

# **National Bank of Serbia**

## **BANKING SECTOR IN SERBIA**

**First Quarter Report 2007**

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## I. Banking sector in the first quarter of 2007

### *Structure of banking sector in Serbia as at 31 March 2007*

#### Number of banks

The number of banks operating in the Serbian market increased by one in Q1 2007, after the savings bank Opportunity stedionica a.d. Novi Sad was issued a licence by the NBS to continue operating as a bank – Opportunity banka a.d. Novi Sad.

|                 | 31 Dec 2005 | 31 Dec 2006 | 31 Mar 2007 |
|-----------------|-------------|-------------|-------------|
| Number of banks | 40          | 37          | 38          |

#### Network of banks

In late March 2007, the organizational network of all banks included a total of 2,195 business units, branches, branch offices and teller units. This is 37 more than at the end of 2006. Largest contributors to bank network expansion in Serbia in Q1 2007 were AIK banka a.d. Nis, Panonska banka a.d. Novi Sad and Piraeus Bank a.d. Beograd, which opened 6 new organizational units each, while Banca Intesa a.d. Beograd reduced the number of its branch offices by 12 and Laiki Bank a.d. Beograd by 9 compared to a quarter earlier.

| Description              | 31 Dec 2005  | 31 Dec 2007  | 31 Mar 2007  |
|--------------------------|--------------|--------------|--------------|
| Number of business units | 114          | 82           | 86           |
| Number of branches       | 327          | 413          | 425          |
| Number of branch offices | 1,162        | 1387         | 1391         |
| Number of teller units   | 264          | 276          | 293          |
| <b>Total</b>             | <b>1,867</b> | <b>2,158</b> | <b>2,195</b> |

#### Banking sector employment

In Q1 2007, the domestic banking system employed a total of 28,587 persons, which is 495 more than in late 2006 (55 of which were employed by Opportunity banka a.d. Novi Sad).

## Ownership structure of banks

At the end of March 2007:

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

## Market share

The table below gives an overview of respective market shares of banks classified by size of balance sheet total:

| Balance sheet total in RSD bln | 31 Dec 2005  |                |              | 31 Dec 2006  |                  |              | 31 Mar 2007  |                  |              |
|--------------------------------|--------------|----------------|--------------|--------------|------------------|--------------|--------------|------------------|--------------|
|                                | No. of banks | in RSD mln     | % share      | No. of banks | in RSD mln       | % share      | No. of banks | in RSD mln       | % share      |
| over 100                       | 1            | 119,423        | 15.4         | 4            | 483,575          | 41.3         | 4            | 507,169          | 40.1         |
| 50–100                         | 3            | 225,073        | 29.0         | 3            | 183,698          | 15.7         | 4            | 248,795          | 19.7         |
| 10–50                          | 17           | 326,953        | 42.2         | 15           | 405,223          | 34.7         | 17           | 434,820          | 34.4         |
| under 10                       | 19           | 103,964        | 13.4         | 15           | 96,775           | 8.3          | 13           | 72,713           | 5.8          |
| <b>Total</b>                   | <b>40</b>    | <b>775,413</b> | <b>100.0</b> | <b>37</b>    | <b>1,169,271</b> | <b>100.0</b> | <b>38</b>    | <b>1,263,497</b> | <b>100.0</b> |

Five banks with the largest end-March balance sheet total and ten banks with the largest end-March balance sheet total accounted for 45.5% and 67.5%, respectively, of the overall balance sheet total of the banking sector. HHI of concentration of balance sheet total equalled 592 or 22 units less than in Q4 2006.

As at 31 March 2007, banks in majority foreign ownership accounted for RSD 991 billion or 78.4%, banks in the majority ownership of the Republic of Serbia for RSD 189 billion or 15.0%, and banks in majority private ownership for RSD 83 billion or 6.6%, of banking sector balance sheet total.

