

# **BANKING SUPERVISION**

**First Quarter Report 2009**

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## I. Banking sector in Q1 2009

### Banking sector structure as at 31 March 2009

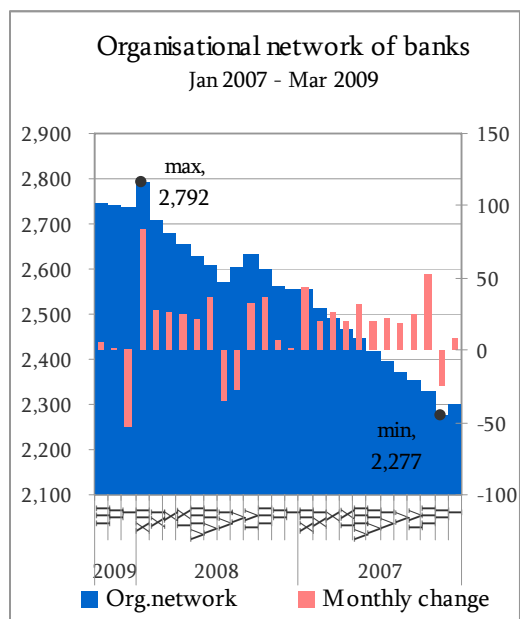
#### Number of banks and their organisational network

The number of banks operating in the Republic of Serbia in Q1 remained the same as in the previous quarter (34).

The overall banking network included 2,728 business units, branches, branch offices, teller units, agencies and exchange bureaus, which is an increase by 17 on Q4 2008.

**Table 1 and Chart 1** - Number of banks and their organisational network

	Dec 2007	Dec 2008	Mar 2009
Number of banks	35	34	34
Number of business units	80	70	70
No. of branches, branch offices and teller units	2321	2607	2624
Other	34	34	34
Total	2435	2711	2728

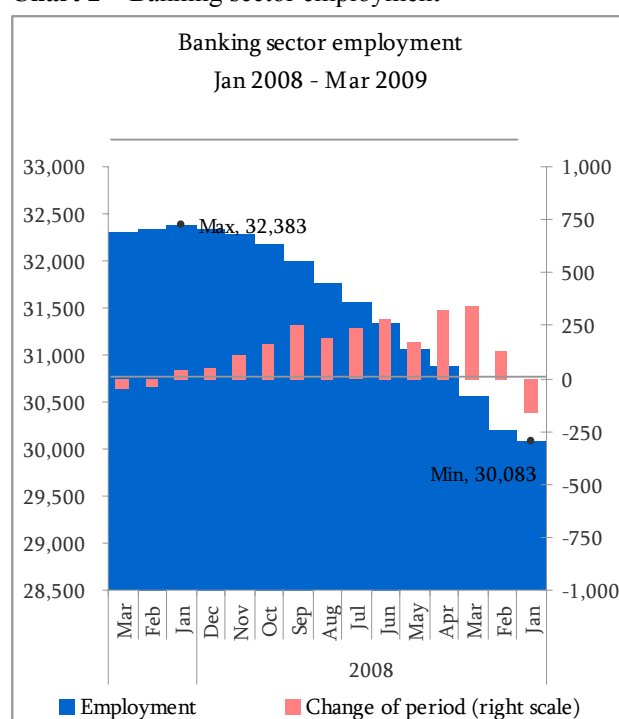


#### Banking sector employment

At end-Q1 2009, 32,292 people were employed in the banking sector. Relative to end-2008, banking sector employment declined by 0.2% or by 50 persons (monthly breakdown: January +41, February -41 and March -50).

Of the total number of banks, three kept their staff numbers unchanged (Credy banka, Marfin banka and Srpska banka). Staff numbers were decreased by 19 (OTP Banka by 36, Raiffeisen banka, Poštanska Štedionica and ProCredit banka by 33) and increased by 12 banks (most notably: Eurobank EFG by 89, Alpha Banka by 85, and Erste Banka by 15).

**Chart 2 – Banking sector employment**



Strong growth in banking sector employment, dating back to 2008 and culminating in record high employment (32,383) at end-January 2009 is slowing down.

**Table 2 – Banking sector employment, Dec 2006–March 2009**

	Banks by ownership structure			
	State-owned	Privately-owned	Foreign-owned	Total
Employment in March 2009	7,374	2,127	22,791	32,292
Changes in employment*	(74)	5	19	(50)
Changes in employment**	326	196	3,678	4,200
CAGR***	0.5%	1.1%	2.0%	1.6%

\*relative to December 2008

\*\*relative to December 2006

\*\*\*Compound Annual Growth Rate – quarterly change

## Bank ownership structure

At end-March 2009:

- 20 banks were in majority foreign ownership,
- 6 banks were in majority ownership of domestic natural persons and legal entities, and
- 8 banks were in majority ownership of the Republic of Serbia.<sup>1</sup>

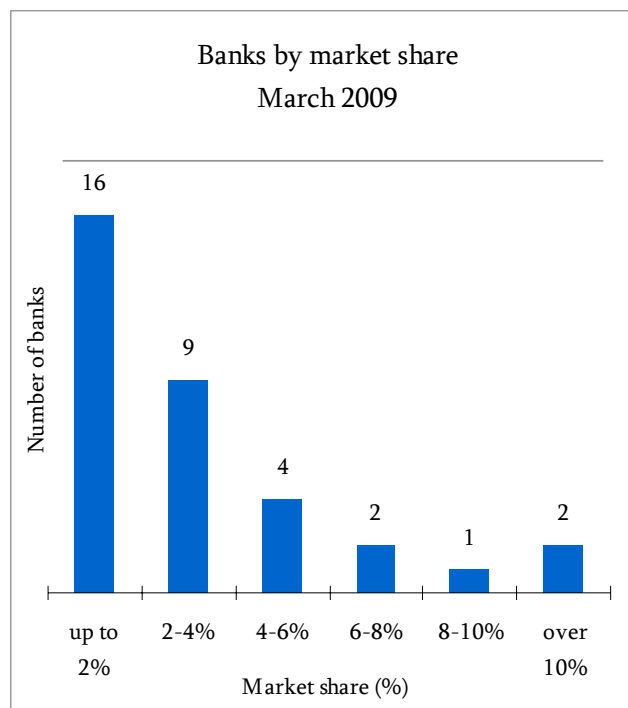
## Market share

Banking sector assets totalled RSD 1,804.9 billion at end-March 2009.

Chart 3 shows the distribution of banks based on their market share.

**Chart 3 – Banks by market share**

<sup>1</sup> Banks in which the RS is the largest, majority or individual, direct or indirect, shareholder.



The banking sector is significantly fragmented, as reflected in the fact that as many as 16 banks hold a market share of less than 2% (measured by the share of individual bank's assets in total banking sector assets).

