

Summary

- **The euro area economy** recorded a real growth of 0.3% in the second quarter of 2023, according to Eurostat, representing a slow growth that was mainly attributed to the high inflation rate, the decline in industrial activity and the tightening of monetary policies. The inflation rate in Q2 2023 continued the growth trend, reaching 6.2%, prompting the ECB to increase the key interest rate for the fifth time within 2023. The inflation rate for 2022 was 8.4%, while the ECB projections suggest a slowdown in inflation dropping to 5.4% in 2023 and 3.0% in 2024.
- **In Q2 2023, economic activity slowed down compared to the same period of the previous year.** Estimates of KAS suggest that Kosovo's economy marked an economic growth of 2.0%, in Q2 2023, mainly as a result of the deficit increase of net exports. The increase of trade deficit was mainly a result of the increase of goods and services import growth, while the export of goods and services marked a slowdown increase. Conversely, consumption has marked a higher increase, as a result of the increase of financing sources and the slowdown increase of consumer prices. Also, investments are estimated to have marked a higher increase compared to the previous quarter, mainly as a result of the increase of public investments and new investment loans. For the second half of 2023, the economic activity is expected to be supported by overall investments, public consumption and export of services, while a negative impact is expected to have export of goods.
- **Kosovo's budget has recorded a positive primary budget balance in Q2 2023**, as a result of the higher growth of budget revenues, while public debt has declined to 17.3% of the GDP, compared to the level of 20.8%, marked in Q2 2022. The improvement of the government's budget balance and the increase in nominal GDP, which reduces the debt to GDP ratio, have been the main factors which influenced the decrease of the level of public debt.
- Inflationary pressures continued to ease in Q2 2023 with the headline inflation decelerating as a result of the impact of the base, easing supply chains and commodity prices in international markets. A slow growth was observed in most of the components in the consumer's basket, while energy prices were characterized with a decline. Similarly, also the core inflation exerted signs of a slowdown pace in Q2 2023.
- Current account recorded a negative balance of EUR 328.0 million in Q2 2023, a dynamic which was mainly determined by developments in trade balance of goods. The balance of goods marked a trade deficit, mainly being impacted the high value of the import of goods. On the other hand, the balance of services, primary income and secondary income had an impact on the contraction of the negative balance of the current account. Within the current account, one of the most important financing sources of consumption, comprised of remittances, recorded an increase of 15.8%, reaching EUR 363.8 million.
- **Despite the challenges from the higher risks with which the economy was facing, such as increased inflation and the weaker economic outlook, the financial system in the country expanded with an accelerated pace.** Banking sector and the overall financial system is exposed to external risks as a result of geopolitical tensions in Southern Europe, whereas inflation remains the main risk.
 - Over the years, the **banking sector** has managed to ensure a high level of capitalization and liquidity, as well as to maintain a low level of nonperforming loans. The satisfactory state of these indicators gives priority to the sector in absorbing shocks from uncertainties caused by geopolitical crises, the increase of inflation and the slowdown of economic activity. In Q2 2023, lending activity was the main contributor to the increase in assets of the financial system, followed by investments in securities and deposits held in other banks (mainly as deposits held at banks abroad). Tightening of monetary policies since the previous year was reflected in an increase of interest rates in loans and deposits also in the domestic market. The increase of interest rates on deposits has had an impact on the increase of deposited assets, where the increase rate reached a record level marked in the last 14 years, for all the segments (household deposits, nonfinancial corporations and other financial corporation deposits).
 - **Pension sector** marked a recovery of the increasing pace, reaching the level marked prior to pandemics, after a pronounced slowdown (especially in the previous year), as a consequence of significant fluctuations in international financial markets after the deterioration of the situation in the Southern Europe. Whereas, until June 2023, pension sector marked a positive return on investments and an increase in the collected contributions. After turbulences caused in financial markets in the first quarter of the year, in the period of April-June 2023, financial markets had a better performance, which was reflected also in the gross return on investments of pension funds in Kosovo.
 - **Insurance sector** was characterized with an accelerated increase of assets compared to the previous year, being affected by the high level of collected premiums. Claims paid during this period were higher compared to the previous year, albeit the significant increase of received premiums has had an impact on the sector to further improve its financial position compared to the previous year statement.
 - **Microfinance sector** was characterized with an accelerated increase of assets, mainly being attributable to the increase of lending activity and to a lower level the increase of leasing, which primarily were financed by loans from the external sector (credit lines) shareholders capital. Financial soundness indicators show as well a stability of the sector in general, while the financial result turns out to have maintained almost the same level as in the previous year.

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Euro area and Western Balkans

Euro area economy marked a real growth of 0.3% in the second quarter of 2023, according to Eurostat. The slowdown increase was influenced by the still high rate of inflation, the decline of industry activity and the tightening of monetary policies by the ECB. The euro area economy was significantly impacted by the increase of consumer prices and the cost of financing. The tightening of monetary policy by the European Central Bank (ECB), the fastest in more than two decades, has affected the level of confidence in businesses and consumers and the weakening of investments sentiment. ECB projections for economic growth in the euro area were revised in June, against the projections of March, to 0.9% for 2023 and 1.5% for 2024.

The inflation rate, in Q2 2023, reached 6.2% (8.0% in Q2 2022), mainly influenced by the increase in food prices. In August 2023, for the fifth time within the year, the ECB proceeded with the increase of three key interest rates: the interest rate on deposits (to 3.75% in August 2023), the rate on refinancing the operations (4.25%) and the marginal lending rate (4.50%). The ECB projections suggest a slowdown in inflation to 5.4% in 2023 and 3.0% in 2024.

In the absence of data for Q2 2023 from the statistics agencies of the Western Balkan countries, the IMF projections suggest that the region is expected to record an average economic growth of 2.1% in 2023 and 3.2% in 2024. Slowed growth in the Western Balkans was estimated to have been affected both by external pressures (slowing down economic growth in the euro area and the increase of prices in international markets), and by internal effects such as dealing with inflation and increasing the cost of financing. The still high prices of energy and food, increased inflationary pressures in all countries of the region, lowering purchasing power, consumer spending and slowing down the overall demand. **The average inflation rate, in Q2 2023, in the countries of the region turns out to have been 8.2%, with the highest rate recorded in Serbia of 14.5% and in the North Macedonia of 11.2%, while Kosovo recorded the lowest inflation rate of 4.2%.** In an effort to combat the inflation hikes, Central Banks in the region countries (the countries which have their own currencies) have continued to increase the key interest rate, also during 2023.

In Q2 2023, the currency exchange market of the EUR against the currencies of the trading partners, namely US dollar and Turkish lira, marked an appreciation. The value of EUR currency remained almost the same against the Serbian dinar and Macedonian denar, whereas it was depreciated against the Albanian lek and British pound.

Main commodity prices in international markets

Main commodity prices in international markets continued to ease in Q2 2023, as a result of, among other things, the growing concerns about a slowdown in global demand following the tightening of monetary policies, the reduction of bottlenecks in supply chains, and the re-arrangement of global trade connections after the start of the war in Ukraine. However, prices of goods still remain high and continue to reflect the high prices of consumption.

Prices of Brent crude oil, according to the World Bank, reached an average of \$78.2 per barrel in Q2 2023, marking a decline of 30.6% compared to the same period of the previous year (\$112.7 per barrel, in Q2 2022) (chart 1). Whereas, compared to the previous quarter, oil prices declined by 3.9% (\$81.4 per barrel in Q1 2023). However, the trajectory of oil prices was volatile throughout the second quarter, where the dynamics were driven by the drop-in demand for oil and reduction in the global supply. However, given the expectations of a slowdown in global demand throughout 2023 and the impact on oil prices, OPEC+ announced a reduction in oil production of 1.7 million barrels per day, from May to the end of 2023, which affected the rise of oil prices to \$84.1 per barrel in April 2023. However, the slowdown of the global demand and the increase of uncertainties in the financial system in USA affected the oil price to decline at an average of \$75 per barrel, in May and June 2023. Meanwhile, growing concerns about shrinking the global oil supply after Saudi Arabia's announcement

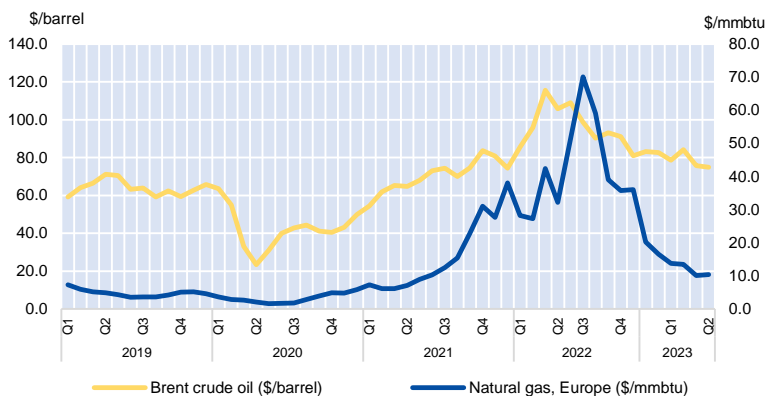
of extending production cuts of 1 million barrels per day throughout August, had an impact on the increase of oil prices up to \$80.1 per barrel in July.

Natural gas prices in Europe continued to show a downward trend marking a decrease of 32.8% compared to the previous quarter, supported by mild climatic conditions that influenced the reduction of natural gas consumption for heating, the import of liquefied natural gas from the USA that softened concerns about securing the supply, as well as measures taken by the EU to increase efficiency and save energy. Also, natural gas prices marked a decline of 64.2% compared to Q2 2022, when natural gas prices in Europe averaged \$31.6/mmbtu as a result of the war in Ukraine. The ease in natural gas prices also affected the drop in the price of coal and artificial fertilizer, which marked an average decline of 57.4% and 51.7%, respectively, in Q2 2023 compared to the same period of the previous year.

The price index of metals and minerals marked a decrease of 7.6% compared to the previous quarter when there was an increase in the prices of metals due to the reopening of China's economy and expectations of increased demand for metals, following China's supportive policies for the construction sector (chart 2). However, the demand for metals was focused on iron ore from China's steel sector, while prices of other metals continued to decline as economic growth turned out to be mainly driven by the services sector. Compared to the same quarter of the previous year, the metal price index recorded a decrease of 17.8%, which can be attributed to the slowdown in global economic growth and the deterioration of the economic outlook, as well as the improvement in supply after a drop in energy prices.

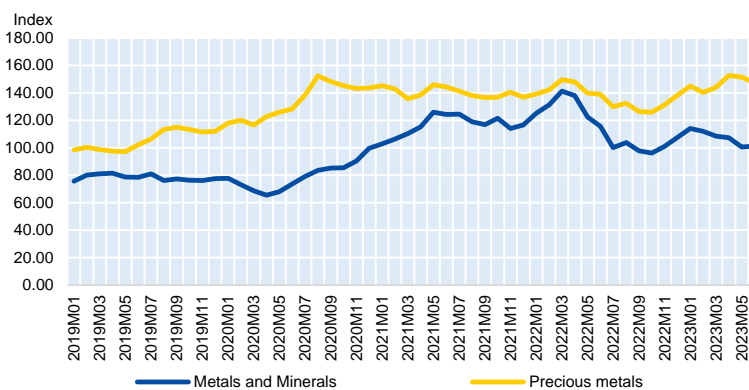
The price index of precious metals recorded an increase of 5.8% compared to the same quarter of the previous year. Silver and platinum prices recorded an annual growth of 6.9% and 7.1%, respectively, driven by increased industrial demand for these metals. Meanwhile, the price of gold recorded an annual increase of 5.8%, reaching the highest prices historically, in the months of April and May as a result of the challenges in the banking system in the

Chart 1. Oil and natural gas prices in international markets



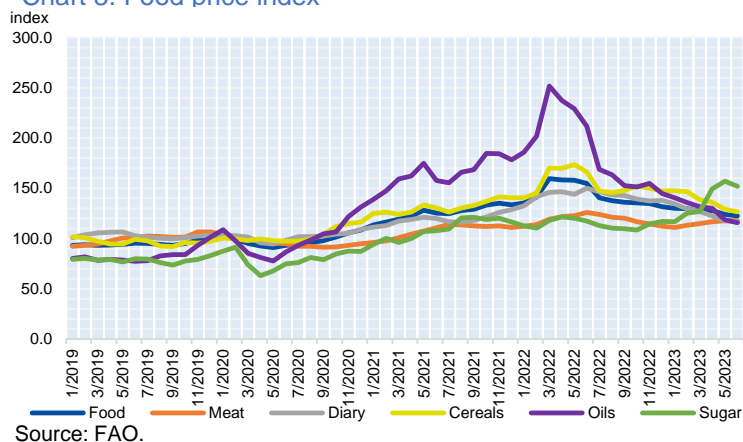
Source: World Bank

Chart 2. Prices of metals and minerals and of precious metals



Source: World Bank.

Chart 3. Food price index



Source: FAO.

US and the weakening of the US dollar. The increase in the prices of

precious metals was also evident against the previous quarter when the index of precious metals recorded an increase of 5.2%.

