BANKING AND PAYMENTS AUTHORITY OF KOSOVO
AUTORITETI BANKAR DHE I PAGESAVE TË KOSOVËS
BANKARSKI I PLATNI AUTORITET KOSOVA

BPK BULLETIN

(Structure of Commercial Banking Sector)

Research
and Statistics
Department

No.1

Pristina 2005

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PUBLISHER Banking and Payments Authority of Kosovo
Research and Statistics Department
33 Garibaldi, Prishtina
Telephone:++381 38 222 243
Fax: ++381 38 243 763

WEB www.bpk-kos.org
E-mail research@bpk-kos.org

PRINTED BY "TEKNIKA" Prishtinë.

Printed in 100 copies.

ABREVIATIONS

ABK	American Bank of Kosovo
ATM	Automated Teller Machine
BE	Economic Bank
BKP	Credit Bank of Pristina
BPB	Bank for Private Business
BPK	Banking and Payments Authority of Kosovo
BRK	New Bank of Kosovo
DEM	Deutsche Mark
EBRD	European Bank for Reconstruction and Development
EUR	Euro
FMO	Financ. Maatschappij voor Ontwikkelings-landen
GDP	Gross Domestic Product
HHI	Herfindahl-Hirschman Index
IFC	International Finance Corporation
IMF	International Monetary Fund
IMF(IMI)	Investment Micro Finance
KFW	Kreditanstalt für Wiederaufbau
KSB	Kasabank
MEB	Micro Enterprise Bank
MEF	Ministry of Economy and Finance
NIM	Net Interest Margin
PCB	ProCredit Bank
PISG	Provisional Institutions of Self Government
RBKO	Raiffeisen Bank of Kosovo
ROAA	Return on Average Assets
ROAE	Return on Average Equity
RZB	Raiffeisen Zentralbank
UNMIK	United Nations Mission in Kosovo

List of Tables

Table 1	**Commercial banking structure by total assets**
Table 2	**Employees and banking units in the commercial banking sector**
Table 3	**Structure of commercial banking sector assets**
Table 4	**Structure of commercial banking sector liabilities**
Table 5	**Structure of commercial banking sector capital**
Table 6	**Structure of commercial banking sector income statement**

List of Figures

Figure 1	**Number of banks**
Figure 2	**Geographical distribution of banking units**
Figure 3	**Percentage change in the number of banking units**
Figure 4	**Number of banking units and ATMs by bank groups**
Figure 5	**Indicators of productivity per employee**
Figure 6	**Herfindahl-Hirschman Index**
Figure 7	**Share of three largest banks assets (deposits, loans) to total assets (deposits, loans)**
Figure 8	**Structure of loans by institutional sectors**
Figure 9	**Structure of loans by industry**
Figure 10	**Structure of loans by maturity**
Figure 11	**Maturity structure of deposits – Depositor structure of deposits**
Figure 12	**Capital adequacy ratio**
Figure 13	**Structure of income**
Figure 14	**Structure of expenses**
Figure 15	**Overhead cost to gross income**
Figure 16	**Return on average assets**
Figure 17	**Return on average equity**
Figure 18	**Net Interest Margin**
Figure 19	**Liquid assets to total assets**
Figure 20	**Structure of liquid assets of total banking sector**
Figure 21	**Loan to deposit ratio**

List of Boxes

Box 1	**Composition of the bank groups**
Box 2	**Productivity by banking groups**
Box 3	**Main categories of assets by banking groups**
Box 4	**Loans granted by banking groups**
Box 5	**Main categories of liabilities by banking groups**
Box 6	**Deposits structure by banking groups**
Box 7	**Structure of capital by banking groups**

Contents

1. Introduction **4**

2. Structure of Commercial Banking Sector in Kosovo **7**

2.1 Banking Population 7
2.2 Geographical Distribution of Banking Units 9
2.3 New Technology 10
2.4 Employment 11
2.5 Concentration in the Banking Activity 14

3. The Structure of Balance Sheet of Commercial Banks in Kosovo **15**

3.1 Structure of Assets 15
3.11 Loans Granted by Commercial Banks in Kosovo 17
3.2 Structure of Liabilities 20
3.21 Deposits of Commercial Banking Sector 22

4. The Structure of Capital of Commercial Banks in Kosovo **25**

5. Financial Performance of Commercial Banks in Kosovo **27**

5.1 Structure of Income and Expenditure Statement 27
5.11 Main Components 27
Structure of Income 28
Structure of Expenditures 29
5.2 Profitability and Efficiency 31
5.3 Liquidity 33

Notes on Methodology **36**

List of banks **43**

1. Introduction

The Banking and Payments Authority of Kosovo (BPK) is launching the new publication "BPK Bulletin" with the aim informing in more detail the public on the main developments in the financial sector in line with regulatory responsibility of the BPK. This issue will put emphasis on the structure of the commercial banking sector which represents largest component of the financial sector in Kosovo. Apart from indicators which reflect main developments in the banking sector as a whole, to facilitate the analysis, the commercial banks are divided in two groups, group 1 comprising banks with majority owned foreign capital and group 2 comprising banks with majority owned domestic capital.

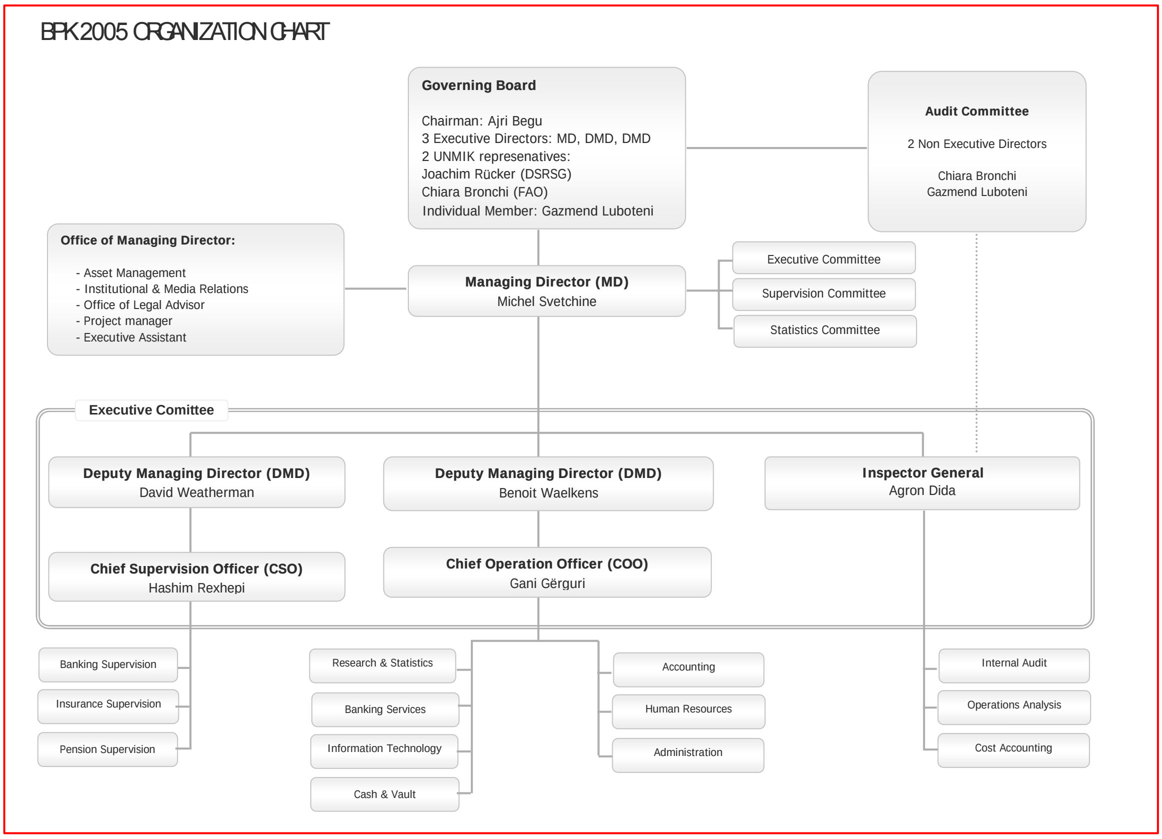
The BPK is established in November 1999 based on the UNMIK Regulation 1999/20, amended in UNMIK Regulation 2001/24, as a public legal entity. The principal objectives of the BPK are to:

- Foster an efficient and safe system for domestic payments;
- Foster the liquidity, solvency, and efficient functioning of a stable market-based financial system, including regulating banks, insurance companies and other financial institutions.

Within these objectives the BPK has, among others, the following specific powers to:

- Recommend broad policy guidelines to the Special Representative of the Secretary-General in areas under its responsibility, under the guidance of the Deputy Special Representative for Economic Reconstruction and Development;
- Conduct regular economic and monetary analysis of the Kosovo economy, make public the results, and submit proposals and measures to the UN Interim Administration in Kosovo on the basis of such analysis;
- License, supervise, and regulate financial institutions and dealers in foreign exchange;
- Act as banker and fiscal agent to the PISG (MEF) and to provide financial advice at its request,

In 2004 the BPK adopted the new organization structure consisting two main pillars: **Supervision of Financial Institutions** and **Operations,** and the function of the **Inspector General**. The reorganization was in the function of Kosovarisation process of the BPK where two high-level management positions were created, namely functions of Chief Supervision Officer and Chief Operations Officer. Also the reorganization was in the function of adjustment to specific tasks and activities that will provide grounds for higher quality of executive and work performance.



As shown in the organizational chart, the first level consists of **BPK Governing Board** that formulates policies, which are then executed by the BPK Management and staff.

Under the Section 9 of the BPK regulation, the BPK shall inform the public on a regular and timely basis of its analysis of macroeconomic and financial market developments and on related statistical information. Research and Statistics Department of the BPK publishes in its Monthly Statistics Bulletin statistics covering entire financial system and other sector statistics. Financial sector statistics has improved in quality and coverage in line with international standards that creates the grounds for analytical work. This will be developed through new publications namely, BPK Bulletin and Working Paper series.

This issue aims to describe key developments in the commercial banking system in Kosovo. The banking sector in Kosovo experienced continuous positive developments in five years of its operation. The banking sector balance sheet total grew by 37.1% in 2004 to 797.0 EUR million, influenced mainly by the continuous expansion of lending and the rise in deposits.

Commercial banks concentrated their lending towards private non-financial corporations, though loans to households experienced improvement in 2004. Up till 2004, deposits were mainly shorter term, whereas in 2004 other (time and savings) deposits composed 59.2% of total consumer deposits. Commercial banks ended their financial year with 90.5% increase in net profits, with net interest income being the largest component. Profitability and cost efficiency also experienced improvement during the course of 2004. The commercial banks' capitalization remains adequate.

2. Structure of Commercial Banking Sector in Kosovo

2.1 Banking population

The banking sector is the largest component of Kosovo's financial sector. As of end 2004, banking sector assets accounted for an excess of 85.0 % of total financial system assets. Immediately, after the war in 1999, there were no banks operating in Kosovo whereas transactions were developed in cash. The first bank established in January 2000 was Micro Enterprise Bank (MEB), now named ProCredit Bank, which was mainly owned by the development agencies and foreign financial institutions. Between March and November 2001 banking sector in Kosovo registered an increase in the number of banks, as six other banks were established which in turn contributed to the increase in competition in the provision of banking services. Although no new bank was granted with a license from the BPK since then, Kosovo’s commercial banks expanded significantly their network through the increase in the number of their operating units accompanied by a provision of a wide range of products.

As of December 2004, banking sector in Kosovo consisted of seven commercial banks: ProCredit Bank (PCB), Raiffeisen Bank of Kosovo (RBKO), New Bank of Kosovo (BRK), Bank for Private Business (BPB), Economic Bank (BE), Kasabank (KSB), and Credit Bank of Pristina (BKP).

