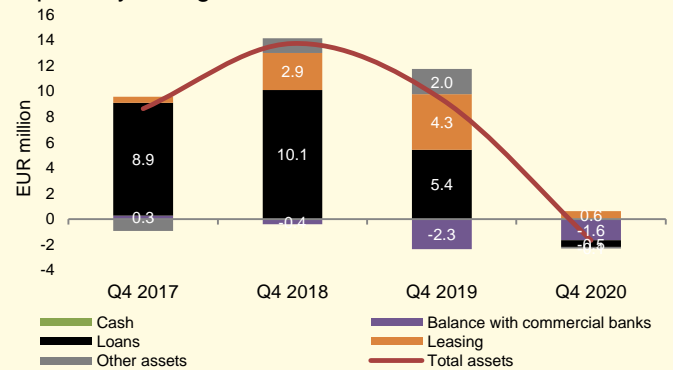
Microfinance sector

Microfinance sector has marked a contraction of its activity in Q4 2020 against the same period of the previous year. However, the sector's performance marked an increase, as a result of the higher decline of expenditures compared to the decline of income. Loans portfolio quality remains high, albeit with a declining trend.

Assets

After four years of a notable expansion of the activity, in December of this year it was marked a slowdown of activity increase of microfinance institutions and non-bank financial institutions.

Chart 26. Assets of the microfinance sector, quarterly change



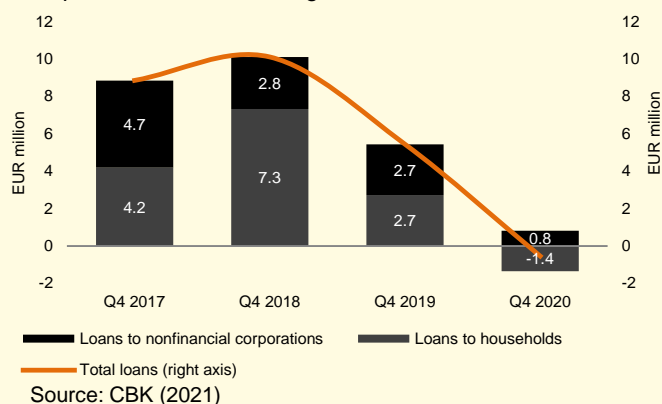
Source: CBK (2021)

The value of assets reached EUR 316.2 million, representing an annual increase of 2.1% (an annual growth of 23.9% in December 2019).

On quarterly basis, assets contracted for EUR 1.7 million, during Q4 2020, compared to the increase of EUR 9.4 million in the same period of the previous year.

The contraction of the sector's activity marked in Q4 2020, was mainly attributable to consequences of Covid-19 pandemic caused to the domestic economy, reflected at lower level on the borrowings issued by external sector. Lending activity was characterized with a decline, while leasing slowed down significantly the increasing trend (chart 26). Also, to the contraction of the sector's activity had an impact the process of expelling from balance items of two institutions which were being revoked the licenses at the end of 2019.

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



Loans

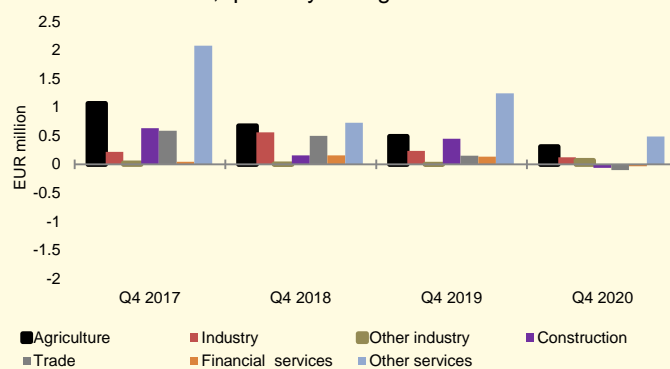
On annual basis, total loans marked a decline of 6.8% by the end of December 2020, while their stock dropped to the value of EUR 205.0 million. Compared to the previous period, loans marked a significant contraction in both categories of nonfinancial corporations and households. Lending to households marked a decline of 9.2% (an annual growth of 21.9% by December 2019), thus reducing the amount at EUR 134.4 million at the end of December 2020. Total loans value, on quarterly basis, decreased by EUR 0.5 million in Q4 2020, compared to the increase of EUR 5.4 million that had been marked in Q4 2019. Only in Q4 2020, loans to households marked a decrease of EUR 1.4 million (chart 27).