In Q1 2023, the food price index according to FAO marked a relatively slight decline of -3.3% compared to the previous quarter (chart 3). Whereas, compared to Q2 2022, food prices decreased by 20.6%, driven by the annual decline in the prices of cereals (-23.1%) and oils (-46.3%) as a result of the progress of the agreement between Russia and Ukraine for the export of cereals from Ukraine to international markets and increased yields of corn and wheat on the global level. Annual decline was also noted in the prices of dairy (-19.0%) and meat (-4.8%), while prices of sugar, after having reached the highest prices within the last 12 years, in May and June began to follow a downward trend as a result of improved harvest in Brazil and slowing the global demand for sugar. Despite this ease marked in Q2 2023, Russia's non-continuation of the agreement on the export of grains from Ukraine and the bombing of ports on the Black Sea and Danube in July 2023, affected the increase in the prices of grains and oils on international markets, while the ban of non-basmat rice exports from India had an impact on increasing the prices of rice in July, thus adding to inflationary pressures on food prices especially for emerging markets and developing economies.

Kosovo's Economy

Economic growth

Economic activity in Kosovo, according to Kosovo Agency of Statistics (KAS) estimates, marked a real growth of 2.0% in Q2 2023.

The slower growth of economic activity was attributed to the negative contribution of net exports of 2.5%, while consumption and investments contributed positively to real GDP growth by 3.8 and 0.7 percentage points, respectively (chart 4).

Consumption marked an increase of 3.7% in Q2 2023, representing a higher increase compared to the previous quarter and the same quarter of the previous year. The higher increase of consumption may be attributable to the increase of remittances, consumer credit, compensation of employees, public consumption, etc., but also to the slowdown increase of consumer prices. Investments increased by 2.0%, representing a higher increase compared to the previous quarters. The increase of overall investments was mainly a result of the increase of public investments but also of the investment loans. As regards to external trade, net exports have deepened the trade deficit for 6.7% in Q2 2023. The increase of trade deficit has come as a result of the increase of import of goods and services with 6.3%, while export of goods and services marked a slowdown increase of 5.9%.

The increase of the economic activity in Q2 2023 was mainly supported by the increase in the added value in the financial activities and insurance sector (3.7%), the sector of processing industry (3.4%), agriculture (2.8%), trade sector (2.4%), etc. Business turnover data confirm this increase, where the turnover in the trade sector has increased by 5.3%, while the sector of processing industry has increased by 2.1%, etc. The activity of the financial and insurance sector has marked a significant increase of 18.5%.

Economic activity was also reflected in the number of registered enterprises, which reached 3,086 enterprises in Q1 2023, namely 9.0% more compared to Q1 2022. Trade, manufacturing, construction, professional activities, hotels and other sectors, marked the highest number of registered enterprises. These

Chart 4. Real GDP growth rate and main contributors to the growth

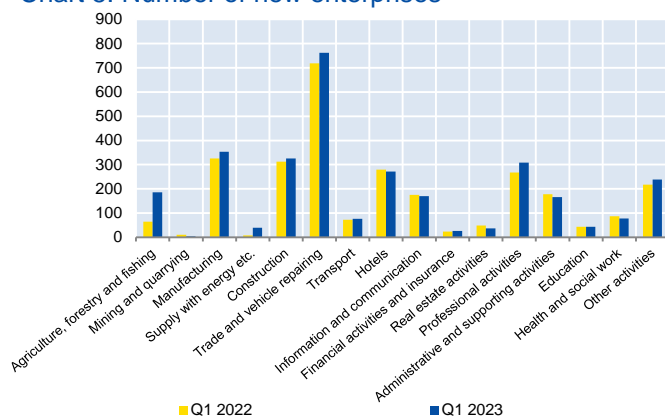


Source: KAS and CBK calculations.

sectors showed a significant increase in the number of enterprises compared to the same period of 2022 (chart 5). On the other hand, during Q1 2023, 446 enterprises were closed, representing a reduction of the number of enterprises of 9.9% compared to Q1 2022.

The CBK forecasts for the second half of 2023 suggest an increase of 3.7% in Q3, and an increase of 4.3% in Q4 2023. General investments, public consumption as well as the export of services, related to diaspora spendings, are expected to be the main drivers of the growth, while expectations for a decrease in the export of goods are expected to negatively affect the overall economic activity.

Chart 5. Number of new enterprises

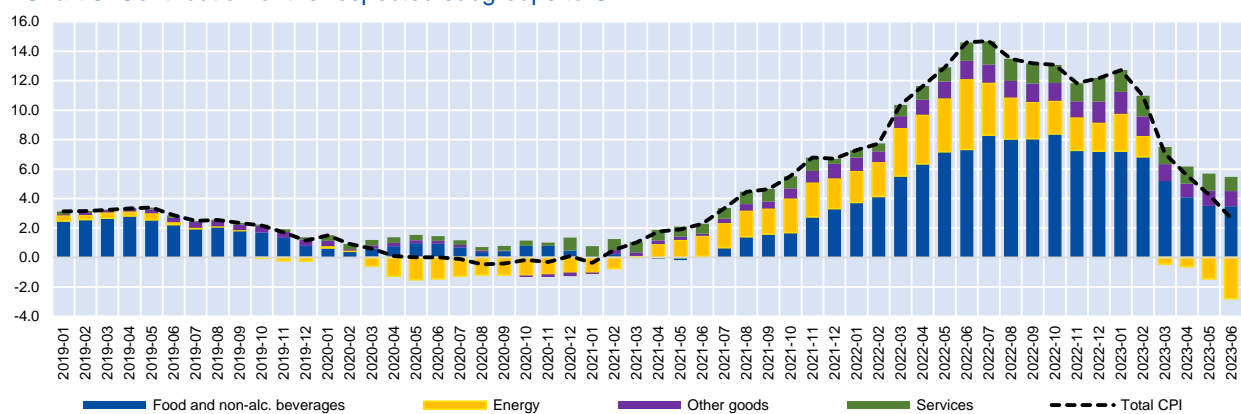


Source: KAS.

Prices

The average annual inflation rate, in Q2 2023, slowed down to 4.2% from 9.9% as it was in the previous quarter, as a result of the base effect and easing in supply chains and commodity prices in international markets. While there was evidence of slower growth in the prices of food, non-energy goods and services, the slowdown in inflation to 2.4% at the end of Q2 2023 was particularly influenced by the decline in energy prices, namely the decline of fuel prices.

Chart 6. Contribution of the respected subgroups to CPI



Source: KAS and CBK calculations.

Food prices marked an annual increase of 9.7% in Q2 2023, which represents a slowdown increase of prices of food against the annual increase of 17.6% marked in the previous quarter. The highest annual growth was recorded in the prices of vegetables (13.6%), food products (13.2%), milk, cheese and eggs (12.6%), sugar, jam, honey, chocolates and sweets (11.9%), bread and cereals (10.3%) and others, while there was a decrease in the prices of oils and fats of 9.7% (chart 6).

Prices of electricity and other fuels within the housing category recorded an average annual increase of 7.9% in Q2 2023, being slowed down compared to the previous quarter (12.8% in Q1 2023) as a result of the favorable climatic conditions and the slowdown in prices of energy in international markets. Prices of transport recorded an annual decline of 7.8% in Q2 2023, with the subcategory of operation of personal transport equipment which marked a decline of 17.5% against the increase of 3.3% in Q1 2023, as a result of the decline of fuel prices in international markets. As in the previous quarter, also in Q2 2023 the higher annual growth

within the transport category was recorded in the prices of services transport (11.4%), a category, which as well, marked a slowdown activity compared to the previous quarter (12.3%).

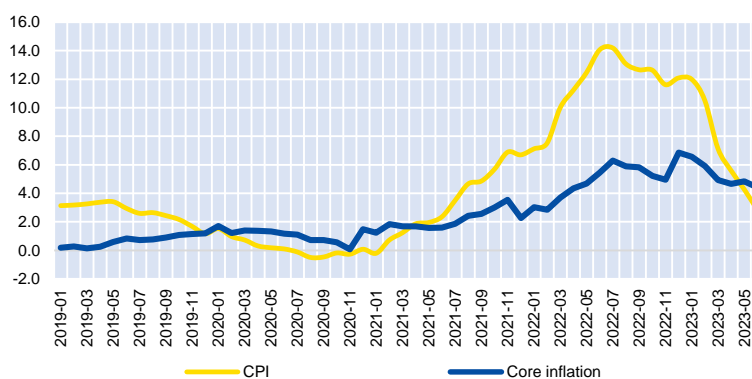
The contribution of food to the average inflation rate in Q2 2023 was 3.4 percentage points, with the highest contribution marked by the increase in the prices of milk, cheese and eggs with 1.0 percentage points, bread and cereals with 0.9 percentage points, meat with 0.7 percentage points, and others. Whereas, the contribution of transport to headline inflation in Q2 2023 dropped down by -1.5 percentage points (a decline of 1.1 percentage points, in Q1 2023), which was mainly defined by the subcategory of operation of personal transport equipment, where fuel is mostly included.

Whereas, the contribution of prices of other non-energy goods marked a decline of 0.3 percentage points reaching 1.0 percentage points in Q2 2023 compared to the previous quarter, mainly as a result of the slowdown of prices increase of alcoholic beverages and tobacco and the purchase of vehicles. Whereas, the average quarterly contribution of services to the total CPI decreased to 1.1 percentage points (from 1.4 percentage points in Q1 2023) after the slowdown in the price increase of hotel services, services for the usual maintenance of the house, transport services, and others.

Core inflation in Q2 2023 marked an annual increase of 4.6%, which compared to the previous quarter, represents a slowdown of 1.2 percentage points (chart 7). Primarily, the contribution to the increase of core inflation was marked by the category of 'furniture, household appliances and house maintenance' with 1.3 percentage points and by the category of 'transport services' with 1.0 percentage points. However, core inflation continued to follow a declining trend, albeit with a slowdown pace, thus being slowed down to 3.4% in July 2023.

The dependence of Kosovo's economy on the import of food commodities and energy, as well as the high degree of their share to the consumption basket, have had an impact on the inflation rate in Kosovo and is largely determined by the prices of imported goods. In Q2 2023, 3.0 percentage points of inflation in Kosovo was imported, while 1.2 percentage points was generated by internal inflationary pressures (chart 9). As a result of the continuous easing of prices of basic goods in international markets, imported inflation in Q2 2023 showed a slowdown pace compared to the previous quarter, which was consequently also reflected in the curbing of domestic inflation.

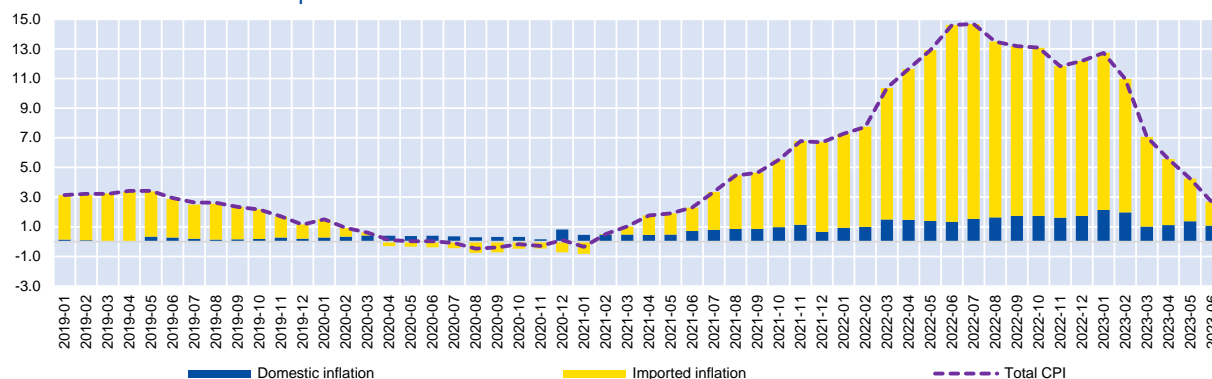
Chart 7. Core and headline inflation of consumption



Source: KAS and CBK calculations.

Fluctuations in the prices of basic goods in international markets, reflected in the prices of imported goods in Kosovo, are summarized through the import price index (IPI), which in Q2 2023 marked an annual increase of 5.0%, representing a slowdown increase against the annual growth of 8.6% marked in Q1 2023. Compared to the same quarter of the previous year, the categories with the highest weight within this index which include i) prepared food items, beverages and tobacco, and ii) machinery and electrical equipment recorded annual growth of 8.3% and 3.2%, respectively, while i) base metals and related articles and ii) mineral products, marked an annual decrease of 5.9% and 3.2%, respectively. Whereas, compared to the previous quarter, IPI recorded an increase of 1.1%, as a result of the continuous acceleration of the prices of i) plant products, ii) prepared food items, beverages and tobacco, iii) machinery and electrical equipment, iv) transport means, and others.

Chart 8. Domestic and imported inflation



Source: KAS and CBK calculations.

The producer price index (PPI) resulted in a decrease of 0.9% in Q2 2023 compared to the same quarter of the previous year as a result of the decrease in prices of i) extraction of iron ore (an annual decline of 14.9%), ii) production of electrical energy, gas, steam and air conditioning supply (-12.9%), iii) manufacturing of motor vehicles (-5.2%), metals (-4.5%), as well as the slowdown in the prices of other components with a significant weight in the PPI, such as the production of non-metallic mineral products, processing of food stuff, and the production of rubber and plastics products.