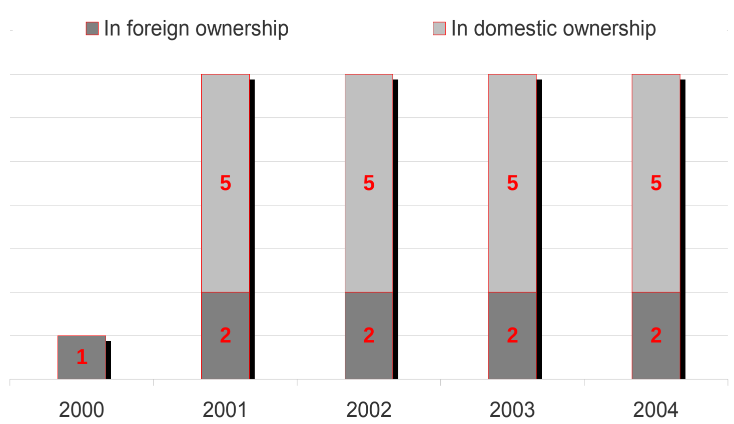
To facilitate the analysis of the banking sector, banks have also been classified into two groups and are commented in the boxes of different chapters. The criterion of banks' majority ownership (foreign versus domestic), which captures the size effect as well, is used as the basis for the analysis of banks in addition to the analysis of the banking sector as a whole. As of end 2004, Group I consisted of two banks in-full-foreign ownership, whereas Group II consisted of five banks with majority (though there are minority foreign shareholders) domestic ownership.

Box 1. Composition of the bank groups

Group I	Group II
	New Bank of Kosovo (BRK)
ProCredit Bank (PCB)	Bank for Private Business (BPB)
Raiffeisen Bank of Kosovo (RBKO)	Economic Bank (BE)
	Kasabank (KSB)
	Credit Bank of Pristina (BKP)

As depicted in Figure 1, the ownership structure of the banking sector does not appear to have changed over this period of four years. However, there were some changes in Group I banks considering that in November 2003 MEB has been transformed into the ProCredit Bank, which is still owned by the development agencies and foreign financial institutions such as EBRD, IFC, FMO (the Netherlands), KFW, IMF (Investment Micro Finance, Frankfurt) and Commerzbank. Additionally, in November 2001, American Bank of Kosovo (ABK) has been transformed into the Raiffeisen Bank of Kosovo (RBKO), following the purchase of 76.0 % of ABK by the Raiffeisen Zentralbank Österreich AG (RZB-Austria) and since July 2003 RBKO is fully owned by RZB-Austria.

Figure 1. Number of banks



With respect to the size of assets at end-2004, Group I bank assets accounted for 62.0 % of total banking system assets, testifying in this way the continuing concentration in the banking system, which is principally dominated by the two largest banks in majority foreign ownership.

Table 1. Commercial banking sector structure by total assets, in EUR thousands and percentage share

	Group	2000	Share in %	2001	Share in %	2002	Share in %	2003	Share in %	2004	Share in %
I	In foreign ownership	102,964	100.0	385,315	74.2	344,380	73.1	370,869	63.8	494,539	62.0
II	In domestic ownership	-	0.0	133,670	25.8	126,813	26.9	210,614	36.2	302,528	38.0
	Banking sector total	**102,964**		**518,985**		**471,193**		**581,483**		**797,067**	

Despite the fact that the largest share of total assets is registered for by Group I banks, over the observed period, the concentration of banks with foreign ownership in terms of their asset size has gradually decreased (see table 1). As of end 2003, the share of Group I banks assets in total assets decreased by 9.3 percentage points relative to the end 2002 reaching the share of 63.8 % in total banking system assets. This decrease in the share of Group I assets in total banking sector assets continued, but to a lesser extent in 2004, representing a fall in the share by 1.8 percentage points.

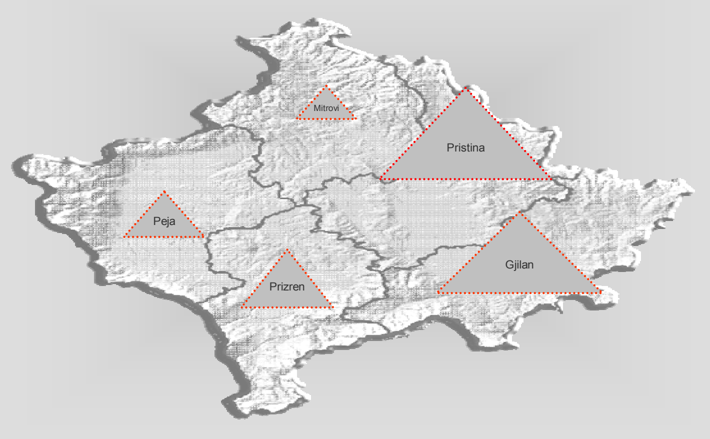
2.2 Geographical Distribution of Banking Units

There were 217 banking units (branches and sub-branches) operating in Kosovo as of December 2004, covering a wide geographical area and being present in all five main regions[1]. Although no new bank has been licensed during the 2001-2004 period, commercial banks have increased their number of banking units in Kosovo with 70 new opened units in 2004. Even if the year-on-year comparison shows significant differences, the yearly average of new opened units reached around 50.

With respect to the regional distribution of operating units, as of end 2004, the highest concentration of banking units was in Pristina, accounting for 25.6 % of total operating units in Kosovo (see figure 2). The second largest concentration was in Gjilan which represents 24.6 % of total operating units. The three remaining regions show mutually comparable shares: Prizren (17.4 %), Peja (16.9 %), and Mitrovica (15.5 %).

[1] Note that the municipalities throughout Kosovo comprise particular region f.i. Ferizaj is included in the Gjilan region. We based our analysis in the five main regions of Kosovo which are: Pristina, Prizren, Peja, Mitrovica and Gjilan.

Figure 2. Geographical distribution of banking units, as of end 2004



As illustrated in figure 3, in 2004 compared with 2003, the largest change in the number of banking units was recorded for by the Prizren region (80.0 %). The next largest increase in relative terms is recorded in Pristina region (55.9%), Mitrovica (39.1 %), and Peja (29.6 %). Gjilan recorded for the smallest change during 2004 with an increase of 18.6 %.

Figure 3. Percentage change in the number of banking units, as of end 2004

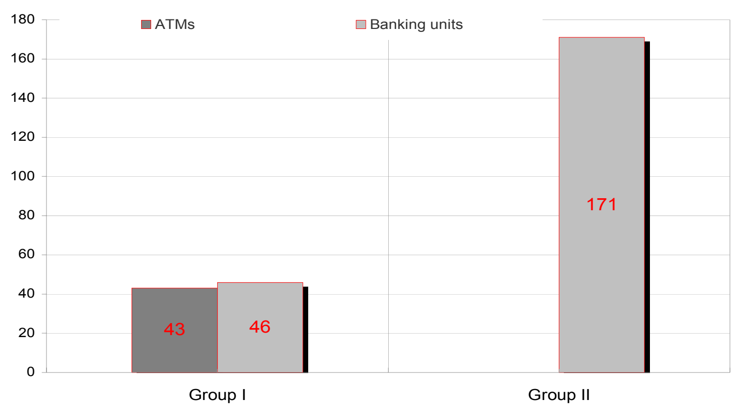
Group II banks, representing 38.0% of total assets, had the largest number of banking units at end-2004. Accounting for 80.2 % of total number of operating units in Kosovo, they expanded their number of operating units in 2004 with 39.3%

2.3 New Technology

From 2002 onwards, banks in Kosovo are optimising their banking network by utilising new technology. The establishment of new technology has enabled banks to increase the security in providing their services, widen the range of the products they provide and creating in turn grounds for them to increase their efficiency. Moreover, new technology (ATMs) has enabled clients to use banking services directly and continuously throughout 24 hours.

As of December 2004, the number of ATMs in the banking sector reached 43. As evidenced by figure 4, Group I banks accounted for 100 % of the total ATMs installed throughout the region, suggesting that new technology in the banking system is initiated by banks in majority foreign ownership.

Figure 4. Number of Banking units and ATM's by Bank Groups, as of end 2004



Following the trend of development of the world banking as well as the changing behaviour of population in Kosovo towards better use of banking services, banks have provided their clients with other new products such as credit and debit cards (Visa, Master Card, Maestro Card) which are mainly promoted by the banks in majority foreign ownership.

As for the regional distribution of ATMs, Pristina region represents 41.9 % of total installed ATMs. The next largest concentrations are Peja and Gjilan (18.6% and 16.3%), whereas Mitrovica and Prizren are the least concentrated regions each accounting for 11.6% of total ATMs installed.

2.4 Employment

In 2004, the trend towards increasing banking units was accompanied with a rise in employment by commercial banks, which by the end of 2004 reached 2,068 full time equivalent employees. In 2004, employment in the banking sector rose by 23.4 % against 20.3% in 2003.

A labour productivity indicator, expressed by the number of employees per banking unit, has shown continuous improvement during the 2001-2004 period (see table 2). In 2004, the number of employees per banking unit amounted 10 which compared to 2001 represents a decrease of 13 employees per banking units. Even so, we should exercise a caution when making a comparison with 2000 and 2001 given that only few banks were operating in Kosovo[2].

Table 2. Employees and Banking Units in the commercial banking sector

Description	2001	2002	2003	2004
No. of banking units	28	110	147	207
No. of employees	637	1,393	1,676	2,068
No of employees per banking unit	23	13	11	10
Total Assets				
Per banking unit, in '000 EUR	18,535	4,284	3,956	3,851
Per employee, in '000 EUR	814.7	338.3	346.9	385.4
Number of citizens (in thousands)	1,867	1,899	1,931	1,964
Per banking unit	66,679	17,264	13,136	9,488
Per employee	2,931	1,363	1,152	950
Loans				
Per employee, in 000' EUR	40.7	62.1	138.9	181.0
Per banking unit, in 000' EUR	925.6	786.3	1,583.5	1,808.4
Deposits				
Per employee, in 000' EUR	772.8	306.7	306.7	331.6
Per banking unit, in 000' EUR	17,581	3,884	3,497	3,313

In addition, the size of assets managed by an operating unit does not point to the rationalisation of banking activities due to the fact that as of end 2004 the volume of assets managed by an operating branch fell, although at a slower rate, as compared to the preceding year. As of end 2004, assets managed per banking unit amounted to 3,9 EUR million which corresponds to a decrease of 2.7% against a decrease of 7.7% in 2003. The increased is most marked for the loans, where the volume of loans granted by a banking unit increased with 14.2% in 2004. On the deposit side, the volume managed by banking unit decreased in 2004 by 5.3% amounting to 3,3 EUR million.

However, productivity measured by the size of assets managed by an employee, reveals an increase over the last three years. The total assets managed by an employee amounted to 385,400 EUR at end-2004 against 346,900 EUR at end-2003 representing a growth of 11.1%. Though, we should also pay attention to the workload during the period of conversion of DEM

[2] Mainly in the large cities

into EUR in 2001, which may also overestimate the productivity indicators during this period. For the total banking sector, loans granted per employee experienced an increase by 30.1% in 2004 compared to 2003, reaching 180,691 EUR, whereas deposits per employee grew by 9.2% and amounted to 331,571 EUR.

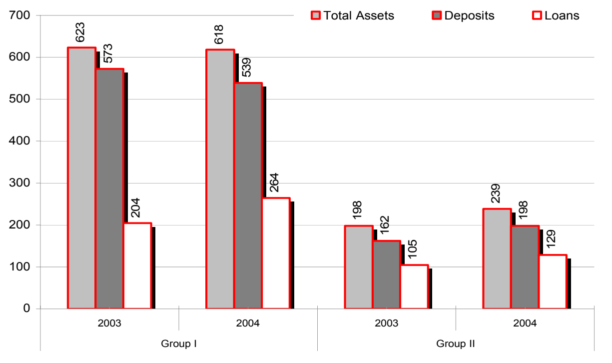
With respect to the indicator of "bankarisation" in Kosovo, measured by the number of inhabitants served by a banking unit, table 2 reveals that the indicator experienced a downward trend. In 2003, the number of citizens per banking unit amounted to 13,136 which is a decrease of 23.9% compared with 2002. Following this decrease, in 2004 the number of citizens served by a banking unit further went down to 9,488, a decrease of 27.8%. Similar picture is revealed from the indicator measuring the number of citizens served by an employee, which in 2004 decreased by 17.6% against 15.5% in 2003 and reached 950 citizens per employee.