Loans stock to nonfinancial corporations declined at the value of EUR 70.6 million at the end of December 2020, representing an annual decline of 1.9% (an annual growth of 15.3% until December 2019). On quarterly basis, during Q4 2020, loans to nonfinancial corporations increased by EUR 0.8 million.

On sectoral terms, on quarterly basis, lending to agriculture sector and other services was characterized

with an increase, albeit at lower level compared to previous period. Whereas, lending to construction and trade sector was characterized with a decline in Q4 2020 (chart 28).

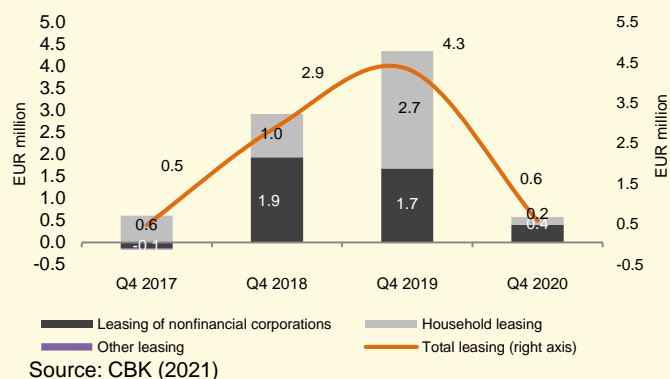
Chart 28. Value of loans to nonfinancial corporations, by economic sectors, quarterly changes



Leasing

In contrast to the developments in lending, microfinance institutions maintained, to some extent, the increasing trend of leasing activity during this period.

Chart 29. Value of microfinance sector leasing



The activity of leasing of the microfinance sector marked an increase with a value EUR 0.6 million during Q4 2020 (EUR 4.3 million in Q4 2019), reaching the value of EUR 57.3 million at the end of the period.

This increase mainly reflects the leasing to nonfinancial corporations, the value of which increased by EUR 0.4 million during this quarter, reaching the value of EUR 31.4 million at the end of the period (chart 29).

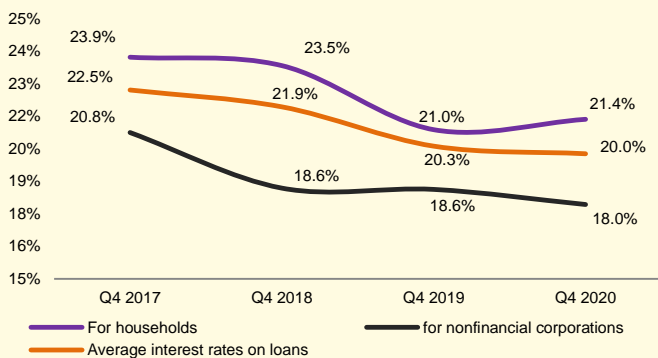
Similarly, also leasing to households increased by EUR 0.2 million in Q4 2020, reaching the total value of EUR 25.9 million at the end of the mentioned period.

Interest rates

During the fourth quarter of 2020, the average interest rate on loans was 20.0%, or for 0.3 percentage points lower compared to the same period of the previous year (chart 30).

The average interest rate on loans to households marked a marginal increase of 0.4 percentage points, reaching 21.4% during Q4 2020 (chart 30). By loan categories, the average interest rate on mortgage loans decreased by 2.5 percentage points falling at 18.4% in Q4 2020. Whereas, mortgage loans were characterized with an increase of 0.9 percentage points, reaching 22.1%.