## Banking sector balance sheet<sup>2</sup>

In RSD million

|  | 31 Dec 2005 |            | 31 Dec 2006 |            | 31 Mar 2007 |            | Growth indices in Q1 2007 | Growth indices for 2006 |
|--|-------------|------------|-------------|------------|-------------|------------|---------------------------|-------------------------|
|  | Amount      | Share in % | Amount      | Share in % | Amount      | Share in % |                           |                         |
| <b>ASSETS</b>  |             |            |             |            |             |            |                           |                         |
| Cash and cash equivalents  | 72,781      | 9.4        | 77,815      | 6.7        | 68,829      | 5.5        | 88                        | 107                     |
| Deposits with the central bank and securities refinaceable with the central bank | 150,827     | 19.5       | 406,735     | 34.8       | 439,831     | 34.8       | 108                       | 270                     |
| Interest and fees receivable   | 3,197       | 0.4        | 4,347       | 0.4        | 4,992       | 0.4        | 115                       | 136                     |
| Lending to domestic banks  | 33,206      | 4.3        | 32,415      | 2.8        | 51,919      | 4.1        | 160                       | 98                      |
| Lending to clients   | 426,528     | 55.0       | 545,059     | 46.6       | 590,831     | 46.8       | 108                       | 128                     |
| Securities and other tradable investment   | 9,875       | 1.3        | 8,584       | 0.7        | 11,957      | 1.0        | 139                       | 87                      |
| Investment in securities held to maturity  | 8,467       | 1.1        | 6,948       | 0.6        | 8,152       | 0.6        | 117                       | 82                      |
| Share in capital and other securities available for sale                         | 10,494      | 1.4        | 15,284      | 1.3        | 9,424       | 0.8        | 62                        | 146                     |

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

<sup>2</sup> Balance sheet items have been derived from the aggregate KNJBIFO form for the banking sector according to final entries for 2005 and 2006 and data as at 31 March 2007. For analytical purposes and for the sake of data comparability, balance sheet items for 31 December 2005 have been disclosed in accordance with new balance sheet forms.

*Banking Sector in Serbia – First Quarter Report 2007*

|  | 31 Dec 2005    |              | 31 Dec 2006      |              | 31 Mar 2007      |              | Growth indices in Q1 2007 | Growth indices for 2006 |
|--|----------------|--------------|------------------|--------------|------------------|--------------|---------------------------|-------------------------|
|  | Amount         | Share in %   | Amount           | Share in %   | Amount           | Share in %   |                           |                         |
| Fixed assets intended for sale and assets from discontinued operations*                          |                |              | 394              | 0.0          | 381              | 0.0          | 97                        |                         |
| Rebate on profit tax*  |                |              | 253              | 0.0          | 622              | 0.0          | 246                       |                         |
| Goodwill**   |                |              |                  | 0.0          |                  | 0.0          |                           |                         |
| Intangible investments   | 4,287          | 0.5          | 5,907            | 0.5          | 6,154            | 0.5          | 104                       | 138                     |
| Investment real estate ***   | 806            | 0.1          | 4,266            | 0.4          | 4,383            | 0.3          | 103                       | 529                     |
| Fixed assets   | 40,579         | 5.2          | 47,038           | 4.0          | 49,415           | 3.9          | 105                       | 116                     |
| Other assets, prepayments and accrued income   | 12,844         | 1.6          | 11,748           | 1.0          | 14,129           | 1.1          | 120                       | 91                      |
| Deferred tax assets  | 1,522          | 0.2          | 2,478            | 0.2          | 2,478            | 0.2          | 100                       | 163                     |
| Losses in excess of capital  |                | 0.0          |                  | 0.0          |                  | 0.0          |                           |                         |
| <b>TOTAL</b>   | <b>775,413</b> | <b>100.0</b> | <b>1,169,271</b> | <b>100.0</b> | <b>1,263,497</b> | <b>100.0</b> | <b>108</b>                | <b>151</b>              |
| <b>LIABILITIES</b>   |                |              |                  |              |                  |              |                           |                         |
| Liabilities to domestic banks  | 35,803         | 4.6          | 63,352           | 5.4          | 86,881           | 6.9          | 137                       | 177                     |
| Liabilities to clients   | 580,715        | 74.9         | 817,704          | 69.9         | 858,759          | 68.0         | 105                       | 141                     |
| Liabilities in respect of interest and fees  | 936            | 0.1          | 980              | 0.1          | 871              | 0.1          | 89                        | 105                     |
| Liabilities in respect of securities   | 7              | 0.0          | 10               | 0.0          | 6                | 0.0          | 60                        | 143                     |
| Liabilities from profit  | 201            | 0.0          | 196              | 0.0          | 188              | 0.0          | 96                        | 98                      |
| Liabilities in respect of current tax on profit  |                |              | 525              | 0.0          | 131              | 0.0          | 25                        |                         |
| Liabilities in respect of fixed assets intended for sale and assets from discontinued operations |                |              | 0                | 0.0          | 0                | 0.0          |                           |                         |
| Other operating obligations  | 7,277          | 0.9          | 8,630            | 0.7          | 9,269            | 0.7          | 107                       | 119                     |
| Provisioning   | 7,320          | 0.9          | 9,376            | 0.8          | 9,346            | 0.7          | 100                       | 128                     |
| Other liabilities, accruals and deferred income****  | 16,973         | 2.2          | 51,511           | 4.4          | 63,521           | 5.0          | 123                       | 303                     |
| Deferred tax liabilities   | 368            | 0.0          | 699              | 0.1          | 700              | 0.1          | 100                       | 190                     |
| <b>LIABILITIES</b>   | <b>649,600</b> | <b>83.8</b>  | <b>952,983</b>   | <b>81.5</b>  | <b>1,029,671</b> | <b>81.5</b>  | <b>108</b>                | <b>147</b>              |
| Capital  | 125,813        | 16.2         | 216,288          | 18.5         | 233,825          | 18.5         | 108                       | 172                     |
| equity and other capital ****  | 106,984        | 13.8         | 182,562          | 15.6         | 192,263          | 15.2         | 105                       | 171                     |
| Reserves   | 19,168         | 2.5          | 30,464           | 2.6          | 33,582           | 2.7          | 110                       | 159                     |
| accumulated profit/loss  | -339           | 0.0          | 3,262            | 0.3          | 7,980            | 0.6          | 245                       | -                       |
| <b>TOTAL</b>   | <b>775,413</b> | <b>100.0</b> | <b>1,169,271</b> | <b>100.0</b> | <b>1,263,497</b> | <b>100.0</b> | <b>108</b>                | <b>151</b>              |
| <b>OFF-BALANCE SHEET ITEMS</b>   | <b>726,007</b> |              | <b>1,163,308</b> |              | <b>1,329,870</b> |              | <b>114</b>                | <b>160</b>              |