Box 2. Productivity by banking groups

Although the banks of Group I outstand the banks of Group II in terms of the level of total assets, deposits and loans per employee, the two groups show opposite tendencies.

The Group II increased all three indicators measured per employee, while Group I did so only for loans. The level of total assets and deposits managed per employee by Group II represents 38.6% (+6.8 percentage points compared to 2003) and 36.7% (+8.3 percentage points compared to 2003) respectively of the level reached by Group I. Regarding the loans managed by employee, the relative position of Group II diminished with 2.4 percentage points compared to 2003, reaching 48.7% of the level obtained by Group I.

Figure 5. Indicators of productivity per employee, in EUR thousands



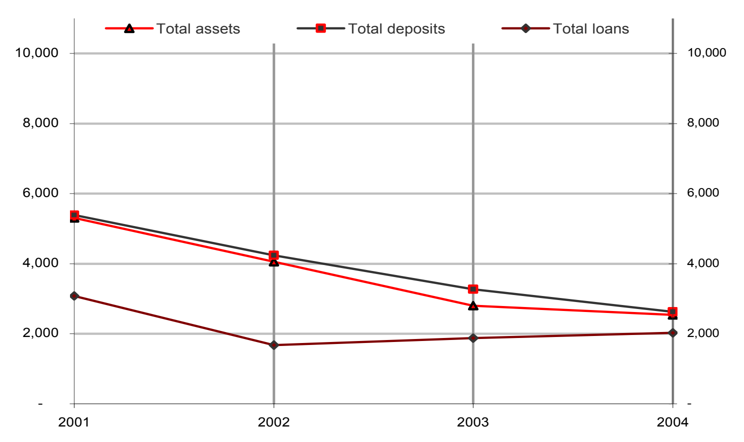
2.5 Concentration in the Banking Activity

The Herfindahl-Hirschman Index (HHI) is used to represent the developments in the structure and the change of the market shares in the banking system. As figure 6 indicates, concentration in the banking sector with respect to total assets experienced a slight decrease from 4,058 at end 2002, over 2,803 points at end-2003, to 2,536 points by end-2004.

Meanwhile, the level of the concentration for deposit taking experienced a downward trend during 2004, reaching the HHI value of 2,625 points. In addition, the concentration for deposit taking experienced a further decrease during 2003, changing from 4,239 points at end-2002 to 3,276 at end-2003. All this change in the concentration level in the banking sector might be the result of a more competitive environment.

Additionally, the increase in the index and hence the decrease of competition was observed in the loan market. During the observed period the HHI concentration for loans experienced an upward trend reaching the value of HH index of 2,053 points at end 2004 which represents an increase of 176 points relative to the end 2003 and 373 points relative to end 2002.

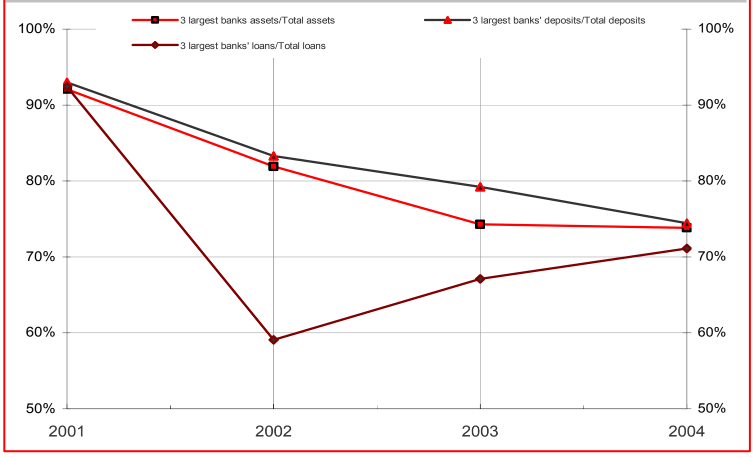
Figure 6. Herfindahl- Hirschman Index (HHI) (All banks)



Another measure of competitiveness in the banking industry is also the concentration of the three largest banks (C3). Figure 7 indicates that the market shares of the three largest banks within the domestic banking market are falling gradually as far as assets and deposits are concerned. As of end 2004, the concentration of the three major banks’ share -measured as a combined participation of the three banks in total banking sector assets- followed a downward trend.

In particular, the share of three largest banks assets in total assets fell by 0.5 percentage points and reached the share of 73.8 % of total banking system assets, while the share of the three major banks' deposits to total banking sector deposits has continuously decreased and accounted for 74.4 % at end-2004 from 79.2 % and 83.3 % at end-2003 and 2002, respectively. On the other hand, the C3 concentration on loans granted reached at 71.1 % at end-2004, which is 4.0 percentage points higher compared with end-2003, whereas in 2002 it stood at 59.1% or 33.3 percentage points higher compared with 2001.

Figure 7. Share of three Largest Banks' Assets (deposits,loans) to Total Assets (deposits,loans)



Regarding the defined group of banks' share, Group I accounted for 62.0% of total assets as of end 2004. The share of Group I banks in total banking sector loans reached 56.4%, which represents 4.2 percentage points increase compared with 2003, while the share of Group I banks in total banking sector deposits decreased by 3.4 percentage points accounting for 63.0 % of total deposits in 2004.

3. The Structure of Balance Sheet of Commercial Banks in Kosovo

3.1 Structure of Assets

Commercial banks in 2004 experienced a further growth in their total assets influenced mainly by the increase in lending on the asset side and a rise in deposits on the liability side.

Total banking sector assets stood at 797.0 EUR million as of end-2004, an increase of 37.1% (or 215.6 EUR million) relative to the end 2003. Total banking sector assets grew from 32.4% of GDP in 2003 to 42.1% of GDP in 2004, whereas they represented 27.2% of GDP in 2002. The share of the main categories of assets in total assets is presented in the table 3. As indicated in the table, liquid and less risky assets (cash, balances with BPK, placements in banks abroad and investments in foreign securities) experienced substantial changes during this five-year period. As of end 2004, they experienced an increase of 24.7% with respect to their volume and amounted to 413.9 EUR million. In terms of their share to balance sheet total, liquid assets experienced a continuous decrease which by the end of 2004 accounted for 51.9% of balance sheet total, representing a decrease of 5.2 and 27.5 percentage points compared with 2003 and 2002, respectively.

Table 3. Structure of commercial banking sector assets, in EUR thousands and percentage

Description	Dec. 2001		Dec. 2002			Dec. 2003			Dec. 2004		
	Amount	Share in %	Amount	Share in %	%∆	Amount	Share in %	%∆	Amount	Share in %	%∆
Currency	88,342	17.0	35,597	7.6	-59.7	46,611	8.0	30.9	43,293	5.4	-7.1
Balance with BPK	176,793	34.1	45,740	9.7	-74.1	59,569	10.2	30.2	73,000	9.2	22.5
Loans to financial corporations(placements)	212,753	41.0	292,725	62.1	37.6	106,205	18.3	-63.7	185,815	23.3	75.0
Securities	7,498	1.4	-	-	-	119,620	20.6	-	111,778	14.0	-6.6
Gross loans to non-financial sector	25,916	5.0	86,498	18.4	233.8	232,773	40.0	169.1	374,339	47.0	60.8
Less: provisions for loan losses	781	0.2	2,522	0.5	222.9	7,715	1.3	205.9	15,947	2.0	106.7
Net Loans	25,135	4.8	83,976	17.8	234.1	225,058	38.7	168.0	358,392	45.0	59.2
Property and equipment, net of depreciation	4,544	0.9	9,498	2.0	109.0	12,265	2.1	29.1	15,051	1.9	22.7
Interest receivable and other assets	3,920	0.8	3,657	0.8	-6.7	12,155	2.1	232.4	9,738	1.2	-19.9
Total assets	**518,985**	**100**	**471,193**	**100**	**-9.2**	**581,483**	**100**	**23.4**	**797,067**	**100**	**37.1**

As of end 2004, the volume of cash and balances with BPK amounted to 116.3 EUR million which represents an increase of 9.5 % compared with 2003. However, with respect to their share in balance sheet total, cash and balances with BPK of the total banking sector experienced 3.7 percentage points decrease mainly due to the decrease in cash, and by the end of 2004 accounted for 14.6% of total assets.

Accounting for a substantial share in total assets, placements in banks abroad and investments in (foreign) securities amounted to 297.6 EUR million at end-2004, an increase by 31.8% compared with 2003. Even though they experienced an increase in outstanding amounts, in 2004, their share in balance sheet total decreased by 1.5 percentage points which was mainly as a result of the decrease of investments in foreign securities which represent 37.6% of total investments abroad.

The lower share of investments abroad was mainly compensated by a higher share of customer credits granted by banks which in 2004 grew by 7.0 percentage points compared with 2003. In addition, they generated positive contribution to the growth of assets by 24.3% and at end 2004 amounted to 374.3 EUR million.

Box 3. Main categories of assets by banking groups

Share of Group I in total banking sector in 2004 and change in percentage points against 2003:

48.2% of Cash and balances with BPK (-4.9 percentage points)

74.1% of placements and investments in securities (-8.8 percentage points)

56.4% of Loans (+4.2 percentage points)

Within Group I, the share of cash and balances with BPK represented 11.3% of total assets as of end 2004 or down by 3.9 percentage points compared with 2003. The corresponding share within Group II was 19.9%, also a decrease of 3.8 percentage points compared with 2003.

Similarly, the share of placements and investments in securities abroad of Group I as part of its total assets reduced and accounted for 44.6%. On the contrary, Group II banks increased in 2004 their placements and investments in securities abroad as a share in their total assets to 25.4%, an increase by 7.1 percentage points compared with 2003.

The share of Group I loans in total Group I assets increased from 32.8% in 2003 to 42.7% in 2004. The share of loans provided by Group II to total Group II assets increased slightly from 52.8% in 2003 to 53.9% in 2004.

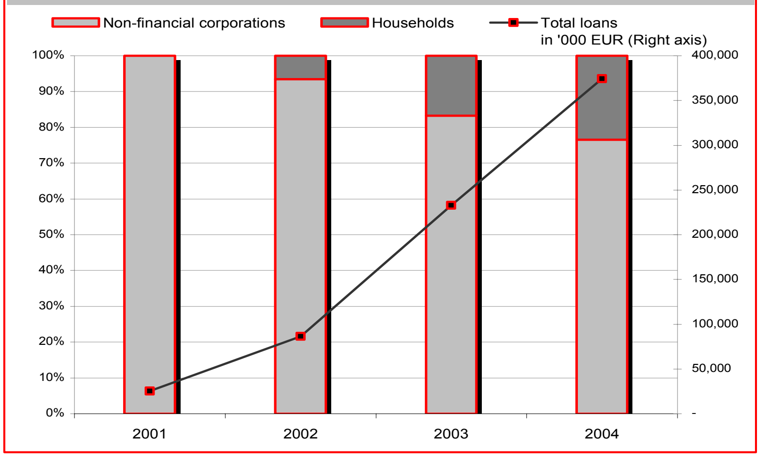
3.1.1 Loans Granted by Commercial Banks in Kosovo

From 2002 onwards, commercial banks in Kosovo have continuously improved their role in providing intermediation to the domestic economy. Loans grew with 60.8% in 2004 with private non-financial corporations being the largest beneficiaries, though loans to households boost with 125.7%. Trading industry is the largest beneficiary whereas commercial banks are directing their activity towards longer-terms loans, with loans over one year accounting, since 2004, for the largest share to total loans.

As of December 2004, total outstanding gross loans granted by banks amounted to 374.3 EUR million, which represents a year-on-year increase of 60.8%. The volume of net loans attained 358.4 EUR million, or a year-on-year increase of 59.2%. Furthermore, the growth rate of loans was higher than the growth of GDP. In 2004, the share of total loans to GDP accounted for 19.7% representing an increase of 6.8 percentage points compared with 2003. The share of loans to balance sheet total reached 47.0% which corresponds to 7.0 percentage points increase compared with 2003.