At end-Q1, two banks had a market share exceeding 10% - Banca Intesa (14.7%) and Komercijalna banka (10.3%).

Table 3 shows the market share-based ranking of banks. On 31 March 2009, the first ten banks accounted for 68.2% of total assets i.e. market.

**Table 3 – Market share of individual banks (March 2009)**

Bank	Share (%)	Bank	Share (%)	Bank	Share (%)
1) Banca Intesa	14.7	13) Erste Bank Novi Sad	2.8	25) Marfin bank	0.8
2) Komercijalna banka	10.3	14) OTP BANKA SRBIJA	2.6	26) FINDOMESTIC BANKA	0.7
3) Raiffeisen banka	8.7	15) Agrobanka	2.5	27) Srpska banka Beograd	0.5
4) Hypo Alpe-Adria-bank	6.5	16) NLB banka	2.2	28) Credi banka	0.4
5) Eurobank EFG	6.2	17) Piraeus bank	2.1	29) Jugoboanka K.Mitrovica	0.4
6) Aik banka Nis	4.9	18) Meridian bank-CA Group	2.1	30) Jubmes banka	0.4
7) UNICREDIT BANK	4.7	19) Univerzal banka	1.5	31) Privredna banka Pančevo	0.4
8) Vojvodjanska banka	4.6	20) Postanska stedionica	1.3	32) Opportunity banka	0.3
9) Societe Gen.Banka Srbija	4.1	21) Metals banka	1.1	33) Moskovska banka a.d.- Beograd	0.1
10) VolksBank	3.5	22) Privredna banka Beograd	1.1	34) Kosovsko metohijska banka	0.0
11) ProCredit Bank	3.5	23) Cacanska banka	1.0		
12) ALPHA BANK	3.1	24) KBC banka	0.9		

At the same time, the Herfindahl Hirschman index<sup>2</sup>, measuring banking sector concentration, is at its nine-month high – 642 index points.

The lowest level of HHI in the past nine months was recorded in October – 611 points. Although the trend of HHI is upward, its value is still significantly below the level indicating moderate concentration (1,000).

**Table 4 – Banking sector competitiveness and concentration indicators**

Year	Month	Share of top five banks (%)	Share of top ten banks (%)	HHI assets
2009	March	46.38%	68.20%	642
	February	45.53%	67.99%	621
	January	45.26%	68.10%	617
2008	December	46.17%	68.49%	627
	November	45.49%	68.31%	616
	October	44.99%	68.41%	611
	September	45.20%	68.71%	617
	August	45.78%	68.77%	621
	July	46.07%	68.49%	620
Correlation coefficient		0.85	(0.18)	1.00

Significant correlation between the HHI and movements in the market share of top five banks (0.85 correlation) comes as no surprise given that methodologically, the HHI attaches greater significance to banks with larger market shares. On the other hand, correlation between the HHI and movements in the market share of top ten banks is negative.

## Banking sector balance sheet

As at 31 March 2009, balance sheet total of the banking sector stood at RSD 1,804.9 billion, which is RSD 28 billion or 2% higher than in Q4 2008.

*Loans, advances and deposits* accounted for the largest part of balance sheet assets of banks (61.2%). Next in size were *callable credits and deposits* (17%). *Cash and cash equivalents* made up 12.4% of the banking sector balance sheet assets, while the share of all other items was below 4%.

<sup>2</sup> *Hirschman Herfindahl Index (HHI)* – below 1000 indicates there is no concentration; 1000-1800 indicates moderate concentration; above 1800 indicates high concentration.

**Table 5 – Banking sector balance sheet<sup>3</sup> (in RSD bln)**

ASSETS	31 Dec 2007		31 Dec 2008		31 March 2009		Growth index for Q1/Q4	Growth index for 2008	Growth index for 2007
	Amount	Share in %	Amount	Share in %	Amount	Share in %			
Cash and cash equivalents	80.3	5.1	266.7	15	222.9	12.4	84	332	111
Callable deposits and credits	551.5	35.3	276.2	15.5	307.4	17.0	111	50	133
Interest, fees and commission receivables, change in fair value of derivatives and other receivables	6.6	0.4	9.7	0.6	13.2	0.7	135	148	131
Loans, advances and deposits	774.3	49.6	1,068.5	60.1	1,103.9	61.2	103	138	144
Securities	19.3	1.2	19.7	1.1	17.3	1.0	88	102	73
Equity investments	6.2	0.4	5.4	0.3	6.4	0.4	118	87	143
Other lending	45.4	2.9	37.6	2.1	40.2	2.2	107	83	131
Intangible assets	6.1	0.4	6.3	0.4	6.5	0.4	103	104	104
Property, plant and equipment and investment property	57.0	3.7	66.2	3.7	66.2	3.7	100	116	113
Non-current assets held for sale and discontinued operations	0.3	0.0	0.2	0.0	0.2	0.0	101	64	85
Deferred tax assets	2.5	0.2	2.5	0.2	2.5	0.1	100	100	102
Other assets	12.3	0.8	17.8	1	18.3	1.0	103	145	96
Losses in excess of capital									
<b>TOTAL</b>	<b>1,561.8</b>	<b>100</b>	<b>1,776.9</b>	<b>100</b>	<b>1,804.9</b>	<b>100.0</b>	<b>102</b>	<b>114</b>	<b>134</b>

LIABILITIES	31 Dec 2007		31 Dec 2008		31 March 2009		Growth index for Q1/Q4	Growth index for 2008	Growth index for 2007
	Amount	Share in %	Amount	Share in %	Amount	Share in %			
Transaction deposits	300.5	19.2	271.3	15.3	248.4	13.8	92	90	134
Other deposits	659.6	42.2	753.4	42.4	807.0	44.7	107	114	149
Borrowings	169.6	10.9	189.5	10.7	174.5	9.7	92	112	79
Liabilities on securities	2.6	0.2	0.0	0	0.1	0.0	241	1	25960
Interest, fees and commissions payable and change in fair value of derivatives	2.8	0.2	2.1	0.1	1.1	0.1	51	75	284
Provisions	11.3	0.8	14.0	0.8	12.8	0.7	91	123	120
Tax liabilities	0.6	0.0	0.7	0.0	0.4	0.0	59		
Liabilities from profit	0.6	0.0	1.2	0.1	0.5	0.0	39	184	90
Liabilities on non-current assets held for sale and discontinued operations									
Deferred tax liabilities	0.6	0.0	0.6	0.0	0.7	0.0	118	104	80
Other liabilities	85.1	5.5	124.2	7	127.5	7.1	103	146	143
<b>LIABILITIES</b>	<b>1,233.3</b>	<b>79</b>	<b>1,357.0</b>	<b>76.4</b>	<b>1,373.0</b>	<b>76.1</b>	<b>101</b>	<b>110</b>	<b>129</b>
Capital	<b>328.5</b>	<b>21</b>	<b>419.9</b>	<b>23.6</b>	<b>432.0</b>	<b>23.9</b>	<b>103</b>	<b>128</b>	<b>152</b>
Share capital and other capital	272.8	17.5	332.7	18.7	337.9	18.7	102	122	149
Reserves	47.6	3	74.3	4.2	87.9	4.9	118	156	156
Unrealized losses on securities			0.1	0.0	-0.2	0.0	-151		
Accumulated gains/losses	8.0	0.5	13.0	0.7	6.3	0.4	49	162	246
<b>TOTAL</b>	<b>1,561.8</b>	<b>100</b>	<b>1,776.9</b>	<b>100</b>	<b>1,804.9</b>	<b>100.0</b>	<b>102</b>	<b>114</b>	<b>134</b>