Compared to the previous quarter, CPI resulted in a decrease of 0.1% mainly due to the decrease in the prices of metal ore extraction, the price of processing food products, the production of beverages, the production of non-metallic mineral products, and others. Conversely, there was marked a monthly increase of 3.0% in the production of electrical energy, gas, steam and air conditioning supply.

The Construction Cost Index (CCI) recorded an annual increase of 1.0% in Q2 2023, driven by the increase in the prices of machinery (an annual increase of 8.2%), transport (3.5%), salaries (3.1%), and other costs (4.2%). On the other hand, compared to Q1 2023, a decrease in CCI of 0.1% was marked, mainly as a result of the decline in the prices of construction materials, as the component with the highest weight in CCI, and other costs, while an increase was noted in the prices of other materials, wages, machinery, transport, and energy.

Regarding the perspective of inflation in Kosovo, the CBK forecasts show that inflation in 2023 will slow down to 2.7%, and for the year of 2023 at 4.8%. Factors expected to contribute to these dynamics include the ongoing easing of supply chain constraints, the downward trend in inflation in the euro area, the transmission of tightening of financing conditions in the domestic demand, and others. However, risks related to inflation are on the upside direction and mainly consist of risks of new disruptions in supply chains as a result of the war in Ukraine, rising of food prices following Russia's violation of the agreement on grain exports from Ukraine, increase in the prices of oil in foreign markets and reduction in the amount of production by OPEC+, shift in inflation expectations, pressures for wage increases, and others. As regards to the banks' expectations for annual inflation in Kosovo for 2023, these have declined to 4.8% in August from expectations for annual inflation of 6.4% that were in June 2023.

Fiscal Sector

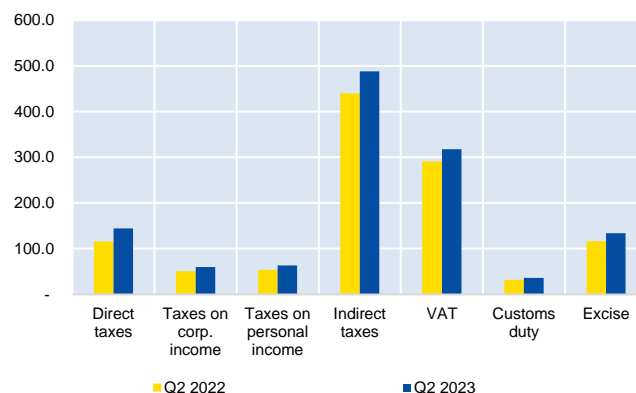
Budget revenues¹, in Q2 2023, reached a net value of EUR 682.5 million, representing an annual increase of 16.4%. Also, budget expenditures² marked an increase of 17.1% and reached the value of EUR 619.5 million. Consequently, Kosovo's budget recorded a primary positive balance of EUR 62.9 million.

¹Within the budget revenues are not included the receipts from financing, and payments from donor designated grants.

²Within the budget expenditures are not included financing payments, and payments for donor designated grants.

Tax revenues reached the value of EUR 621.3 million, marking a considerable increase of 17.2% compared to Q2 2022. Within tax revenues, almost all the categories have marked an increase. With a higher increasing rate were characterized direct tax revenues, which reached a value of EUR 144.2 million or 24.8% more compared with Q2 2022. The increase of the direct tax revenues which are mainly realized by Kosovo Tax Administration, was a result of an improvement of the collected income, the decrease of the taxation gap, the strengthening of the voluntary fulfillment of tax payments by taxpayers, etc. Within this category, personal income tax, which comprises the main category, marked an annual increase of 18.8%, while corporate income tax, marked an annual increase of 18.0%. Indirect tax revenues marked an increase of 11.0% reaching the value of EUR 488.0 million. The increase of indirect tax revenues, as the main category of budget revenues, was mainly interlinked with the high inflation rate, which despite of being significantly decreased, continued to remain high. Within indirect taxes, VAT income and customs duty marked an increase of 9.2% and 12.7%, respectively, being significantly affected by increase of prices. Also, the excise tax recorded a significant increase of 15.1%, despite the slowdown in the growth of the import of goods (chart 9). Besides tax revenues, also **non-tax revenues marked a growth of 9.0%, reaching the value of EUR 61.2 million.** Within non-tax revenues, the revenues from the central government reached the value of EUR 35.7 million, marking a growth of 10.9%, while the revenues from the local government increased by 4.2%, amounting to EUR 15.1 million.

Chart 09. Tax income structure



Source: MFLT and CBK calculations.

Regarding budget expenditures, current expenditures increased by 6.6%, while capital expenditures were doubled. In the category of current expenditures, expenses for wages increased by 16.1% and reached the value of EUR 191.1 million, expenses for goods and services, including municipal expenses, increased by 24.2% and reached the value of EUR 96.1 million, while expenses for subsidies and transfers decreased by 5.9% and reached the value of EUR 222.1 million. Capital expenditures marked an increase of 114.8% and reached the value of EUR 110.2 million.

Debt to GDP ratio was 17.3% in Q2 2023, compared to 20.8% as it was in Q2 2022. This decrease was a result of the improvement of the government's budget balance and the increase in nominal GDP, which reduces the debt to GDP ratio. This level of public debt is far from the threshold provided by law of 40% of the GDP, as well as far from the average of the countries of the region. In absolute terms, the public debt has reached EUR 1.67 billion in Q2 2023, marking a decline of 2.5% compared to Q2 2022. The decrease of public debt is attributed to the decline of domestic public debt of 11.2% reaching EUR 1.0 billion, while external public debt marked a growth of 14.7%, reaching EUR 663.9 million. External debt is comprised of liabilities to International Agency for Development (36%), International Bank for Reconstruction and Developments (14%), International Monetary Fund (8%), etc. Whereas, domestic debt primarily is comprised of Kosovo's Government debt to pension funds (48%), commercial banks (22%), public institutions (22%), etc.

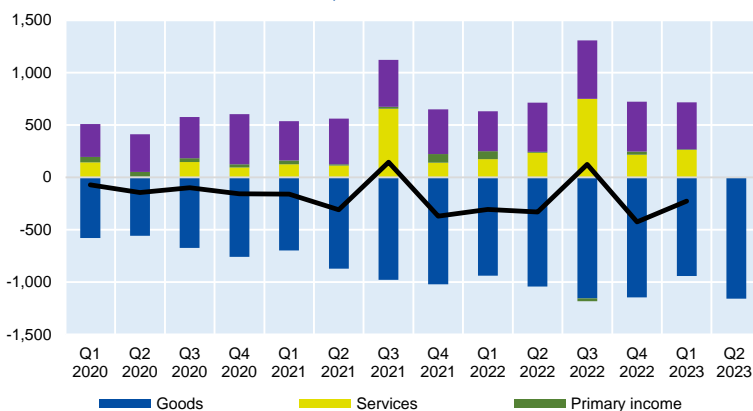
External Sector

Current account reached EUR 328.0 million in Q2 2023 (EUR 331.5 million in Q2 2022). Dynamics in the current account in the period April-June 2023 have continued to be determined mainly by developments in the trade balance of goods, a component which was deteriorated by the increase in the import of goods. Meanwhile, in the same period of time, the primary income, secondary income and services had an impact in declining the negative balance of current account (chart 10).

Trade balance of goods in Kosovo, in Q2 2023, marked an annual increase of trade deficit of 4.7%, reaching EUR 1.22 billion. The main reason for the increase in the trade deficit is related to the high value of goods imported, a dynamic that mainly was impacted by the increase in the goods quantity imported into the country. The economy of Kosovo turns out to have imported an amount of EUR 1.43 billion, while in the same period, it exported in the amount of EUR 210.7 million. Exports have covered imports by only 14.7%, representing a trade ratio of 1:6.8 (chart 11).

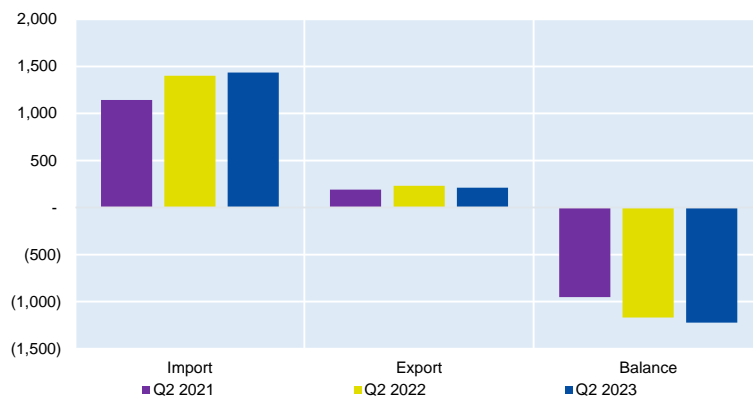
The total value of export was EUR 210.7 million, in Q2 2023, representing a decline of 9.1% compared to the same period of the previous year. While the structure of goods according to categories remains unchanged, the decline in exports, in Q2 2023, was mainly influenced by the decrease recorded in the export of basic metals for 27.6%, a category that reached the value of EUR 45.8 million (EUR 63.3 million, in Q2 2022). This dynamic mainly corresponds with the weakening of the demand in the external market of metals. To the decline of export, an impact was also given by plastics and rubber products (16.7%), which marked the value of EUR 29.6 million (EUR 35.5 million, in Q2 2022) (chart 12).

Chart 10. Current account, EUR million



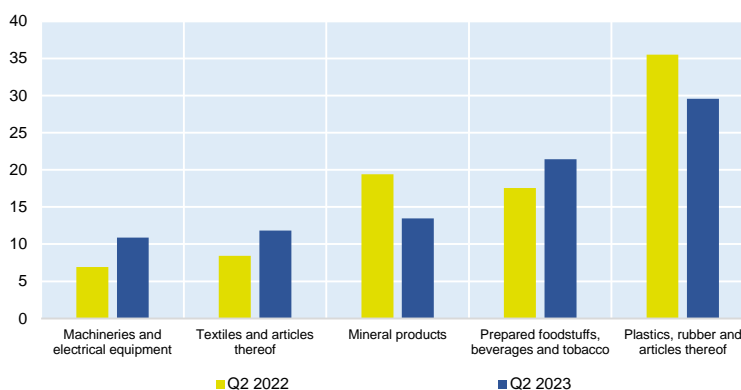
Source: CBK.

Chart 11. Trade balance of goods



Source: KAS.

Chart 12. Main categories of exported goods, EUR million



Source: CBK.

The main partners for the export of goods, in Q2 2023, remain the Western Balkans with 41.8% of total exported goods, and EU countries with 30.5%.

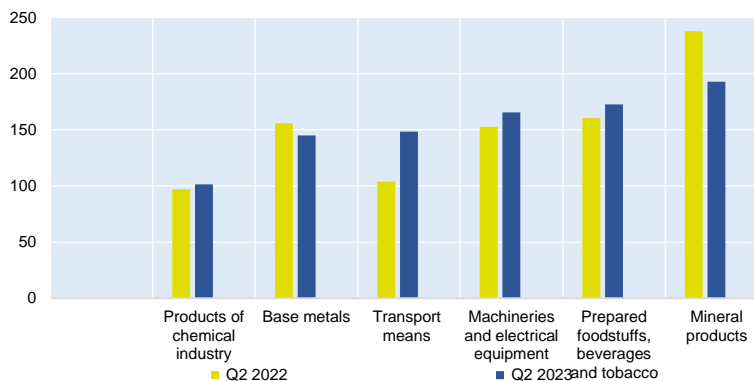
The value of imports, in Q2 2023, reached EUR 1.43 billion, representing an annual increase of 2.5%.

The slight increase of import of goods was impacted by the overall quantity and weight, marking an annual growth of 7.3% and 8.2%, respectively. The structure of imported goods continued to be dominated by import of mineral products, food commodities, and machineries, including household appliances. The share by the main categories of imported goods was dominated by the category of intermediary goods of 46.8%, consumer goods 33.2%, while the category of capital goods continues to remain low at 10.2% of total import. According to the main economic categories, intermediary goods recorded a decrease of 8.4%, mainly influenced by price dynamics in international markets, while the category of capital and consumer goods recorded an annual growth of 6.4 and 8.5%, respectively, mainly as a result of the demand growth marked in the country.

Around 42.9% of goods imported came from European Union countries (EUR 614.4 million), among which, Germany continues to have the main weight with 13.4% of total imports. Kosovo imported from the region countries 17.3% of total imports or EUR 247.6 million. Meanwhile, the import of goods from Turkey has reached the amount of EUR 210.3 million or 14.7% of the total imports (chart 13).