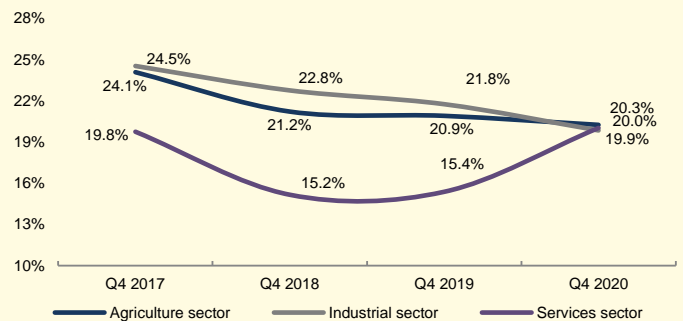
Chart 30. Average interest rates on microfinance sector loans



Source: CBK (2021)

Unlike households, the interest rate on loans to nonfinancial corporations the interest rate on loans decreased slightly for 0.6 percentage points, falling at 18.0%. On sectoral terms, a more favorable interest rate was marked for loans to industry, followed to services and agriculture. The quarterly average interest rate on loans to agriculture and industry marked an annual decline for 1.9 and 0.7 percentage points, respectively. However, the most significant increase was marked by interest rates on loans to services sector, which historically had more favorable conditions for loans, reaching 20.0% during Q4 2020 (an increase of 4.7 percentage points compared to Q4 2019) (chart 31).

Chart 31. Average interest rates on loans to enterprises, by economic sectors



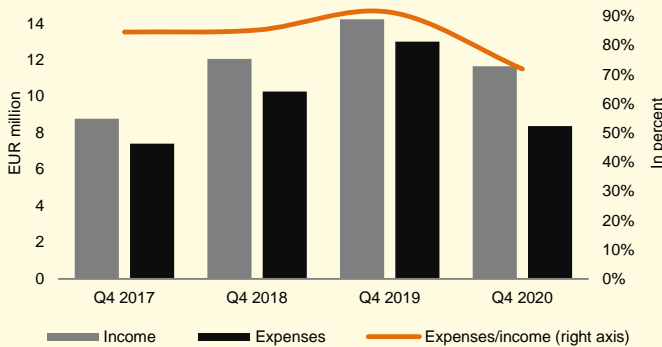
Source: CBK (2021)

Performance of the microfinance sector

Microfinance sector recorded a profit of EUR 0.3 million in 2020, which significantly is lower compared to the profit of EUR 9.3 million marked in the previous year. This contraction was a result of a more accelerated decline of expenditures against the decrease of income. Whereas, concerning the quarterly performance, in Q4 2020, the sector realized a profit

with a significantly higher value compared to the same period of the previous year, as a result of the higher decline of expenditures against income. During this quarter, income of the sector amounted to EUR 11.7 million, representing a decline of EUR 2.6 million compared to the same quarter of the previous year. This decline came as a result of the decrease of interest income of EUR 2.7 million, falling at EUR 10.6 million during Q4 2020 (chart 32). Non-interest income increased by EUR 0.1 million during this quarter, reaching the value of EUR 1.0 million, which primarily reflects the trend of income from services.

Chart 32. Microfinance sector income and expenses



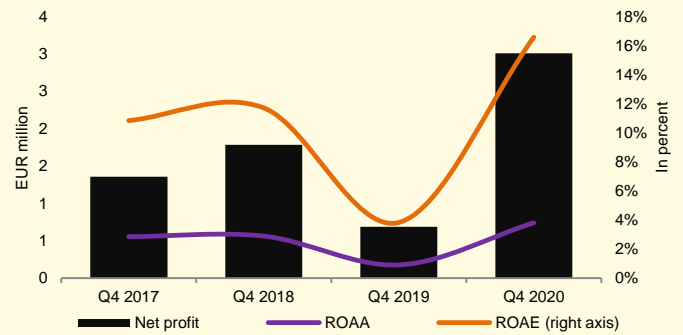
Source: CBK (2021)

Expenditures of the sector marked the value of EUR 8.7 million in Q4 2020, representing a value which is lower for EUR 4.9 million compared to the same quarter of the previous year. The decline of expenditures mainly reflects the decrease of operating expenses and non-interest expenses (loan loss provisions).