<sup>3</sup> As of 1 July 2008 the following regulations are in force: new *Chart of Accounts and Content of Accounts within the Chart of Accounts for Banks*, *Guidelines on the Obligation and Methodology of Recording, Compiling, Processing and Delivery of Data on the Stock and Structure of Lending, Receivables and Liabilities of Banks*, and *Rules on the Forms and Content of Items in Financial Statement Forms to be Completed by Banks*. Data for 2007 are presented for the sake of comparison.



Borrowed funds accounted for 76.1% of the banking sector balance sheet liabilities, and capital for the remaining 23.9%. Borrowed funds consisted primarily of *other deposits*, *transaction deposits* and borrowings (44.7%, 13.8% and 9.7% of total liabilities, respectively).

Bank capital reached RSD 432 billion rising by RSD 12.1 billion or 3% on Q4 2008. *Share capital and other capital* increased by 2% on a quarter earlier, amounting to RSD 337.9 billion.

Off-balance sheet items of banks came to RSD 2,411.2 billion, up by RSD 255 billion on the quarter before. The largest single off-balance component were *other off-balance sheet assets*<sup>4</sup> (53.8%), followed by *guarantees and sureties* (18.1%). Most of off-balance sheet assets were non risk-weighted – in March mere 27% of off-balance sheet assets (RSD 655.5 billion) was classified as risky.

## Lending activity

The table below gives an overview of changes in the composition of bank lending:

**Table 6 – Bank lending (in RSD bln)**

Sector	31 Dec 2007		31 Dec 2008		31 March 2009		Growth index for Q1/Q4	Growth index for 2008	Growth index for 2007
	Amount	Share in %	Amount	Share in %	Amount	Share in %			
ENTERPRISES	437.4	57.5	632.2	61.5	699.1	63.0	111	145	135
HOUSEHOLDS	302.5	39.8	364.3	35.5	374.9	33.8	103	120	154
housing construction	89.4	11.8	160.8	15.6	172.0	15.5	107	180	189
PUBLIC SECTOR	13.9	1.8	17.4	1.7	21.6	1.9	125	125	64
Serbia&Montenegro	0.0	0	0.0	0	0.0	0.0	0	0	0
Republic of Serbia	7.0	0.9	8.2	0.8	12.0	1.1	145	117	42
Local government	6.9	0.9	9.1	0.9	9.7	0.9	106	132	146
OTHER FINANCIAL ORGANISATIONS	1.2	0.1	10.6	1	11.2	1.0	106	867	161
NONPROFIT INSTITUTIONS	5.8	0.8	3.1	0.3	3.1	0.3	99	54	138
<b>TOTAL</b>	<b>760.9</b>	<b>100</b>	<b>1,027.6</b>	<b>100</b>	<b>1,109.9</b>	<b>100.0</b>	<b>108</b>	<b>135</b>	<b>139</b>

In Q1 2009, bank lending rose by RSD 82.3 billion or 8%.

In terms of sectoral distribution, dominant was lending to enterprises (63%). Its increase by RSD 67 billion accounted for the bulk of lending growth in Q1. Next in size was lending to households (33.8%) which rose by RSD 10 billion. In the same period, housing loans increased by RSD 12 billion.

<sup>4</sup> Received guarantees and other sureties, funds from custody operations and other off-balance sheet assets.

**Table 7 – Loan concentration indicators**

Year	Month	Share of top five banks (%)	Share of top ten banks (%)	HHI Loans
2009	March	47.17%	69.57%	660
	February	47.10%	69.48%	648
	January	46.87%	68.92%	641
	December	48.13%	69.94%	668
	November	46.64%	68.46%	628
	October	45.40%	67.76%	615
	September	44.82%	67.60%	610
	August	45.12%	67.62%	606
2008	July	45.14%	67.35%	605
Correlation coefficient		0.97	0.99	1.00

The share of top five and top ten banks in terms of the value of approved loans in total bank lending was 47.2% and 69.6%, respectively. The HHI of loan concentration equalled 660.

The share of top ten banks in total lending correlates highly positively with the HHI (practically 1), which is not the case with their share in total assets and deposits where the same coefficient is even negative. Clearly, competition for clients in terms of lending is of utmost significance for all banks given that this is the only category<sup>5</sup> where the top ten banks are not lagging behind. Considering the increase in the share of both top five and top ten banks, the burden of their credit expansion is probably felt by all other banks too.

### Deposit activity

The table below gives a breakdown of deposits by sector:

**Table 8 – Bank deposit activity (in RSD bln)**

Sector	31 Dec 2007			31 Dec 2008			31 March 2009			Growth index for Q1/Q4	Growth index for 2008
	dinars	foreign currency	total	dinars	foreign currency	total	dinars	foreign currency	total		
<b>Total deposits</b>	<b>344.0</b>	<b>616.2</b>	<b>960.2</b>	<b>317.6</b>	<b>707.1</b>	<b>1,024.7</b>	<b>282.4</b>	<b>773.1</b>	<b>1,055.5</b>	<b>103</b>	<b>107</b>
Banks	30.2	93.4	123.7	56.1	98.3	154.4	46.8	50.2	97.0	63	125
Public enterprises	31.9	7.8	39.7	25.4	22.5	47.9	25.6	23.8	49.4	103	121
Other enterprises	185.1	105.6	290.7	152.8	115.2	268.0	119.8	136.6	256.4	96	92
Public sector	26.6	0.9	27.4	20.1	1.0	21.1	33.3	2.2	35.5	168	77
Foreign legal and natural persons	6.4	24.6	31.0	3.6	54.2	57.8	5.2	105.9	111.1	192	186
Households	46.8	381.4	428.2	52.4	414.5	467.0	46.2	452.2	498.4	107	109
Other	17.1	2.4	19.5	7.1	1.5	8.6	5.5	2.2	7.7	89	44

<sup>5</sup> Assets, loans and deposits.

Household deposits accounted for the largest share of total deposits (47.2%), followed by the deposits of enterprises (24.3%) and foreign entities (10.5%).