The volume of loans granted to non-financial corporations increased from 193.9 EUR million in 2003 to 286.6 EUR million in 2004 (see figure 8), which represents an increase of 47.8% compared with 2003. However, loans to non-financial corporation experienced a reduction (6.7 percentage points compared with 2003) in terms of their share to total loans, and they accounted by the end of 2004 for 76.6% of total loans.

Figure 8. Structure of Loans by institutional sectors

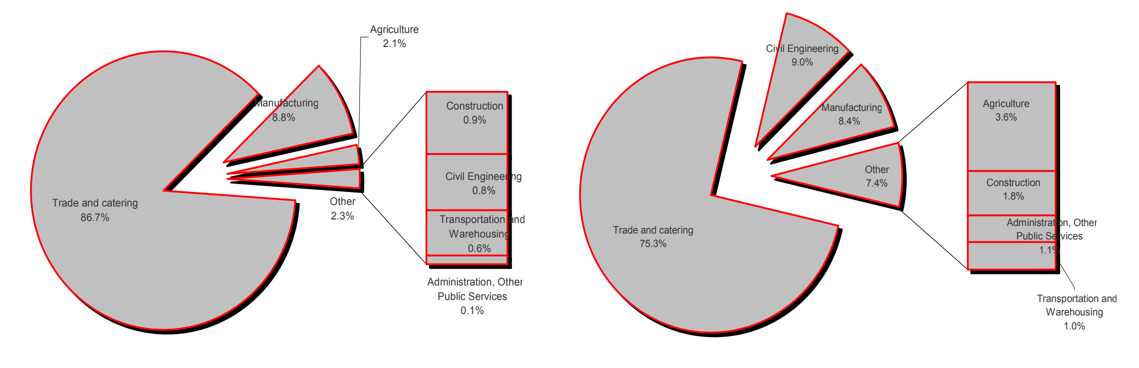


Loans granted to non-financial corporations, were for 99.6% channelled to private enterprises representing an increase of 47.8% compared with 2003 whereas the volume as well as the share of loans granted to public and social enterprises remains negligible.

The volume of loans granted to households attained 87.8 EUR million in 2004, which in comparison to 2003 represented an increase by 125.7% pointing to a significant increase in loan activities towards households. Following their increase in volume, loans extended to households increased in terms of their share to total loans as well. In 2004, the share of loans granted to households reached 23.4% which correspond to 6.7 percentage points increase compared with 2003.

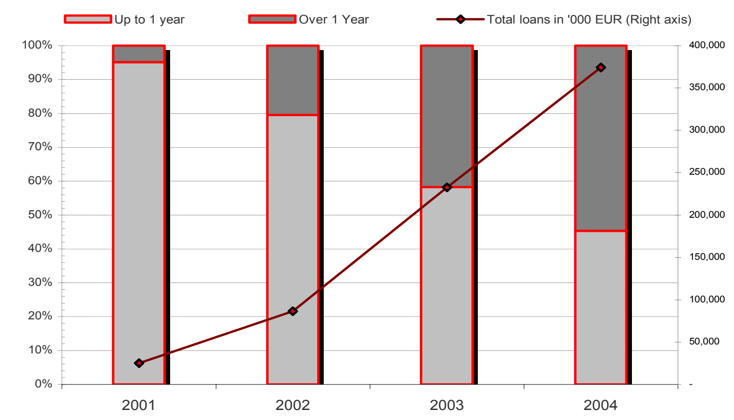
The structure of loans by economic activity continued to be in proportion to the industry structure of the economy of Kosovo, where the trade had the dominant position. As of end 2004, from the total volume of loans granted by the banking sector, 214.3 EUR million were channelled to the trading industry which corresponds to 15.7% year-on-year increase. As illustrated in figure 9, the share of loans channelled to the trading industry reduced in 2004 to 75.3% while in 2003 they accounted for 86.7% of total loans.

Figure 9. Structure of loans by industry, Dec. 2003, in % Dec. 2004, in %



Additionally, significant increase is recorded for by the loans granted to civil engineering (25.6 EUR million by end-2004), increasing their share to total loans to 9.0%, an increase of 8.2 percentage points compared with 2003. The share of loans to manufacturing industry (23.8 EUR million as of end 2004) in total loans remained stable around 8.4%, while agriculture, with outstanding loans of 10.1 EUR million, increased their share with 1.5 percentage points to 3.6%. The loans to administration and public services increased in 2004 their share in total loans to 1.1%, against 0.1% in 2003.

Figure 10. Structure of Loans by maturity



As illustrated in figure 10, the term structure of loans has also experienced changes during the course of 2004. In 2004, loans with maturities of over one year amounted to 204.6 EUR million in 2004 which corresponds to the increase of 110.7 % compared with 2003. Owing to this significant increase in volume, loans with maturities of over one year experienced an increase in their share to total loans as well, reaching 54.7% in 2004.

Loans with maturities of up to one year amounted to 169.8 EUR million which represents an increase by 25.1% on year-on-year basis. Their share in total loans decreased by 12.9 percentage points in 2004 compared with 2003, accounting for 45.3% of total loans.

Box 4. Loans granted by banking groups

Representing with over 60.0 % of total banking sector assets in 2004, Group I banks managed 56.4 % of total loans granted. While their share in total banking sector loans granted to non-financial corporations accounted for 53.0 %, their share in loans granted to households accounted for 68.3 %.

Group I banks were relatively, compared to Group II banks, less active in lending to non-financial corporations given that at end-2004 loans to non-financial corporations represented 71.6% of their total loans while for Group II they accounted for 83.0% of their total loans.

Group I banks represent 29.4% of total banking sector loans up to one year; an increase of 1.4 percentage points compared with 2003, and 78.9% of total banking sector loans with longer term maturities.

3.2 Structure of Liabilities

The liabilities of the banks are dominated by deposits. The composition within those deposits has undergone a substantial change overtime in which the transferable deposits represent the lesser part since 2004 given that other deposits account for 59.2% of total customer deposits Although still modest, banks continued to expand borrowings from other banks and financial institutions. Banks further increased their own funds, representing 8.5% of the balance sheet total in 2004, against 7.1% in 2002.

Following their increase in volume as of end- 2004, deposits by banks amounted to 12.8 EUR million (see table 4). Owing to this increase in their volume, in 2004, deposits by banks also increased in terms of their share in balance sheet total by 1.3 percentage points representing now 1.6% of balance sheet total.

The increased share of deposits by banks was partly compensated by lower customer deposits whose share to balance sheet total decreased by 2.4 percentage points and at end-2004 amounted to 685.7 EUR million.

Borrowings experienced a substantial increase in terms of their volume (60.3% by end 2004) amounting 14.3 EUR million, which corresponds to 0.3 percentage points increase in their share to balance sheet total .

Table 4. Structure of commercial banking sector liabilities, in EUR thousands and percentages

Description	Dec. 2001		Dec. 2002			Dec. 2003			Dec. 2004		
	Amount	Share in %	Amount	Share in %	%Δ	Amount	Share in %	%Δ	Amount	Share in %	%Δ
Deposits By banks and OFC		-		-		1,802	0.3		12,753	1.6	607.7
Customer deposits	492,257	94.8	427,194	90.7	-13.2	513,994	88.4	20.3	685,689	86.0	33.4
Transferable deposits in EUR	365,891	74.3	295,909	69.3	-19.1	290,453	56.5	-1.8	279,687	40.8	-3.7
Residents	353,584	96.6	281,380	95.1	-20.4	273,376	94.1	-2.8	269,580	96.4	-1.4
Non-financial corporations	137,089	38.8	159,882	56.8	16.6	138,969	50.8	-13.1	125,734	46.6	-9.5
Households	216,495	61.2	121,498	43.2	-43.9	134,407	49.2	10.6	143,846	53.4	7.0
Nonresidents	12,307	3.4	14,529	4.9	18.1	17,077	5.9	17.5	10,107	3.6	-40.8
Other deposits in EUR	126,366	25.7	131,285	30.7	3.9	223,541	43.5	70.3	406,002	59.2	81.6
Residents	124,789	98.8	128,280	97.7	2.8	220,605	98.7	72.0	403,443	99.4	82.9
Non-financial corporations	31,318	25.1	23,921	18.6	-23.6	87,131	39.5	264.2	185,610	46.0	113.0
Households	93,471	74.9	104,359	81.4	11.6	133,474	60.5	27.9	217,833	54.0	63.2
Nonresidents	1,577	1.2	3,005	2.3	90.6	2,936	1.3	-2.3	2,559	0.6	0.0
Borrowings	5,045	1.0	5,418	1.1	7.4	8,893	1.5	64.1	14,253	1.8	60.3
Interest Payable and other liabilities	1,249	0.2	4,046	0.9	223.9	9,742	1.7	140.8	9,253	1.2	-5.0
Subordinated debts	-	-	1,291	0.3		2,045	0.4	58.4	7,045	0.9	244.5
Total Liabilities	498,551	96.1	437,949	92.9	-12.2	536,476	92.3	22.5	728,993	91.5	35.9
Shareholder's Equity	20,435	3.9	33,244	7.1	62.7	45,007	7.7	35.4	68,074	8.5	51.3
Total liabilities and shareholders' equity	**518,986**	**100**	**471,193**	**100**	**-9.2**	**581,483**	**100**	**23.4**	**797,067**	**100**	**37.1**

Additionally, the share of subordinated debt to balance sheet total remained stable around 0.9%, amounting 9.3 EUR million. Shareholders equity, as a decisive component of own funds, recorded a significant increase in their volume in 2004, attaining 68.1 EUR million which represents 51.3% increase compared with 2003. Their share in balance sheet total reached 8.6 % in 2004 from 7.7% in 2003.

Box 5. Main categories of liabilities by banking groups

Share of Group I in total banking sector in 2004 and change in percentage points against 2003.

63.0% of total deposits (-3.4 percentage points)

49.1% of Shareholders' equity (+5.1 percentage points)

The customer deposits, representing the bulk of total deposits in the market, of Group I to their balance sheet total decreased, accounting for 87.7% in 2004 against 92.3% in 2003. On the contrary, the share of customer deposits of Group II in total Group II balance sheet total experienced a slight increase and at end-2004 accounted for 83.3% of total Group II assets.

The share of Group I shareholders' equity to total Group I balance sheet reached 6.8% as of end-2004, whereas Group II banks shareholders' equity accounted for 11.5% of Group II balance sheet total.

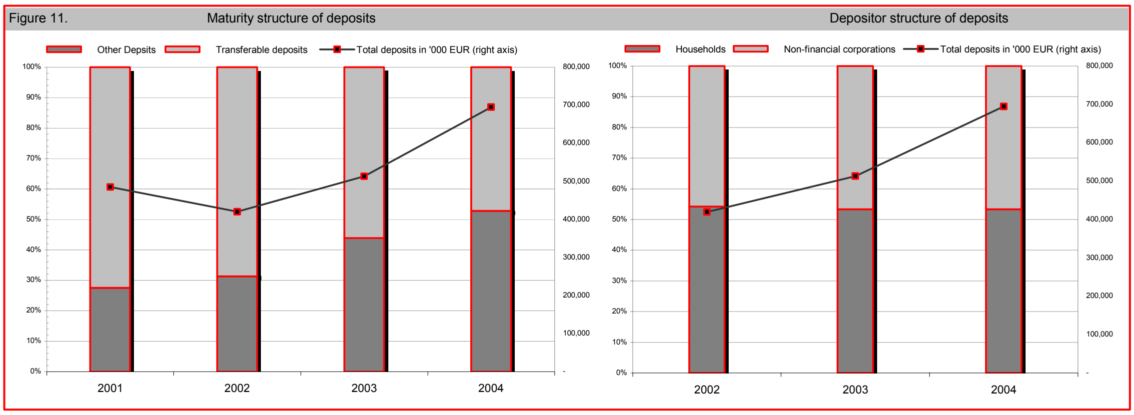
3.2.1 Deposits of Commercial Banking Sector

Customer deposits retain their position representing a decisive component of commercial banks' external funds. The largest share of customer deposits as of end 2004 consisted of deposits received by households which grew with 35.5% in 2004. Term and savings deposits represented the largest share of total customer deposits for the first time in 2004 following their increase of 62.8%.

