BANKA SLOVENIJE

BANK OF SLOVENIA

REPORT

ON SUPERVISION OF BANKING OPERATIONS IN THE YEAR 1999 AND THE FIRST HALF OF 2000

SEPTEMBER 2000
Year 4

BANKA SLOVENIJE
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In accordance with the third paragraph of Article 54 of the Law on the Bank of Slovenia (Official Gazette of the Republic of Slovenia, No.1/91 – I) and Article 2 of the Decision on the Enforcement of Supervision of the National Assembly of the Republic of Slovenia on Operations of the Bank of Slovenia (Official Gazette of the Republic of Slovenia, No. 7/99), this Report on Supervision of Banking Operations in 1999 and the first half of 2000 is presented to the National Assembly of the Republic of Slovenia.

The purpose of this Report is to provide a review of the Bank of Slovenia functions and highlight priorities of banking supervision, with particular bearing to the developments in the Slovenian banking sector in the course of 1999 and in the first half of 2000.

In our efforts to promote general stability of the banking system, and to encourage transparency of operations conducted by banks and savings banks, as well as of products and services offered by them and standards they adhere to, we are releasing this Report to the general public.

MISSION STATEMENT

By fostering effective banking supervision, the Bank Supervision Department promotes safety and soundness of banking operations.

OBJECTIVE

The primary responsibility of the Bank Supervision Department is to ensure depositor protection and thereby maintain the stability of the financial system and boost confidence in the financial intermediation system as a whole. Effective banking supervision the Bank Supervision Department subscribes to shall be the underlying objective and its fulfilment lies with all organisational units and people who exercise powers conferred upon the Bank Supervision Department.

PHILOSOPHY

We are committed to promoting safety and soundness of banks and savings banks. The principles advocated within the framework of market economy assume that banks are managed by professionals chosen by the owners who lay down the guidelines to be adhered to. The Bank Supervision Department must not make decisions instead of the owners and must not interfere with the responsibilities conferred upon banks' management. By promulgating decrees, recommendations, instructions and guidelines we strive to contribute to expanding the range of banking services and products, stepping up competitiveness, and spreading high ethical principles at all levels of decision-making. Regular open communication between the Bank Supervision Department on the one hand and banks and savings banks on the other help keep up the standards of safe and sound banking, while appropriate corrective actions taken by the Bank of Slovenia are yet another tool of effective supervision.

ROLE OF MANAGEMENT AND INTERNAL AUDITORS

Management teams that are at the helm of banks and savings banks have responsibility to owners but also regulators, who strive to ensure sound and effective operations of banks and savings banks as well as adequate oversight over their business activities. These are essential components of a regulated economic environment. As regards ensuring responsibility of bank management for safety of banking operations, it is their duty to introduce clearly defined rules as to management of all kinds of risks banks are exposed to. Banks cope with industry-related risks by setting up a system of internal controls. With regard to supervision of both owners and regulators, banking supervisors must require from bank management to set out in writing rules to be followed and mechanisms deployed for the purpose of risk management. As for benchmarking business results, bank management teams must have in place long-term business strategy, which shall be implemented by means of business policies tailored for each area of banking operations. A step further is the need to have in place a well-developed internal audit department, which is in charge of monitoring and assessing the adequacy and appropriateness of aforementioned functions, and who shall promptly notify bank directors on findings and put forward recommendations. It is essential that bank directors and senior officers recognise the role and importance, as well as the scope of responsibilities conferred upon the internal audit department, and to duly consider its findings and recommendations. To keep this communication channel navigable is in the best interest of both sides.

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For the Slovenian banking sector, the year 1999 was another good year and this performance has continued also in the first half of the year 2000. It was in the financial area that the year 1999 posed major challenges to policymakers and market participants alike. A new phase in Slovenia's development was marked by the entry into force of the EU-Slovenia Europe Agreement on 1 February 1999 and fully exposed Slovenia's financial and banking system to market forces. The new Banking Act followed suit and became effective later in February. Further steps were taken to increase the competitiveness of the domestic banking sector. The intrabank agreement on capping deposit interest rates expired on 1 March, new foreign exchange legislation was passed in April, and value added tax replaced sales tax on 1 July. In addition, the computer bug scare prompted efforts to ensure that banks are fully Year 2000 compliant, changing economic fortunes hit many countries in the first half of the year, and Slovenia was once again at a stone's throw from a war crisis. Weaknesses exposed in the international financial system have spread a general feeling of insecurity.

In addition to institutional changes, in the first half of 1999 there were changes in the method of issuing base money. Tolar transactions generated a rise in base money as oposed to the past years when foreign exchange transactions between the Bank of Slovenia and commercial banks where a cause for the rise. The said change in the method of issuing base money had an impact on somewhat impaired liquidity of the banking system during the first months of the year 1999. Nevertheless, all banks complied with requirements to set aside mandatory reserves and to maintain minimum foreign exchange minimum. Impaired liquidity of banks did not contaminate the real sector.

As already highlighted the two hallmark events in 1999 with far-reaching consequences for Slovenia's banking industry were the entry into force of the EU-Slovenia Europe Agreement and the promulgation of the new Banking Act. Although allowing foreign banks to establish branches in Slovenia was seen by many as a threat to the domestic banking industry, it has not changed the structure of the banking system as only one foreign bank decided to open a branch in Slovenia during the period under review.

The entry into force of the new Banking Act on 20 February 1999 marked the beginning of a new phase in the development of the Slovenian banking industry and its provisions cover transposition of the European banking directives. Implementation and enforcement of principles adhered to by EU Member States is regarded as a prerequisite for the accession, and no time was wasted in the rollout phase. Thus in line with the Banking Act, the Bank of Slovenia promulgated a number of by-laws in 1999 and in the first half of 2000. In addition, the Banking Act conferred upon the Bank Supervision Department a wide array of new tasks and responsibilities in connection with supervision and surveillance of legal entities connected with banks. The Banking Act also provides for supervisory intervention in cases where other legal entities are suspected of providing banking services without being duly authorised by the Bank of Slovenia. After the transitional period expires, the Bank of Slovenia will also be responsible for the supervision of savings and loan undertakings.

There is no doubt that the introduction of the value added tax had a strong impact on economic developments in 1999, and also in the course of 2000. Inflation expectations feeding on the new tax system boosted domestic spending, and as a result heated lending activities of banks. In the second phase, the value added tax pushed up the consumer price index (CPI), which in turn triggered a change in the base interest rate and consequently influenced interest margin and the composition of bank earnings. If we draw the line, however, the influence of the introduction of the value added tax on the rise recorded at the general price level was not as significant as expected.

Economic environment proved to be rather favourable for banking operations during the period under review – its principle feature was vigorous economic prosperity at home while the countries, which are Slovenia’s most important trading partners, picked up the brisk pace of economic growth. In the wake of economic crisis in Russia and in Asia in 1998, and a crisis in the immediate vicinity of Slovenia, economic conditions at the beginning of 1999 could be described as volatile in many countries around the world. Despite difficulties experienced by a number of countries, Slovenia escaped unscathed and its hefty and sustainable GDP growth continued. All these developments were reflected on banking operations of banks’ customers and banks’ lending activities in particular. Favourable economic trends have continued also in 2000. The growth in banks’ total assets in 1999 notched 14.3 per cent – a rather modest performance if 8 per cent inflation (December-December) and 4.9 per cent GDP growth are taken into account. By the end of June 2000, banks’ total assets rose by 8.9 per cent in nominal terms; it is conventional wisdom that during the period of general prosperity the banking sector grows somewhat faster than other sectors. The share of aggregate total assets of banks and savings banks accounted for just over 74 per cent of GDP at the end of 1999 and it ranks us at the very top of transition countries, but it still lags behind countries of the European Union.

After a more pronounced fall of inflation from the beginning of 1998, the process of lowering inflation culminated in the first half of 1999 and hit the bottom at just above 4 per cent. Due to the introduction of the value added tax, consumer price grew faster and by the end of the year soared to 8 per cent (December-December). Fuelled by unfavourable externalities (rising crude oil prices and the surging exchange rate for US dollar), inflation recorded in June 2000 increased to 9.7 per cent on a year-on-year basis. Since the inflation rate is used as a basis for the calculation of the base interest rate, the correlation between price fluctuations and movements in interest rates has been rather notable. Consequently, interest rates paid on deposit and charged for loans in 1999 continued to go down and converged with interest rates prevailing in the European Union. Although the interbank agreement on maximum deposit interest rates expired on 1 March 1999, banks opted to follow recommendations on top interest rates paid on deposits within the framework of the Bank Association of Slovenia - a step towards further stability of interest rates. In the first half of 2000, movements in interest rates and interest margins actually diverged.

Turning to the structure of the banking system and the number of banks at the end of 1999 and interim figures for 2000, there were no substantive changes. Yet in the absence of dramatic developments, it would be wrong to conclude that during the period under review, efforts to consolidate the banking sector ground to a halt. On the contrary – a number of banks were engaged in merger talks and industry experts were busy exploring every avenue that should lead to honing competitive edge of banks across Slovenia. In the dry language of figures, the market share of the largest seven banks has been constant at just above 73 per cent or in the range of 85 per cent if the banking group of NLB is taken into account. The consolidation process in the Slovenian banking system failed to gain momentum and the number of banks remained the same as at the end of the previous period. However, the notion of the necessity to keep the M&A process running has already been embraced by market participants and is a guarantee that the consolidation of the banking sector will be back on track in the second half of 2000 and will run at full steam in 2001. By joining forces, Slovenian banks would have a better chance of competing with foreign competitors in the race for winning banking business even before Slovenia becomes a full-fledged member state of the European Union. Cost cutting would be another advantage made possible by rationalising operations in the wake of a merger. As for the ownership structure, the two largest Slovenian banks still remain in state hands. Since the Republic of Slovenia also has equity stakes in two smaller banks, it controls the larger portion of the banking system. After the first steps to gradually privatise Nova Ljubljanska banka d.d. and Nova Kreditna banka Maribor d.d. in the middle of 1999, there has been an impasse in the process.