Foreign currency deposits made up 73.2% and dinar deposits 26.8% of total deposits. Demand deposits<sup>6</sup> (46.3%) were dominant, followed by short-term time deposits (49.5%). Long-term deposits accounted for mere 4.3% of total deposits.

Total deposits rose by RSD 30.8 billion in Q1. All categories of deposits recorded an increase save banks, other enterprises and category other (down by RSD 57.4 billion, RSD 11.6 billion and RSD 0.9 billion, respectively).

The share of top five and top ten banks in total banking sector deposits was 51.1% and 71.7%, respectively. HHI of deposit concentration stood at 758 v. 693 a quarter earlier.

**Table 9 – Deposit concentration indicators**

Year	Month	Share of top five banks (%)	Share of top ten banks (%)	HHI Deposits
2009	March	51.07%	71.70%	758
	February	49.89%	71.27%	722
	January	50.20%	71.33%	722
2008	December	49.79%	71.66%	693
	November	50.02%	72.28%	710
	October	49.37%	72.52%	698
	September	49.42%	72.74%	705
	August	49.69%	72.75%	707
	July	49.81%	72.34%	707
Correlation coefficient		0.91	(0.46)	1,00

Out of assets, loans and deposits, it is the category of deposits that the highest level of concentration is recorded for – both for the top five and top ten banks. However, even though the HHI for deposits is at its historical high (July 2008 onwards) and above the HHI for assets and loans, it remains significantly below the level indicating moderate concentration (1,000).

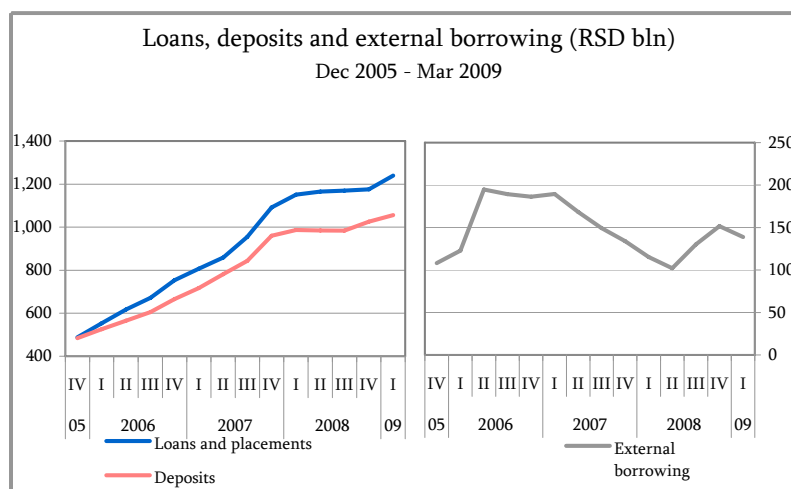
### External borrowing by the banking sector

Total external borrowing by the banking sector (credits from foreign banks and foreign legal entities and natural persons) came to RSD 138.7 billion and related mostly to borrowing maturing in more than five years (61.2%). Two foreign owned banks accounted for 43% of total borrowing.

<sup>6</sup> Deposits with no initial maturity, with no set term and up to 14 days.

During Q1 2009, external borrowing by banks declined by RSD 13 billion.

**Chart 5 – Loans<sup>7</sup>, deposits and external borrowing**



## Banking sector risks

### 1. Credit risk

#### 1.1. Quality of balance sheet and off-balance sheet assets

In order to ensure adequate and efficient risk management by banks, the National Bank of Serbia prescribed in its Decision on the Classification of Bank Balance Sheet Assets and Off-Balance Sheet Items, an obligation for banks to classify on a quarterly basis all receivables that carry credit risk into five categories by the assessed level of their collectibility and financial standing of the borrower. This in effect means that banks are required to classify those receivables that constitute the risk-weighted balance sheet and off-balance sheet assets (hereinafter: BA and OA), which includes not only credits, but other balance sheet assets and certain off-balance sheet items as well, as defined in the above Decision.

The new Decision on the Classification of Bank Balance Sheet Assets and Off-Balance Sheet Items brought some changes to the classification criteria<sup>8</sup> - the most adversely classified assets are now classified in categories D and E. In

<sup>7</sup> Including NBS repo lending.

<sup>8</sup> Changes to classification criteria relate to the number of days in default.

Q1 2009, risk-weighted (classified) assets accounted for 44.1% of gross balance sheet assets and off-balance sheet items.

**Table 10** – Classified balance sheet and off-balance sheet assets (RSD bln)

		Total classified assets	Classified assets		D + E / total classified assets (%)
			A+B+C	D+E	
March 2009	Balance sheet assets	1,270	1,031	239	18.80
	Off-balance sheet items	656	605	50	7.68
	TOTAL	1,925	1,636	289	15.01
December 2008	Balance sheet assets	1,178	982	196	16.64
	Off-balance sheet items	662	624	38	5.78
	TOTAL	1,840	1,605	234	12.73
September 2008	Balance sheet assets	1,078	914	164	15.20
	Off-balance sheet items	590	549	40	6.86
	TOTAL	1,668	1,464	204	12.25

Special reserves for potential losses on classified balance sheet assets and off-balance sheet items totalled RSD 283.3 billion, while balance sheet asset value adjustments and provisioning on off-balance sheet items reached RSD 125.9 billion.

## 1.2. Non-performing loans (NPLs)

According to the NPL Composition Reports submitted by banks to the National Bank of Serbia, on 31 March 2009 the share of NPLs in total loans approved was 8.12% in net terms.

**Table 11** – NPLs by sector (%)

	March 2009	December 2008	September 2008
Financial sector	8.93	0.36	0.31
Public enterprises	2.20	1.14	0.74
Other enterprises	11.60	7.11	5.82
Entrepreneurs	3.94	2.79	2.97
Public sector	1.13	0.61	0.20
Households	3.58	3.81	2.66
Foreign entities	1.67	2.75	3.65
Private households with employees and registered agricultural producers	5.28	5.72	3.67
Other clients	2.78	2.07	1.93
TOTAL	8.12	5.29	4.33

Of the nine sectors, the following three recorded a decrease in the share of NPLs relative to December 2008:

- households (from 3.81 to 3.58% in Q1 this year),
- foreign entities (from 2.75 to 1.67%) and
- private households and registered agricultural producers (from 5.72 to 5.28%).

The strongest increase in the share of NPLs was registered in the financial sector (from 0.36% in December to 8.93% in March amid a sharp rise in loans to *other legal entities* engaging primarily in finance<sup>9</sup>), and, most importantly, in the sector of *other enterprises* (from 7.11% in December to 11.6% in March 2009).