In 2004, total banking sector deposits accounted for 36.5% of GDP which represented an increase of 7.9 percentage points compared with 2003. As of end 2004, the volume of total banking sector deposits attained 685.7 EUR million corresponding to the 34.7% increase compared with 2003.

As for the maturity structure of deposits, other deposits (time and savings) represent the most important component of total deposits. In 2004, as figure 11 shows, the volume of other deposits amounted to 366.9 EUR million representing an increase by 62.8% compared with 2003. As a result of this increase, other deposits increased as a share in total deposits as well which by the end of 2004 accounted for 52.8% of total deposits corresponding to 8.9 percentage points increase compared with 2003.

Figure 11.



As of end 2004, the volume of transferable deposits attained 327.9 EUR million or 13.9% increase compared with 2003. Their share in total deposits saw a slight decline which at end-2004 accounted for 47.2% of total deposits.

With respect to the structure of deposits by type of depositor, the largest share is registered to households' deposits. Specifically, as of end 2004, the volume of households deposits was 370.9 EUR million which compared with 2003 represented an increase of 35.5%. 53.4 % of total banking sector deposits in 2004 correspond to the deposits of households.

The volume of non-financial corporations' deposits in 2004 attained 323.9 EUR million or up by 35.3% compared with 2003. However, their share in total banking sector deposits did not experience significant change in 2004 compared with 2003 and remained at 46.6% of total deposits.

Box 6. Deposit structure by banking groups

Share of Group I in total banking sector in 2004 and change in percentage points against 2003:

70.5% of Transferable deposits (-2.3 percentage points)
56.4% of other deposits (-1.8 percentage points)
69.9% of deposits held by households
55.2% of deposits held by non-financial corporations (-7.2 percentage points)

By nature of deposit

The share of transferable deposits with Group I in total Group I deposits experienced a decline by 8.7 percentage points, though they accounted for a largest share (52.8%) in total Group I deposits. Accounting for 37.7% of total deposits of Group II, the share of Group II transferable deposits declined from 45.4% in 2003 to 37.7% in 2004.

In 2004, other deposits of Group I banks accounted for 47.2% of total Group I deposits and this corresponds to 8.7 percentage points increase compared with 2003. Even though other deposits account for a smaller proportion of total deposits of Group I, the data reveal that their share is continuously increasing with a concurrent fall of the share of transferable deposits in total Group I deposits. On the contrary, the share of other deposits of Group II in total Group II deposits accounted 62.3% in 2004, which represents an increase by 7.7 percentage points compared with 2003.

By nature of client

In 2004 Group I banks represented 69.9% of total banking sector households' deposits showing minor changes in their share compared with 2003. On the other hand, the share of households deposits of Group I in total Group I deposits increased by 3.1 percentage points in 2004 compared with 2003 and accounted for 59.2%. On the contrary, the share of households' deposits of Group II banks in total Group II deposits decreased slightly from 47.8% in 2003 to 43.5% in 2004.

Furthermore, from the total deposits received by banks in Group I, 40.8% correspond to deposits of non-financial corporations which compared with 2003 fell by 3.1 percentage points. In contrast, as of end-2004 total deposits of Group II banks were dominated by deposits of non-financial corporations which compared with 2003 rose by 4.3 percentage points and accounted for 56.5% of total Group II deposits.

4. The Structure of Capital of Commercial Banks in Kosovo

The table below illustrates the developments in the capital structure of the banking sector in Kosovo. Total banking system capital amounted to 68.1 EUR million as of end 2004, which is an increase of 51.3 % compared with 2003. Due to this increase, the share of banking sector capital in balance sheet total increased as well from 7.7% in 2003 to 8.5% in 2004.

Table 5. Structure of Commercial Banking Sector Capital, in EUR thousands and percentage

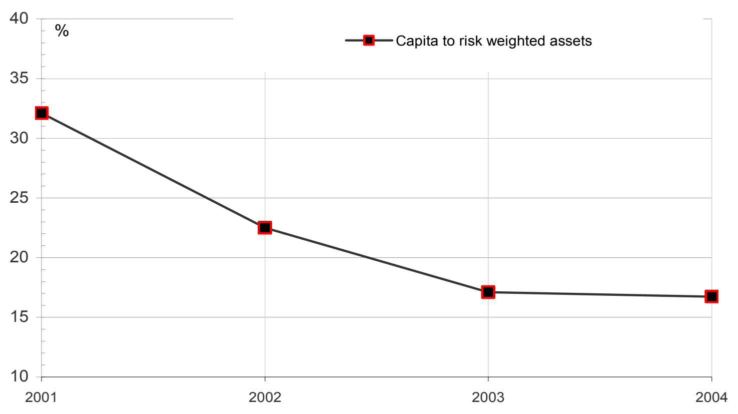
Description	Dec. 2001		Dec. 2002			Dec. 2003			Dec. 2004		
	Amount	Share in %	Amount	Share in %	%∆	Amount	Share in %	%∆	Amount	Share in %	%∆
Share capital	18,467	90.4	30,764	92.5	66.6	44,061	97.9	43.2	57,678	84.7	30.9
Contigency reserve	512	2.5	511	1.5	-0.2	511	1.1	0.0	613	0.9	20.0
General reserve	-	-	150	0.5	-	435	1.0	190.0	192	0.3	-55.9
Retained profit	1,457	7.1	1,819	5.5	24.9	-	-	-	9,591	14.1	-
Total shareholder's equity	**20,435**	**100**	**33,244**	**100**	**62.7**	**45,007**	**100**	**35.4**	**68,074**	**100**	**51.3**

Share capital, being the main component of the total banking sector capital, amounted to 57.7 EUR million as of end 2004, representing 30.9% increase compared with 2003. Its share in total capital fell from 97.9% in 2003 to 84.7% in 2004, still retaining its dominant position in total structure of capital. Another component of the structure of the banking sector capital, retained profit attained 9.6 EUR million at end 2004. Its share in total banking sector capital was 14.1%.

Using the capital adequacy ratio as the measure of the financial strength of commercial banks, usually expressed as a ratio of capital[3] to the risk weighted assets, figure 12 indicates that banks are adequately capitalized. As of December 2004, the average capital adequacy attained 16.7%, which represents year-on-year decrease of 2.3%. The banking sectors' average capital adequacy ratio in 2003 was 17.1 %, which correspond to a decrease of 5.4 percentage points compared with 2002. Capital adequacy figures continuously declined for the period of 2000-2003 as in 2000 it attained 23.0 %, whereas in 2001 it reached the highest ever ratio of 32.1%.

[3] The calculation of capital used to obtain banks' risk adjusted capital is based on the amended rule of the BPK on the capital adequacy of banks. i.e. the amount of capital which BPK requires commercial banks to hold in order to cover adequately the risks to which they are exposed, and which is based on the Basel Accord and its amendments

Figure 12. Capital adequacy ratio



The capital adequacy ratio of the banking sector as a whole has deteriorated somewhat during 2004. The growing share of loans granted to the private sector in the banking loan portfolio contributed to the faster growth of risk weighted assets relative to the rate of regulatory capital growth. However, all banks in the banking sector of Kosovo managed to maintain their capital adequacy ratio above the requirement of minimum 8%.

Box 7. Structure of capital by banking groups

Share of Group I in total banking sector in 2004 and change in percentage points against 2003

49.1% of Shareholders' equity (+5.0 percentage points)

48.2% of Share capital (-3.5 percentage points)

53.1% of Retained profit

The share of capital of Group I in Group I banks' balance sheet total increased by 1.4 percentage points and stood at 6.8%. On the contrary, the share of capital of Group II in balance sheet total of Group II experienced a slight decline and reached 11.5%.

Share capital of Group I represented in 2004 83.2% (+ 22.0% compared with 2003) of total Group I capital whereas the share of Group II share capital in total Group II capital stood at 86.2% in 2004, against 84.5% in 2003.

Group I banks' retained profit accounted for 15.2% of total Group I capital structure , an increase of 32.8 percentage points against 2003 whereas Group II experienced a slight decrease in the retained profit as a share to total Group II capital by 0.8 percentage points accounting for 13.0%.

5. Financial Performance of Commercial Banks in Kosovo

5.1 Structure of Income and Expenditure Statement

As of end 2004, banking sector in Kosovo has shown a favourable picture of its financial performance. Financial results have improved repeatedly during 2001-2004 period despite the increased competition due to expanding business activities of banks, regulatory requirements for the proper provisioning against loan losses as well as the increase in the minimum capital requirements by the BPK. Commercial banks ended their financial year with 13.0 EUR million net profits mainly on account of the increase in net interest income which grew by 73.2% in 2004.

5.1.1 Main Components

Owing to the significant increase of net interest income, the after tax profit of the banking system for 2004 stood at 13.0 EUR million, which represents 90.5% increase compared to the preceding year. On the other hand, as table 6 indicates, the before tax profit for the banking sector attained 15.1 EUR million as of end 2004 corresponding to 72.8% increase compared with 2003.

Table 6. Structure of Commercial Banking Sector Income Statement, in EUR thousands and percentage

Description	2001	2002		2003		2004	
	Amount	Amount	%Δ	Amount	%Δ	Amount	%Δ
Net Interest Income	**5,867**	**14,348**	**144.6**	**25,416**	**77.1**	**44,021**	**73.2**
Interest income	7,179	17,818	148.2	30,695	72.3	53,999	75.9
Interest expenditures	1,312	3,470	164.4	5,279	52.1	9,978	89.0
Net non-interest income	**7,895**	**8,242**	**4.4**	**7,761**	**-5.8**	**4,510**	**-41.9**
Non-Interest income	9,402	14,034	49.3	17,984	28.1	19,449	8.1
Non-Interest expenditures	1,507	5,792	284.4	10,223	76.5	14,939	46.1
General and administrative expenses	**7,271**	**19,130**	**163.1**	**25,379**	**32.7**	**33,952**	**33.8**
Net operating income	**6,491**	**3,460**	**-46.7**	**7,798**	**125.4**	**14,579**	**87.0**
Net gains/losses from dealing securities	-	-	-	342	-	-441	-228.9
Net gains/losses from dealing in foreign exchange	699	509	-27.2	658	29.3	328	-50.2
Net gains losses from foreign currency revaluations	-19	53	-380.2	-85	-260.4	593	-797.6
Net operating income before taxes	**7,172**	**4,022**	**-43.9**	**8,713**	**116.6**	**15,059**	**72.8**
Provision for taxes	456	1,306	186.7	1,912	46.4	2,104	10.0
Net profit/Loss for the period	**6,716**	**6,186**	**-7.9**	**6,801**	**9.9**	**12,955**	**90.5**
Retained profit	**1,457**	**4,068**	**179.3**	**6,801**	**67.2**	**12,955**	**90.5**

With respect to main components of the structure of income statement, significant changes were recorded for the period under review, with interest revenues recording the largest influence on the banking system profit. Thus, net interest income increased by 73.2 % compared with 2003 and amounted to 44.0 EUR million. Meanwhile, as evidenced by table 6, net non-interest income has experienced a fall by 41.9% and as a result, in 2004 they amounted to 4.5 EUR million.

General and administrative expenses increased by 33.8% in 2004 compared with 2003 and as a result they attained 33.9EUR million. However, regarding their share in total expenses, in 2004 general and administrative expenses composed 57.7% of total expenses which corresponds to 4.4 percentage points decrease compared with 2003.

The volume of banks net income from other banking activities (net gain/losses from dealing securities, net gain/losses from dealing in foreign exchange and, net gain/losses from foreign currency revaluation) in 2004 amounted to 480,000 EUR, which represents 47.5% decrease compared with 2003.