Financial results of banking operations for the year 1999 were below the figures for 1998. The explanation for this lacklustre performance is that banks carved out bad assets from their balance sheets, and they also had to make higher provisions for credit risk (net provisions rose by 7.6 billion tolars in 1999). In addition, interest margins thinned as banks stepped up efforts to atract clients. Profit before taxes was 20.1 billion tolars for the financial year and resulted in return on average assets (ROAA) of 0.8 per cent – a significant drop on a year-on-year basis when ROAA was 1.2 per cent. Squeezed by sliding interest rates across the industry and thinner revaluation profit, interest margin fell to 4.0 per cent in 1999 (1997: 4.9 per cent; 1998: 4.5 per cent). On the other hand, interest margin remained too high in comparison with margins earned by the banks from the European Union. During the first half of 2000, the base interest rate grew to 4.6 per cent fuelled by rising consumer prices. Consequently, the results posted in the first half of 2000 were significantly better reaching 1.2 per cent ROAA. The figures posted in the profit and loss account reflect a favourable trend in movements of expenses, although there is ample room for further improvement (operating expenses incurred by the banking sector accounted for 3.6 per cent of average assets in 1998, while in 1999 and in the first half 2000 they were 3.4 per cent and 3.2 per cent, respectively). Nevertheless, expenses of Slovenian banks compare unfavourably with banks from the European Union; as for their international competitiveness, there is still a lot to be done as the overall trend in the efficiency of the banking sector continues.

The downward trend of capital adequacy ratio across the banking system has been noticeable since 1995, and it continued during the period under review. Thus at the end of 1999, average capital adequacy ratio was 14.0 per cent (1998: 16.0 per cent) and as at 30 June 2000 it was 13.6 per cent. However, capital adequacy ratio achieved by banks was well above regulatory capital requirement of 8 per cent. Since it is expected that banks with the lowest capital adequacy ratios will inject fresh capital, it is assessed that capital adequacy ratio across the banking system will stabilise at the level reported at mid-2000.

In 1999 and in the first half of 2000, banks focused efforts on the implementation of provisions laid down in the new Banking Act. In particular, the stress was on the field of risk management and a lot of attention was paid to responsibilities conferred upon bank management and senior officers for safe and sound banking operations. Furthermore, the Banking Act highlights all forms of supervision and surveillance, underpins internal controls and internal audit function, the role of supervisory board, independent external audit, and the function of the Bank of Slovenia in its capacity of a banking supervisor.

The need for more full-scope and targeted examinations of banks and savings banks becomes more apparent as the financial regulatory regime is beefed up around the world.

Within the framework of negotiations with the European Union with regard to freedom to provide services, Slovenian negotiation team has proposed two transitional periods for the banking industry. Namely, the position that savings and loan undertakings established prior to the effectiveness of the Banking Act should be granted additional time to comply with capital requirements and to abide by other requirements pertinent to safe and sound banking operations, has been approved. As for the proposal to grant a transitional period for the protection of domestic deposit-guarantee scheme, it is still in the pipeline. There are also two more issues addressed in the Europe Agreement that still have to be fully aligned with European directives: the principle of single banking licence and the home country control principle. It has been agreed to implement these two principles as of the date of Slovenia's full-fledged membership.

How acute the need for the enhancement of supervision and surveillance of the banking system is, has become more obvious over the past years in the aftermath of recent financial crises, and particularly when it became clear that those crises were triggered by inherent deficiencies in banking systems. Such financial crises are even more threatening than they may seem at first since they do not affect only the country in which the crisis bursts out but contaminate other countries as well.

We are pleased to declare that we have achieved a satisfactory level of compliance with the Core Principles – the most comprehensive set of principles which has been generally accepted as the framework for enhancing the soundness and stability of the international banking system and a valuable tool for supervisors. In the middle of 1999, the Bank Supervision Department carried out an in-house assessment of the compliance with the Core Principles and the result showed that 17 principles could be considered as fully compliant, 6 principles were substantially compliant, and two principles were complied with up to a limited extent. By the promulgation of new by-laws – the Decree on the Supervision of Banks and Savings Banks on a Consolidated Basis and the Decree on Deposit-Guarantee Scheme - and enhanced liaison with supervisory authorities of other countries finalised through memoranda of understanding on the co-operation with banking supervisors - the compliance level has been raised further. The most recent self-assessment carried out indicates that as at the first half of 2000, Slovenia fully complies with 20 principles, 4 principles have been implemented up to a large extent, while only one principle has been partly implemented. Full compliance with all Core Principles for Effective Banking Supervision is to be achieved by the end of the year 2001.

In order to further increase the quality of carrying out banking supervision, the strategic plan for 2000 and 2001 envisages the following:

- Enhance resources for monitoring and supervising risks at the level of banking groups,
- Monitor developments and movements in the field of consolidated supervision,
- Raise awareness of all participants in the financial markets with regard to the importance of supervision of banking operations,
- Develop the co-operation and exchange of information between supervisory authorities both in the domestic and international financial environment,

- Keep abreast of activities and progress with reference to international standards and ensure that the Slovenian banking legislation is amended promptly and adequatly,
- Further develop banking legislation in the segment that refers to good practice in banking operations,
- Implement requirements laid down in banking directives in the field of exposure to market risks and implement deposit-guarantee scheme designed for depositor protection,
- Pay more attention to supervision of electronic banking (cyber money),
- Use on-site examinations to highlight management of all kinds of banking risks, including operational risk and the setting up of the internal controls system,
- Pursue the work in the field of ‘early-warning’ system to identify problems in the banking sector,
- Host a seminar or a workshop in the field of risk management in the ambit of banking industry,
- Pursue human resource policy endorsed by the Bank Supervision Department in line with the strategic orientation, etc.

In closing, I use this occasion to thank my staff and experts from other departments. My particular gratitude goes to the Governor and Deputy Governor of the Bank of Slovenia for their commitment and endeavour as well as for their guidance in day-to-day activities. My sincere appreciation goes to other supervisory authorities and the Ministry of Finance for their valued inputs and for their continued co-operation. Looking to the future, I believe that this ongoing co-operation will cement safety and stability of the banking system and help us meet the challenges of a changing world.

Mojca Majič, M.A.
Director
Bank Supervision Department

I. DEVELOPMENTS RELATED TO BANKING SUPERVISION

1. PRUDENTIAL SUPERVISION OF FINANCIAL INSTITUTIONS IN SLOVENIA

Three supervisory authorities responsible for financial institutions in Slovenia

Several supervisory authorities are responsible for individual segments of the financial system in Slovenia. Slovenia's central bank, the Bank of Slovenia, is an independent institution that carries out the tasks conferred upon it by the Bank of Slovenia Act. The responsibility for the implementation and enforcement of the Bank of Slovenia's supervisory function is conferred upon the Bank Supervision Department. The Bank Supervision Department derives authority and responsibility to supervise banks (including the Slovene Export Corporation – banking operations) and savings banks from the Banking Act. Supervision of savings and loan undertakings established prior to the effectiveness of the Banking Act will be gradually transferred to the Bank of Slovenia – no later than five years from the entry into force of the Banking Act. By that time, savings and loan undertakings will have to fully comply with the provisions of the Banking Act.

The Securities Market Agency is a self-governing and independent legal entity with full power to supervise stock-broking companies, management companies, investment funds, as well as some other institutions (e.g. Central Securities Clearing Corporation, Ljubljana Stock Exchange, etc.).

The Insurance Supervisory Agency became operational on 1 June 2000 as a self-governing and independent legal entity whose responsibility is the supervision of insurance companies, reinsurance companies, companies and agents who engage in insurance-related activities, as well as some other institutions (insurance operations carried out by the Slovene Export Corporation, Nuclear Pool, Institute for Health Insurance – Voluntary Health Insurance Unit[1] , and Pension Investment Fund.[2] Prior to the establishment of the Insurance Supervisory Agency, the above-mentioned institutions were under the scrutiny of the Insurance Supervision Authority of the Republic of Slovenia operating within the framework of the Ministry of Finance.

To facilitate the comparison of the scope of supervisory activities, the figures relevant to the size of individual segments of the financial system are given below.

Total assets of banks and savings banks at end-1999 accounted for 74% of GDP.

At the end of 1999, there were 25 operating banks (24 banks and one foreign branch) in Slovenia with aggregate total assets amounting to 2,687.6 billion tolars, and 6 savings banks with aggregate total assets amounting to 11 billion tolars. The share of aggregate total assets of banks and savings banks in the national gross domestic product (hereinafter referred to as GDP) at the end of

1 As from 1 November 1999, Institute for Health Insurance - Voluntary Health Insurance Unit operates as Vzajemna zdravstvena zavarovalnica (Mutual Health Insurance).

2 As from 1 January 2000, Pension Investment Fund operates as Kapitalska družba pokojninskega in invalidskega zavarovanja (Pension Fund Management).

1999 was 74 per cent. When total assets of savings and loan undertakings are added, then aggregate total assets rise to 75.5 per cent of GDP. Prudential supervision during the period under review was conducted by 39 employees (on 30 June 2000 this number rose to 42 employees) working in the Bank Supervision Department.

At the end of 1999, the Securities Market Agency supervised 42 stock-broking companies[3], 22 management companies[4], 46 authorised investment companies, and 17 mutual funds. At the end of 1999, there were 26 employees responsible for carrying out supervision of these institutions.

Total assets of stock-broking companies at end-1999 accounted for 18% of GDP.

As at 31 December 1999, stock-broking companies disclosed investments made for their own account in the amount of 116.9 billion tolars (3.2 per cent of GDP), 19.2 billion tolars in assets under management (0.5 per cent of GDP), and 516.9 billion tolars in investments made for the account of third parties (14.2 per cent of GDP). To summarise, aggregate investments of stock-broking companies totalled 653 billion tolars (almost 18 per cent of GDP). A year-on-year comparison shows a 21.2 per cent increase. Total assets of authorised investment companies posted at 31 December 1999 amounted to 599 billion tolars - a one-per-cent rise over the balance stated as at 31 December 1998. These assets accounted for 16.5 per cent of GDP including unutilised privatisation vouchers that still average more than half of all funds. Total assets of mutual funds soared by as much as 94.6 per cent to 8.7 billion tolars (0.23 per cent of GDP). To summarise, management companies had 608 billion tolars in assets under management at the end of 1999.