Expenses-to-income ratio, as an indicator of the sector's performance, marked a decline of 19.5 percentage points compared to the previous period, standing at the level of 71.9% in Q4 2020. This implies that for every EUR 1 invested, the microfinance sector spends around

EUR 0.719. The higher decline of expenditures against income has affected the significant increase of the net profit compared to the previous period, marking an amount of EUR 3.0 million during Q4 2020 (chart 33).

Chart 33. Profitability indicators of microfinance sector

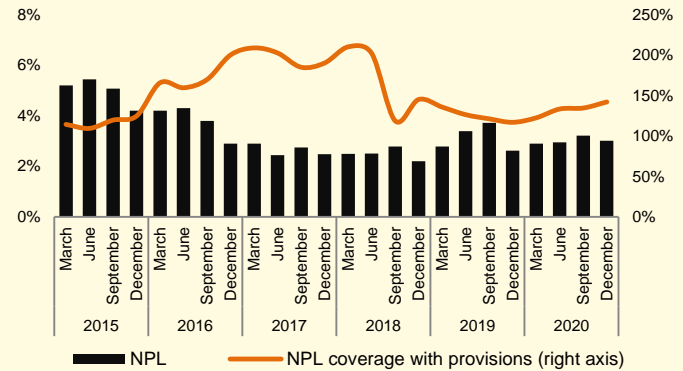


*Profit was annualized for the respective quarter

Source: CBK (2021)

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 marked an increase compared to Q4 2019 (chart 33).

Chart 34. Indicators of loans portfolio quality



Source: CBK (2021)

Regarding the indicators of loans portfolio quality in microfinance institutions, nonperforming loans continued to stand at low levels and were characterized with good coverage with provisions. Until the end of the

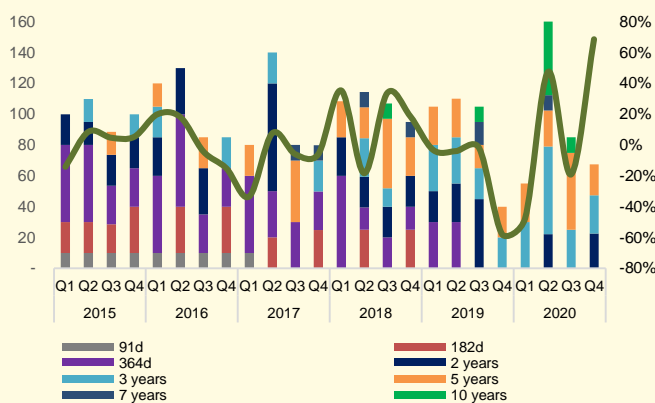
period, nonperforming loans stood at 3.0%, while the NPL coverage with provisions reached 142.2% by the end of Q4 2020 (chart 34).

Securities market

During the fourth quarter of 2020, Kosovo’s Government issued debt with a significant higher value compared to the same quarter of the previous year. This level decline of sovereign debt reflects the higher need for being financed by the Kosovo’s Government due to the decline of sources of income and the increase of expenditures, as a result of the circumstances caused by Covid-19.

The debt issued by Kosovo’s Government marked an annual growth of 68.8% in Q4 2020, compared to Q4 2019, reaching the value of EUR 67.5 million (chart 35).

Chart 35. Amount of issued debt, annual increase

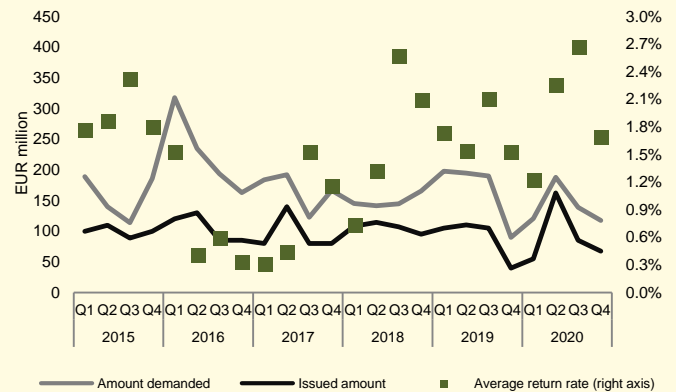


Source: Ministry of Finance (2021)