The share of NPLs in total lending to natural persons (Table 11) remained at the December 2008 level – 3.62%. Cash loans (4.09% in Q1), credit cards (1.58%) and housing construction (3.02%) are the segments where the share of NPLs declined relative to Q4 2008.

**Table 12 – NPLs – natural persons (%)**

	March 2009	December 2008	September 2008
Cash loans	4.09	4.61	2.97
Credit cards	1.58	1.77	1.66
Current account overdrafts	3.58	2.69	2.58
Consumer loans	3.88	2.59	3.88
Agricultural activity	5.82	5.74	3.06
Performance of other activities	3.23	1.75	1.43
Housing construction	3.02	3.58	1.82
Other	14.29	5.90	6.92
TOTAL	3.62	3.63	2.58

In terms of other categories of natural persons' loans that recorded an increase in NPLs, category *other*<sup>10</sup> should be singled out (from 5.90% to 14.30% in Q1), consumer loans (from 2.59% to 3.88%), as well as current account overdrafts (from 2.69% to 3.58%).

<sup>9</sup> Make up around 8% of the financial sector's position and relate primarily to broker-dealer companies. Their share of NPLs rose from 1.63% to as much as 41.2%.

<sup>10</sup> This category includes non-standard loans to natural persons.

According to the Credit Bureau<sup>11</sup> data on the stock of debt on bank credits<sup>12</sup> and overdue obligations (over 90 days), the balance is as follows:

**Table 13 – Overdue obligations (over 90 days) (RSD bln)**

		Default in excess of 90 days		
		Outstanding debt	Total loans	Amount in default
2009	March	1,320.76	120.68	61.93
	December	1,232.95	71.43	43.77
2008	September	1,037.15	62.27	35.34
	June	1,009.01	53.61	31.65
	March	1,008.26	44.08	27.87
	December	865.45	44.21	28.12
2007	September	809.42	42.05	27.18
	June	749.17	35.14	24.44
	March	660.92	29.92	21.46
	December			

The Credit Bureau data also reveal an upward trend in the share of NPLs in bank portfolios. March share of NPLs (9.14%) represents a considerable increase compared to the historical average over the previous seven quarters of around 5.2%.

A more detailed overview is given in the table below.

**Table 14 – NPLs by sector (%)**

		Legal entities	Entrepreneurs	Natural persons	Total
2009	March	11.05	5.29	5.38	9.14
	December	6.86	3.66	3.80	5.79
2008	September	6.99	3.45	4.18	6.00
	June	6.21	3.41	3.65	5.31
	March	5.05	4.48	2.92	4.37
	December	6.50	3.93	2.68	5.11
2007	September	6.50	3.77	2.86	5.20
	June	5.60	3.14	3.03	4.69
	March				

## 2. Liquidity risk

In March 2009, liquidity ratio for the banking sector as a whole averaged 1.88. Liquidity ratios of state and foreign-owned banks were practically the same (1.81 and 1.80, respectively), while that of private banks was significantly higher - 2.65.

<sup>11</sup> Of the Serbian Banking Association.

<sup>12</sup> Total loans approved (gross, prior to deduction of allowances for impairment) with overdue interest and fees for legal entities and calculated interest and fees for private individuals.

It can be said that such liquidity is satisfactory especially in light of the regulatory minimum liquidity ratio (1) and the fact that even in the direst times for the global economy (October 2008) the liquidity ratio for the Serbian banking sector ratio stood at 1.71, the lowest being for the privately-owned banks -1.63.

A detailed overview of the level and movements in the liquidity ratio is shown in the table below.

**Table 15 – Average monthly liquidity ratio of the banking sector**

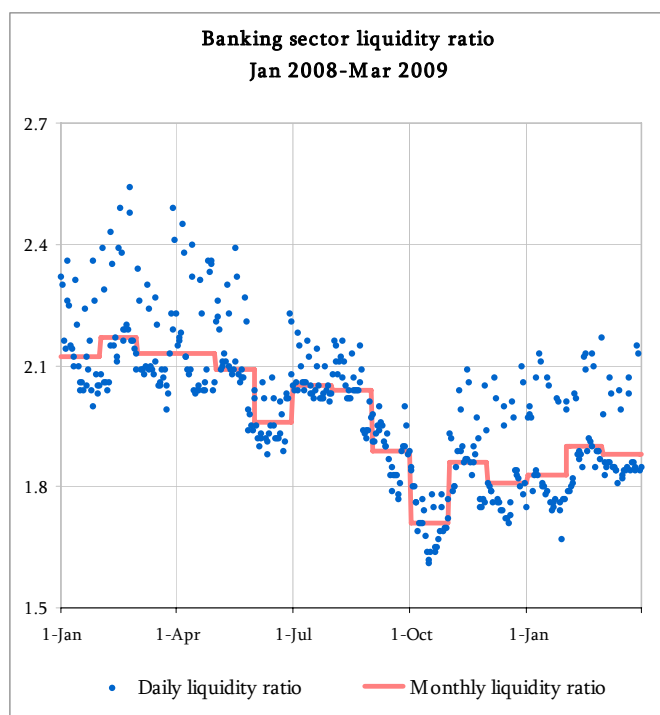
		Type of ownership			Banking sector
		State-owned	Privately-owned	Foreign-owned	
2009	Mar	1.81	2.65	1.80	1.88
	Feb	2.15	2.38	1.79	1.90
	Jan	1.92	2.61	1.72	1.83
2008	Dec	1.70	2.73	1.73	1.81
	Nov	1.71	2.20	1.84	1.86
	Oct	2.03	1.63	1.67	1.71
	Sep	1.74	1.63	1.96	1.89
	Aug	2.15	1.76	2.06	2.04
	Jul	2.50	1.73	2.03	2.05
	Jun	2.17	1.60	1.97	1.96
	May	2.88	1.89	2.00	2.09
	Apr	3.27	1.81	2.01	2.13
	Mar	2.36	1.77	2.13	2.13
	Feb	2.85	1.86	2.11	2.17
	Jan	2.65	1.97	2.06	2.12

During the three months under review, liquidity ratios of individual banks stayed within the prescribed limits.