At the end of 1999, there were 12 insurance companies, 3 reinsurance companies, 293 companies and agents who carried out other insurance transactions, the Slovene Export Corporation, and the Nuclear Pool operating in Slovenia. Total assets of insurance companies (excluding the Slovene Export Corporation and the Nuclear Pool) disclosed in partly audited figures as at 31 December 1999 amounted to 222.6 billion tolars, while total assets of reinsurance companies totalled 41.9 billion tolars; hence aggregate assets added up to 264.6 billion tolars.

Table 1: The number of financial institutions in Slovenia

Type of financial institution	31 Dec 1995	31 Dec 1996	31 Dec 1997	31 Dec 1998	31 Dec 1999
Banks	*33*	*31*	*28*	*24*	*25*
Savings banks	*10*	*7*	*6*	*6*	*6*
Savings and loan undertakings	*72*	*71*	*70*	*70*	*68*
Investment firms*	*44*	*46*	*43*	*42*	*42*
Management companies	*28*	*26*	*26*	*23*	*22*
Authorised investment companies	*68*	*72*	*60*	*46*	*46*
Mutual funds	*18*	*15*	*15*	*15*	*17*
Insurance companies	*12*	*12*	*13*	*13*	*12*
Reinsurance companies	*2*	*2*	*2*	*3*	*3*

* Including 10 banks authorised to carry out trading operations.
Source: Bank of Slovenia, Securities Market Agency, Insurance Supervisory Agency

[3] Including 10 banks authorised to carry out trading operations.

[4] 12 management companies manage only authorised investment companies, two management companies manage only mutual funds, while the other 8 run both types of funds.

Table 2: Exposure of banks and savings banks to financial institutions and share in aggregate gross on- and off-balance sheet

in millions of Tolars, in %

	31 Dec 1998		31 Dec 1999		30 Jun 2000	
	Amount	Share in agregate exposure	Amount	Share in agregate exposure	Amount	Share in agregate exposure
Stock-broking companies	6,257	0.22	10,178	0.32	10,512	0.30
Authorised investment companies	2,738	0.10	6,046	0.19	8,194	0.23
Management companies	6,414	0.23	7,813	0.25	8,547	0.25
Insurance companies	7,296	0.26	9,557	0.30	12,044	0.35
Total	**22,705**	**0.81**	**33,594**	**1.06**	**39,297**	**1.13**

Source: Bank of Slovenia

Indirect exposure of *banks* to **insurance companies** on the basis of bank loans granted and insured with insurance companies as at 30 June 2000 amounted to 296,521 million tolars, while indirect exposure of *savings banks* to insurance companies stated on the same day totalled 2,862 million tolars.

2. COMPLIANCE WITH THE CORE PRINCIPLES FOR EFFECTIVE BANKING SUPERVISION

Core Principles are the most significant global standard for regulating and supervising safe and sound bank operations.

The Basel Core Principles for Effective Banking Supervision[5] (hereinafter referred to as the Core Principles) have become the most important global standard pursued by banking regulators and supervisors in their endeavour to promote safety and soundness in banking systems. The Core Principles, which represent minimum requirements for the implementation of prudential banking supervision and consequently form a basis for the evaluation of the effectiveness of banking supervisory regimes, have been elaborated by the Basel Committee on Banking Supervision and banking supervisory authorities from other (non-G-10) countries.

In the wake of the most recent financial disturbances, it has become widely accepted that only through the enhancement of prudential requirements, it will be possible to improve the architecture of the banking industry and deliver systemic stability. Since banking and wider financial crises are not restricted only on the country in which they start but is likely to spill over national borders, to monitor banking systems and early detection of signs of the crisis is essential for banking supervisors. All countries – industrialised countries, countries undergoing transition and developing ones – must strive for an early and thorough implementation of the Core Principles and therefore for an effective application of internationally recognised and tested methods of supervision, which represent best practices in the pursuit of safety and soundness of banking systems across the globe.

5 The Core Principles were issued by the Basel Committee in September 1997 and endorsed by the international financial community at the annual conference of the International Monetary Fund held in Hong Kong in October 1997. In April 1998, the Basel Committee proceeded with the research of the Core Principles compliance level by individual countries. The research involved active participation of more than 120 countries, including Slovenia. The results of the research were the central topic of the discussion at the International Conference of Banking Supervisors held in Sydney in October 1998.

First step is to assess alignment of regulatory and supervisory framework with Core Principles.

The first step towards a full implementation of Core Principles in each country is the assessment of the actual level of compliance achieved with regard to banking legislation and supervisory practice. Such an assessment serves as a basis for the promulgation of measures designed to eliminate discrepancies, i.e. mitigate deficiencies within the existing regulations and banking supervision. The compliance self-assessment has already been made by a number of countries, and external evaluations made by the World Bank and the International Monetary Fund have been completed in some countries.

The Core Principles call for a qualified judgement to be passed on the degree of alignment achieved; hence such an assessment cannot be fully objective. On the other hand, the Core Principles leave room for some flexibility in the planning and implementation of concrete actions in practice, albeit their interpretation must be basically uniform. For the purpose of ensuing that the tools or vehicles used by banking supervisors in different countries would basically be the same, a detailed methodology for the assessment of compliance has been designed and put in place. Nonetheless, it must not escape banking supervisors that compliance assessment is not an end to itself but a tool for the achievement of a crucial goal: the preparation of a strategy for the improvement of the banking supervisory system.

Assessment of bank supervision effectiveness includes assessment of macroeconomic environment.

The list of prerequisites for effective banking supervision includes consistent and comprehensive macroeconomic policies, a well-developed public infrastructure, market discipline, procedures designed to provide efficient solutions to problems banks are likely to face, as well as mechanisms to provide safeguards against systemic risks. Although banking supervisors cannot exercise a direct influence on the fulfilment of the aforementioned prerequisites, deficiencies or weaknesses in those fields may significantly reduce capabilities for the effective deployment of the Core Principles. The assessment of the effectiveness of banking supervision also involves a judgement of the macroeconomic environment of the respective country.

The first assessment of the compliance with the Core Principles was made in Slovenia at the time when the first banking legislation after gaining independence was in force (Law on Banks and Savings Banks adopted in 1991). The assessment was presented in the Report on Supervision of Banking Operations in 1997 and the First Half of 1998 after it had been endorsed by the Governing Board of the Bank of Slovenia in June 1998. In line with the provisions of the Banking Act, a new assessment of implementation of the Core Principles was made and presented in the Report on Supervision of Banking Operations in 1998 and the First Half of 1999 and the Governing Board of the Bank of Slovenia examined it at its session held in August 1999. The comparison of both assessments indicates progress made in compliance with individual principles largely facilitated by the adoption of the Banking Act and the promulgation of secondary legislation derived from the Banking Act. Differences arise partly from the requirements laid down in the amended assessment methodology. Namely, yardsticks are more detailed and call for a more critical approach to the determination of the level of compliance achieved by banking regulations and the supervision system put in place with individual principles.

Latest self-assessment shows alignment also with Principles 1(6), 20, 23, 24 and 25.

In the wake of the promulgation of the Decree on Supervision of Banks and Savings Banks on a Consolidated Basis in December 1999 and after finalising a memorandum of understanding with a foreign supervisory authority in January 2000, updated self-assessment of the compliance with the Core Principles was made. This most recent assessment exercise has proved that

Core Principle 1(6), 20, 23, 24 and 25 are fully complied with. The updated assessment of how far Slovenia has gone in the alignment with the Core Principles is summarised below.

Principle 1(6): Arrangements for sharing information between supervisors and protecting the confidentiality of such information should be in place.

Assessment:
Compliant. The sharing of information between supervisors is legally regulated by the Banking Act provisions relating to the cooperation between home and foreign supervisory bodies. A preliminary condition for such sharing of information is the obligation of protecting the confidentiality of such shared information. The sharing of information with foreign supervisory bodies is exercised in practice as well on the basis of signed Memoranda of Understanding which represent a legal foundation for such cooperation.

Principle 20: An essential element of banking supervision is the ability of the supervisors to supervise the banking group on a consolidated basis.

Assessment:
Compliant. According to the Decree on the Supervision of Banks and Savings Banks on a Consolidated Basis, the parent banks of banking groups are obliged to make up consolidated financial statements and provide consolidated prudential (risk management) reports. The consolidated banking supervision is supplemented by the Banking Act with the provision on the supervision of corporate borrowers connected to the bank. The Bank of Slovenia also has the authority to supervise foreign corporate entities connected to the bank, which has been already put into practice. Consolidated supervision is one of the most demanding tasks of banking supervision; therefore, supervisor training represents a priority activity in this area.

Latest self-assessment of compliance with Core Principles shows compliance with the consolidated supervision principle.

Principle 23: Banking supervisors must practise global consolidated supervision over their internationally active banking organisations, adequately monitoring and supplying appropriate prudential norms to all aspects of the business conducted by these banking organisations world-wide, primarily at their foreign branches, joint ventures and subsidiaries.

Assessment:
Compliant. The Bank of Slovenia has the possibility to supervise Slovenian banks' foreign branches and subsidiaries by reviewing their reports and other documentation required from the parent bank by the central bank's supervisors and also by means of an inspection performed abroad on the basis of informal and formal cooperation agreements concluded with foreign supervisory bodies. Global consolidated supervision is exercised in practice as well, in future, however, our supervisors will need some additional education to carry out this type of tasks.

Principle 24: **A key component of consolidated supervision is establishing contact and information exchange with the various other supervisors involved primarily host country supervisory authorities.**

Assessment:

Co-operation with a foreign supervisory authority has been finalised in a MoU.

Compliant. Cooperation with foreign supervisory institutions in the supervision of banks abroad has been formally established due to the conclusion of the first Memorandum of Understanding between the Bank of Slovenia and a foreign supervisory authority. The Banking Act has eliminated all major barriers to the free exchange of information between the Bank of Slovenia and foreign supervisory bodies; its provisions practically mean a mandate to set up the home country supervision principle, which will become fully effective with Slovenia's full EU membership.

