

MONETARY POLICY PROGRAMME OF THE NATIONAL BANK OF SERBIA FOR THE YEAR 2006

1. The principal monetary policy objective for 2006 is a considerable reduction of the inflation rate relative to the end of 2005, and maintenance of financial system stability.

2. The National Bank of Serbia will further liberalize the foreign exchange market with a view to enhancing its competitiveness, i.e. so as to direct the flow of foreign exchange towards banks, that is the interbank market, and reduce direct interventions of the National Bank of Serbia in that market. In 2006 the National Bank of Serbia will gradually withdraw from exchange transactions.

3. The exchange rate of the dinar will be formed freely on the basis of supply and demand in the foreign exchange market, whereas through its interventions in the foreign exchange market, the National Bank of Serbia will ensure that the exchange rate is consistent with medium-term sustainable balance of payments position of the country with a view to reducing the inflation rate.

4. The National Bank of Serbia will monitor the movement of foreign financial loans, and overall country indebtedness, and, within its scope of competences, take indirect measures in order to contain foreign indebtedness within sustainable limits.

5. The starting point for projections of monetary aggregates are the objectives and assumptions which constitute the basis of the economic policy contained in the Memorandum of Budget, Economic and Fiscal Policy for 2006, with projections for 2007 and 2008. GDP growth is expected to amount to 5% in 2006, while the rise in net foreign assets of the banking sector is expected to amount to USD 660 million at the median rate of exchange as of December 31, 2005.

6. The National Bank of Serbia estimates that, in view of the defined economic policy, the accomplishment of monetary policy objectives for 2006 will be attended by a 6% to 7% rise in the reserve money and a 15 to 16% rise in dinar money supply M2.

7. In 2006, the National Bank of Serbia will continue to develop and strengthen market monetary regulation instruments, primarily repo operations, as well as stimulating a further development of the interbank money market with a view to ensuring a more efficient banking sector liquidity management. In addition, the National Bank of Serbia will use non-standard measures, such as the issuing of savings bills and their sale to households, in order to bring down the level of euroization and encourage dinar savings and money withdrawal.

8. The National Bank of Serbia will employ the rate of banks' required reserves held with the National Bank of Serbia as an instrument in case other monetary regulation instruments do not yield appropriate results.

9. The National Bank of Serbia will monitor developments in banks' lending activity and take additional monetary regulation measures falling within its scope of competences if it estimates that increased lending activity of banks threatens the accomplishment of the principal monetary policy objective, i.e. reduction of the inflation rate.

10. In open market operations, the National Bank of Serbia will conduct the policy of real positive interest rates, where the interest rate on two-week repo operations will serve as the reference (signaling) interest rate.

11. With a view to regulating banking system liquidity, in 2006 the National Bank of Serbia will enable banks to use lending and deposit facilities. In the event that banks experience temporary illiquidity, the National Bank of Serbia can allow banks to use liquidity loans.

12. Subject to the enacted Law on Banks, in 2006 the National Bank of Serbia will focus its supervisory activity on risk management in banks' operations. Through constant activities aimed at ensuring a financially sound and stable banking system capable of protecting the interests of bank depositors, meeting households' and corporate needs for banking services, and supporting further economic growth in the country, the National Bank of Serbia will create conditions for a further development of the banking market, as well as monitoring and evaluating the types and levels of risks to which banks are exposed in their operations. Supervision of risk management procedures systems in banks, management quality and banks' ability to provide adequate capital, and supervision of solvency and legality of banks' operations, will be conducted in conformity with contemporary standards and principles.

13. In 2006, the National Bank of Serbia will continue to improve its function of supervision of insurance companies, based on international standards and principles. The National Bank of Serbia will continue to be guided by the principal objective of creating a safe and stable insurance sector with a view to protecting the funds of insurance holders.

14. In 2006, the National Bank of Serbia will also conduct supervision of financial leasing activities, which have been growing in significance. If it estimates that financial leasing activities lead to an excessive rise in demand, the National Bank of Serbia will regulate such demand by employing the instrument of requiring lessors to allocate reserves, which would, at the same time, ensure equal terms for all participants in the financial market. The objective of the National Bank of Serbia is to still further enhance financial market transparency in that way, to strengthen competition and conduct consolidated supervision of the financial sector in a more efficient manner.

15. Subject to the Law on Voluntary Pension Funds and Pension Schemes, in 2006 the National Bank of Serbia will conduct supervision of operations of voluntary pension funds management companies, as well as performing other activities defined in that law.

16. The National Bank of Serbia will continue to regulate, upgrade, supervise and control dinar payment transactions in banks, and to establish, maintain and administer IT infrastructure for the performance of payment transactions in the Republic of Serbia, with the aim of ensuring that payment transactions are performed in an efficient and safe manner, in line with European Union principles and standards.