\* New items.

\*\* Until 31 December 2006 included in item Intangible investment.

\*\*\* Until 31 December 2006 included in item Fixed assets.

\*\*\*\* Until 31 December 2006 item Other "capital" – non-operating was disclosed within Other liabilities, accruals and deferred income. As new balance sheet forms envisage that the above item be disclosed within item Equity and other capital, balances for 31 December 2005 were also transferred for analytical purposes.

As at 31 March 2007, balance sheet total of the banking sector stood at RSD 1,263.5 billion, which is RSD 94 billion or 8% higher than at end-2006.

Receivables in respect of approved credits and lending (lending to domestic banks, lending to clients and interest and fees receivable) accounted for the largest part of balance sheet assets of banks (51.3%). Next in size are deposits with the National Bank of Serbia and securities refinanceable with the National Bank of Serbia (34.8%)<sup>3</sup>. Cash and cash equivalents made up 5.5% of balance sheet assets of the banking sector.

Borrowed sources of financing made up 81.5% of banking sector balance sheet liabilities, while capital or own sources of financing accounted for 18.5%. Deposit potential accounted for the largest portion of borrowed sources, with 57.9% of total liabilities.

<sup>3</sup> Rise in this item in 2006 resulted from the transfer (in line with new balance sheet forms) of NBS lending under repo transactions (RSD 144.9 billion) from item Lending to banks to item Deposits with the central bank.

Balance sheet capital of banks reached RSD 234 billion (in 2006, it rose by 71.9%, and in Q1 2007, by 8.1%). Within capital, equity and other capital stood at RSD 192 billion, which is 5.3% higher than in late December 2006.

Off-balance sheet items of banks reached RSD 1,330 billion, having risen by RSD 167 billion compared to end-2006. The largest individual off-balance sheet item was *Other off-balance sheet assets*,<sup>4</sup> which made up 48.1% of all off-balance sheet items. Second in size was item *Receivables in respect of bonds issued against foreign currency savings*, which accounted for 19.4% of total off-balance sheet items.

### **Lending activity**

The table below gives an overview of composition and developments in bank lending:

in RSD million

| Sector                        | 31 Dec 2005    |              | 31 Dec 2006    |              | 31 Mar 2007    |              | Growth indices in Q1 2007 | Growth indices for 2006 |
|-------------------------------|----------------|--------------|----------------|--------------|----------------|--------------|---------------------------|-------------------------|
|                               | Amount         | Share in %   | Amount         | Share in %   | Amount         | Share in %   |                           |                         |
| ENTERPRISES                   | 281,855        | 64.8         | 322,972        | 59.2         | 351,159        | 59.0         | 109                       | 115                     |
| HOUSEHOLDS                    | 124,651        | 28.7         | 195,873        | 35.9         | 222,276        | 37.3         | 113                       | 157                     |
| Housing construction          | 23,289         | 5.4          | 47,334         | 8.7          | 55,811         | 9.4          | 118                       | 203                     |
| PUBLIC SECTOR                 | 23,812         | 5.5          | 21,644         | 4.0          | 17,348         | 2.9          | 80                        | 91                      |
| SCG                           | 981            | 0.2          | 220            | 0.0          | 234            | 0.0          | 106                       | 22                      |
| Republic of Serbia            | 20,683         | 4.8          | 16,693         | 3.1          | 12,073         | 2.0          | 72                        | 81                      |
| Local government              | 2,148          | 0.5          | 4,731          | 0.9          | 5,041          | 0.9          | 107                       | 220                     |
| OTHER FINANCIAL ORGANIZATIONS | 444            | 0.1          | 756            | 0.1          | 686            | 0.1          | 91                        | 170                     |
| NON-PROFIT INSTITUTIONS       | 3,765          | 0.9          | 4,236          | 0.8          | 4,212          | 0.7          | 99                        | 112                     |
| <b>TOTAL</b>                  | <b>434,527</b> | <b>100.0</b> | <b>545,481</b> | <b>100.0</b> | <b>595,681</b> | <b>100.0</b> | <b>109</b>                | <b>125</b>              |