Principle 25: **Banking supervisors must require the local operations of foreign banks to be conducted to the same high standards as are required of domestic institutions and must have powers to share information needed by the home country supervisors of those banks for the purpose of carrying out consolidated supervision.**

Assessment:

Compliant. Branches of foreign banks in Slovenia must observe the same rules that apply to Slovenian banks. They are also subject to the Bank of Slovenia supervision, which is a guarantee for a non-discriminatory treatment of both home and foreign banks operating in Slovenia. Once Slovenia is admitted to full EU membership, branches of banks from EU member countries will be subject to the single banking licence and home country control principles which ensure the observance of the uniform European banking standards by foreign banks in Slovenia.

Partly compliant are principles 1(2), 6, 10, 12, and 13.

The assessment of the levels of compliance with the Basel Core Principles for Effective Banking Supervision shows that out of the total number of 25 principles, there are areas where full compliance has not been achieved (Principles 6, 10, 12, 13), or has been partly achieved (Principle 1(2)). The areas to be addressed are new products and services introduced by Slovenian banks that either have to be regulated or that have not been adequately addressed from the standpoint of banking supervision (e.g., market and operational risks). Hereinafter only the principles compliant with up partly or up to a large extent, are elaborated upon, and achieving full compliance with these principles remains a priority task for banking standard-setters i.e. supervisors.

Principle 1(2): **Each agency involved in the supervision of banks should possess operational independence and adequate resources.**

Assessment:

Largely compliant. The Bank of Slovenia is an independent, autonomous institution which has the necessary financial resources in order to carry out its tasks and exercise its powers in the sphere of banking supervision, while the provision of adequate professional staffing represents a permanent problem due to a staff turnover and somewhat lower salaries as compared with some other financial institutions. Nevertheless, the supervision department has been considerably strengthened by new professional staff.

Principle 6: **Banking supervisors must set minimum capital adequacy requirements for banks that reflect the risks that the bank undertakes, and must define the components of capital, bearing in mind its ability to absorb losses. For internationally active banks, these requirements must not be less than those established in the Basel Capital Accord.**

Assessment:

Largely compliant. The setting of capital requirements for credit risk in Slovenia is in line with the international practice. Although the newly adopted Banking Act also gives the Bank of Slovenia the authority to lay down capital requirements for foreign exchange and other market risks, the Bank of Slovenia has, for the time being, defined only the methodology of determining the capital necessary to offset foreign exchange risks. Capital requirements for market risks will be set by the Bank of Slovenia in the year 2000. A small volume of trading and consequently also the relating market risks in our banks for the time being does not justify the requirement for the use of a standardised model of monitoring of capital requirements relating to market risks and costly investments in information systems of banks, especially in view of the other new requirements that must be complied with by banks after the adoption of the new banking legislation. A consolidated supervision of capital and capital adequacy has also been regulated by the Banking Act, and its implementation is more accurately defined in the Decree on the Supervision of Banks and Savings Banks on a Consolidated Basis.

The Bank of Slovenia will define capital requirements in relation to market risk by the end of 2000.

Principle 10: **In order to prevent abuses arising from connected lending, banking supervisors must have in place requirements that banks lend to related companies and individuals on an arm's-length basis, that such extensions of credit are effectively monitored, and that other appropriate steps are taken to control or mitigate the risks.**

Assessment:

Largely compliant. A restrictive treatment of loans granted to persons having a special relationship with the bank and persons connected to them is provided as such lending is subject to obtaining the approval of the banks' supervisory boards if it is not done on an arm's length basis. The law itself as well as the relevant secondary legislation bind the banks to an effective monitoring of related-borrower lending and proper risk management. The Bank of Slovenia does not require the banks to implement any special procedure which would deprive them of the benefits derived from the preparation, i.e. granting of loan requests.

Banks are required to have in place effective policy and practice to manage risks associated with connected lending.

Principle 12: **Banking supervisors must be satisfied that banks have in place systems that accurately measure, monitor and adequately control market risks; supervisors should have powers to impose specific limits and/or a specific capital charge on market risk exposures, if warranted.**

Assessment:

Materially non-compliant. The Bank of Slovenia has a legal authority to impose market risk-related capital requirements; however, the Bank of Slovenia has not yet exercised this option (with the exception of foreign exchange risk). Market risk supervision by the Bank of Slovenia is in place but lacks all the necessary elements. Owing to the Slovenian banks' small volume of trading activities, the Bank of Slovenia has issued recommendations for the carrying out of trading activities and laid down the method of dealing securities valuation within its current regulations. Additional training of supervisors in this area will be required in future.

Principle 13: **Banking supervisors must be satisfied that banks have in place a comprehensive risk management process (including appropriate board and senior management oversight) to identify, measure, monitor and control all other material risks and, where appropriate, to hold capital against these risks.**

Assessment:
Largely compliant. The Banking Act regulates the monitoring of risks and the obligation of providing security against such risks. In addition to the secondary legislation of a compulsory nature which mainly relate to the quantitative risk management, the Bank of Slovenia also issued comprehensive recommendations to banks relating to credit, liquidity, interest, exchange and some other risks. The recommendations include essential qualitative elements which should be observed by the banks when setting its policies and procedures for management of all kinds of risks and at the same time represent guidelines to supervisors in their work. For the time being, the Bank of Slovenia requires the banks to hold capital against credit risk and foreign exchange risk.

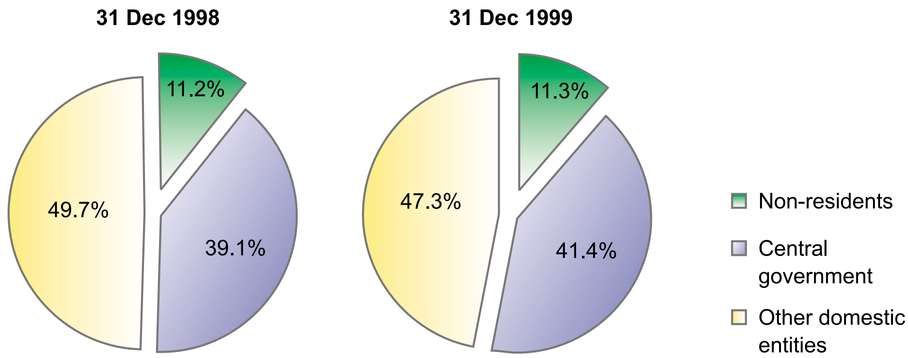
3. OWNERSHIP STRUCTURE OF THE BANKING SECTOR AND PRIVATISATION OF STATE-OWNED BANKS

Banks in Slovenia are mostly in private hands.

Banks in Slovenia are mostly in private hands with the exception of Nova Ljubljanska banka d.d. (hereinafter referred to as NLB), Nova Kreditna banka Maribor d.d. (hereinafter referred to as NKBM), and Slovenska investicijska banka, d.d. (Slovenian Investment Bank). NLB and NKBM, the two largest banks in terms of total assets, came under state ownership when they were placed in the bank rehabilitation programme in 1993. In addition, the Republic of Slovenia acquired almost a 37 per cent stake in shareholders' equity of Slovenska investicijska banka (Slovenian Investment Bank), i.e. a 20 per cent stake in voting shares. Poštna banka Slovenije d.d. (Slovenian Post Office Bank) is indirectly in state hands.

Savings banks are entirely owned by private domestic shareholders.

Figure 1: Ownership structure of the banking sector as at 31 December 1998 and 31 December 1999 measured by shareholders' equity[6]



Source: Bank of Slovenia

[6] Shareholders' equity is a sum of subscribed capital, share premium account, reserves, capital revaluation adjustment, net profit or loss brought forward, net profit or loss for the current financial year less subscribed capital unpaid and own shares bought back.

The amount of foreign shareholders' equity increased from 28.6 billion tolars as at 31 December 1998 to 31.5 billion tolars as at 31 December 1999 - a 10.2 per cent increase in nominal terms. Total shareholders' equity grew from 255 billion tolars as at 31 December 1998 to 279.3 billion tolars as at 31 December 1999 - a 9.5 per cent rise in nominal terms. In spite of the fact that in 1999 one subsidiary and one branch were established by respective foreign banks, the share of foreign shareholders as at 31 December 1999 remained practically on a par with holdings of foreign shareholders as at 31 December 1998.

The wider definition of state-owned bank assets[7] that takes into account indirect state holdings and also considers voting shares in shareholders' equity, rose from 99.8 billion tolars carried as at 31 December 1998 to 115.6 billion tolars stated as at 31 December 1999. This represents a nominal rise of 15.9 per cent (as at December 1998, this figure was 29.5 per cent). Since the increase in shareholders' equity was more moderate (just 9.5 per cent), it resulted in beefing up state-owned holding as at 31 December 1999 year-on-year. If we take into account direct state ownership of shareholders' equity (for this purpose, entire shareholders' equity is considered including holdings of own shares), then the stake in state hands as at 31 December 1999 amounted to 35.2 per cent.

Since the successful completion of the rehabilitation programme of two state-owned banks in July 1997 (that in the case of Ljubljanska banka d.d., was instigated by the decision of the Bank of Slovenia in January 1993 and in the case of Kreditna banka Maribor d.d., in March 1993), several privatisation models have been on the table. The combined market share of the two state-owned banks has accounted for approximately 40 per cent of total banking assets over the last six years. Following the decision adopted by the Government of the Republic of Slovenia in July 1999, the first phase of privatisation was launched in 2000. The concept of gradual privatisation, however, is generally approved and the first phase envisages the privatisation of both banks up to the amount of 30 per cent of the state-owned equity stake.

10% of government equity holdings has been transferred to Pension Fund Management and Slovenian Compensation Company.

A 10 per cent holding of the Republic of Slovenia has already been transferred to the Pension Investment Fund (transformed in January 2000 to the Pension Fund Management) and the Slovenian Compensation Fund (recently transformed to the Slovenian Compensation Company), i.e. has been swapped for shares of other enterprises, which are owned by the aforementioned funds/companies. These shares are used for the closing of the so-called privatisation gap. For the remaining portion of state ownership in the two banks, there are several privatisation scenarios. Different possibilities are being explored with regard to the final ownership structure of the banks and privatisation proceeds. The Government has engaged a foreign financial consultant to assist it in the preparation of privatisation strategy who will eventually help in the implementation of the selected privatisation model.