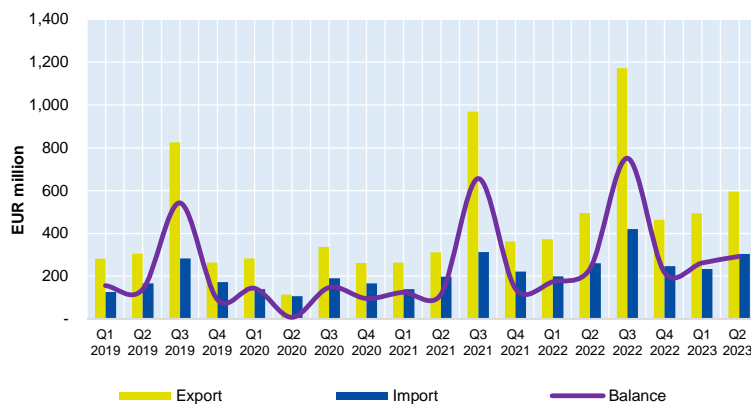
Services continued to increase their positive contribution within the current account, with an annual growth of positive balance of 24.6%, reaching the value of EUR 292.2 million, in Q2 2023. Export of services was attributable mainly to the increase of services in the category of travel with 16.8%, a category which reached the value of 404.5 million, and the category of computer services marking an increase of 44.0%, reaching the value of EUR 75.0 million (EUR 52.1 million in Q2 2022). On the other hand, the increase in import of services was attributed to the increase in travel and transport components, which comprise 66.3% of the total import of services (chart 14).

Chart 13. Main categories of imported goods, EUR million



Source: CBK.

Chart 14. Balance of services

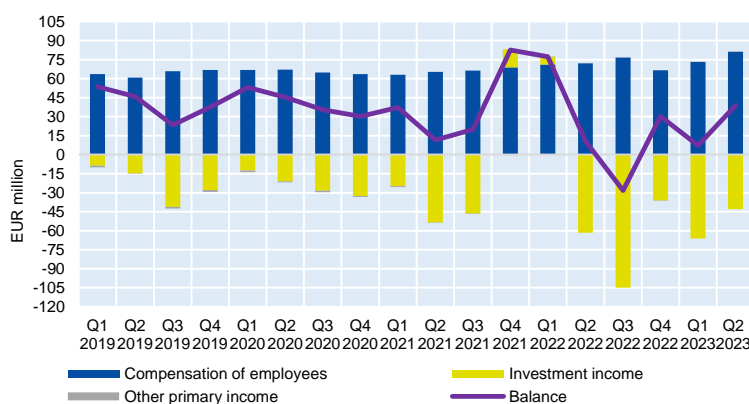


Source: CBK.

The balance of primary income recorded a growth of 28.0 million in Q2 2023, reaching the value of EUR 38.7 million (EUR 10.7 million in In Q2 2022).

The decrease in primary income was mainly influenced by the balance of income from investments, as a result of the return of dividend in the amount of EUR 69.2 million from direct investments in the period of April-June 2023. Meanwhile, the balance of income from compensation of employees has recorded an increase of 12.3%, being impacted by the increase in income from resident workers employed abroad (chart 15).

Chart 15. Balance of primary income

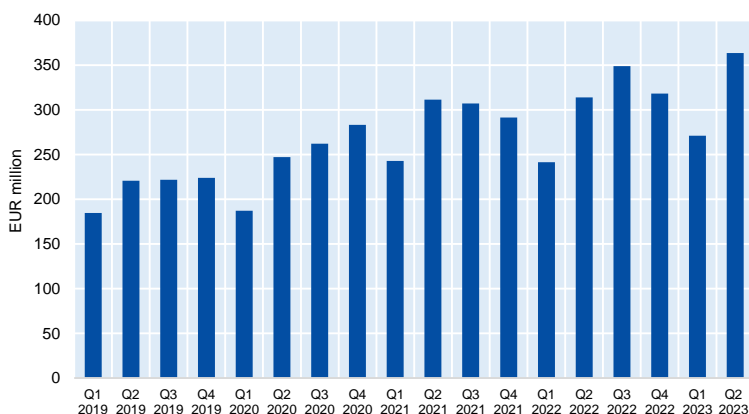


Source: CBK.

The value of remittances received, in Q2 2023, reached EUR 363.8 million, representing an increase of 15.8% compared to the same period of the previous year.

Structure of remittances by countries remains unchanged, where Germany has a share of 37.4% of remittances, Switzerland with 18.0% and USA with 7.4% of total remittances received in Kosovo. Remittances by formal channels (banks and other institutions) have recorded an increase in the value of EUR 29.4 million, while there has been an increase of EUR 20.2 million in remittances received through non-formal channels. Considering that the largest amount of remittances received in Kosovo have the main source the euro area countries (60.0%), the slowdown economic activity in the euro area may have implications on remittances received in Kosovo (chart 16).

Chart 16. Remittances



Source: CBK.

Foreign direct investments, in Q2 2023, result to have marked a decline of 12.5%, reaching the value of EUR 184.4 million.

The FDI decline was mainly recorded in the sectors of real estate, construction and mining sector including quarry. The real estate sector covers 60.0% of total FDI or EUR 110.6 million, for the period of April-June 2023. Foreign direct investments of residents from Kosovo in other countries have marked an increase in the period of April-June 2023, reaching the value of EUR 53.1 million (EUR 50.7 million in April-June 2022), investments destined to the countries of the region and mainly oriented to the real estate sector (chart 17).

Chart 17. Foreign Direct Investments



Source: CBK.

Financial system

Despite the challenges from the higher risks with which the economy was facing, such as increased inflation and the weaker economic outlook, the financial system in the country expanded with an accelerated pace.

Financial system assets in the country accelerated their annual growth for 6.4 percentage points against the previous year, and their value reached EUR 10.2 billion, at the end of June 2023. All the constituent sectors were characterized with an accelerated annual increase of assets (chart 18).

The banking sector, in June 2023, represented around 67.5% of total assets of the financial system, thus giving the main contribution to the expansion of the total assets of the financial system (chart 19). The second sector by weight to the financial system was presented by pension funds, which marked an accelerated increase of assets compared to the previous year (chart 19). Other sectors, the one of microfinance, insurance and financial auxiliaries, marked a higher double-digit increase, hence significantly contributing to the growth of total assets of the financial system, despite their low weight of share they have.

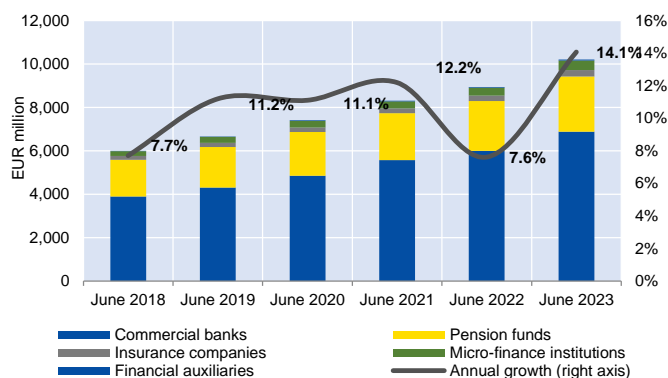
1. Banking Sector

Banking sector and the overall financial system is exposed to external risks as a result of geopolitical tensions which may escalate in Southern Europe, whereas the inflation remains the main risk. Although the situations that have an impact on the increase of inflation have softened and the monetary policies of central banks are having an effect, the consequences of inflation transmitted to other segments are still a concern, inflation is persistent (stable) and with a slow decline. The banking sector in Kosovo due to its weight, structure and low complexity, does not have high exposure to the external sector and any potential consequences of any crises or panic in the financial sector would not put at risk the banking sector in a direct way. Whereas, the negative effects which come from inflation have a more direct impact in the domestic banking market, and the main soundness indicators of the banking sector should be monitored.

Assets

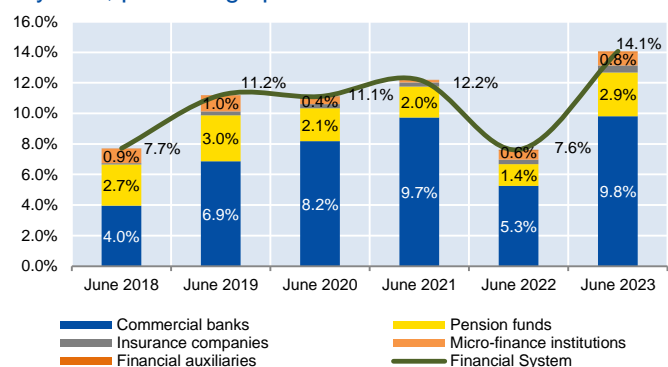
Banking sector assets reached the value of EUR 6.88 billion in June 2023, which corresponds with an accelerated annual increase of 14.6% compared to the increase of 7.8% in the same period of the previous year (chart 20). The main contribution to the growth was given by lending expansion which is the main activity of the banking sector. Investments in securities was the second component which contributed to the acceleration of assets increase, followed by the category of assets held at other

Chart 18. Assets value of Kosovo's financial system



Source: CBK.

Chart 19. Contribution to assets growth of financial system, percentage points



Source: CBK.

banks. Both of these latter categories marked an accelerated increase compared to the annual decline recorded in the same period of the previous year. **Whereas, the item of cash and the balance with the CBK remained at the same level as in the previous year.**

Lending

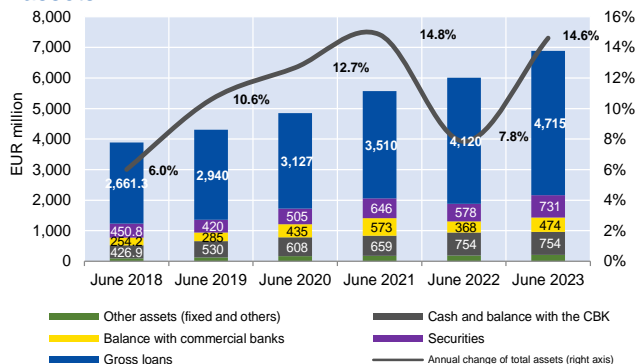
Lending activity of the sector marked an annual growth of 14.5%, which corresponds to a lower increasing rate compared to the previous year.

According to the Bank Lending Survey, lending dynamics also in the second quarter of 2023, as in Q1 2023, were largely influenced by credit demand, since credit supply had marginal changes. Credit demand for enterprises in general was characterized with an increase, albeit lower than in the previous quarter, whereas the credit supply had marginal negative movements. The demand for loans from households in general marked an increase during the second quarter of 2023 at an approximate level for consumer credit and for mortgage loans. Credit standards were eased to some extent for housing loans, whereas they changed marginally for consumer credit. The lending dynamics in the first half of 2023 generally reflect a more careful approach of consumers in undertaking additional debts, in an environment of the increase of life cost, and at the same time, a more careful approach and monitoring the banks in lending. According to the survey, the incentive factor of the lending activity in the following quarter is expected to be marked by the demand for consumer credit, as the demand for loans from enterprises is expected to remain unchanged.

The segment of nonfinancial corporations recorded an annual loans stock of 12.9%, which coincides with the acceleration of the annual growth trend of 3.8 percentage points (chart 21). Meanwhile, loans to households recorded an annual increase of 16.8%, which compared to the previous year represents a slowdown in growth by 0.7 percentage points. Due to the higher share in total loans, the segment of nonfinancial corporations had the highest contribution to the growth of total lending of the banking sector (chart 22).

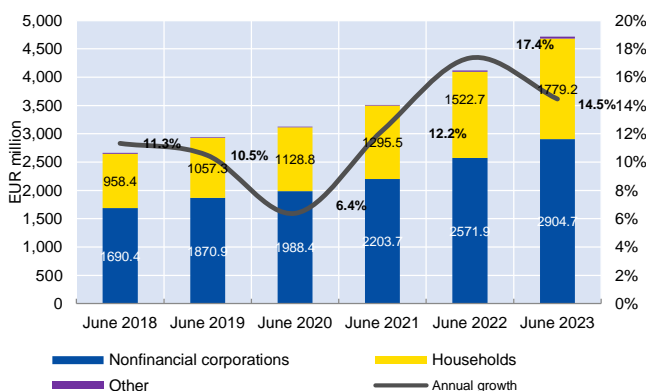
New loans, in the first half of 2023, halved down the increasing rate, standing at 9.0% from 18.5% as it was in the same period of the previous year. The sector of enterprises was characterized by a slowdown in the annual

Chart 20. Balance sheet of the banking sector - assets



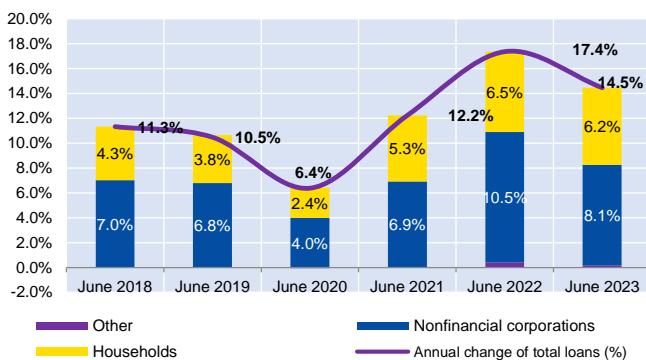
Source: CBK.

Chart 21. Stock of total loans, annual change



Source: CBK.