Lending activity of banks rose by 9.2% in Q1 2007, with strongest growth recorded for lending to households (13.5%).

Lending to enterprises (59.0%) and households (37.3%) dominate in the composition of lending. Lending to enterprises rose most in nominal terms (RSD 28.2 billion), while lending to households recorded the strongest growth in relative terms (by 13%). The share of the latter sector in overall lending activity thus climbed from 35.9% to 37.3%.

Five banks with the largest amount of approved credits and ten banks with the largest amount of approved credits accounted for 44.3% and 67.1%, respectively, of total lending activity of the banking sector. HHI of credit concentration equalled 561.

### **Deposit activity**

The table below gives a breakdown of deposits by sector:

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

in RSD million

| Sector                                     | 31 Dec 2005 |                  |         | 31 Dec 2006 |                  |         | 31 Mar 2007 |                  |         | Growth indices in Q1 2007 | Growth indices for 2006 |
|--|-------------|------------------|---------|-------------|------------------|---------|-------------|------------------|---------|---------------------------|-------------------------|
|  | dinars      | foreign currency | total   | dinars      | foreign currency | total   | dinars      | foreign currency | total   |                           |                         |
| Total deposits                             | 142,211     | 342,472          | 484,683 | 227,382     | 438,908          | 666,290 | 238,095     | 478,820          | 716,915 | 108                       | 137                     |
| Banks                                      | 7,315       | 64,964           | 72,279  | 25,102      | 73,122           | 98,224  | 33,552      | 64,866           | 98,418  | 100                       | 136                     |
| Public enterprises                         | 18,468      | 13,058           | 31,526  | 24,619      | 9,402            | 34,021  | 18,721      | 7,039            | 25,760  | 76                        | 108                     |
| Other enterprises                          | 65,934      | 53,928           | 119,862 | 105,344     | 72,489           | 177,833 | 106,963     | 79,316           | 186,279 | 105                       | 148                     |
| Public sector                              | 14,082      | 946              | 15,028  | 21,103      | 723              | 21,826  | 23,380      | 7750             | 24,130  | 111                       | 145                     |
| SCG  | 284         | 401              | 685     | 226         | 32               | 258     | 592         | 4                | 596     | 231                       | 38                      |
| RS   | 2,370       | 506              | 2,876   | 6,778       | 682              | 7,460   | 7,363       | 731              | 8,094   | 108                       | 259                     |
| Local govt.                                | 11,428      | 39               | 11,467  | 14,099      | 9                | 14,108  | 15,425      | 15               | 15,440  | 109                       | 123                     |
| Other clients                              | 9,193       | 3,324            | 12,517  | 11,507      | 2,362            | 13,869  | 11,795      | 2,531            | 14,326  | 103                       | 111                     |
| Foreign legal entities and natural persons | 1,578       | 16,334           | 17,912  | 2,736       | 19,639           | 22,375  | 3,678       | 30,812           | 34,490  | 154                       | 125                     |
| Households                                 | 22,268      | 190,025          | 212,293 | 33,523      | 260,746          | 294,269 | 35,789      | 293,270          | 329,059 | 112                       | 139                     |
| Other                                      | 3,372       | -107             | 3,265   | 3,448       | 425              | 3,873   | 4,217       | 236              | 4,453   | 115                       | 122                     |

The largest percentage of deposits were household deposits (45.9%), followed by enterprise deposits (29.6%) and bank deposits (13.7%).

Foreign currency deposits made up 66.8% and dinar deposits 33.2% of total deposits. Demand deposits (47.4%) and short-term time deposits (43.1%) were dominant.