In addition to the transfer of shares to the First Pension Fund established under the law promulgated in June 1999 with the aim to close the so-called privatisation gap, NLB is planning to sell state-owned shares on foreign financial markets by issuing Global Depository Receipts (GDRs) against deposited shares. In addition, the recapitalisation of NLB will be done by issuing new shares to be offered to domestic investors.

[7] Central government refers to direct users of the budget of the Republic of Slovenia as laid down in the Decree on Direct and Indirect Users of Central and Local Government Budgets (Official Gazette of the Republic of Slovenia, No. 13/00).

Contrary to NLB, which is endeavouring to consolidate its banking group in the course of the privatisation process, NKBM has opted for selling 20 per cent of capital to a strategic partner.

The Government agenda is to use privatisation of both banks to enhance corporate governance, contribute to greater effectiveness of both banks and consequently contribute to greater effectiveness of all Slovenian banks. At the same time, it is keen to optimise privatisation proceeds.

4. ORGANISATIONAL STRUCTURE AND TASKS OF THE BANK SUPERVISION DEPARTMENT

Bank Supervision Department has three operational units.

The Bank Supervision Department was established at the beginning of April 1992 within the framework of the Bank of Slovenia. The Department comprises three separate units:

- Licensing
- Off-site supervision of banking operations
- On-site supervision of banking operations

Under the new Banking Act, the Bank Supervision Department has new tasks and responsibilities.

The nucleus of the Bank Supervision Department was a 15-strong staff that increased by the end of June 2000 to 42 people. The breakdown of the head-count at end-June 2000 shows that there were 8 people in the executive and administrative section, 14 employees were working in the off-site supervision section, 17 people were engaged in on-site examinations, while 3 employees handled licensing issues. With the effectiveness of the Banking Act, the Bank Supervision Department has been given a mandate to discharge new tasks (supervision on a consolidated basis, supervision of legal and natural persons suspected of unauthorised provision of banking services, supervision of savings and loan undertakings, etc.); hence it is scheduled to increase the number of employees to 45 by the end of 2000.

The Bank Supervision Department subscribes to a pro-active human resource policy. In addition to the careful selection of new recruits from the ranks of dedicated professionals, it pays a lot of attention to vocational and on-the-job training of staff. As many as 32 employees are university graduates (two are Masters of Science) and efforts are focused on developing skills required for coping with new challenges in an ever-changing business environment. High standards have been achieved through a combination of hands-on experience and up-to-minute theoretical knowledge acquired either at post-graduate studies, or at tailored courses. Seminars, workshops, and working visits to high-profile foreign supervisory authorities were the most common forms of professional training during the period under review.

Core tasks carried out by individual units of the Department:

Granting authorisations (Licensing)

- Preparation of secondary legislation that governs licensing requirements and/or rules,
- Advising on the implementation of secondary legislation that governs licensing requirements and/or rules,
- Processing applications and the preparation of reports on authorisations granted,

- Drafting decisions and explaining grounds for the decisions taken,
- Monitoring of the enforcement of the decisions issued.

Off-site supervision of banking operations

- Drawing up the legal framework for the carrying out supervision and surveillance of banks and savings banks,
- Monitoring international recommendations in the field of supervision,
- Counselling in the implementation of financial legislation,
- Preparation of instructions with regard to implementation of accounting standards and accounting counselling,
- Controlling operations carried out by banks and savings banks on the basis of prudential reports and statutory returns,
- Corrective actions launched with the aim of resolving non-compliance identified in operating activities of banks and savings banks, and monitoring of implementation of such corrective actions,
- Analysis of results of operations of banks and savings banks,
- Co-operation with domestic and international institutions,
- Participation in the preparation for on-site examinations in banks and savings banks,
- Legal counselling,
- Electronic data processing and other related services.

On-site supervision of banking operations

- Preparatory activities leading to on-site examination on the basis of prudential reports of banks and savings banks and other statutory returns,
- On-site examinations of business operations of banks and savings banks, elaboration of reports and proposals for corrective measures,
- Implementation of corrective measures designed to mitigate deficiencies that have been detected in operations of banks and savings banks,
- Monitoring of the enforcement of corrective measures taken against banks and savings banks,
- Advising within on-site supervising function on the way to improve banking operations of banks and savings banks,
- Monitoring banks and savings banks,
- Preparation of measures aimed at preventing deterioration in the financial position of banks and savings banks,
- Co-operation in assessing conditions for instituting special administration in banks and savings banks,
- Co-operation in assessing conditions for liquidation of banks and savings banks,
- Co-operation in assessing conditions for bankruptcy of banks and savings banks,
- Governing and managing banks and savings banks in special cases,
- Co-operation with local and foreign supervisory authorities,
- Co-operation with foreign chartered accountants/certified auditors, etc.

5. GRANTING AUTHORISATIONS (LICENSING)

The establishment of banks are laid down in the directives of the European Union (First Banking Directive (77/780/EEC), Second Banking Directive (89/646/EEC), and Post BCCI Directive (95/26/EC).

The list of financial services has been aligned with European banking directives. Specific banking services are receiving deposits or other repayable funds from the public and granting credits for their own account.

In terms of its legal status, a bank is a joint-stock company incorporated in the Republic of Slovenia and authorised by the Bank of Slovenia to accept deposits and provide banking services, as well as selected financial services.

Minimum initial capital for banks is 1 billion tolars.

The amount of initial capital for banks has been set at 1 billion tolars irrespective of the scope of banking services. Consequently, the "old", multi-tier licensing system has been abolished. The minimum amount of initial capital for savings banks has been set at 186 million tolars. The same threshold will apply to savings and loan undertakings after a five-year transitional period.

Terms and conditions for obtaining authorisation for the provision of banking services and other financial services are laid down in the Banking Act. Within the framework of its regulatory tasks, the Bank of Slovenia is authorised to set standards regarding human resource, and to establish criteria for organisational and technical issues essential to the provision of banking and other financial services. Under the Banking Act the so-called universal banking licence issued by the Bank of Slovenia is the authorisation given to banks and savings banks to carry out banking services and selected financial services.

Authorised banks may provide all kinds of banking and selected financial services.

The following financial services fall within the scope of banking services:

- Accepting deposits from individuals and legal entities and granting credits for its own account, and
- Services, which in line with law, may be provided only by banks.

Banking services may only be provided by:

1. A bank i.e. a savings bank, which has been duly authorised by the Bank of Slovenia to perform banking operations,
2. A branch of a foreign bank established on the basis of the authorisa tion granted by the Bank of Slovenia,
3. A bank from a Member State, which in accordance with the Banking Act establishes a branch on territory of the Republic of Slovenia, i.e. which has been authorised in accordance with the said law to provide banking services on the territory of the Republic of Slovenia.

Banks may also engage in other financial services, subject to the authorisation issued by the Bank of Slovenia, and provided they fulfil terms and conditions laid down in the law governing the provision of other financial services.

Other financial services under the Banking Act are the financial services listed below:

1. Factoring,
2. Financial leasing,
3. Issuing of guarantees and other commitments,
4. Lending operations including consumer credits, mortgages, and financing of commercial transactions,
5. Trading in foreign means of payment including foreign exchange transactions,
6. Trading in financial derivative instruments,
7. Compilation, analysis and dissemination of information on credit standing of legal entities,
8. Mediation in sales of insurance policies in accordance with the law governing the insurance sector,
9. Issuing and administering of payment instruments (e.g. payment and credit cards, travellers' cheques, banks' bills of exchange),
10. Safe custody services,
11. Mediation in the conclusion of loan and credit transactions,
12. Services in connection with securities in accordance with the law governing the securities market,
13. Management of pension and investment funds in accordance with the law governing pension and investment funds, and
14. Performance of payment transactions.

A bank may engage in other ancillary banking services, *viz*.:

- Directly connected with the provision of banking services, and
- Connected with real estate management, management of the administration of data processing system, and other activities of similar nature in relation with core business of one or more banks.

A bank may not engage in any other activities.

Foreign banks apply to the Bank of Slovenia to establish a branch in Slovenia.

Foreign banks may provide banking and other financial services listed in the Banking Act through a branch in the Republic of Slovenia. A foreign bank may establish a branch on the territory of the Republic of Slovenia, subject to the authorisation granted by the Bank of Slovenia. The Bank of Slovenia may require that a foreign bank, which has requested to open branch on the territory of the Republic of Slovenia, shall deposit endowment capital, pledge another type of financial assets or other adequate collateral as a security that liabilities arising from business transactions concluded on the territory of the Republic of Slovenia will be duly settled.

Branches of foreign banks in Slovenia are offices of these banks and they do not have legal personality. Nonetheless, the provisions laid down in the Banking Act apply meaningfully to branches of foreign banks in the field of risk management, confidentiality of information/data, books of account and annual reports and accounts, internal and external audit, etc. Provisions that stipulate criteria applicable to bank management (to be fit and proper), shall apply also to branch managers.

Deposits made with Slovenian branches of foreign banks are covered by the deposit-guarantee scheme established in the bank's home state. However, the level and scope of cover provided by the home state scheme for deposits with Slovenian branches may not be greater than is available under the Slovenian scheme set up in line with the provisions of the Banking Act. In the absence of a deposit-guarantee scheme in the home state, or if it is less generous than the Slovenian scheme, branches of foreign banks shall join the deposit-guarantee scheme of the Republic of Slovenia to supplement the cover available under their home state scheme. The Bank of Slovenia determines the level and scope of cover to be available under the Slovenian scheme.

Banks are to comply with provisions of the Banking Act by 20 August 2000.