Chart 22. Contribution to the growth of total loans, in percentage points



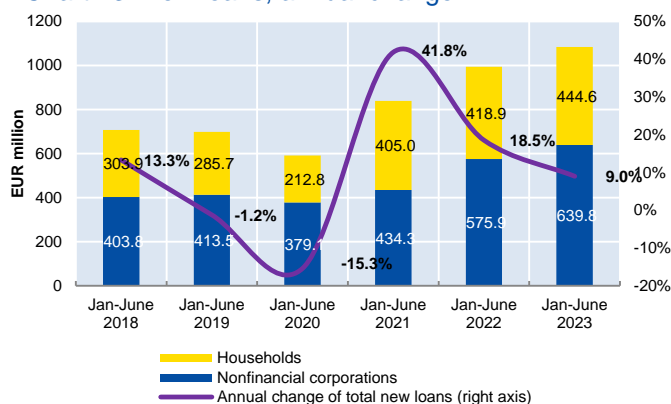
Source: CBK.

growth rate of new loans, while that of households recorded an accelerated growth compared to the previous year (chart 23).

Until June 2023, new nonfinancial corporate loans increased by 11.1% compared to the growth of 32.6% marked in the first half of 2022. Loans with investments purpose increased by 13.6%, and loans with non-investment purpose marked an annual increase of 11.6%. New loans to households marked an accelerated annual increase of 6.1%. Within the household segment, new consumer credit recorded an annual increase of 10.6%, from a decrease of 6.1% in the first half of 2022, while new mortgage loans recorded an annual decrease of 9.6%, in contrast to an increase of 16.3% marked in the same period of the previous year. Foreign direct investments in the real estate sector showed a declining trend until May 2023. This, along with the decline in mortgage loans, may suggest a declining sentiment for real estate investment, influenced by rising interest rates as well as the increase of prices in the real estate sector.

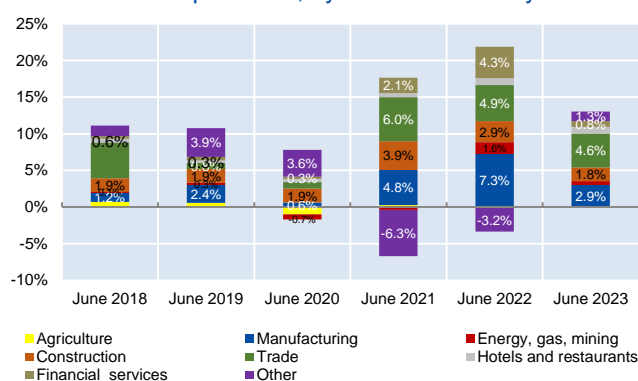
In terms of loans to nonfinancial corporations, lending to the trade sector was at the highest levels over the years, followed by the manufacturing and construction sector, which have gradually expanded in the recent years, thus increasing their share to total loans of the banking sector. As at end of March 2023, lending to trade sector had the highest contribution to the growth of total loans to nonfinancial corporate segment (chart 24), as a result of the high weight in this segment and the annual growth of 10.8% (chart 25). The manufacturing sector, which last year had the highest weight in the growth of total lending for this segment, in June 2023 recorded a slower annual growth of 15.1% from 45.6% that had been marked in the previous year, when it was also supported by the subsidy measures of the Government within the economic recovery package. Lending to the construction sector marked a slower annual growth as well, reaching 13.5% in June 2023, from 21.5% that had been marked in the previous year. The slowdown in lending for this sector may also have been influenced by the high rate of inflation marked in 2022 - the increase in the price of construction materials that has been transmitted to the slowdown of construction dynamic or their temporary interruption. Agriculture sector, which is at the same time the least credited sector by commercial banks, was characterized with an increase of 2.9%, unlike in the previous year when it had been marked a decline of 4.0%.

Chart 23. New loans, annual change



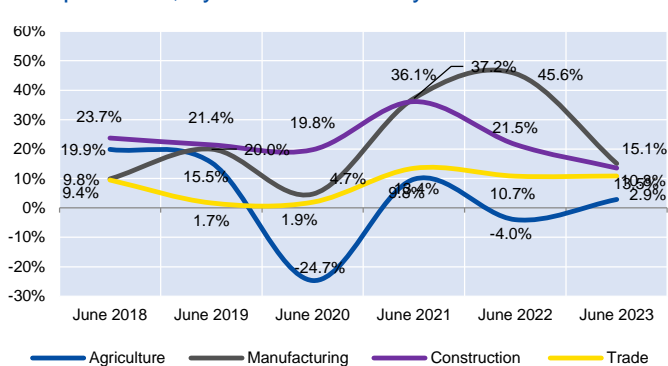
Source: CBK.

Chart 24. Contribution to the growth of total lending to nonfinancial corporations, by economic activity



Source: CBK.

Chart 25. Annual change on loans to nonfinancial corporations, by economic activity



Source: CBK.

1.1. Liabilities and own resources

Financing of the banking sector activities continued to rely on customer's deposits and own capital, namely retained earnings from the previous periods and realized earnings during the first half of 2023.

Both of these items comprise 92.9% of liabilities and equity, where 81.5% is comprised only by deposits. The tightening of monetary policies on the global level which has had an impact on the overall increase of interest rates, and also being reflected on the domestic market since the second half of 2022 was associated with a sustainable increase of the total value of deposits.

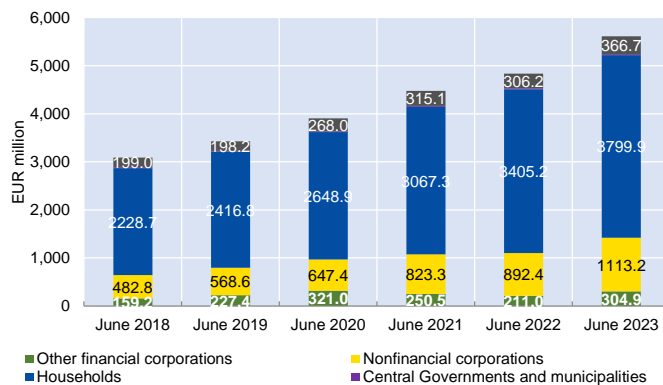
1.1.1 Deposits

The value of the stock of deposits, at the end June 2023, reached EUR 5.61 billion (chart 26), representing an accelerated annual growth of 16.0%, from 8.0%, in June 2022. Deposits of both private sector segments marked an accelerated increase and determined the growth trend of total deposits. Moreover, also deposits collected from the public corporations and pension funds marked a significant increase, thus contributing to the highest increasing rate marked in the last 14 years.

Household deposits marked an annual growth of 11.6% in June 2023, from the increase of 11.0% marked in the previous year, representing a dynamic which was impacted by the increase of interest rates on deposits. In June 2023, the value of household deposits reached EUR 3.80 billion, thus, also determining the overall trend of deposits in the banking sector (chart 27). Regarding the level of new deposits collected from households, which include only time deposits, during the period of the first half of 2023, reached the value of EUR 192.2 million, representing an annual increase of 21.5%, slightly lower compared to the annual increase of the previous year of 26.4% (chart 28).

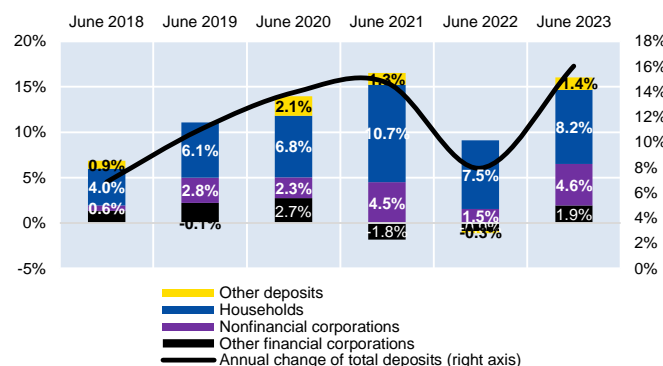
The stock of nonfinancial corporation deposits reached EUR 1.11 billion at the end of June 2023, representing an annual increase of 24.7%

Chart 26. Stock of total deposits



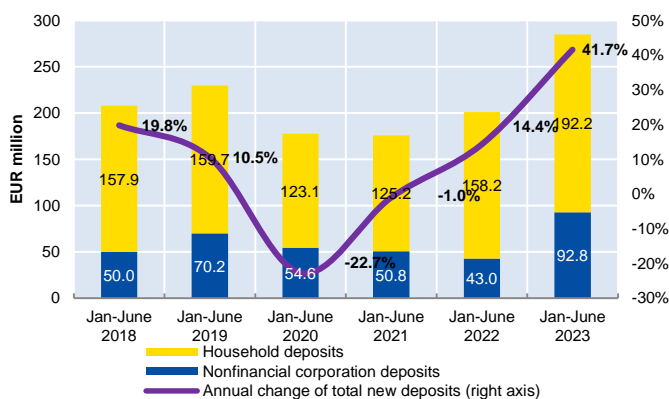
Source: CBK.

Chart 27. Contribution to annual growth of total deposits, percentage points



Source: CBK.

Chart 28. New deposits, annual change



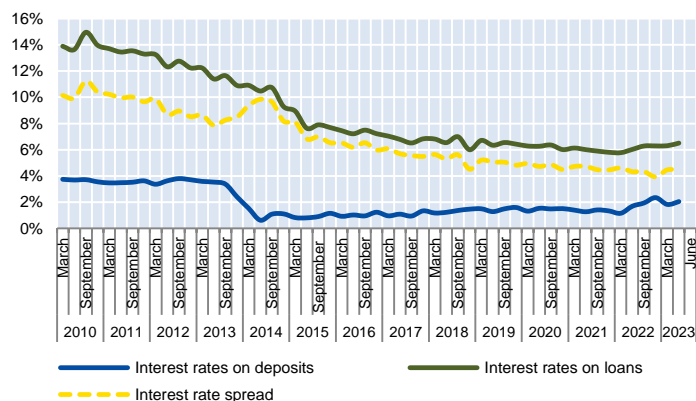
Source: CBK.

from 8.4% marked in the same period of the previous year. New deposits collected during the first half of 2023 from this segment increased to EUR 92.8 million from EUR 43.0 in the same period of 2022. The tightening of financing conditions by the measures taken to control inflation, has influenced the continuous increase in competition in the country for securing and holding deposits, thus offering more attractive conditions for depositing funds mainly through the increase of interest rates on deposits.

1.2. Interest rates

Interest rates on new loans and deposits had gradually increased since the beginning of last year, implicated by the application of tight monetary policies by central banks in combating inflation. In the banking market, interest rates on new deposits have been affected at a higher level than interest rates on new loans. In June of this year, the interest rate on loans reached 6.5% from 6.0% in June 2022, when inflation intensified and discussions on monetary policy intervention began. Also, the average interest rate on deposits increased to 2.1% from 1.7% as it was in June 2022, and 1.9% in September 2022,

Chart 29. Interest rate on loans and deposits

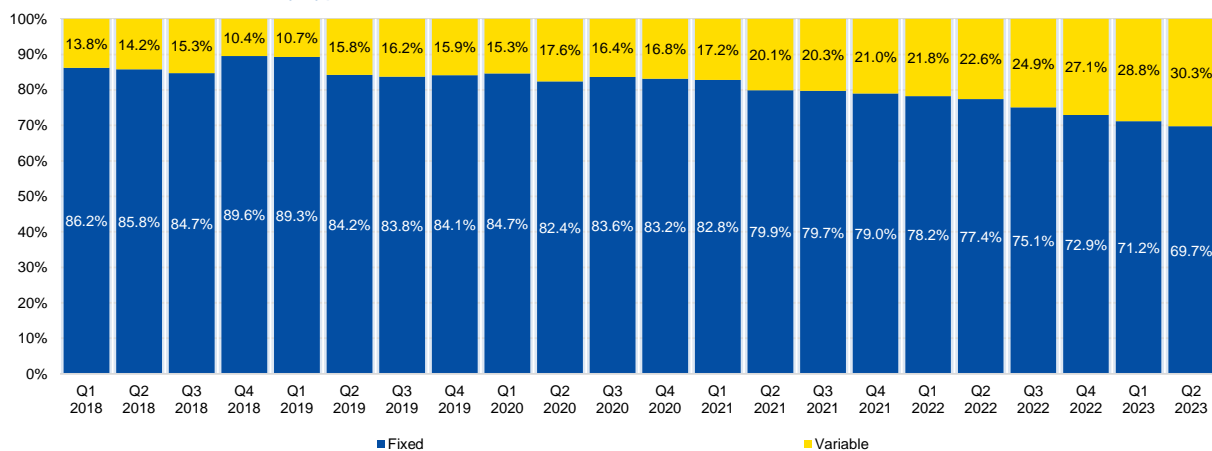


Source: CBK.

when concerns over holding deposits in the banking sector and consequently the liquidity risk were further highlighted. The interest rate spread of loans and deposits expanded to 4.45 percentage points from 4.32 percentage points, due to the higher increase of interest rate on loans (chart 29).

The dynamics of interest rates influenced by developments at the global level, as well as the increase in liquidity risk and uncertainties about future developments as a result of increased inflationary pressures, in addition to driving the banks in the country to increase interest rates on loans and deposits, at the same time have influenced the change in the structure of loans according to the type of interest rates. While during the years 2020-2021, loans with variable interest rates, which are mainly determined by the movements of the Euribor rate for the additional margin, accounted for an average of 16.5% of the loan portfolio and 19.6%, respectively, where this level has risen to 24.1% in 2022, and until June 2023 was further increased to 30.3% (chart 29a).

Chart 29a. Loans stock by types of interest rates



Source: CBK.