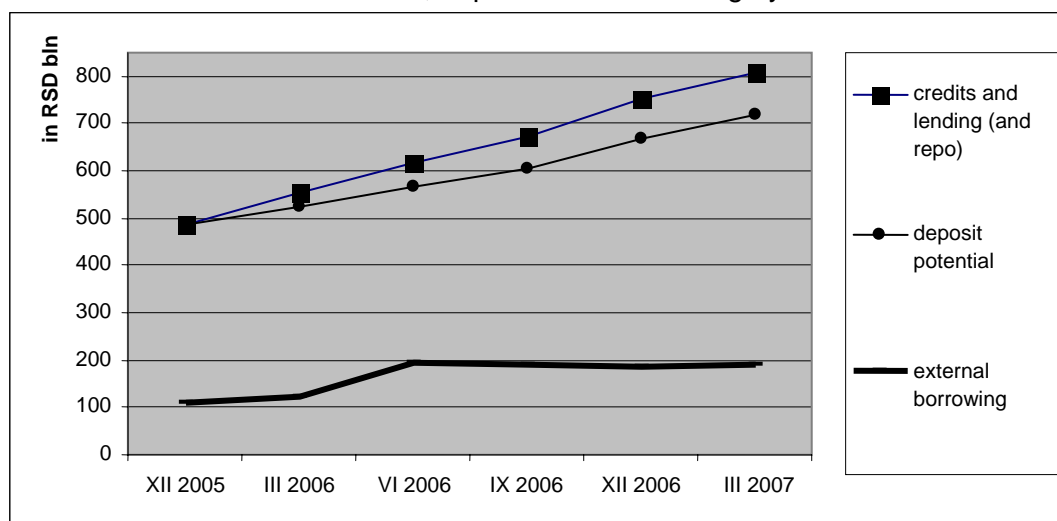
Overall deposit potential grew by RSD 50.6 billion or 7.6% in Q1 2007. Foreign currency deposits increased by RSD 39.9 billion or 9.1%, while dinar deposits went up by RSD 10.7 billion or 4.7%.

Breakdown by sector shows that household deposits and deposits of foreign persons increased most in Q1 2007 – by RSD 34.8 billion or 11.8% and RSD 12.1 billion or 54.1%, respectively.

Five banks with the largest amount of deposits and ten banks with the largest amount of deposits accounted for 47.0% and 67.4%, respectively, of total banking sector deposits. HHI of deposit concentration stood at 641 and was 42 units lower than in Q4 2006.

### **External borrowing by the banking sector**

Total external borrowing by the banking sector (credits from foreign banks and foreign legal entities and natural persons) amounted to RSD 189.7 billion. This is entirely foreign currency borrowing and 97.2% of it matures in over one year. Although in Q1 2007 external credits of banks rose by RSD 3.4 billion (1.8%), their share in overall balance sheet liabilities of the banking sector declined from 15.9% (end-2006) to 15.0% on 31 March 2007.

**Chart 1: Credits, deposits and borrowing by banks**


## Banking sector risks

### 1. Quality of assets

In order to ensure adequate and efficient risk management by banks, in its Decision on the Classification of Bank Balance Sheet Assets and Off-Balance Sheet Items the NBS prescribes that banks should classify all receivables that carry credit risk into five categories on a quarterly basis, depending on the assessed level of collectibility of receivables and financial standing of the borrower. This means that banks are to classify receivables that constitute risk-weighted balance sheet and off-balance sheet assets (hereinafter: BA and OA), i.e. not only credits but also other items of balance sheet assets and certain off-balance sheet items, as defined in the above Decision.

The table below gives an overview of quality of banking sector assets, as defined above, on 31 December 2006 and 31 March 2007.

|  |                  | In RSD million   |              |              |               |
|--|------------------|------------------|--------------|--------------|---------------|
|  |                  | As at            | A+B          | C + D + E    | TOTAL         |
| <b>Total BA and OA</b>                     | <b>1</b>         | 31 Dec 06        | -            | -            | 2,437,339     |
|  |                  | 31 Mar 07        | -            | -            | 2,700,420     |
| <b>Gross risk-weighted assets</b>          | <b>2</b>         | 31 Dec 06        | 624,930      | 307,360      | 932,290       |
|  |                  | 31 Mar 07        | 740,430      | 312,296      | 1,052,726     |
| <b>Share in gross risk-weighted assets</b> | <b>3</b>         | <b>31 Dec 06</b> | <b>67.0%</b> | <b>33.0%</b> | <b>100.0%</b> |
|  |                  | <b>31 Mar 07</b> | <b>70.3%</b> | <b>29.7%</b> | <b>100.0%</b> |
| <b>Reductions (total)</b>                  | <b>4 = 5+6+7</b> | 31 Dec 06        | 218,008      | 185,358      | 403,366       |
|  |                  | 31 Mar 07        | 255,134      | 180,869      | 436,003       |
| <b>collaterals*</b>                        | <b>5</b>         | 31 Dec 06        | 202,082      | 102,146      | 304,228       |
|  |                  | 31 Mar 07        | 237,171      | 96,135       | 333,306       |
| <b>provisions against income</b>           | <b>6</b>         | 31 Dec 06        | 9,569        | 80,081       | 89,650        |
|  |                  | 31 Mar 07        | 9,444        | 81,135       | 90,579        |
| <b>provisions against capital</b>          | <b>7</b>         | 31 Dec 06        | 6,357        | 3,131        | 9,488         |
|  |                  | 31 Mar 07        | 8,519        | 3,599        | 12,118        |
| <b>Net risk-weighted assets</b>            | <b>8=2-4</b>     | 31 Dec 06        | 406,922      | 122,002      | 528,924       |
|  |                  | 31 Mar 07        | 485,296      | 131,427      | 616,723       |
| <b>Share in net risk-weighted assets</b>   | <b>9</b>         | <b>31 Dec 06</b> | <b>76.9%</b> | <b>23.1%</b> | <b>100.0%</b> |
|  |                  | <b>31 Mar 07</b> | <b>78.7%</b> | <b>21.3%</b> | <b>100.0%</b> |