After the effectiveness of the new Banking Act, banks continued to provide banking services in accordance with the authorisation they had obtained and they had 18 months to complete changes with regard to their legal status and comply with new requirements. The transitional period left to banks to comply with provisions laid down in the Banking Act expired on 20 August 2000. The most important requirements comprise minimum initial capital for banks in the amount of 1 billion tolars, all shares shall be issued as registered shares, preference shares may not exceed one third of all shares, shares shall be issued in a non-material form, all shareholders with qualifying holdings shall be approved by the Bank of Slovenia, articles of association shall be aligned with the Banking Act, supervisory and management boards shall be set up in conformity with provisions of the Banking Act, management shall be composed of at least two members assessed to be fit and proper by the Bank of Slovenia, and competent professionals shall be in charge of internal audit. Banks shall fully comply with all prudential rules, excluding only those where the Banking Act provides for a longer transitional period.

When a bank has fulfilled all provisions of the Banking Act, the Bank of Slovenia grants authorisation for banking services and those other financial services that the respective bank used to provide under the old law. As for all other financial services, which a bank would like to provide for the first time, the applicant will be authorised subject to its ability to prove that it has human resource, as well as technological and organisational resources necessary for these other financial services.

In accordance with provisions of the Banking Act, the Governing Board of the Bank of Slovenia takes under scrutiny all proposals prepared by the Bank Supervision Department to grant or withhold i.e. reject authorisations. One Committee that assists the Governing Board of the Bank of Slovenia is responsible for the assessment of banks' applications and for the preparation of opinions on the decision to authorise operations of a bank or a savings bank. Another Committee of the Governing Board of the Bank of Slovenia is responsible for the preparation of opinions in relation to authorisations to be issued or withheld i.e. rejected to nominated members of banks' management boards. The range of authorisations is presented below:

- Authorisations for the provision of banking services,
- Authorisations for the provision of other financial services,
- Authorisations for the acquisition of a qualifying holding,
- Authorisations for mergers and acquisitions,
- Authorisations for the establishment of cross-border branches,
- Authorisations for the establishment of branches of foreign banks in the Republic of Slovenia, and
- Authorisations for the establishment of representative offices of foreign banks, and
- Authorisations for discharging responsibilities and duties of a member of the bank's management board.

Table 3: Authorisations granted and withheld in 1999 and the first half of 2000

	Type of authorisations*	1999		First half of 2000	
		Number of authorisations granted	Number of authorisations withheld	Number of authorisations granted	Number of authorisations withheld
1	Authorisations for the provision of banking services	2	0	5	0
2	Authorisations for the establishment of branches of foreign banks in the Republic of Slovenia	1	0	0	0
3	Authorisations for mergers and acquisitions	1	0	1	0
4	Approvals/Authorisations for the establishment of representative offices of foreign banks	2	0	0	0
5	Approvals to domestic shareholders to acquire a stake exceeding 15 per cent of the capital,	2	0	-	-
	Authorisations for the acquisition of a qualifying holding	8	5	5	0
6	Authorisations to provide the so-called additional banking services,	1	2	-	-
	Authorisations for the provision of other financial services	24	0	6	1
7	Authorisations to provide securities-related services	1	0	-	-
8	Authorisations for discharging responsibilities and duties of a member of the bank's management board	18	1	16	0
	Total	60	8	33	1

* Both the wording and the contents of the terminology used with regard to authorisations granted to banks and savings banks under the 1991 Law on Banks and Savings Banks differ in certain cases from the wording and contents of the terminology used in the Banking Act effective from 20 February 1999.

Source: Bank of Slovenia

6. BANKING GROUPS

Number of banking groups has dropped from 4 in 1997 to just one - NLB banking group.

In the year 1997, first banking groups were formed. The formation of banking groups was the first step in the direction of the consolidation of the banking sector. Under the 1991 Law on Banks and Savings Banks, a banking group was formed when one bank directly or indirectly acquires at least a 40 per cent stake in the capital of another bank, or if it controls another bank directly or indirectly. In accordance with this definition, banking groups were parented in 1997 by Banka Celje, Nova Ljubljanska banka, SKB banka, and Banka Koper.

Consolidation was in some cases cost-led, while for other banks it meant access to new skills and technologies. In addition, the impact produced by prudential measures introduced by the Bank of Slovenia was for some banks the argument that tipped the scale in favour of a merger. In 1998, in addition to the take-over of Creditanstalt d.d by Bank Austria d.d. Ljubljana and the liquidation of Hipotekarna banka d.d. Brežice, two banks with controlling stakes in their respective banking groups finalised take-overs. Namely, Banka Celje d.d. took over Hmezad banka d.d. Žalec, and SKB banka d.d. Ljubljana took over UBK univerzalna banka d.d. Ljubljana. The trend continued in the second half of 1999 when Banka Koper d.d. completed the take-over of M banka d.d., Ljubljana. The direct bearing of these developments on the composition of the banking sector is that instead of four banking groups, there is currently only one operating banking group – the one headed by NLB. The banking group of NLB is composed of Banka Zasavje d.d., Trbovlje, Pomurska banka d.d., Murska Sobota, Koroška banka d.d., Slovenj Gradec, Banka Velenje d.d., Velenje, Banka Domžale d.d., Domžale and Dolenjska banka d.d.

Minimum requirements for the establishment of banking groups were laid down by the Bank of Slovenia in 1997. Banks in a banking group would conclude a legally binding contract to harmonise both current and development policies in the field of cross-border banking operations, marketing, development of new products, information technology, lending operations, ATM network, etc. Risk management policy issues were addressed at the level of the banking group. Banks in a banking group would provide funds to a bank faced with liquidity problems, after the bank with liquidity problems had exhausted regular ways to borrow funds in the money market or within the framework of accommodation provided by the Bank of Slovenia. Funds were to be provided under terms and conditions and up to the limits agreed upon in advance. If a bank was faced with solvency problems, other members of the banking group would take steps aimed at mitigating solvency risk on terms and up to the limits agreed upon in advance. The parent bank plays a leading role within the banking group. All banks in the banking group were to apply the same accounting standards on a consistent basis, and internal control and audit function was set up in accordance with standards observed by the internal audit department of the parent bank. In accordance with the contract on the establishment of a banking group, the same external auditor was to be appointed to conduct audit both of the parent bank and of all members of the banking group.

Banking Act has modified the definition of banking groups.

The definition of a banking group has been changed under the 1999 Banking Act. In particular, the Banking Act has introduced a broader definition of a banking group unlike the strict limits laid down in the 1991 Law on Banks and Savings Banks. Namely, a banking group exists when a bank or a financial holding incorporated in the Republic of Slovenia is a parent company to one or more banks, i.e. other financial institution(s) or a company for auxiliary banking services.

A bank or a financial holding is considered to be a controlling (parent) undertaking, if it meets any of the criteria listed below:

- The parent undertaking has direct or indirect majority holding, or
- The parent undertaking has direct or indirect majority of voting rights, or
- The parent undertaking has the right to appoint the majority of the members of the management or supervisory board, or
- The parent undertaking has the right to exercise dominant influence, or
- The parent undertaking exercises dominant influence, or
- The parent undertaking is duly authorised under a binding contract concluded with one or more shareholders or partners in the controlled undertakings to exercise their voting rights, so as to obtain in combination with its own voting rights the majority necessary for the appointment of the members of the management or supervisory board, or
- The parent undertaking has directly or indirectly at least 20 per cent of voting rights or participation in the capital of the controlled undertaking, and to exercise this participation jointly with one or more legal entities, who are not members of the banking group.

Under the new definition, there are 14 banking groups in Slovenia.

If a banking group is defined in the light of the above requirements, then at present, the actual number of banking groups in Slovenia is higher than the number of banking groups under the definition in the 1991 Law on Banks and Savings Banks. Thus there is only one banking group in Slovenia under the old definition and as many as 14 banking groups under the new definition (including the banking group parented by NLB).

The Bank of Slovenia derives authority and responsibility from the Banking Act to stipulate the method and scope of consolidation, as well as the contents of consolidated financial statements. It drafts detailed rules on the contents of statutory returns and sets time limits for prudential reporting. Even though the consolidation of financial statements was obligatory under the 1991 Law on Banks and Savings Banks, the 1999 Banking Act goes a step further and introduces consolidated supervision of banks with the purpose of checking whether an individual bank or a banking group as a whole abides by the risk management rules.

The Decree on Supervision of Banks and Savings Banks on a Consolidated Basis was promulgated at end-1999.

At the end of 1999, the Bank of Slovenia passed the Decree on Supervision of Banks and Savings Banks on a Consolidated Basis. The Decree elaborates on the section of the Banking Act that envisages consolidated supervision and crowns efforts of Slovenian regulators to incorporate provisions laid down in the Directive on Supervision of Banks on a Consolidated Basis (92/30/EEC) into Slovenian legislation.

Supervision on a consolidated basis was implemented in 2000 and is mandatory for every bank, which controls one or more other banks, other financial institutions or companies for auxiliary banking services, or has a holding in one or more of these undertakings. The legal definition for other financial institutions valid in Slovenia includes insurance companies – a step in the direction of the extension of the scope of consolidated supervision with respect to the requirements laid down in the Directive. Even a bank, which is controlled by a financial holding, is subject to supervision on the grounds of consolidated financial position of the financial holding. The Decree also determines in which cases a particular entity is exempt from consolidated supervision. Such exemptions comply fully with the exemptions laid down in the Directive. The Decree is limited to those cases where the Bank of Slovenia is in charge of conducting consolidated supervision, while with regard to international banking groups with Slovenian banks as member banks, liaison and co-operation between competent supervisory authorities is envisaged. Whether an undertaking is to be included in consolidated financial statements depends on the type of interconnection with other members of the group. The same criterion applies to the choice of the method of preparation of such statements (full consolidation, partly consolidation, capital method). Consolidated financial statements are a basis for the preparation of prudential reports for banks in the group.

Banks shall fulfil on a consolidated basis requirements laid down with regard to minimum capital amount, they shall abide by minimum capital adequacy ratio, limits set on the exposure of the entire group to individual counterparties or a group of related counterparties and capping of investments in non-financial institutions. Related parties shall provide adequate internal audit function, so as to ensure corectness and completeness in establishing facts and reporting findings, which are significant to consolidated supervision.