In June 2023, the average interest rate on loans to nonfinancial corporations was 6.8%, or for 0.7 percentage points higher compared to the same period of the previous year. More favorable interest rates on loans were offered for industry sector (6.4%), while the highest average interest rate of 6.8% was for agriculture sector (chart 30).

The average interest rate on loans to households was 6.1%, which is for 0.2 percentage points higher compared to the same period of the previous year. The more favorable interest rates have been applied to mortgage loans with an average of 5.4%, since they are considered to have a lower risk as being covered by collateral (mortgage). However, consumer credit continues to have higher interest rates with an average of 6.3% (chart 31).

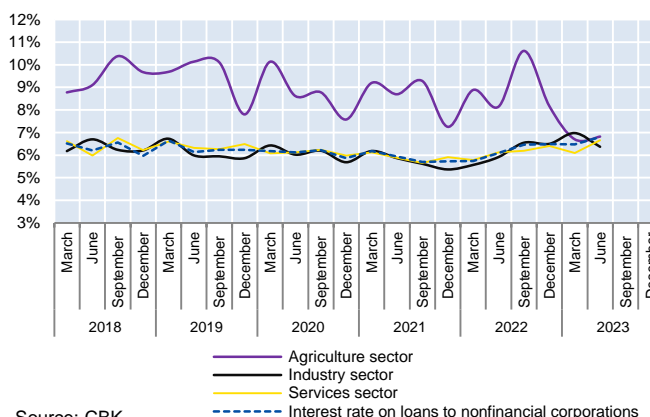
Interest rates on deposits started the upward trend since June 2022, reaching an average of 2.4% at the end of the previous year. In June 2023 the average interest rate on deposits reached 2.1%, which is for 0.4 percentage points higher than in June 2022, but lower for 0.3 percentage points compared to December 2022. Interest rates on nonfinancial corporation deposits increased by 0.4 percentage points, reaching 2.5%. Also, for household deposits the interest rate was increased by 0.4 percentage points, reaching 1.9% in June 2023 (chart 32).

Performance of the banking sector

The banking sector, until the second half of 2023, realized a net profit of EUR 82.6 million, reaching a record level compared to the same periods of the previous years. Such a financial result was enabled by the higher increase of income compared to the increase of expenditures (chart 33).

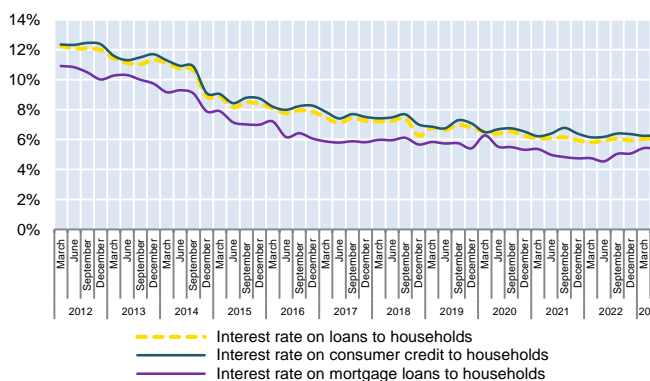
Total income reached the value of EUR 202.5 million, representing an annual increase of 19.9% (an increase of 11.6% marked in June 2022). Interest income, which represent 74.7% of total income, gave the main contribution to the growth of income. In the context of interest income, the collection of interest from loans had the main contribution to this increase, a category which was influenced by the significant increase in lending, especially in the previous two years. Moreover, the yield from placements with the banks were increased significantly compared to the same period of the previous year.

Chart 30. Norma e interesit në kredi për korporatat jofinanciare



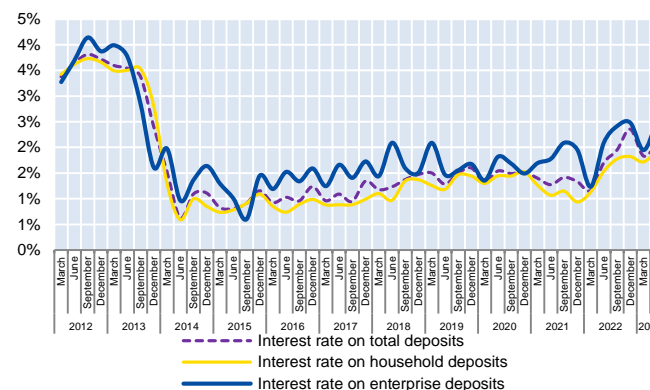
Source: CBK.

Chart 31. Interest rate on loans to households



Source: CBK.

Chart 32. Interest rates on deposits

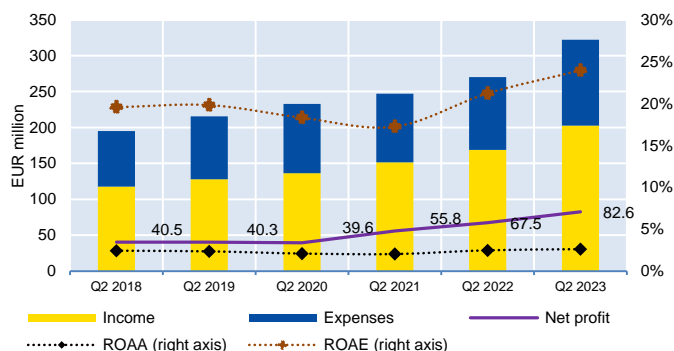


Source: CBK.

Whereas, the category of non-interest income, mainly from fees and commissions, marked a slower annual growth of 6.1% after the significant increase of 13.3% marked in the previous year, reaching the value of EUR 44.6 million at the end of June 2023.

The value of expenditures of the banking sector reached EUR 119.9 million, until June 2023. With an accelerated annual increase were characterized also expenditures, reaching 18.3% from 6.1% as they were until June of the previous year. The highest contribution to this increase was marked by general and administrative expenses and interest expenses. The category with the largest weight in total expenditures, which consists of general and administrative expenses with a share of 59.2%, increased by 15.5% compared to the previous year (an increase of 8.6% in the previous year), and reached the value of EUR 71.0 million at the end of June 2023. The increase of general and administrative expenses mainly reflects the increase of personnel expenses, in order to adjust the wages level to inflation increasing trend. Also interest expenses recorded an annual increase of 51.7% from the increase recorded in the previous year of 4.0%, which is attributed to the increase in interest rates on deposits and simultaneously to the increase in the stock of deposits.

Chart 33. Profit and profitability indicators of the banking sector



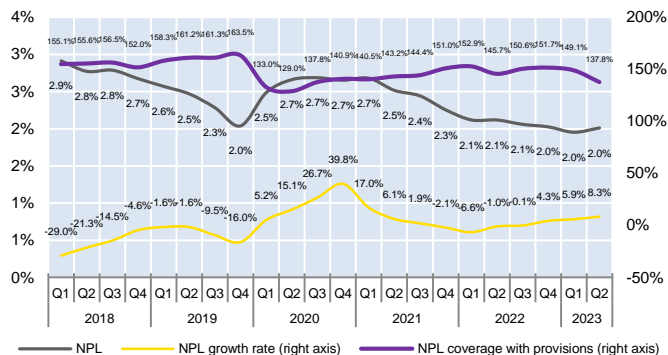
Source: CBK.

Financial Soundness Indicators

Over the years, the banking sector has managed to ensure a high level of capitalization and liquidity, as well as to maintain a low level of nonperforming loans. The satisfactory state of these indicators gives priority to the sector in absorbing shocks from uncertainties caused by geopolitical crises, the increase of inflation and the slowdown of economic activity.

Credit quality marked an improvement starting from the last quarter of 2021 until September of the previous year, where the value of nonperforming loans had a downward trend with an average of 2.5%. Since the last quarter of 2022, the declining trend changed direction, where the value of NPL increased by 4.3% and 8.3% at the end of 2022 and, namely, at the end of June 2023. The value of nonperforming loans increased by around EUR 7.3 million as of June of the previous year. NPL to total loans ratio for the household segment continued to remain low, with 1.3%. Whereas, for the segment of the nonfinancial corporations, NPL rate stood at 2.5%, and their value marked an annual increase of 3.9% compared to the second quarter of the previous year. With an increase of NPL value was characterized also the sector of energy and manufacturing, which increased by EUR 3.8 million and EUR 3.4 million, respectively, whereas as a ratio to loans, it increased for 7.0 percentage points and 0.4 percentage points, reaching the level of 9.6% and 1.8%, respectively. The NPL value for the trade sector decreased for EUR 2.2 million, whereas the NPL to total loans ratio for this sector fell at 1.9% from 2.3%. Conversely, for other sectors, the NPL value and ratio suffered marginal movements compared to the previous year.

Chart 34. Nonperforming loans and loan loss provisions



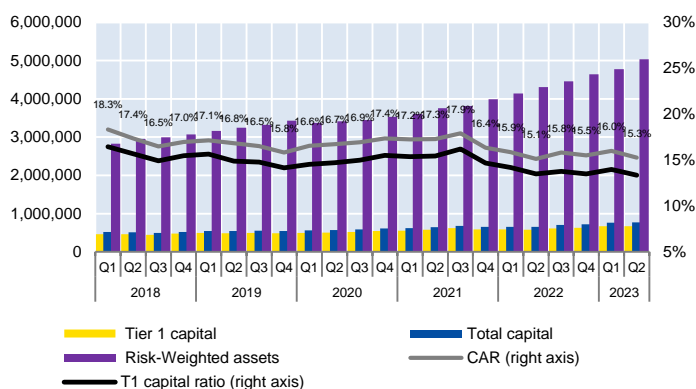
Source: CBK.

A more significant increase in lending in the reporting period had an impact on the overall nonperforming loans to total loans ratio of the banking sector, thus consequently decreasing to 2.0%, from 2.1% as it was in June of the previous year. The coverage by loan loss provisions declined slightly to 137.8%, from 145.7% as it was in June 2022, due to the higher increase marked in the value of nonperforming loans than the value of provisions dedicated for loan losses (chart 34).

The capital adequacy ratio increased to 15.3% from 15.1% as it was in June 2022, as a result of a more significant increase in capital compared to risk-weighted assets. The profit retained from the previous year and the one realized in the second quarter of 2023 has had an impact on the equity to record a more significant increase compared to the increase of the risk-weighted assets (chart 35).

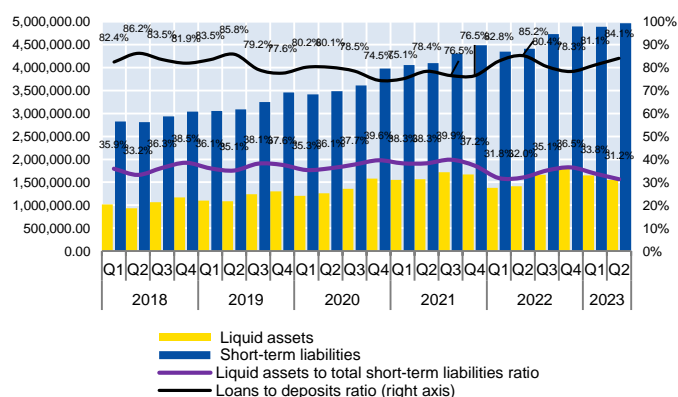
The ratio of liquid assets to total short-term liabilities in June 2023 was 31.2%, which is for 0.8 percentage points lower compared to the previous year (chart 36). The decrease, although marginal, in the liquidity ratio, was due to the more pronounced increase in short-term liabilities of 12.5% compared to the increase in liquid assets of 9.7%. Within the liquid assets, investments in securities of foreign governments recorded the most significant growth, followed by deposits and placements in foreign banks. Meanwhile, short-term liabilities marked an increase due to the increase of deposits, compared to June 2022. Loans to deposits ratio decreased to 84.1% from 85.2% as it was in the previous year, which is a result of the higher increase of deposits to the increase of loans, during the recent period.

Chart 35. Solvency indicator



Source: CBK.

Chart 36. Liquidity indicators



Source: CBK.

Pension sector

Assets of the pension sector recovered the growth pace of the previous years, after the pronounced slowdown marked in the previous year, as a result of large fluctuations in the financial markets influenced by the deterioration of the geo-political situation in Eastern Europe. Pension sector until June 2023 marked positive return from investments and increase in income from the pension contributors.

With the second highest share in total assets of the financial system, assets of pension funds increased by 11.2% at the end of June 2023, which is significantly higher than in the previous year, when it had reached 5.5% in the previous year (chart 37). The value of pension funds' assets reached EUR 2.54 billion, of which 99.6% are represented by Kosovo Pension Saving Trust (KPST), whereas the remainder belongs to Slovenian-Kosovo Pension Fund (SKPF). While the KPST recorded an annual asset increase of 11.1%, assets of the Slovenian-Kosovo Pension Fund (SKPF) recorded an annual growth 6.6%, in June 2023.