\* Reductions do not represent the total value of collateral, but only a part of such value, in line with the prescribed conversion factor which is used as the basis for calculating provisions for potential losses.

Overall balance sheet assets and off-balance sheet items came to RSD 2,700,420 million as at 31 March 2007, of which RSD 1,052,726 million or 39% referred to total gross risk-weighted assets (balance sheet assets and off-balance sheet items). In Q1 2007, the share of total gross risk weighted assets in categories C, D and E declined from 33.0% to 29.7%.

If collaterals that serve as security are taken into account, receivables classified in categories C, D and E accounted for RSD 96,135 million. In order to safeguard against potential losses in respect of receivables from borrowers classified in categories C, D and E, banks provisioned a total of RSD 84,734 million against their income and capital. Taking into account the above items, the share of net risk-weighted BA and OA classified in categories C, D and E in net risk-weighted BA and OA came to 21.3%, which is an improvement compared to 23.1% in late 2006.

## 2. Liquidity risk

The table below presents daily liquidity ratios of banks as at 31 March 2007:

In RSD thousand

| Banks                           | Gyro-account balances | Calculated required reserves | Difference (2-3) | Deposited excess liquidity | Liquidity loans against collateral of securities |
|---------------------------------|-----------------------|------------------------------|------------------|----------------------------|--|
| Total in the Republic of Serbia | 25,976,330            | 25,931,338                   | 44,992           | 6,479,000                  | 0  |

Of the total number of banks, 23 banks used required reserve assets in the total amount of RSD 3,173 million or 12.2% of total calculated required reserves of such banks. No bank used liquidity loans.

During the quarter under review, liquidity ratio of individual banks remained within prescribed limits, ranging from 1.00 to 139.46<sup>5</sup>.

## 3. Foreign exchange risk

An analysis of foreign currency positions of the banking sector as at 30 March 2007 shows that total open foreign currency position was RSD 34.5 billion, which is RSD 4.1 billion lower than at the end of Q4 2006<sup>6</sup>. Thus, foreign exchange risk exposure of the banking sector subsided compared to a quarter earlier, with the foreign exchange risk ratio equalling 17.5% (compared to 21.1% in Q4 2006).

In RSD million

| Open position in EUR |       | Open position in USD |       | Open position in CHF |       | Open position in other currencies |       | Total open position |       | Total open fcy position |
|----------------------|-------|----------------------|-------|----------------------|-------|-----------------------------------|-------|---------------------|-------|-------------------------|
| long                 | short | long                 | short | long                 | short | long                              | short | long                | short |                         |
| 27,552               | 916   | 3,412                | 657   | 788                  | 479   | 580                               | 78    | 32,384              | 2,131 | 34,515                  |

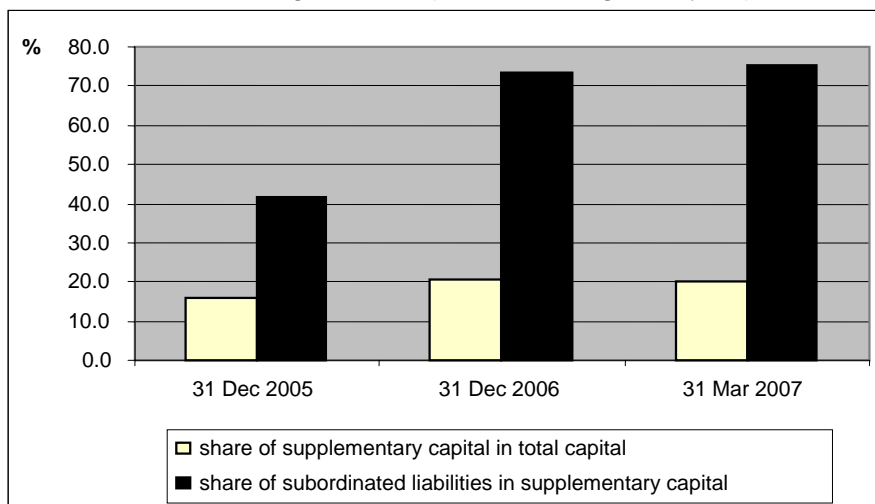
<sup>5</sup> Opportunity banka a.d. Novi Sad.