Structure of Income

From the **interest income** side, the volume of *interest income from loans* attained 48.1 EUR million as of end 2004 which is 102.3% increase compared with 2003. Moreover, the share of interest income from loans to total interest income increased as well, accounting for the largest share (89.1 %) which corresponds to an increase by 11.6 percentage points compared with 2003 (see figure 13).

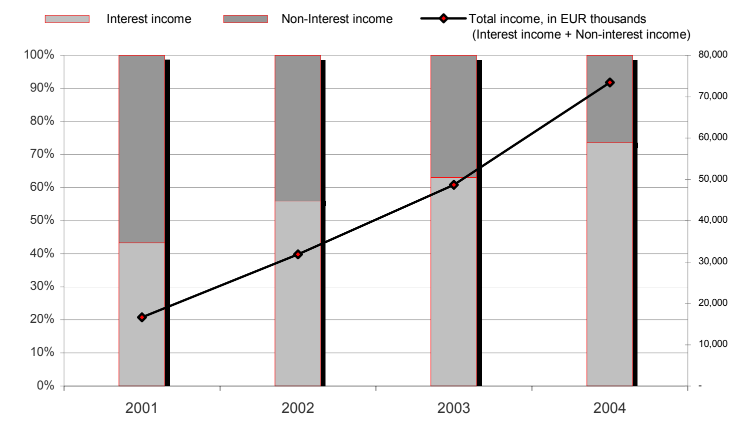
Income from placements with other banks decreased by 59.8% in 2004 compared with 2003 amounting to 2.5 EUR million. As a result, income from placements with other banks accounted for mere 4.5 % of total interest income representing a decrease of 15.3 percentage points compared with 2003.

Income from securities, mainly dominated by banks in Group I, amounted at end 2004 to 3.4 EUR million or 317.6 % increase compared with 2003. Following this significant increase in their volume, income from securities increase in terms of its share to total interest income as well and accounted for 6.4% in 2004.

The structure of **non-interest income** saw a moderate changes relative to the interest income side, which in 2004 amounted to 19.4 EUR million or 8.1 % higher compared with 2003.

With respect to the structure of non-interest income, *income from fees and commissions* increased by 4.6% in 2004 and as a result amounted to 17.5 EUR million. However, in terms of their share to total non-interest income, income from fees and commissions experienced 3.0 percentage points decline compared with 2003 and accounted for 90.1 % of total non-interest income.

Figure 13. Structure of Income



The volume of banking sector *other operating income* reached 1.9 EUR million as of end 2004, registering an increase by 56.2% compared with 2003. Due to this significant increase in their volume, banking sector other operating income also increased as a share in total non-interest income by 3.0 percentage points and amounted to 9.9%.

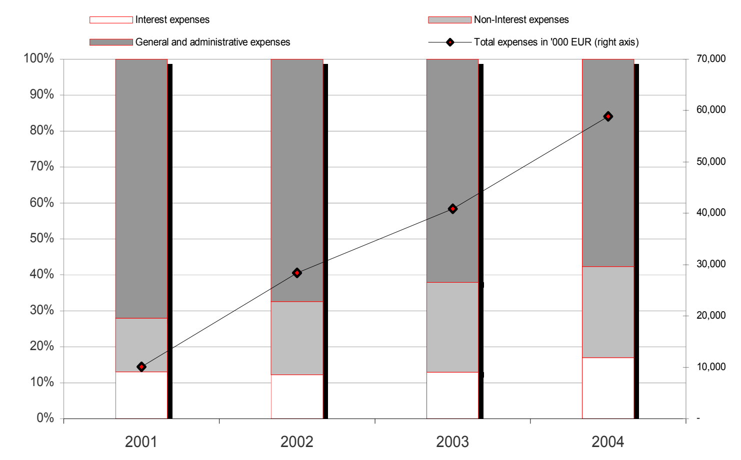
Structure of Expenditures

With respect to the structure of expenditures, **interest expenses** in 2004 increased by 89.0% compared with 2003 and amounted to 10.0 EUR million. Due to this considerable increase, the share of interest expenses to total banking sector expenses increased as well from 12.9% in 2003 to 16.9% in 2004.

Significant part of **interest expenses** of total banking sector is composed by the *interest expenses on deposits* which in 2004 attained 9.2 EUR million or 93.2% increase compared with 2003. Following this increase in volume, interest expenses on deposits increased as a share in total interest expenses as well and accounted for 92.6%.

In respect to the *interest expenses on borrowings*, in 2004 they were characterized by an increase of 49.1% and reached 0.7 EUR million. However, as a share in total interest expenses, interest expenses on borrowing experienced a decline by 2.0 percentage points and accounted for mere 7.4%.

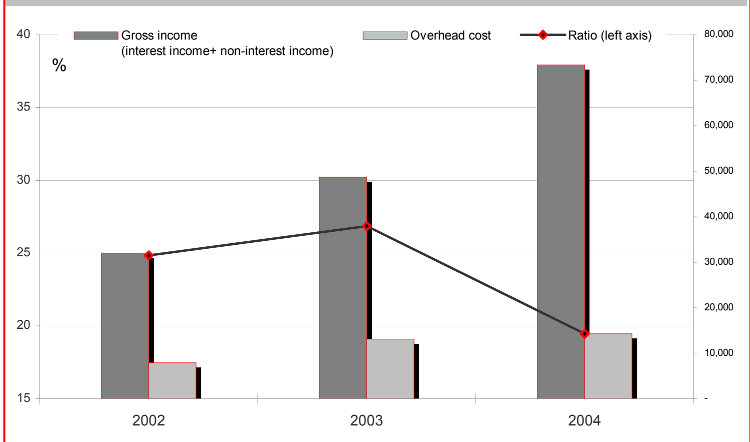
Figure 14. Structure of Expenses



As regards the **non-interest expenses**, figure 14 reveals that they experienced an increase by 46.1% in 2004 and attained 14.9 EUR million. As a share in total expenses, non-interest expenses experienced a slight increase and accounted for 25.4% of total expenditures.

Provisions for loans losses were characterized by an increase of 43.4% in 2004 and amounted to 11.1 EUR million. However, this increase in volume was not reflected in their share to total non-interest expenses as in 2004 the share of provisions for loans losses decreased by 1.4 percentage points and accounted 74.1%.

Figure 15. Overhead cost to gross income

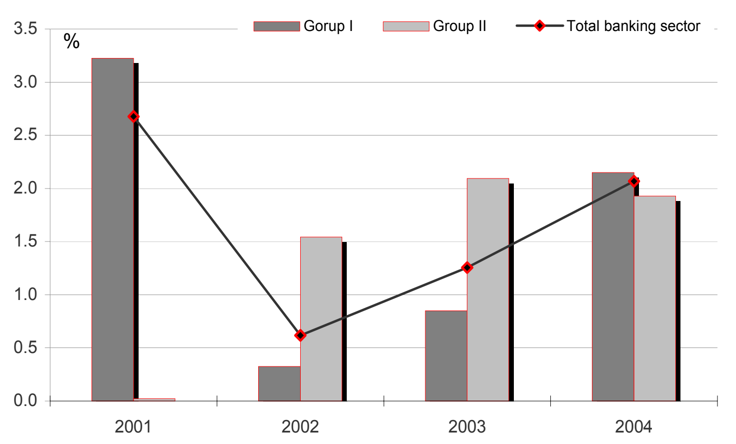


It is important to point out that **general and administrative expenses** made up the largest part of total expenses in 2004. Figure 15 illustrates the ratio between overhead expenses and gross income (interest income + non-interest income), an indicator of efficiency of banking sector. It shows that the ratio is continuously declining, partly as a result of the significant increase in total income (+50.9% compared with 2003) and a slight increase in the overhead expenses (+9.3% compared with 2003). Thus, the ratio reached 19.5% in 2004 representing 7.4 percentage points decrease compared with 2003.

5.2 Profitability and Efficiency

The positive trends of the profitability of banking sector, which began to appear in 2003, continued in 2004. An indicator measuring how efficiently the assets of the banking sector are used, the return[4] on average assets (ROAA), reached by the end-2004 2.1 % an improvement of 0.8 percentage points compared with 2003 (see figure 16). The fall in ROAA of total banking sector is registered in 2002 (9.7%), which is due to a fall of ROAA of Group I banks.

Figure 16. Return on average assets (ROAA) , expressed in %



Nevertheless, the largest contribution to the increase in the return on average assets in 2004 is accounted for by the Group I banks, the ROAA of which grew by 1.2 percentage points compared with the end 2003 and reached 2.1%. Banks in Group II experienced a modest decline in their ROAA, which in 2004 fell to 1.9% from 2.1% in 2003 and as a result the total banking sector ROAA increased from 1.3% in 2003 to 2.1% in 2004.

As illustrated in figure 17, the rate of return on average equity at end-2004 was 24.6%, which corresponds to 5.8 percentage points increase compared with end-2003. Due to a considerable increase of net profit after tax and a concurrent moderate increase in the equity, the banking sector ROAE in 2003 reached 18.8% whereas in 2002 it stood at 9.7%.

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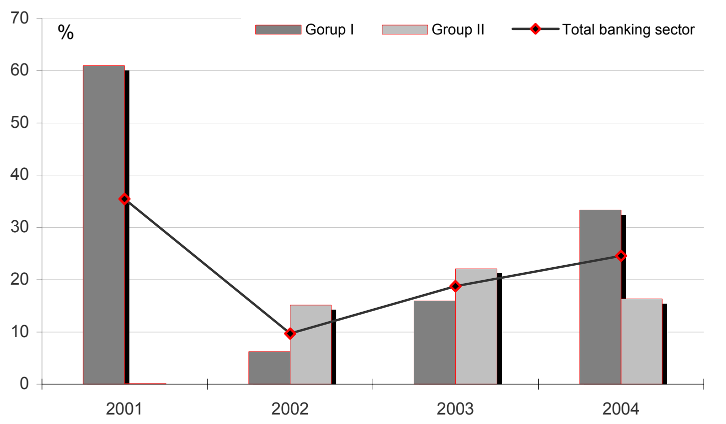
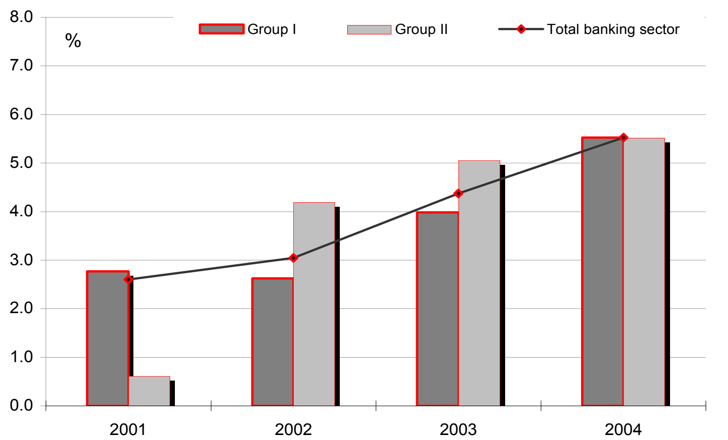
[4] Measured by the net profit after tax

Figure 17. Return on average equity (ROAE), expressed in %



The largest rate of return on average equity in 2004 is registered for by Group I banks which increased to 33.4% from 15.9% in 2003. Group II banks have recorded a negligible downturn in their ROAE during 2004. This was mainly due to the steady growth in the average equity against a concurrent fall in their net profit after tax. Thus, in 2004 Group II banks had the average rate of return on equity of 16.4 % while in 2003 it reached 22.1%.

Figure 18. Net Interest margin, expressed in %



In respect to the net interest margin (NIM), banks in Kosovo have improved their position in 2004. The net interest margin for the total banking sector in 2004 was 5.5% which corresponds to 1.2 percentage points increase compared with 2003. A continuous rise in interest margin of the total banking sector, during the observed period, has contributed significantly to the banking sector profitability.