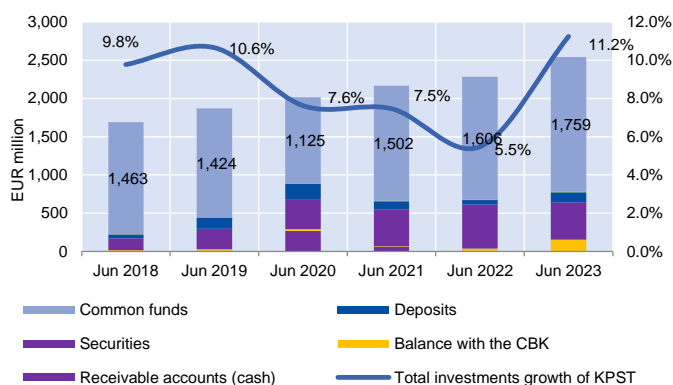
Assets of KPST are mainly invested in external market (69.7% of investment portfolio), in mutual funds with a value of EUR 1.76 billion (or 69.7% of total assets of KPST). The remainder of investments are diversified in securities of the Government of Kosovo in the amount of EUR 488.4 million or 19.3% of the total investment portfolio and certificates of deposit in the local banking sector in the amount of EUR 128.9 million (5.1% of the total investments). Also, the structure of SKPF investment portfolio of SKPF structure is similarly diversified as KPST investment portfolio, being mainly oriented to the external market, in the shares that comprise 76.1% of the investment portfolio, and in securities with an investment share of 3.8%, of total investments. Meanwhile, investments within the country are mainly focused on Kosovo's Government securities which account for 14.4% of total investments portfolio. Whereas the remainder of assets held in the country (around 2.1%) is comprised by cash and deposits held at commercial banks.

KPST is characterized with a marginal decline of investment portfolio in the external market along with the increase of investments marked in the domestic market, whereas SKPF increased investments in the external market, against the contraction of investments marked in the domestic market (chart 37a).

The value of contributions collected by SKPF until June 2023 reached EUR 337.1 thousand, which represents an annual increase of 14.3%, influenced by the increase of the number of contributors. Meanwhile, the gross cumulative return from investments until June 2023 reached EUR 481.7 thousand, compared to losses in the amount of EUR 801.6 thousand marked in the previous year, which was the result of the turbulences created in the financial markets, mainly caused by geo-political developments in the Eastern Europe.

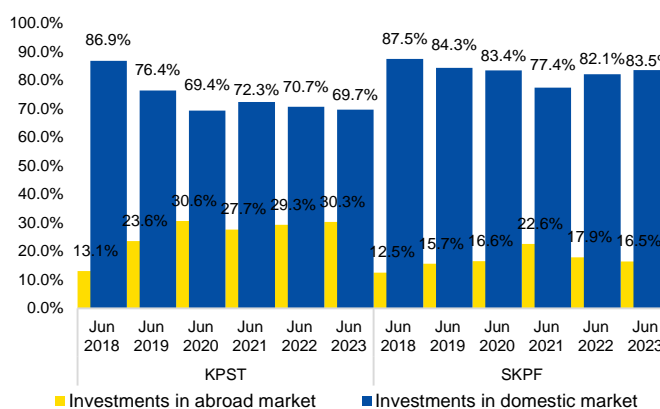
The value of contributions collected by the KPST, for the first half of 2023, marked an annual growth of 15.9%, reaching the value of EUR 134.7 million. The high double digit increase of collected contributions, among others, reflects also the increase in salaries of civil servants, which was effective as of the beginning of 2023. Whereas, gross return on investments until June 2023 reached the value of EUR 24.1 million, against the losses of the value of EUR 161.6 million marked in the previous year. The positive return on investments, in the first

Chart 37. Assets of the pension sector



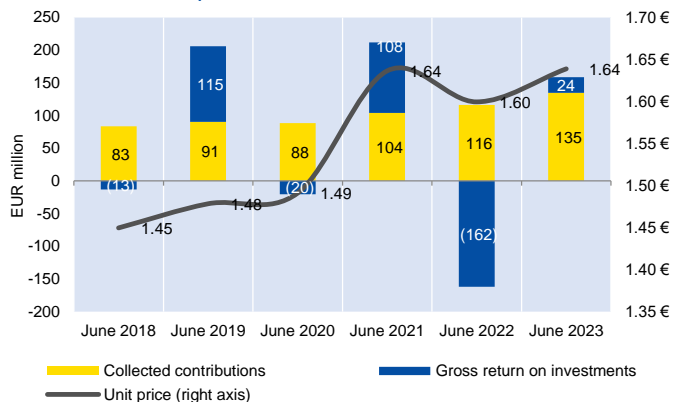
Source: CBK.

Chart 37a. Structure of pension funds investments



Source: KPST, SKPF

Chart 38. KPST performance



Source: KPST

Source: KPST.

half of 2023, reflects the improvement of global financial markets, especially in the second quarter of the year, which was reflected in the fund's performance in the external sector (chart 38).

Insurance sector

Insurance sector marked a double-digit increase for the second consecutive year, a considerable increase of written premiums and a higher financial performance compared to the recent years.

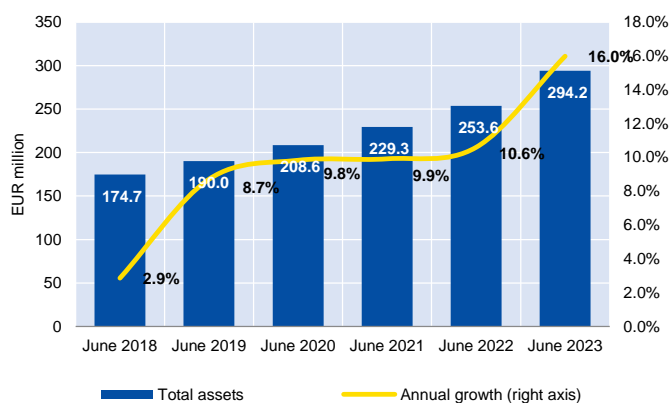
Insurance sector assets represented 2.9% of total financial system assets, at the end of June 2023. The value of total expenditures at the end of 2023 reached EUR 294.2 million, representing an annual increase of 16.0% (chart 39). The expansion of the sector came mainly as a result of the technical reserves increase, which source

out from the written premiums, and own capital of the insurers. Within assets, the most significant increase was recorded in the category of deposits held at commercial banks, which are mainly in the form of time deposits. The second category in terms of weight, that of Kosovo's Government Securities, recorded an increase compared to the situation in June 2022, but which is slower, as a result of the lower level of debt issued by the Government of Kosovo during the first half of 2023 (new issues only during the period January-March 2023).

The value of written premiums reached EUR 70.3 million at the end of June 2023, representing an annual increase of 14.5%. The increase in written premiums mainly reflects the increase in written premiums of "health insurance", within the category of voluntary insurance and "motor third party liability" within the compulsory insurance. The written premiums against compulsory insurance continue to have the largest weight, reaching 54.5% of the total non-life written premiums. The increase in premiums within the "health insurance" (for 20.8%) is a positive signal for the increase in the number of citizens who have health insurance (policies). Moreover, also the number of policies for this category was increased to 173.3 thousands from 115.8 thousands as they were at the end of June 2022. Whereas the increase in compulsory insurance premiums mainly reflects the category of "motor third party liability – MTPL internal" "MTPL+", which marked an annual increase of 8.6% and 15.8%, respectively.

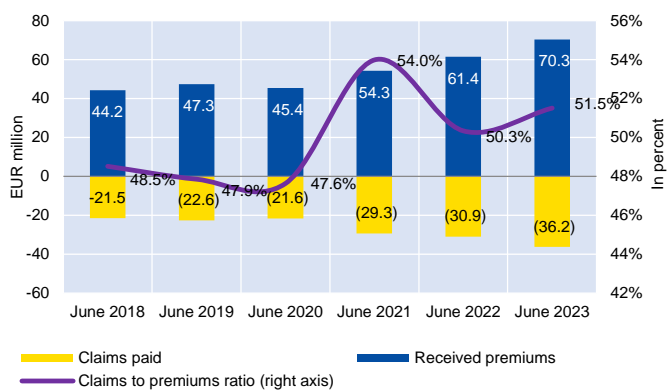
On the other hand, the value of claims paid by insurance companies and the Kosovo Insurance Bureau until June 2023, reached the value of EUR 36.2 million, representing an annual growth of 17.2% (an increase of 5.5% marked in the previous year) (chart 40). The value of claims paid by KIB decreased by 34.2%, while the claims paid by insurance companies marked an annual increase of 26.3%. The significant increase of claims paid originated from the segment of "non-life insurance", namely "fire and natural disasters insurance", and "health insurance". The category of "motor third party liability" continues to have the largest weight of 53.6% of the total claims paid by the "non-life" segment, but compared to the reporting period of the previous year, they

Chart 39. Assets of insurance sector



Source: CBK.

Chart 40. Written premiums and claims paid



Source: CBK.

increased by only 0.4%. The insurance sector, in the first half of 2023, realized a profit in the amount of EUR 5.9 million (EUR 2.5 million in the same period of the previous year). The highest value of realized profit against the previous year came as a result of the higher value of income collected from the written premiums compared to expenditures value for claims paid.

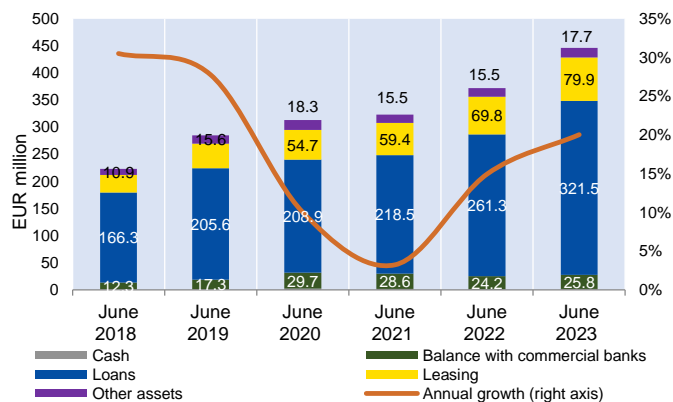
Microfinance sector

The microfinance sector, in the first half of 2023, marked an accelerated growth of assets, mainly influenced by the expansion of lending, which was financed by borrowings and own capital. The sector maintained roughly the level of last year's profits, while loans with problems continue to be low and well provisioned. However, the microfinance sector is expected to face increased funding costs due to the increase in the base interest rates as part of the tight monetary policies applied by many central banks in terms of managing inflation. These dynamics can be reflected in further increase of interest rates for loans, due to the high dependence on financing the activity from the external borrowings (61.5% of liabilities and equity).

Assets

Assets of the microfinance sector recorded an accelerated annual growth of 20.0% in June 2023, reaching the value of EUR 446.6 million at the end of the period (chart 41). The main contribution to this growth was given by the increase of lending and to a lesser extent by increase of leasing. Lending activity of the sector continued to be supported by borrowings (credit lines) from abroad, which increased by 20.0%. Also, the increase of the level of capital contributed to the increase of the activity of the sector, mainly through the profit retained over the years, and the profit realized until June 2023.

Chart 41. Assets of the microfinance sector



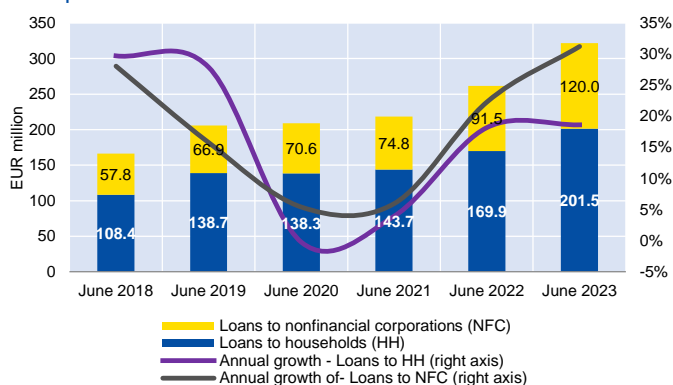
Source: CBK.

Loans

The activity of the microfinance sector continued to increase with a more accelerated pace for the second consecutive year, reaching the trend as it was before the pandemics (2016-2019).

Total loans issued by the microfinance sector marked an accelerated growth of 23.0% at the end of June 2023, while their stock reached the value of EUR 321.5 million. Lending of the sector increased for both economic segments, namely for nonfinancial corporations and households. More specifically, lending to households marked an annual increase of 18.6% (an annual increase of 18.2% marked in June 2022), reaching the value of EUR 201.5 million at the end of June 2023 (chart 42). Loans stock to nonfinancial corporations marked a value of EUR 120.0 million, representing an annual increase of 31.2% (an annual increase of 22.3%, in June 2022).

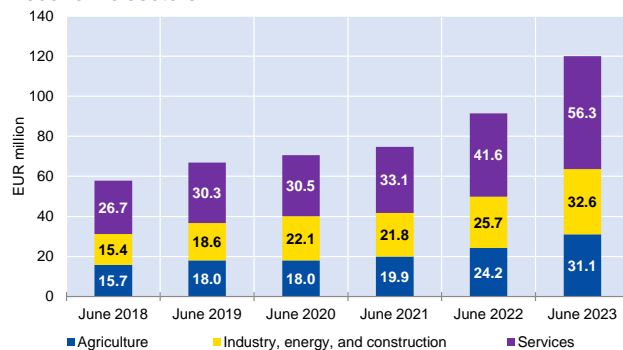
Chart 42. Value of loans to households and to nonfinancial corporations



Source: CBK.