**Table 16 – Banking sector liquid assets**  
(in RSD mln and %)

Period	Liquid assets	Share in total balance sheet assets
March 2009	516,176	28.6
December 2008	542,786	30.6
November 2008	570,934	31.6
October 2008	588,576	33.2
September 2008	601,687	35.1

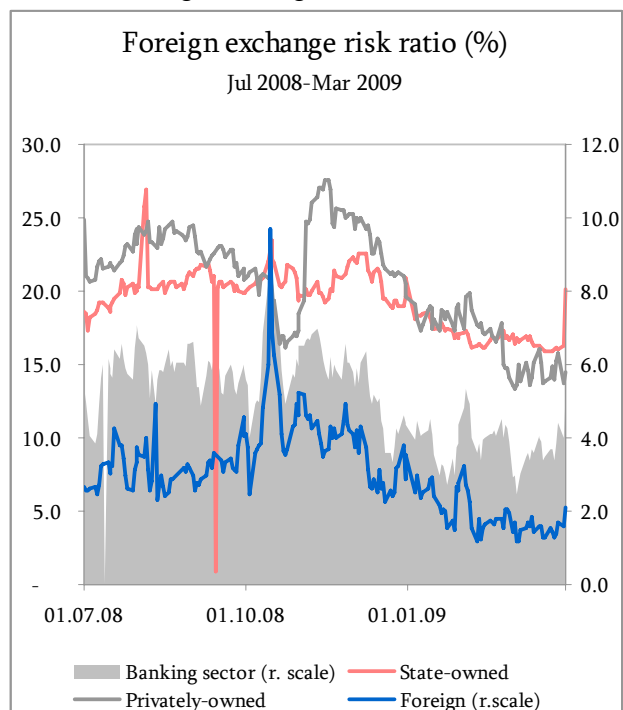


**Chart 6 - Banking sector liquidity ratio**

### 3. Foreign exchange risk

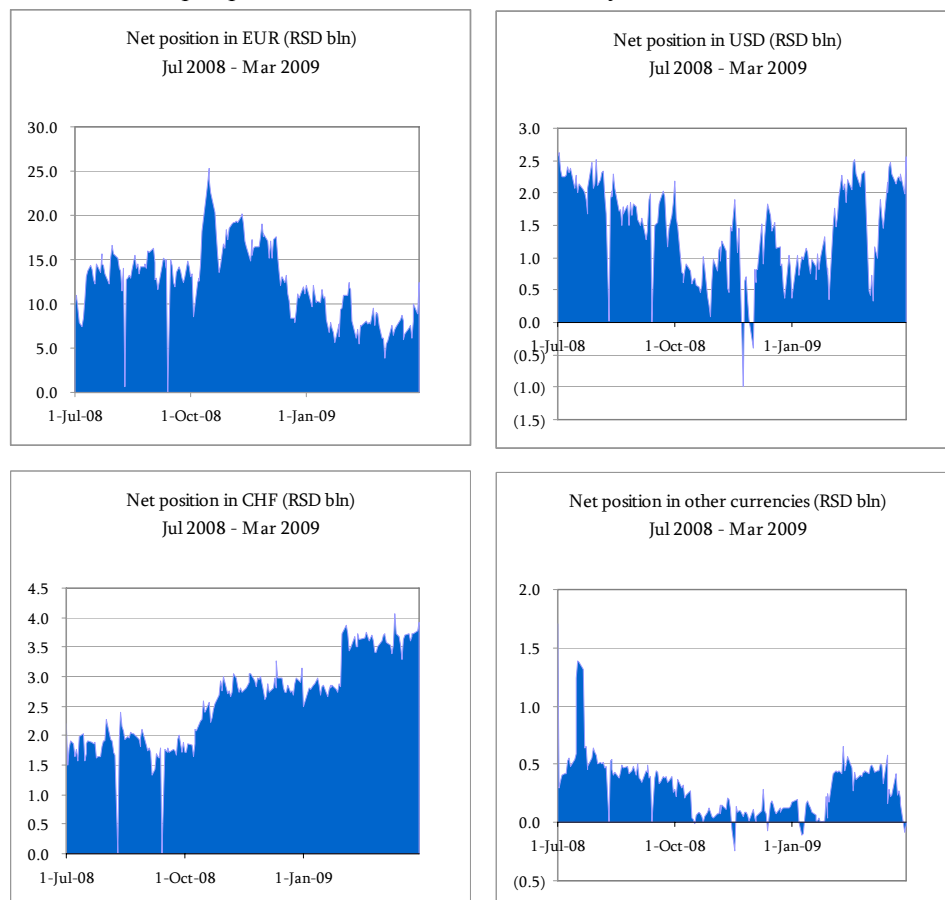
On 31 March 2009 the foreign exchange risk ratio of the Serbian banking sector equalled 5.16% of regulatory capital. Over the first quarter it ranged from the minimum 2.46% to maximum 5.33%. Its movements are shown in greater detail in Chart 7.

The foreign exchange risk ratio is on a downward path – both for the banking sector as a whole and individual groups of banks.

**Chart 7 - Foreign exchange risk ratio**

Since July 2008, i.e. introduction of the new methodology for the calculation of foreign currency position, the Serbian banking sector has had a net long open foreign currency position in all currencies save the US dollar (for a very brief time period) and currencies within the category *other*.

Movements in net open position by individual currencies (EUR, USD, CHF and other) in the past three quarters are shown in Chart 8.

**Chart 8** – Net open position in selected currencies, July 2008 – March 2009

## Capital adequacy

A mildly declining trend in the banking sector capital adequacy ratio continued in 2009. Namely, the capital adequacy ratio declined from 21.89% in Q4 2008 to 20.81% in Q1 2009.

The capital adequacy ratio decreased for two reasons:

1. Regulatory capital fell by RSD 10 billion (around 2.8%) as the growth in deductions from capital (up by RSD 18.7 billion from RSD 85.8 billion) was outstripped by the growth in core capital (up by RSD 6.9 billion) and supplementary capital 1 and 2 (up by RSD 1.7 billion).

2. Overall risk-weighted assets rose by RSD 37.8 billion (around 2.3%) primarily on account of a RSD 41.6 billion increase in the credit risk-weighted assets. At the same time, a negligible decline was recorded in assets exposed to

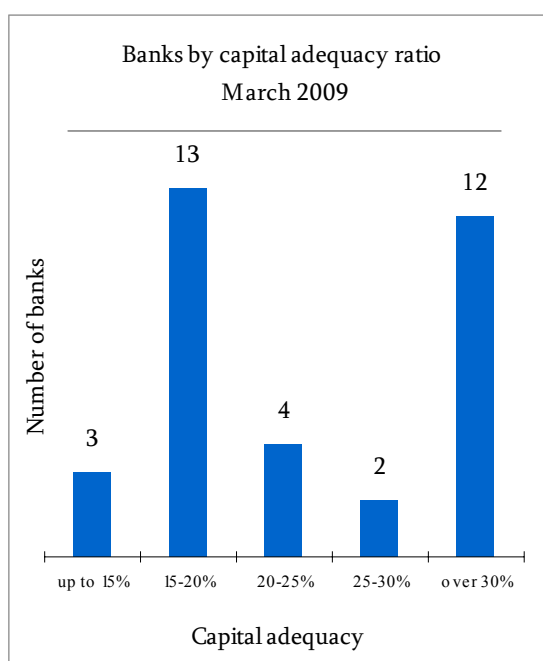
foreign exchange risk (down by RSD 2.8 billion) and other market risks (down by RSD 1.1 billion).