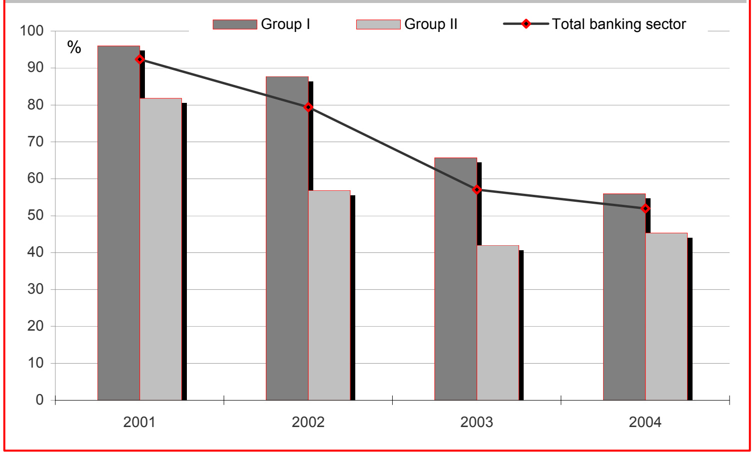
As figure 18 depicts, the ratio of net interest margin has experienced an increase for both banking Groups and at end 2004 it amounted 5.5% for both groups. However, the value of the ratio in 2004 corresponds to a 1.5 percentage points increase compared with 2003 for banks in Group I whereas the ratio for Group II banks rose by mere 0.4 percentage points.

5.3 Liquidity

According to the liquidity ratios, banking system liquidity risk might be judged as increasing, due to the increase in the loan-to-deposit and the accompanying concurrent fall in the ratio of liquid assets.

The ratio of liquid assets (which comprise cash, balances with BPK, accounts with other banks, placements abroad and security investments) to total assets for the entire banking sector also experienced a substantial decrease during the 2001-2004 period. As of end 2004, the fall by 9.1 % in the liquid assets ratio was driven by the faster increase in total assets as compared to the increase in the liquid assets. As a result, in 2004 the ratio declined to 51.9 % from 57.1 % in the preceding year.

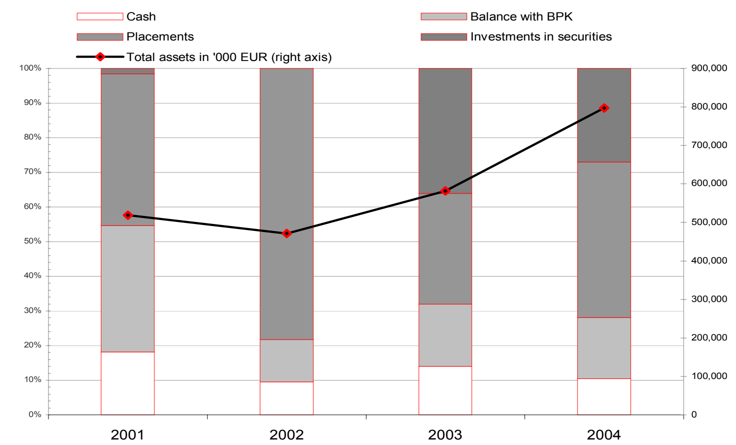
Figure 19. Liquid assets to total assets, expressed in %



With respect to the defined group of banks, the downward trend in the ratio of liquid assets to total assets was experienced by Group I banks, the ratio of which dropped from 65.7 % in 2003 to 56.0 % in 2004. Liquid assets of Group I increased by 13.6 % in 2004 against a decline of 19.3% in 2003, while total assets increased by 33.4 % in 2004, following an upsurge of 7.7 % in 2003.

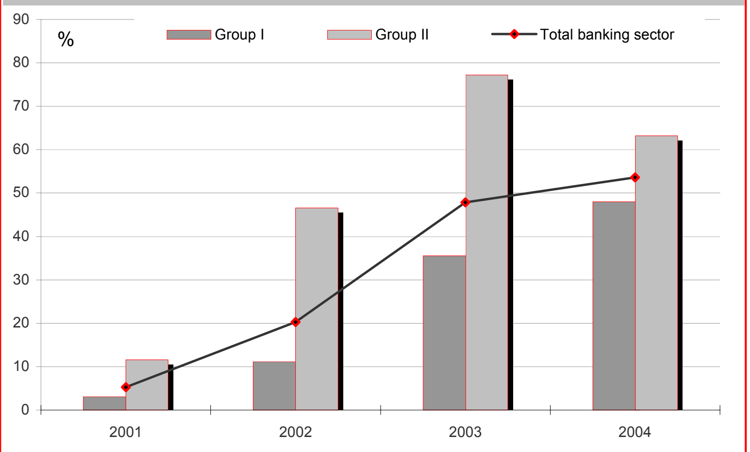
Quite the reverse, Group II banks had to cope with an increase in the ratio by 3.4 percentage points, which during 2004 reached 45.3 %, due mainly to the increase of 55.3 % of liquid assets and 43.6 % of total assets in 2004 compared with 2003.

Figure 20. Structure of liquid assets of total banking sector



Compared with 2003, the overall volume of liquid assets increased by 24.7 % in 2004 due mainly to the 55.3% increase in the liquid assets of banks in Group II. Regarding the composition within liquidity, investment in securities increased substantially in 2003 which was mainly at the expense of the decrease in placements abroad. However, in 2004, placements abroad turned up again at the expense of investments in securities and hence the largest share of liquid assets is accounted for by the placements abroad and investments in securities and, to a lesser extent to cash and deposits in the BPK (including mandatory reserves).

Figure 21. Loan to deposit ratio, expressed in %



As indicated in figure 19, banking sectors' loan-to-deposit ratio increased to 50.5% in 2004 from 33.7% in 2003. The increase in the ratio of the total banking system was mainly attributed to the fast increase in loans and the accompanying moderate increase in deposits. In particular, loans increased by 106.7% in 2004 compared with 2003, whereas deposits grew at a rate of 34.9%.

With respect to the defined group of banks, banks in Group II had the highest loan-to-deposit ratio which in 2004 reached 63.2%. Nevertheless, Group II banks have seen improvement in their liquidity position during 2004 given that their loan-to-deposit ratio decreased by 14.0 percentage points compared with 2003 which was mainly on account of the faster rate of growth of received deposits compared with the rate of lending growth. By contrast, Group I banks experienced a continuous increase in the loan-to-deposit ratio. As of end 2004, the loan-to-deposit ratio of Group I reached to 48.0% or 12.5 percentage points increase compared with 2003.

Notes on methodology

Figure 1. Number of banks

According to the ownership structure, commercial banks in Kosovo are classified into two groups: foreign owned and domestic owned, and thus named as Group I, and II respectively. Group I comprises banks which have more than 50.0 % of foreign ownership whereas Group II comprises those banks which are in majority domestic ownership. The figure shows the number of banks during the period 2000-2004, which also captures the ownership structure. The data on the number of banks in Kosovo are obtained by the BPK statistics.

Table 1. Commercial banking sector structure by total assets

The table shows the comparison between groups of banks with respect to their size of assets which also captures the ownership structure of the banking sector in Kosovo. It includes the amounts and the percentages share to total assets by banking groups whereas the schedule BS is the source of data on the amounts of assets (Statistical Bank Report, BPK Form No. 11)

Figure 2. Geographical distribution of banking units

The figure illustrates the concentration of branches and sub-branches by regions. The triangles positioned along the regions of Kosovo represent the concentration, with the largest triangle representing the largest concentration of banking units of the particular region relative to other regions. The largest triangle is taken as a benchmark for comparing the remaining concentrations throughout Kosovo. In this case, Pristina region represents the largest concentration and hence it is labelled by the largest triangle whereas Mitrovica is three times less concentrated by the number of banking units therefore it is denoted by the triangle that is three times smaller.

Figure 3. Percentage change in the number of banking units

The figure depicts the percentage change in the number of banking units throughout Kosovo in 2004 compared with 2003, which is presented by the size of cycles. The largest cycle stands for the largest percentage change of the banking units in the particular region relative to the preceding year. In this case, the largest cycle positioned in the Prizren region denotes the largest relative change whereas the Gjilan has recorded three times lower percentage change in the number of banking units compared with Pristina and hence it is represented by the three times smaller cycle. Regions that recorded no change are not denoted by a cycle.

Figure 4. Number of banking units and ATM's by Bank Groups

The figure illustrates the number of banking units for the particular banking group as well as the number of total ATM's installed by the banking group during the course of 2004.

Table 2. Employees and banking units in the commercial banking sector

According to the number of banking units of total banking system the labour productivity was measured on the year-on-year basis. Moreover, the number of employees per branch was also a good indicator for measuring the developments of the productivity of labour. The number of employees per banking unit was calculated as the ratio between the number of employees for the total banking sector and the total number of banking units for the total banking sector. The ratio of total assets managed by the banking unit and by an employee is calculated in the same manner. The ratio between the number of citizens[5] and the number of banking units and/or number of employees is calculated to capture the “bankarisation” degree in Kosovo. Total banking sector loans per employee/banking unit and deposits per employee/banking unit is measured as the ratio between total banking sector loans (deposits) and total number of employees/banking units.
The schedule BS (Balance Sheet) is the source for data on the amount of assets, loans, and deposits whereas BPK is the source of data on the number of banking units and the number of employees.

Figure 5. Indicators of productivity per employee by banking group

In order to capture the labour productivity for the particular banking group, the ratios of assets, loans, and deposits per employee are calculated. The calculations were made in the similar way as for the total banking sector but the figures are divided by banking groups.

[5] The data for the number of citizens is taken from the IMF staff estimates- mission in 2004

Figure 6. Herfindahl-Hirschman Index (HHI) (All banks)

The concentration of assets, loans and deposits for the each bank is calculated using the formula of HHI.

This formula is calculated as follows:

$$\left(\frac{Assets\ (deposits, loans)}{Total\ banking\ \mathrm{sec}tor\ assets\ (deposits, loans)} \cdot 100\right)^2$$

Schedule BS is the source for the data on the amounts of assets, deposits, and loans (Statistical Bank Report, BPK Forms No. 11).

Figure 7. Share of three largest banks' Assets (deposits, loans) to total assets (deposits, loans)

The criterion of banks asset size was used for selecting of three largest banks in the banking sector in Kosovo. Accordingly, the share of the three largest banks assets to total assets was calculated as a ratio between the sum of assets of the three largest banks and the total banking sector assets. The same was applied for calculating the share of the three largest banks to total deposits and total loans. The schedule BS is the source of data on the assets, deposits and loans (Statistical Bank Report, BPK Forms No. 11).

Table 3. Structure of assets of commercial banking sector in Kosovo

The table presents each category of assets in volume and their share in total assets for the particular period. In addition, the change for each item in the year-on-year basis is calculated, showing the percentage change of the item relative to the balance reported in the preceding year. Schedule BS is the source for the data on the amount of assets for the banking sector in Kosovo.

Figure 8. Structure of loans by institutional sectors

The sectoral diversification of the loan exposure is presented by the type of beneficiaries. First, the share of loans for each category in total banking sector loans is calculated and presented by bars in the figure. Than, total loans for each sector are added up and presented with a line which corresponds to the right axis of the figure. The schedule BS/LBM is the source of loans by institutional sectors.

Figure 9. Structure of loans by industry

The table shows the industrial diversification of loan exposure during the course of 2003 and 2004. Total loans extended by industrial sector of each bank are added up and then the share of loans extended to each industry in total loans extended is calculated for each year. Schedule BS/LBI (Loans By Industry) is the source of data for the amounts of loans extended.

Figure 10. Structure of loans by maturity

The maturity structure of loans is reported for the period 2001-2004 for the total banking sector in Kosovo. Loans are split up by their maturity and presented by bars which represents their shares in total loans, whereas the line corresponds to the total banking sector loans presented in volume. Schedule BS/LBM (Loans By Maturity) is the source of data for the maturity structure of loans.