<sup>6</sup> Total open long foreign currency position of the banking sector stood at RSD 32.4 billion, which is an increase by RSD 6.2 billion. Total open short foreign currency position stood at RSD 2.1 billion, which is a decrease by RSD 10.3 billion.

## Capital adequacy

Regulatory capital of banks rose in Q1 by RSD 15.0 billion or 8.2%. Equity capital rose by RSD 12.5 billion or 0.8%, while subordinated liabilities increased by RSD 3.4 billion or 12.3%.

Chart 2: Changes in composition of regulatory capital



In compliance with regulations, banks are required to maintain their capital adequacy ratio at a level of not less than 12% of risk-weighted assets.

The table below shows the value of the capital adequacy ratio of banks at the end of Q1 2007:

| Capital adequacy ratio | Number of banks | Share in overall balance sheet total (in %) |
|------------------------|-----------------|---|
| Under 20%              | 11              | 41.4  |
| From 20 to 30%         | 10              | 32.2  |
| From 30 to 50%         | 12              | 24.6  |
| Over 50%               | 5               | 1.8   |
| Total                  | 38              | 100.0                                       |

Average capital adequacy ratio for the banking system came to 24.5%.

## Banking sector profitability indicators

The table below gives an overview of profitability indicators:

| Banking sector | PROFITABILITY INDICATORS <sup>7</sup> (%) |  |   |  | Financial result (in RSD thousand) |
|----------------|---|--|---|--|------------------------------------|
|                | Gross income/balance sheet assets         | Net interest income/balance sheet assets | Operating expenses/balance sheet assets | Operating expenses/net income from interest and fees |                                    |
| 31 Dec 2005    | 33.63                                     | 4.47                                     | 5.55                                    | 80.95  | 7,271,925                          |
| 31 Dec 2006    | 39.46                                     | 4.13                                     | 5.20                                    | 86.30  | 16,530,318                         |
| 31 Mar 2007    | 33.00                                     | 4.43                                     | 4.76                                    | 74.76  | 8,253,139                          |

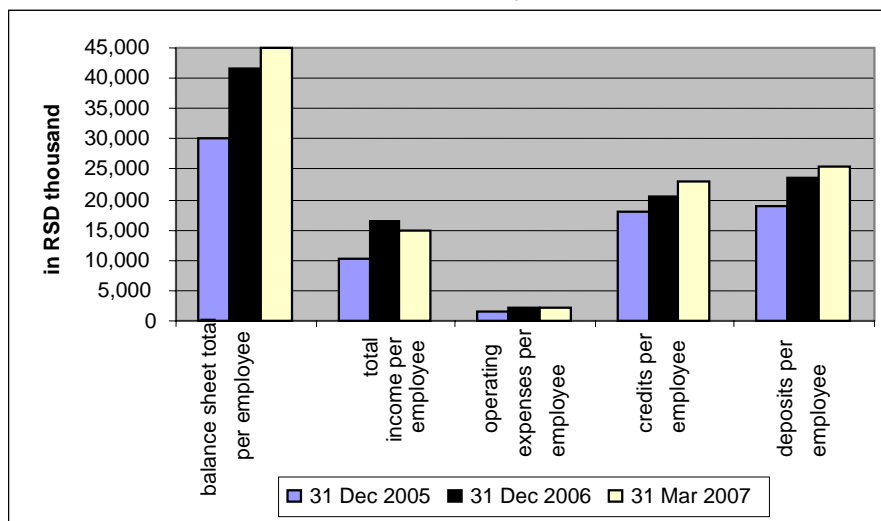
<sup>7</sup> All indicators are calculated at annual level.

| Banking sector | ROA (%) | ROE (%) | NIM (%) |
|----------------|---------|---------|---------|
| 31 Dec 2005    | 1.13    | 6.46    | 7.66    |
| 31 Dec 2006    | 1.70    | 9.67    | 7.46    |
| 31 Mar 2007    | 2.71    | 14.68   | 6.93    |

### Banking sector productivity indicators

Values of balance sheet assets, deposits and credits per employee increased in Q1 2007. Total income and operating expenses per employee declined on a quarter earlier. Overview of the above indicators is given in the chart below.