**Table 17** – Elements of capital and risky assets (RSD bln)

	Mar 2009	Dec 2008	Sep 2008
1. Capital	353.8	363.8	346.2
i. Core capital	385.8	378.9	363.8
ii. Supplementary capital 1 and 2 included in the bank's capital	72.5	70.8	65.0
iii. Deductions from capital	104.5	85.8	82.5
2. Total risky assets	1,700.1	1,662.3	1,486.3
i. Credit risk-weighted assets	1,675.4	1,633.8	1,455.0
ii. Foreign exchange risk exposure	23.1	25.9	27.9
iii. Exposure to other market risks	1.6	2.7	3.4
3. Capital adequacy ratio (%)	20.81	21.89	23.30

The chart below gives an overview of banks by the level of their capital adequacy ratios in Q1 2009.

**Chart 9** – Banks by capital adequacy ratio, March 2009



In Q1, sixteen banks had an up to 20% capital adequacy ratio, six banks had a capital adequacy ratio between 20 and 30%, while one bank's ratio exceeded 30%. One bank, which was under temporary measures of the National Bank of Serbia, had a capital adequacy ratio below 12%.

## Banking sector profitability indicators

In the first three months of 2009, the banking sector posted a RSD 6.86 billion pre-tax profit, down by 37% relative to the same period a year earlier (RSD 11.02 billion).

The coverage of operating expenses with net interest income may be considered satisfactory. From March 2008 onwards, net interest income fully covered the operating expenses. In Q1 2009, this ratio stood at 1.07x. Net income from fees and commissions included, the coverage of operating expenses equalled 1.49x.

A detailed overview of the levels and movements of the above ratio is shown in the table below.

**Table 18** – Banking sector profitability\* – Overall result and coverage of operating expenses

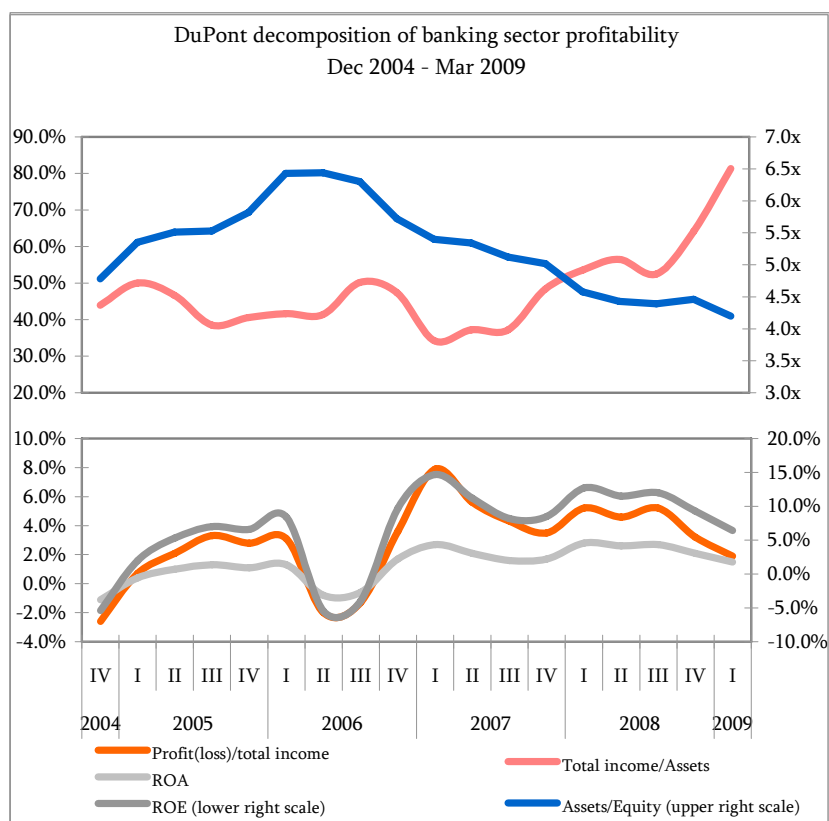
		Profit (loss)** (RSD bln)	Net interest income / Operating expenses	Net interest and commissions income / Operating expenses
		1	2	3
2009	Mar	6.86	1.07	1.41
	Dec	34.74	1.11	1.46
2008	Sep	33.68	1.12	1.54
	Jun	20.89	1.12	1.53
	Mar	11.02	1.06	1.49
	Dec	23.27	0.88	1.26
2007	Sep	15.61	0.92	1.32
	Jun	13.31	0.92	1.31
	Mar	8.25	0.93	1.34
	Dec	16.53	0.79	1.16
2006	Sep	-4.42	0.78	1.15
	Jun	-3.77	0.75	1.13
	Mar	2.65	0.81	1.22
	Dec	7.27	0.81	1.24
2005	Sep	5.63	0.86	1.32
	Jun	2.66	0.86	1.31
	Mar	0.49	0.88	1.32
2004	Dec	-4.99	0.74	1.18

\*Annualized data

\*\* Pre tax

Chart 10 and Table 19 show the decomposition of the banking sector's financial result according to the *DuPont* methodology.

**Chart 10 – DuPont decomposition of profitability**



**Table 19** – Banking sector profitability at quarterly level –  
*DuPont* decomposition (annualized data)

		Profit (loss) / Net income	Net income / Assets	ROA	Assets / Equity	ROE
		1	2	3=1x2	4	5=3x4
2009	Mar	1.90%	81.30%	1.50%	4.20	6.40%
	Dec	3.20%	64.10%	2.10%	4.46	9.30%
2008	Sep	5.20%	52.50%	2.70%	4.39	12.00%
	Jun	4.60%	56.50%	2.60%	4.43	11.50%
	Mar	5.20%	53.50%	2.80%	4.58	12.70%
2007	Dec	3.50%	48.40%	1.70%	5.02	8.50%
	Sep	4.30%	37.20%	1.60%	5.12	8.20%
	Jun	5.60%	37.20%	2.10%	5.34	11.20%
	Mar	7.90%	34.30%	2.70%	5.40	14.70%
	Dec	3.60%	47.40%	1.70%	5.72	9.70%
2006	Sep	-1.30%	50.20%	-0.60%	6.30	-4.00%
	Jun	-2.00%	41.40%	-0.80%	6.44	-5.50%
	Mar	3.10%	41.60%	1.30%	6.43	8.40%
	Dec	2.80%	40.60%	1.10%	5.82	6.60%
2005	Sep	3.30%	38.50%	1.30%	5.53	7.00%
	Jun	2.10%	46.60%	1.00%	5.51	5.30%
	Mar	0.70%	50.00%	0.40%	5.35	2.00%
	Dec	0.70%	50.00%	0.40%	5.35	2.00%
2004	Децембар	-2,60%	43,90%	-1,10%	4,78	-5,40%

Profitability of the banking sector should also be analyzed from the aspect of additional decomposition of the profit and loss account presented in the table below.