The Bank of Slovenia derives authority from the Banking Act to carry out the co-operation with domestic supervisory authorities in other financial sectors, and the responsibility for the consolidated supervision will be enstrusted to the Bank of Slovenia as the principal supervisory authority as far as all groups which comprise at least one bank are concerned. One of the preconditions for effective consolidated supervision is adequate professional level in all three sectors and mission-driven environment.

7. REPORTING REQUIREMENTS

Banks are required to submit prudential reports to the central bank on daily, monthly, quarterly, semi-annual and annual basis. These routine reports (statutory returns) are listed below.

Daily	·	on expected incoming and outgoing payments of largest depositors in tolars,
	·	on expected tolar liquidity flows.
Monthly	·	on book account balances,
	·	on deposits of thirty largest depositors.
Quarterly	·	on regulatory capital,
	·	on the classification of on- and off-balance sheet items,
	·	on large exposure,
	·	on equity investments in non-financial institutions,
	·	on lending and deposit interest rates.
Semi-annually	·	on capital investments.
Annually	·	auditor's report.

8. EFFECTIVE SUPERVISION OF BANKS AND SAVINGS BANKS

Ongoing bank supervision has been ensured through regular on-site examinations and off-site surveillance.

Supervision and surveillance of banks and savings banks is a continuous process based on prudential reports, on analysis and control of these reports carried out by analysts of the Bank Supervision Department, and on-site examinations.

The Bank Supervision Department subscribes to the so-called four-eye-principle. This approach combines off-site analysis (surveillance) and on-site examination as part of monitoring operations of banks and savings banks. How many banks and savings banks will be scrutinised by an analyst-examiner team depends on the scale of operations of banks and a savings banks selected.

Analysts participate in assessing operating results of banks and savings banks, and in procedures related to granting new and amending existing authorisations for banking operations. They evaluate proposals for new systematic solutions, advise banks and savings banks as to the implementation of standards for safe and sound banking operations, monitor compliance with requirements for safe and sound banking operations, and monitor efficency of banking operations on the basis of information and data at least once a month. Analysts also participate in preparations for on-site examinations of banks and savings banks and in meetings held with management teams of banks and savings banks and other institutions. Furthermore, they prepare different materials for the bodies of the Bank of Slovenia, etc. Analysts immediately inform examiners and management of the Bank Supervision Department about any findings that diverge from normal banking operations for the respective bank or a savings bank. A qualified judgement whether the examiners of the Bank Supervision Department will undertake on-site examination of the particular bank or a savings bank is made on the basis of such information.

In cases of non-compliance identified in operations of banks or savings banks, both analysts and examiners take corrective actions and monitor the implementation of such actions.

Every year full-scope examinations are carried out in 9 to 13 banks and savings banks.

Over the last three years, full-scope examinations were carried out each year in 9 to 13 banks and savings banks plus targeted examinations conducted in 18 to 30 banks and savings banks each year (examination of selected areas).

In line with the strategic plan pursued by the Governing Board of the Bank of Slovenia, the number of full-scope examinations is to be decreased to 7 to 9 annually, while targeted examinations focused on individual segments of banking operations is increase to at least 30 target examinations of banks and savings banks scheduled per year. As it has been common so far, a certain bank or a savings bank could be examined several times in a year. Either a full-scope or targeted examination should be conducted in each bank or a savings bank at least once a year. The areas to be examined are selected in line with a risk-focused approach to supervision, but assessment of risks associated with information technology will come to the fore in the near future.

In 1999, examiners of the Bank of Slovenia conducted 39 examinations in banks and savings banks, out of which 9 were full-scope examinations of banking operations and 30 targeted only particular segments. The breakdown further shows that 8 full-scope and 22 targeted examinations were conducted in banks, while one full-scope and 8 target examinations were carried out in savings banks.

In the light of the widely expected Y2K date-processing problem, thought 1999 examiners focused on preparations carried out in banks and savings banks. The way in which management and information technology departments handled potentially dangerous problems of the Y2K transition was under the looking-glass of banking supervisors particularly in the second half of 1999. The Governing Board of the Bank of Slovenia was briefed on the project disciplines on a quarterly basis. Driven by the need to ensure that preparations for the year 2000 were made with due thoroughness, all banks and savings banks were subject to on-site targeted examinations in the course of 1999.

Banking Act gives mandate to the Bank of Slovenia to supervise legal persons connected with banks.

As from the effective date of the Banking Act, the Bank of Slovenia is authorised to supervise business operations of persons who are connected with a bank, provided it serves the purpose of supervising bank operations. Supervisory competence conferred upon the Bank of Slovenia has been extended to cover other persons in cases of a grounded doubt that these persons provide banking services without the authorisation issued by the Bank of Slovenia. In line with these provisions, on-site examinations were carried out in 1999 in 3 companies, subsidiaries of two banks. Additionally, based on the report of the Market Inspectorate General of the Republic of Slovenia, on-site examinations of three companies suspected of providing banking services without being authorised by the Bank of Slovenia were carried out.

Regular annual meetings take place with members of management board and senior managers of bank and savings banks, either within the framework of full-scope examination or with the aim to discuss relevant issues. These meetings are convened to evaluate operating results, the current position of the respective bank i.e. savings bank, and development strategy endorsed by the particular bank i.e. savings bank. Exchange of views and information sharing is a two-way process and calls for commitment on both sides, since it makes timely and appropriate action possible in the case where difficulties are encountered by banks or savings banks in the ordinary course of operations.

There is also ongoing exchange of views and information between supervisors of the Bank of Slovenia and other supervisory authorities at home and abroad. In addition to sharing information and expert opinion on supervising financial market participants connected with banks, 8 targeted examinations were conducted in 1999 together with the representatives of the Securities Market Agency (control of securities depots in Slovenia).

In the first half of the year 2000, examiners of the Bank of Slovenia conducted four full-scope examinations: 3 in banks and one in a savings bank. In addition, 12 targeted examinations were completed: 10 in banks and 2 in savings banks.

Exchange of views goes on between the Bank of Slovenia and other supervisory authorities at home and abroad.

The co-operation with the Securities Market Agency and the Market Inspectorate General of the Republic of Slovenia continued in the first half of 2000. Examiners of the Bank of Slovenia joined forces with the examiners of the Securities Market Agency and examined three banks (connected entities were examined), four examinations were conducted together with the inspectors of the Market Inspectorate General of the Republic of Slovenia (examinations of companies suspected of engaging in operations for which they have not been authorised by the Bank of Slovenia).

It was for the first time in 2000 that the Bank of Slovenia, State of New York Banking Department and Federal Deposit Insurance Corporation carried out a joint on-site examination of a subsidiary bank of the largest Slovenian bank in the USA.

In accordance with the endorsed strategic plan of the Bank Supervision Department, the stress has been shifted to targeted examinations, i.e. examinations of selected areas. The rationale for this is to enable in-depth insight into the business areas with a high degree of inherent risks or to collect information pertinent to those areas about which the Bank of Slovenia has inadequte information.

On-site examinations in banks focus on appropriate classification of on- and off-balance sheet items.

Since exposure of Slovenian banks and savings banks to credit risk is regarded as the most significant risk, the examinations carried out during the period under review highlighted adequate classification of on-balance sheet assets and off-balance sheet items. Special attention was paid to supervision on a consolidated basis – examination of a bank and persons connected to it. The examiners of the Bank of Slovenia analysed financial statements prepared by connected persons, the bank's current and future policy in relation to connected persons, quality of assets – investments of connected persons, management and the relationship with the bank, as well as operational risks. Information compiled served to examiners to decide whether provisions established and value adjustments for the bank's exposure (credits, equity investments) to connected persons were adequate.

Within the framework of the payment systems reform, examiners of the Bank Supervision Department together with co-workers from other departments of the Bank of Slovenia assisted in checking criteria set for the migration of payments to commercial banks.

The full-scope examinations of banks and savings banks focused on the following areas:

- loan and securities portfolio,
- compliance with capital adequacy requirements,
- compliance with risk management requirements,
- assessment of bank profitability,
- bank liquidity and customer deposits,
- assessing adequacy and effectiveness of internal controls systems,

- equity investments and fixed assets,
- bank management and internal audit function,
- information technology with special emphasis on Y2K 2000 compliance, etc.

Target examinations primarily focused on the following areas:

- loan portfolio (corporate and retail lending),
- securities portfolio,
- bank management and internal audit function,
- connected lending,
- fairness of accounting data disclosed,
- information technology, with special emphasis on Y2K 2000 compliance, etc.

9. ASSESSING INTERNAL CONTROLS SYSTEMS AND INTERNAL AUDIT DEPARTMENT

The effective internal controls system and appropriate functioning of the internal audit department are key elements for assessing a bank's policies and methodologies for managing and controlling risks associated with banking operations with the ultimate goal to encourage safe and sound banking practices and avert a crisis.

The enactment of the new Banking Act is a further step in the direction of equipping the Slovenian banking system with resources and skills required to stand up to full-size market pressures. By identifying the place, role and competence of internal audit department, the implementation of widely accepted principles for effective banking supervision with the underlying significance of adequate effective internal controls system has been facilitated. It is of paramount importance that a bank has in place an adequate internal controls system, which is fully operational, while the motive for the effective performance of the internal controls function is the need to have risks inherent in banking business on short rein. Under the condition that the internal audit department fulfils all statutory requirements, internal auditors for banks function in accordance with internal audit standards and code of conduct that lays down professional ethics for internal auditors, then solid foundations have been laid for banking supervisors to enforce principles required for safe and sound banking operations.

Assessment of properness and effectiveness of internal controls system is integral part of on-site examinations of banks and savings banks.

Assessing the adequacy and effectiveness of internal controls system is the centrepiece of full-scope on-site examinations. In the light of the importance of internal controls function, this area deserves constant attention. By being compliant with the Principle 14 of Core Principles for Effective Banking Supervision, sound and comprehensive internal controls function is highlighted.

The role of banking supervisors is essential in the process, since it is up to banking supervisors to see that all banks, irrespective of their size, have in place effective internal controls systems, which must be commensurate to the type complexity and scale of risks assoociated with their on- and off-balance sheet operations, and which will enable them to respond promptly to changes in banking environment and market conditions. In the cases where banking supervisors conclude that internal controls system is not commensurate to risks the respective bank is exposed to shall take immediate action against the deliquent bank and require that the bank shall promptly improve its internal controls system.