The demand to invest in Kosovo’s Government securities continued to exceed the offer, which was for 1.74 times higher than the demanded amount, albeit compared to the previous year, it stood at lower levels. The average interest rate on securities was 1.7% in Q4 2020, representing a higher rate for 0.2 percentage points than in Q4 2019 (chart 36). The increase of

interest rate compared to the previous period reflects the trend of securities issuance towards long-term maturities. The securities structure is dominated by government bonds, with a maturity of 3 years, followed by securities with a 2-year maturity.

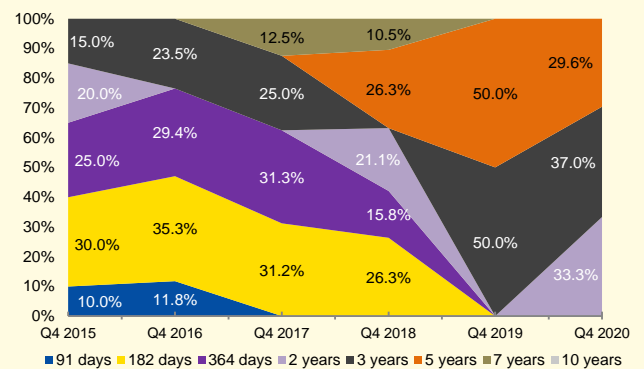
Chart 36. Bid to cover ratio



Source: Ministry of Finance (2021)

It is worth noting that for the second consecutive year, there is no issuance of treasury bills, whose longest maturity does not exceed 364 days (chart 37).

Chart 37. Government securities structure, in percent



Source: Ministry of Finance (2021)

The banking sector, pension funds and insurance companies continued to represent the investment institutions in the primary market of Kosovo’s Government securities, where the pension sector continues to be the most exposed sector.

The suggested citation of this publication:

CBK (2021): Quarterly Assessment of Financial System No. 33 Q4 2020, Central Bank of the Republic of Kosovo, Prishtina

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Macroeconomic selected indicators

Description	December 2019	December 2020
Real sector 1/		
Gross Domestic Product (GDP) (in millions of EUR)*	5,212.7	4,902.3
Consumer prices (annual average)	2.7%	0.2%
Consumer prices (end of period)	1.1%	0.1%
Fiscal Sector 2/		
Budget Revenues (in millions of EUR)	1,888.2	1,721.2
Budget Expenditures (in millions of EUR)	2,070.0	2,205.2
Primary balance (in millions of EUR)	-181.8	-484.1
Financial sector (in millions of EUR) 3/		
Assets of financial corporations	7,259.9	7,907.8
of which : Banks	4,760.5	5,353.1
Loans	3,031.9	3,246.4
Deposits	3,908.1	4,358.8
<i>Interest Rate s on Loans, end of period</i>	6.4%	6.0%
<i>Interest Rate s on Loans, end of period</i>	1.6%	1.5%
Interest rate gap	4.8%	4.5%
External sector,(in millions of EUR) 3/		
Balance of payments		
Current accounts	-399.5	-429.4
of which: remittances	851.7	980.1
Financial account	-163.0	-502.2
Foreign Direct Investmentsin Kosovo	254.6	321.7
Portfolio investments, net	59.0	-81.6
Other investments, net	-128.8	-195.3
International Investment Position (PNI), net*	-304.6	-773.6
Assets	5,185.2	5,198.6
Liabilities	5,489.8	5,972.2
External debt, total*	2,160.9	2,381.1
Private external debt	1,662.1	1,883.7
Public external debt	498.8	497.4

Source:

1/ KAS (2020);

2/ MF (2020);

3/ CBK (2020).

*Data on IIP and external debt are as of September 2020.