Table 4. Structure of commercial banking sector liabilities

The calculation of commercial banking sectors' liabilities is made in the same manner as the calculation of assets. First, each category of the liability side of balance sheet is stated in volume. Second, for each category of balance sheet the share in balance sheet total is stated in the second column of the corresponding year. Finally, the change in balance sheet categories indicates their percentage change relative to their balance recorded in the preceding year. Schedule BS is the source of data on the amount of the liability side of total banking sector balance sheet.

Figure 11. Structure of deposits

The structure of deposits by testimony date and by depositors is computed in the following manner. First the breakdown of deposits with respect to their maturity is made into the transferable and other (term and savings) which are then presented by bars as a share to total deposits. The line corresponds to the total deposits stated in volume. The right panel of figure shows the breakdown of deposits by the type of depositor into the non-financial corporations and households which are stated as the share in total deposits. Total deposits are presented with line which corresponds to the right axis. The schedule BS/DBM (Deposits By Maturity) is the source for the amount of data on deposits.

Table 5. Structure of commercial banking sector capital

The table illustrates the detailed developments of the banking sector capital structure. The share of main components of capital in the total banking system capital is expressed as the ratio between each capital component and total banking sector capital and thus multiplied by 100. The change in capital depicts the percentage change compared with the capital items recorded in the previous year. Schedule BS is the source for the data on the banking system capital.

Figure 12. Capital adequacy ratio

Capital adequacy ratio is calculated in accordance with the rule on Capital Adequacy of Banks. The figure illustrates the ratio between the consolidated total capital and the risk-weighted assets and then multiplied by 100. This calculation is made by the supervision department of the BPK based on the amended rule on capital adequacy.

Table 6. Structure of commercial banking sector income statement

For the four-year period, each category of the income statement is summed up for the total banking sector. Additionally the change in the income statement is the percentage change for the each item in comparison to the statement recorded in the preceding year. Schedule IS (Income Statement) is the source of the data on the amounts of income statement items for the banks.

Figure 13. Structure of Income

The figure plots the structure of the particular component of income for the total banking sector. It shows the amounts for the total income represented by the line and corresponds to the right axis and the share of each component of the income structure to the total income presented by bars. The Schedule IS is the source of data on the banks' income.

Figure 14. Structure of expenses

Same as in the previous figure, the structure of expenditures for the total banking sector is plotted, with interest expenditures, non interest expenditures, and the general and administrative expenses presented by bars. The bars in the figure show the share of each expenditure component while the line presents total expenditures stated in volume. Schedule IS is the source of data on the expenses of banking sector.

Figure 15. Overhead cost to gross income

The amounts of income and the overhead expenses of total banking sector are presented by bars and stated in volume corresponding to the right axis. The ratio between overhead cost and the gross income is then plotted by line and stated in percentage (left axis). Schedule IS is the source of data on the amounts of overhead cost and gross income.

Figure 16. Return on average assets

The ratio between the after-tax profit and the average assets is calculated for each group of banks as follows. First, the after tax profit for each bank recorded for the particular period is added up for all banks in the group of banks. Than the banks' assets are added up for each group. Than the amounts thus calculated are divided and multiplied by 100. The same applies for the total banking sector.

The average assets are calculated as the sum of the monthly averaged assets for each bank for the particular period.

Schedule IS is the source of data for the profit after tax whereas BS is the source for the amount of assets for the banking sector.

Figure 17. Return on average equity

The ratio between after tax profit and average equity for each group of banks is calculated as follows. First, the after tax profit for the particular period is added up for each defined group of banks. Than the average equity is calculated and added up for each group. The summed amounts are thus divided and multiplied by 100.

The average equity is expressed as arithmetic mean, which is calculated as the sum of the monthly averaged equity for the particular year for each bank. Schedule IS is the source for data on the banks' profits and schedule BS is the source for data on equity.

Figure 18. Net Interest Margin (NIM)

To analyse the profitability of defined group of banks as well as the total banking sector, the ratio between banks' interest margin and total assets is calculated. The interest margin is measured using the following formula: (Interest Income – Interest Expense). This amount thus is divided by total assets of a particular group and multiplied by 100. The schedule IS and BS is the source of data for the interest income and interest expenses and for total assets.

Figure 19. Liquid assets to total assets

Each bank group ratio between liquid assets and total assets is calculated as follows. First liquid assets of each bank are added up in the banks group. Second Total assets for each bank group are added up. The sum of liquid assets of each bank group and total assets of each banks group are expressed as a ratio and thus multiplied by 100.

Liquid assets are calculated as the sum of the cash, balances with BPK, accounts with other banks, placements abroad and security investments.

Schedule BS is the source for data on liquid assets and for total assets for each bank and thus bank group.

Figure 20. Structure of liquid assets

The figure plots the components of liquid assets as a share in total liquid assets for each year. Total assets are presented by line which corresponds to the right axis (in volume).

Figure 21. Loan to deposit ratio

The ratio between loans granted and customer deposits received is calculated as follows. First, total loans granted by each bank are added up for the particular group and for the particular period. Second, the customer deposits received for each bank in the bank group are added up for the specific period. The totals then are expressed as a ratio and multiplied by 100. The ratio for the total banking sector is calculated in the same manner. Schedule BS/LBM is the source for the data on loans granted whereas schedule BS/DBM is the source for the data on deposits.

List of banks

As of December 2004

RAIFFEISENBANK KOSOVO

Address: UÇK Street 51, Pristina

Phone: ++381 38/ 226 400, 401

Fax: ++38138/ 226 408

e-Mail: info@raiffeisen-kosovo.com

Internet: www.raiffeisen-kosovo.com

Balance sheet, as of December 2004, in EUR '000

STRUCTURE OF ASSETS		STRUCTURE OF LIABILITIES	
Cash and balances with BPK	14,933	Deposits by banks and OFI	1,545
Loans to financial instutitions(placement)	31,777	Costumer deposits	127,725
Securities	-	**Total deposits**	**129,270**
Gross loans to non-financial institutions	101,536	Borrowings	-
Less: Provisions for loan losses	3,841	Ineterest payable and other liabilities	3,128
Net loans	97,695	Subordinated debts	-
Property and equipment, net of deprecations	3,057	**Total liabilities**	**132,398**
Interest receivable and other assets	2,753	Total shareholder's equity	17,817
Total Assets	**150,215**	**TOTAL (liab. and shareholder's equity)**	**150,215**

PROCREDIT BANK

Address: Skenderbeu Street, Pristina

Phone: ++381 38/ 240 248

Fax: ++38138/ 248 777

e-Mail: info@procreditbank-kos.com

Internet: www.procreditbank-kos.com

Balance sheet, as of December 2004, in EUR '000

STRUCTURE OF ASSETS	
Cash and Balance with BPK	41,138
Loans to financial instutitions(placement)	114,250
Securities	74,638
Gross loans to non-financial institutions	109,771
Less: Provisions for loan losses	2,567
Net loans	107,204
Property and equipment, net of deprecations	3,546
Interest receivable and other assets	3,548
Total Assets	**344,324**

STRUCTURE OF LIABILITIES	
Deposits by banks and OFI	-
Custumer deposits	311,156
Total deposits	**311,156**
Borrowings	9,318
Ineterest payable and other liabilities	1,218
Subordinated debts	7,045
Total liabilities	**328,737**
Total shareholder's equity	15,587
Total (liab. and shareholder's equity)	**344,324**

BANK FOR PRIVATE BUSINESS

Address: “Vellusha” street, no.6, Pristina

Phone: ++381 38/ 244 666

Fax: ++38138/ 243 656, 243 657

e-Mail: hq@bpb-bank.com

Internet: www.bpb-bank.com

Balance sheet, as of December 2004, in EUR '000

STRUCTURE OF ASSETS		STRUCTURE OF LIABILITIES	
Cash and Balance with BPK	10,982	Deposits by banks and OFI	-
Loans to financial instutitions(placement)	14,022	Custumer deposits	46,938
Securities	-	**Total deposits**	**46,938**
Gross loans to non-financial institutions	30,805	Borrowings	1,399
Less: Provisions for loan losses	2,072	Ineterest payable and other liabilities	301
Net loans	28,733	Subordinated debts	-
Property and equipment, net of deprecations	1,209	**Total liabilities**	**48,638**
Interest receivable and other assets	2,012	Total shareholder's equity	8,320
Total Assets	**56,958**	**Total (liab. and shareholder's equity)**	**56,958**

CREDIT BANK OF PRISTINA

Address: Tirana Street Nr. 29, Pristina
Phone: ++381 38/249 851
Fax: N/A
e-Mail: N/A
Internet: N/A

Balance sheet, as of December 2004, in EUR '000

STRUCTURE OF ASSETS		STRUCTURE OF LIABILITIES	
Cash and Balance with BPK	10,606	Deposits by banks and OFI	3,517
Loans to financial instutitions(placement)	10,830	Custumer deposits	45,832
Securities	-	**Total deposits**	**49,349**
Gross loans to non-financial institutions	33,786	Borrowings	-
Less: Provisions for loan losses	917	Ineterest payable and other liabilities	1,930
Net loans	32,869	Subordinated debts	-
Property and equipment, net of deprecations	1,331	**Total liabilities**	**51,279**
Interest receivable and other assets	975	Total shareholder's equity	5,332
Total Assets	**56,611**	**Total (liab. and shareholder's equity)**	**56,611**

NEW BANK OF KOSOVO

Address: Mother Teresa No. 54, Pristina
Phone: ++381 38/225 871 ; 223 976
Fax: N/A
e-Mail: N/A
Internet: www.brk-bank.com

Balance sheet, as of December 2004, in EUR '000

STRUCTURE OF ASSETS		STRUCTURE OF LIABILITIES	
Cash and balances with BPK	15,843	Deposits by banks and OFI	-
Loans to financial instutitions(placement)	15,600	Costumer deposits	51,029
Securities	-	**Total deposits**	**51,029**
Gross loans to non-financial institutions	26,607	Borrowings	-
Less: Provisions for loan losses	1,268	Ineterest payable and other liabilities	586
Net loans	25,339	Subordinated debts	-
Property and equipment, net of deprecations	766	**Total liabilities**	**51,615**
Interest receivable and other assets	58	Total shareholder's equity	5,991
Total Assets	**57,606**	**TOTAL (liab. and shareholder's equity)**	**57,606**

KASA BANK

Address: Pal Palucaj No. 1, Pristina

Phone: ++381 38/543 688

Fax: N/A

e-Mail: N/A

Internet: www.kasabank.com

Balance sheet, as of December 2004, in EUR '000

STRUCTURE OF ASSETS		STRUCTURE OF LIABILITIES	
Cash and Balance with BPK	14,336	Deposits by banks and OFI	-
Loans to financial instutitions(placement)	25,065	Custumer deposits	79,421
Securities	-	**Total deposits**	**79,421**
Gross loans to non-financial institutions	54,965	Borrowings	3,536
Less: Provisions for loan losses	4,896	Ineterest payable and other liabilities	1,703
Net loans	50,069	Subordinated debts	-
Property and equipment, net of deprecations	4,422	**Total liabilities**	**84,660**
Interest receivable and other assets	174	Total shareholder's equity	9,406
Total Assets	**94,066**	**Total (liab. and shareholder's equity)**	**94,066**

ECONOMIC BANK

Address: UCK Street No. 5, Pristina

Phone: ++381 38/ 248 997

Fax: N/A

e-Mail: N/A

Internet: www.bankaekonomike.com_

Balance sheet, as of December 2004, in EUR '000

STRUCTURE OF ASSETS	
Cash and Balance with BPK	8,455
Loans to financial instutitions(placement)	11,411
Securities	-
Gross loans to non-financial institutions	16,869
Less: Provisions for loan losses	386
Net loans	16,483
Property and equipment, net of deprecations	720
Interest receivable and other assets	218
Total Assets	**37,287**

STRUCTURE OF LIABILITIES	
Deposits by banks and OFI	-
Custumer deposits	31,279
Total deposits	**31,279**
Borrowings	-
Ineterest payable and other liabilities	387
Subordinated debts	-
Total liabilities	**31,666**
Total shareholder's equity	5,621
Total (liab. and shareholder's equity)	**37,287**