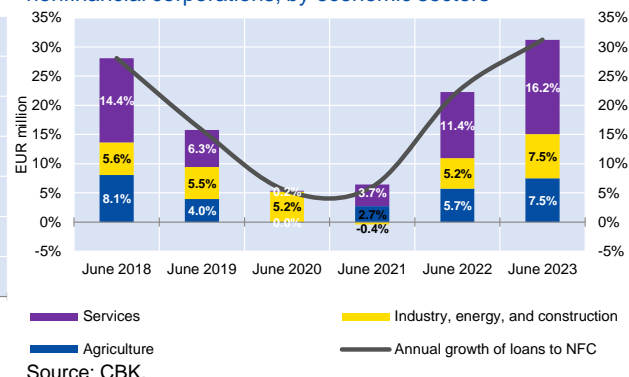
Lending to nonfinancial corporations by economic sectors has followed an increasing trend, marking a rise in each of the economic sectors (chart 43). In contrast to the banking sector, the stock of loans to the agriculture segment has the largest weight to total lending to nonfinancial corporations MFI-s/NBFI-s, with 25.9%.

Chart 43. Value of loans to nonfinancial corporations, by economic sectors



Source: CBK.

Chart 44. Contribution to the growth of lending to nonfinancial corporations, by economic sectors



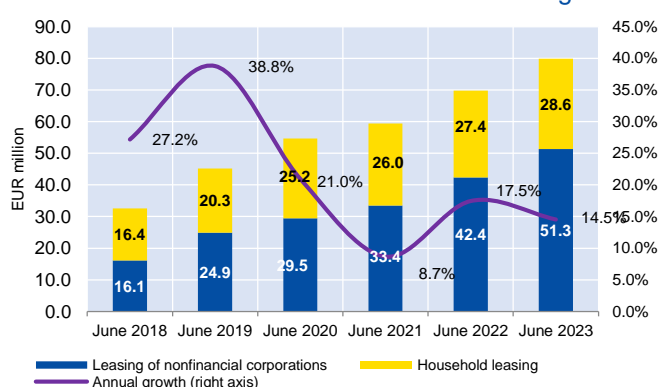
Source: CBK.

Moreover, this segment had the highest contribution to the growth of total lending to nonfinancial corporations (chart 44), marking an annual growth of 28.4% in June 2023, reaching the value of EUR 31.1 million. The guarantee offered by the KCGF to cover the risk for loans to the agriculture sector, had an impact on the increase of loans to the agriculture segment for SMEs.

Leasing

Leasing continue to be the second most important category in terms of weight in the assets structure of the microfinance sector (17.9%). Leasing activity for the second consecutive year recorded a double-digit growth, and reached the value of EUR 79.9 million at the end of June 2023 (chart 45). Nonfinancial corporations continued to make the main contribution to the increase in leasing, while the contribution of leasing to households was more limited.

Chart 45. Value of microfinance sector leasing



Source: CBK.

Interest Rates

The average interest rate on issued loans by this sector was 19.0% in June 2023, or for 0.1 percentage points higher compared to the same period of the previous year (chart 46). Unlike the banking sector, which has a rate of almost three times lower due to the low cost of financing activities (through deposits), MFIs/NBFIs are mainly financed by loans received from the external sector, which have higher interest rates. The latest developments in the financial sector, namely the increase in the basic interest rates from the central banks, is expected to be reflected in the cost of financing the sector and potentially, it is translated into a further increase of interest rate on loans offered by this sector.

Interest rates on loans to households marked a decline of 0.4 percentage points, dropping at 21.1%. According to loans classification, the average interest rate on consumer credit increased by 1.3 percentage points, reaching 22.9%. Meanwhile, mortgage loans continued to have the lowest interest rates, at an average of 17.0% in June 2023, which compared to the previous year it marked a decline of 1.1 percentage points.

For nonfinancial corporations, the average interest rate increased by 0.9 percentage points, reaching 15.9% in June 2023 (chart 47). The interest rate on loans to the agriculture and industry sector decreased by 1.7 and 0.5 percentage points, standing at 17.8% and 17.3%, respectively, at the end of June 2023. Whereas, loans to services sector, which have a more favorable interest rate, at the end of June 2023, had an interest rate of 14.8%, representing an annual increase of 2.3 percentage points.

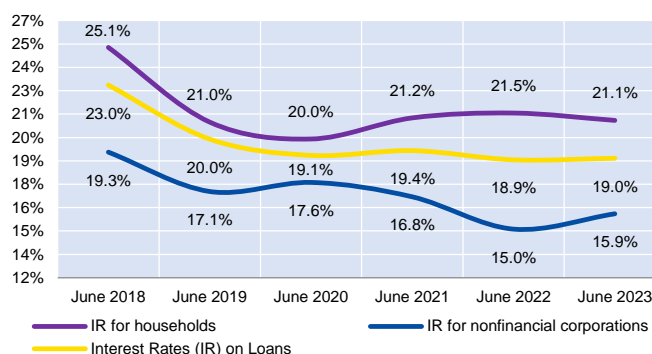
Performance of the microfinance sector

Microfinance sector, until June 2023, managed to maintain almost the same level of the profitability, which had been marked in the same period of the previous year, despite that the sector was facing a cost increase of financing its activities. At the end of June 2023, this sector marked a net profit with a value of EUR 8.2 million, representing a lower level for EUR 0.6 million marked at the end of June of the previous year (chart 48).

The more significant increase in expenses of 25.1%, compared to the lower increase in income of 14.6%, had an impact on the sector to have a weaker financial performance compared to the previous year.

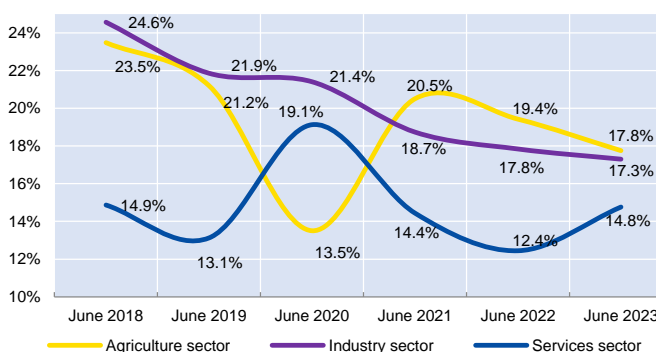
Within income, interest income, representing the dominant category of income (91.3%), recorded an annual increase of 18.6% (16.7% until June 2022), as a result of the significant increase in lending, in the previous two years. The non-interest income, until June of 2023, marked an annual decrease of 15.3% (an increase of 57.7% marked in the previous year), as a result of the decrease of the category of other operating income.

Chart 46. Average interest rate on microfinance sector loans



Source: CBK.

Chart 47. Average interest rate on loans to enterprises, by economic sectors



Source: CBK.

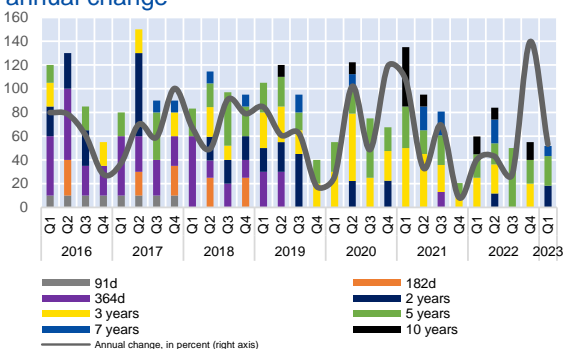
In the context of expenses, the increase mainly was attributable to personnel and administrative expenses. This subcategory marked an annual increase of 16.1% (22.5% in the previous year), which may be attributed to the increase of expenses for employees' salaries in order to maintain inflation adjustment, and to a lower extent to administrative expenses. Meanwhile, the category of interest expenses (24.8% of total expenses) recorded an annual increase of 44.2% at the end of June 2023 (-0.1% in the previous year), reflecting the increase of the level of borrowings from the external sector, as well as from the increase in the cost of financing which was a result of the increase of interest rates. The level of nonperforming loans to total loans remains low and it further declined by 0.4 percentage points, dropping to 1.8%. Whereas, the coverage level of nonperforming loans with loan loss provisions, in June 2023, increased to 151.7% (144.5% in June 2022) (chart 49).

Republic of Kosovo's Government securities market

For the first time since the beginning of the issuance of securities by the Treasury Department within the Government of Kosovo, there were no new issuance of state debt in the second quarter of the year, because the foreseen auctions were canceled. Below are presented

the data on the progress of the issuance of securities during the period January-March 2023.

Chart 50. Amount and maturity of issued debt, annual change

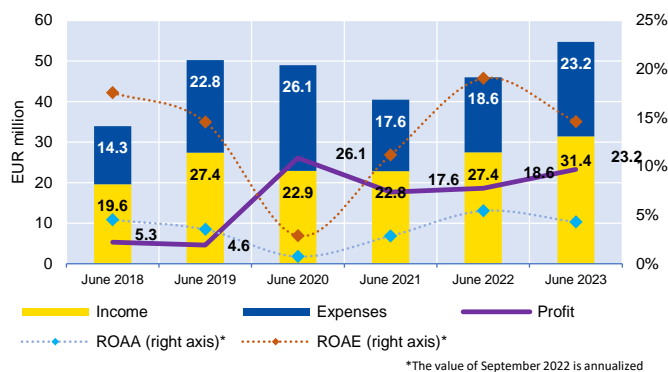


Source: Ministry of Finance, Labor and Transfers.

Issuance of government securities, up to March 2023, was significantly lower compared to the same period of the previous year, while the demand to invest in these securities continued to exceed the supply side of the government.

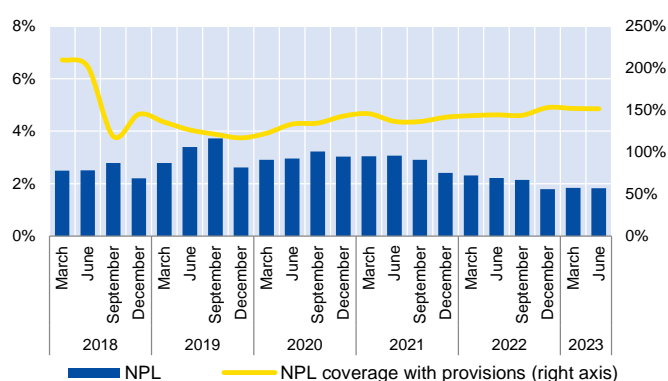
Until March 2023, Kosovo's Government issued debt with a value of EUR 51.8 million, which is for 13.4% less than in the previous year (chart 50). Meanwhile, the demand to invest, in the absence of investment alternatives for asset diversification, has continuously exceeded the supply side. The demand to invest in

Chart 48. Profit and profitability indicators of the microfinance sector



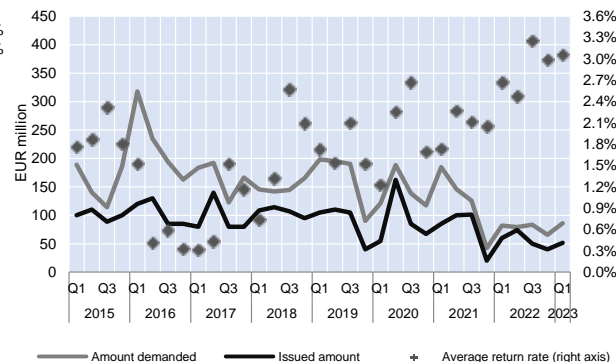
Source: CBK.

Chart 49. Quality indicators of credit portfolio



Source: CBK.

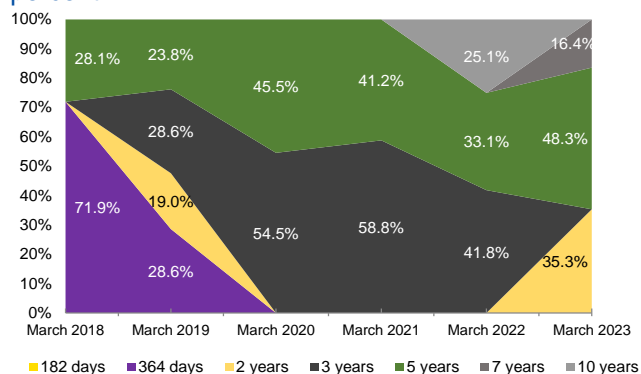
Chart 50a. Bid to cover ratio



Source: Ministry of Finance, Labor and Transfers.

securities of Kosovo's Government was 1.66 times higher than the amount offered by the Government, while in the previous year it was 1.37 times higher (chart 50a). The main investors in government debt in the form of securities are pension funds, which, this year have increased their share to total government debt to 64.1% from 62.5% in March 2022, while commercial banks have reduced their share to 30.4% from 32.7% as it was in the previous year. Until March 2023, the stock of Kosovo's Government securities held by commercial banks, pension funds and insurance companies reached the value of EUR 859.2 million (EUR 873.3 million in March of the previous year). The structure of Kosovo's Government securities, over the years, has undergone gradual changes towards the issuance of securities with longer maturities. During the period of January-March 2023, the structure was dominated with 48.3% by government bonds with a maturity of "5 years", unlike in the previous year, when the issuances of "3 years" government bonds had a share of 41.8% (chart 51).

Chart 51. Government securities structure, in percent



Source: Ministry of Finance, Labor and Transfers.

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World Bank: Commodity Markets: [Commodity Markets \(www.worldbank.org\)](#)



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