Chart 3: Productivity indicators



### Aggregate report on income and expenses

| Item   | in RSD million      |                     |                     |
|--|---------------------|---------------------|---------------------|
|  | 1 Jan – 31 Dec 2005 | 1 Jan – 31 Dec 2006 | 1 Jan – 31 Dec 2007 |
| NET PROFIT/LOSS IN RESPECT OF INTEREST                   | 34,654              | 48,245              | 14,003              |
| Interest income  | 49,015              | 76,937              | 23,616              |
| Interest expenses  | 14,361              | 28,692              | 9,613               |
| NET PROFIT/LOSS IN RESPECT OF FEES AND CHARGES           | 18,469              | 22,178              | 6,148               |
| Income from fees and charges                             | 23,478              | 28,372              | 7,758               |
| Expenses for fees and charges                            | 5,009               | 6,194               | 1,610               |
| NET PROFIT/LOSS IN RESPECT OF INTEREST, FEES AND CHARGES | 53,123              | 70,423              | 20,151              |
| NET PROFIT FROM SALE OF SECURITIES                       | 1,592               | 981                 | 95                  |
| Profit in respect of securities                          | 1,622               | 1,766               | 101                 |
| Losses in respect of securities                          | 30                  | 785                 | 6                   |
| NET INCOME/EXPENSES FROM EXCHANGE RATE GAINS/LOSSES      | 9,978               | 10,543              | - 2,496             |
| Exchange rate gains                                      | 122,529             | 274,179             | 48,541              |
| Exchange rate losses                                     | 112,551             | 263,636             | 51,037              |

| Item  | 1 Jan – 31 Dec<br>2005 | 1 Jan – 31 Dec<br>2006 | 1 Jan – 31 Mar<br>2007 |
|---|------------------------|------------------------|------------------------|
| INCOME FROM DIVIDENDS AND STAKES  | 243                    | 185                    | 0                      |
| OTHER OPERATING INCOME  | 57,372                 | 65,316                 | 15,359                 |
| EXPENSES IN RESPECT OF INDIRECT WRITE-OFF OF LENDING AND PROVISIONING           | 73,396                 | 61,938                 | 15,820                 |
| OTHER OPERATING EXPENSES  | 47,061                 | 64,174                 | 15,718                 |
| NET INCOME/EXPENSES IN RESPECT OF CHANGE IN THE VALUE OF ASSETS AND LIABILITIES | 5,425                  | - 4,805                | 6,682                  |
| Income from change in the value of assets and liabilities                       | 6,500                  | 14,602                 | 8,894                  |
| Expenses from change in the value of assets and liabilities                     | 1,075                  | 19,407                 | 2,212                  |
| PROFIT/LOSS FROM REGULAR OPERATIONS   | 7,275                  | 16,530                 | 8,253                  |
| NET EXTRAORDINARY INCOME/EXPENSES   | -3                     |                        |                        |
| Extraordinary income*   | 10                     |                        |                        |
| Extraordinary expenses*   | 13                     |                        |                        |
| Profit from discontinued operations**   |                        |                        |                        |
| Losses from discontinued operations**   |                        |                        |                        |
| <b>PRE-TAX PROFIT/LOSSES</b>  | <b>7,272</b>           | <b>16,530</b>          | <b>8,253</b>           |

\* Items abolished from balance sheet forms as of 31 December 2006.

\*\* Newly introduced items.

In Q1 2007, the banking sector recorded pre-tax profit of RSD 8,253 million. A total of 30 banks recorded profit and 8 banks operated with losses.

Such result was due to strong growth in income from cancelling unused write-off of lending and provisioning and income from change in the value of assets and liabilities, especially in March. The net effect of income and expenses in respect of exchange rate gains/losses remained negative, while interest income continued stable and high (in three months, it amounted to almost 1/3 of total income recorded in that respect in 2006).

The share of exchange rate gains in total income of banks equalled 46.6%, while exchange rate losses accounted for 53.2% of expenses. Next in relative significance were interest income (22.6%) and income from cancelling unused write-off of lending and provisioning (14.1%) on the income side, and indirect write-off of lending and provisioning (16.5%) and operating expenses (8.8%) on the expenses side.

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

In Q1 2007, the National Bank of Serbia enacted the following pieces of secondary legislation (decisions and guidelines) coming under its regulatory remit (in the field of banking supervision):

- **Decision Amending the Decision on Terms and Conditions of Performing Exchange Transactions**, which specifies the types of cash that can be the subject of exchange transactions.
- **Guidelines Amending Guidelines for Implementing the Decision on Terms and Conditions of Performing Exchange Transactions**, which specify in more detail actions to be taken in the event of termination of exchange office operations.
- **List of external auditors that may conduct audit of financial statements of banks** – The National Bank of Serbia prepared a list of external auditors which meet the criteria prescribed in the Decision on External Bank Audit ("RS Official Gazette," No. 57/2006) and may conduct audit of financial statements of banks.