**Table 20** – Banking sector profitability – Decomposition of the profit and loss account

као % просечне активе										
Нето камате и накнаде		Нето камате и накнаде	Нето ефекат курса*	Нето остали приходи**	Нето исправке и резервисања	Оперативни расходи	Резултат пре опреозивања (ROA)	Активна / Капитал	Принос на капитал (ROE)	
1	2	3=1+2	4	5	6	7	8=3+4+5+6+7	9	10=8x9	
Март	5,25	1,66	6,90	1,12	0,28	(1,83)	(4,94)	1,53	4,20	6,44
2009 Фебруар	5,31	1,60	6,91	1,33	0,31	(0,90)	(4,83)	2,82	4,20	11,83
Јануар	5,11	1,73	6,83	2,31	0,06	(0,95)	(4,64)	3,61	4,23	15,27
Децембар	5,70	1,83	7,53	1,01	0,33	(1,56)	(5,24)	2,08	4,46	9,28
Новембар	5,37	1,98	7,34	1,02	0,24	(0,87)	(4,97)	2,77	4,45	12,33
2008 Октобар	5,42	1,99	7,41	1,00	0,26	(0,90)	(4,95)	2,83	4,43	12,53
Септембар	5,46	2,01	7,47	0,75	0,29	(0,81)	(4,96)	2,74	4,39	12,03
Август	5,45	2,02	7,48	0,81	0,31	(0,64)	(5,00)	2,96	4,38	12,96
Јул	5,46	2,06	7,52	0,88	0,33	(0,86)	(5,03)	2,84	4,36	12,41

\*Збир нето курсних разлика и нето промене вредности имовине и обавеза

\*\*Приходи од дивиденди и учешћа, ХоВ и остали приходи

## Summary statement of income and expenses

In Q1 2009, the banking sector recorded (pre-tax) profits of RSD 6,856 million. A total of 23 banks recorded a positive financial result, while 11 operated with losses.

A detailed overview of income and expenses is presented in the table below.

**Table 21** – Summary statement of income and expenses (RSD mln)

Item	Dec-07	Dec-08	Mar-09
NET INTEREST INCOME/EXPENSES	63,404	95,935	23,494
Interest income	106,942	157,770	41,442
Interest expenses	43,538	61,835	17,948
NET FEES AND COMMISSIONS INCOME/EXPENSES	27,451	29,832	7,414
Fees and commissions income	34,433	38,954	10,301
Fees and commissions expenses	6,983	9,122	2,887
NET INTEREST, FEES AND COMMISSIONS INCOME/EXPENSES	90,854	125,767	30,908
NET INCOME FROM THE SALE OF SECURITIES	3,293	926	-154
Securities income	3,295	1,195	39
Securities expenses	2	269	-192
NET EXCHANGE RATE GAINS/LOSSES	6,959	-53,201	-35,698
INCOME ON DIVIDENDS AND EQUITY INVESTMENTS	1,081	985	3,259
OTHER OPERATING INCOME	53,445	81,473	28,168
EXPENSES ON INDIRECT WRITE-OFFS AND PROVISIONING	61,149	103,899	-34,953
OTHER OPERATING EXPENSES	72,712	87,189	-22,131
NET INCOME/EXPENSES ON CHANGE IN THE VALUE OF ASSETS AND LIABILITIES	1,702	70,094	40,712
Income on change in the value of assets and liabilities	64,271	209,070	76,092
Expenses on change in the value of assets and liabilities	62,569	138,976	35,380
OPERATING PROFIT/LOSS	<b>23,473</b>	<b>34,956</b>	<b>6,856</b>
Profit from discontinued operations	0	0	0
Losses from discontinued operations	0	0	0
<b>PROFIT/LOSSES BEFORE TAX</b>	<b>23,473</b>	<b>34,956</b>	<b>6,856</b>

The net effect of exchange rate gains/losses and changes in the value of assets and liabilities was positive – around RSD 4 billion. The share of income from interest and commissions declined mildly from Q4 reaching 14.2% in Q1, while the share of expenses on interest and commissions made up 5.9% of total expenses.



**Table 22** – Banking sector competitiveness indicators – Total income

Year	Month	Share of top five banks (%)	Share of top ten banks (%)	HHI Total income
2009	March	52.37	74.63	772
	February	54.63	76.74	847
	January	54.35	78.37	840
2008	December	50.91	74.28	740
	November	48.55	72.70	700
	October	48.43	72.79	697
	September	47.96	72.56	679
	August	48.14	73.03	690
	July	48.32	73.05	693
Correlation coefficient		0.99	0.96	1.00

From July 2008 the share of top five banks in total income rose by around 4%. At the same time, the share of top ten banks in total income increased by around 1.6%. The HHI consequently rose from 693 to 772, hitting a nine-month high of 847 index points in February 2009.

The correlation coefficient of the share of top five and top ten banks and the HHI is close to 1. In this respect, total income is similar to total loans – top ten banks are not losing, but rather increasing their market share, though not at the same pace as the top five banks.

As indicated by the HHI, there is no concentration in terms of total income, though HHI for this category shows the largest degree of volatility<sup>13</sup> among all categories observed.

## II. Regulatory activity of the National Bank of Serbia

During Q1 2009, the National Bank of Serbia amended the following regulations coming under its regulatory remit in the field of banking supervision:

- ***Decision on Temporary Measures for Preserving Banking Sector Stability in the Republic of Serbia (“RS Official Gazette”, No.12/2009).*** Pursuant to amendments, upon borrower’s request submitted until 31 December 2009, banks may extend the repayment period of cash loans disbursed before 30 September 2008 by up to 12 months from the originally contracted maturity date on condition such loans are converted into dinars, without charging any

<sup>13</sup> Ranking by volatility (volatility coefficient) in the past nine months (ascending order): assets (0.01), deposits (0.03), loans (0.04), total income (0.09).

extra fee on the repayment period extension and/or loan conversion into dinars.

- ***Decision on Temporary Measures for Preserving Financial Stability in the Republic of Serbia.*** The amendments further relax the provisions of the Decision on the Classification of Bank Balance Sheet Assets and Off-Balance Sheet Items as banks are no longer obligated to downgrade receivables from natural persons approved and disbursed after 1 January 2009 against a deposit or downpayment lower than 30% of the value of receivables into category E, which calls for 100% allocation of reserves for estimated losses.
- ***Decision on Adjusting Gross Household Lending and Share Capital of Banks.*** Pursuant to amendments, as of 28 February 2009 banks are to adjust their gross household lending to their share capital so that at the end of each calendar month such lending is lower than or equivalent to 200% of the value of share capital.