Examiners evaluate internal controls systems.

Although management and supervisory board are ultimately responsible for effective functioning of a bank's internal controls system, it is up to banking supervisors to assess the internal controls system of a bank within the framework of their ongoing supervisory function. It is essential to establish whether management of the examined bank pay appropriate and immediate attention to the problems identified through internal audit function. In other words, banking supervisors must be satisfied that the attitude of the bank's management towards reports drawn up by internal auditor is appropriate and that both the response time and the reaction to such a report are adequate for the nature and scale of the particular bank's business. In cases where management failed to react in response to important findings included in the internal auditor's report, banking supervisors still may decide to use such reports. However, this fact would raise doubts as to their value in the process of boosting effectiveness of controls. It is essential that banking supervisors do not limit their assessment on how effective the entire internal controls system is, but also to evaluate individual controls incorporated primarily in those areas associated with high levels of risk (e.g., areas characterised by particularly high profitability, fast growth, and new products). Banking supervisors shall pay particular attention to banking policies and procedures issued in writing.

Besides, banking supervisors must always have a means of reviewing findings and recommendations made by external auditors in relation to effectiveness of internal controls. Banking supervisors must also check if the bank's management and supervisory board have taken any remedial actions in accordance with recommendations given by external auditors. The scale and nature of problems identified by auditors associated with control procedures shall be taken into account also when banking supervisors assess effectiveness of internal controls that the bank has in place.

Although there is always room for improvement of adequacy and effectiveness of internal audit function, the quality of performance and the qualification structure of staff working in internal audit departments have been steadily improving; the number of auditors certified by the Slovenian Institute of Auditing has been growing since banks must meet the requirements laid down in the Banking Act. Namely, each bank shall have at least one employee who is a certified i.e. qualified internal auditor to discharge tasks and responsibilities delegated to internal audit function.

Need to extend the scope of internal audit to information technology is becoming acute.

There are still rather significant differences in the number of internal auditors and their professional skills from one bank to another. How many skilled experts in this field will a bank recruit is commensurate to the scale of its operations and resources a particular bank allocates to internal audit function. Due to the ever-increasing role of information technology and risks associated with that area, auditors are stressing the importance of vigilance and sophisticated control tools in monitoring and controling information technology risk.

It is a key factor that bank management acknowledges how important and beneficial internal audit function is. The bottomline is that bank management are responsible for safe, efficient and lucrative banking operations; therefore, they have to recognise in internal audit function a tool for achieving the set targets through monitoring of timely implementation of policies and actions and by taking the necessary steps to avert adverse business situations.

10. CO-OPERATION WITH SUPERVISORY AUTHORITIES

10.1. Co-operation with domestic supervisory institutions

Universal banks typical of the Continental Europe and Slovenia, are authorised to engage in all operations of commercial and investment banking. In addition, there are also contractual and capital ties between banks and insurance companies. Since banking and insurance fall under the jurisdiction of different supervisory authorities, effective supervision of financial institutions calls for harmonised action of all supervisory authorities. In line with the Banking Act, the Code of Practice for the Co-operation between Supervisory Authorities was adopted in 1999 (Official Gazette of the Republic of Slovenia, No. 55/99). Prior to the effectiveness of the Code of Practice, terms of co-operation between the Bank of Slovenia and other supervisory authorities were detailed in protocols.

Effective supervision calls for harmonised actions of all supervisory authorities.

The Code of Practice articulates the scope and method of co-operation among the Bank of Slovenia, the Securities Market Agency and the Insurance Supervisory Authority of the Republic of Slovenia (recently tranformed to the Insurance Supervisory Agency). This co-operation covers the following areas:

Code of Practice elaborates on nature and scope of co-operation between supervisory authorities.

- strategic development issues, annual planning of joint actions to be endorsed by the steering committee and monitoring the implementation of the memoranda of understanding (MoU), signed by domestic supervisory authorities,
- sharing information necessary in the course of supervision of financial institutions with other supervisory authorities,
- exchange of information necessary in the process of granting authorisations,
- exchange of information on facts and events in relation to connected persons and which may have an impact on financial position or operations of the entity, which is being examined by another supervisory authority,
- dissemination of information necessary in the course decision-making with regard to other individual issues,
- organisation of joint examinations,
- sharing information on irregularities, which a supervisory authority finds out in the course of the examination, provided such findings are important for the work of other supervisory authorities,
- other joint activities, which contribute to the harmonised supervision, boost effectiveness of supervisory authorities and enhance effectiveness of the financial market.

In line with the afore-mentioned Code of Practice, a steering committee was set up. Members of the steering committee are: the Governor of the Bank of Slovenia, the Minister of Finance, the President of the Council of Experts of the Securities Market Agency and the President of the Council of Experts of the Insurance Supervisory Agency. Since the Code of Practice envisages that memoranda of understanding should be finalised between supervisory authorities, in November 1999 the Bank of Slovenia and the Securities Market Agency finalised a memorandum of understanding. Another memorandum of understanding was finalised between the Bank of Slovenia and the Ministry of Finance – Insurance Supervisory Authority of the Republic of Slovenia. (as at 1 June 2000 Insurance Supervisory Agency)

Code of Practice lays ground for signing MoU between supervisory authorities.

The Code of Practice provides a formal basis for signing memoranda of understanding and elaborates on the existing protocols on co-operation between domestic supervisory authorities. The Bank of Slovenia has already signed memoranda of understanding with the Securities Market Agency and the Insurance Supervisory Authority of the Republic of Slovenia (as of 1 June 2000 Insurance Supervisory Agency). Details of the scope of co-operation between supervisory authorities, tools to be used for that purpose and dissemination of information are elaborated in memoranda of understanding that can be regarded as redesigned protocols on co-operation duly aligned with the Code of Practice. A liaison group is responsible for the implementation of memoranda of understanding signed by supervisory authorities and tasks adopted by the steering committee. The liaison group meets at least every three months. The liaison group is composed of the Deputy Governor of the Bank of Slovenia, i.e. Director of the Bank Supervision Department of the Bank of Slovenia, Director of the Securities Market Agency, and Director of the Insurance Supervisory Agency.

The co-operation with supervisory authorities has been going on smoothly in line with memoranda of understanding in the form of regular exchange of information and data and dissemination of designated information upon the request of other supervisory authority. As a precondition for the exchange of information under the Banking Act, supervisors have the obligation of professional secrecy and shall honour confidentiality of information. Supervisory authorities have responsibility to inform other supervisory authority on irregularities detected, which fall within the framework of its jurisdiction. Supervisory authorities co-operate also in joint examinations.

The Memorandum of Understanding between the Bank of Slovenia and the Securities Market Agency has become operational and the two supervisory authorities have already carried out joint examinations in banks and stock-broking companies. Smooth co-operation is also witnessed in the exchange of information and expert opinions between the Bank of Slovenia and the Securities Market Agency.

Steering committee for supervisory authorities of financial institutions and liaison group have started work this year.

In January 2000, the members of the steering committee of supervisory authorities of financial institutions met for the first time to discuss the plan of future actions. The conclusion of the meeting was that the liaison group is responsible for keeping a watchful eye on all issues in relation to the implementation of new regulations. In addition, the liaison group will draw the attention of the members of the steering committee of supervisory authorities of financial institutions to problems, which arise primarily due to loopholes in covering activities of financial intermediaries. When grey areas are spotted, the liaison group is to sound the alarm and propose modifications or amendments to legislation.

The liaison group has met twice so far and has addressed issues in relation to financial conglomerates. For the purpose of enhancing sophistication in this area and boosting capabilities to cope with ever-increasing complexity of interrelations, the co-operation between supervisors has been developed at fast pace. With regard to the area of penal jurisdiction to be conferred upon supervisors, the Bank of Slovenia and the Securities Market Agency have presented a motion to the Ministry of Finance to draft a bill of a special law that would give power to supervisory authorities to impose fines or penalty payments for failure to comply with obligations, i.e. for contraventions of regulations, in their respective area of responsibility. The law would also elaborate on all steps of imposing sanctions (ruling, appeal, execution).

10.2. CROSS-BORDER CO-OPERATION

The Bank of Slovenia is affiliated to the Group of Banking Supervisors from Central and Eastern Europe.

In its capacity of a supervisory authority, the Bank of Slovenia is a member of the Group of Banking Supervisors from Central and Eastern Europe. Professionals working in the Bank Supervision Department are regular participants of meetings, seminars, workshops and conferences that bring together supervisors from member countries.

In September 1999, the Bank of Slovenia hosted the 12th Conference of the Group of Banking Supervisors from Central and Eastern Europe. Among participants of the Annual Conference, there were experts from the Basel Committee on Banking Supervision and the Financial Stability Institute.

As outlined above in the chapter on the compliance with the Core Principles for Effective Banking Supervision, there is ongoing exchange of information between Slovenian and foreign supervisory authorities also in practice. In line with the Memorandum of Understanding signed with State of New York Banking Department, arrangements for the co-operation with foreign supervisory authorities have been made formal. Liaison with the foreign supervisors of Slovenian banks has been going on even in the absence of formal memoranda of understanding. On-site examination of the Italian branch of Slovenia's largest bank conducted in 1998 is an example of opening a pipeline with Banca d'Italia even though a formal memorandum of understanding was not signed. The Bank of Slovenia continues to pursue a pro-active stance on formalising relationships with regulatory and supervisory authorities abroad. Currently, efforts are focused on formalising the relationship with the Federal Ministry of Finance and Oesterreichische Nationalbank with regard to subsidiaries of Austrian banks, as well as the branch of an Austrian bank in Slovenia.

The Banking Act has lifted all major barriers to information sharing with foreign supervisory authorities.

The Banking Act has lifted all major barriers to the exchange of information between the Bank of Slovenia and foreign supervisory authorities. Its provisions lay ground for setting up home country control principles, which will be fully implemented with full-fledged membership of the EU. Even before the entry into effect of the Banking Act, the Bank of Slovenia exercised surveillance of branches and subsidiaries of Slovenian banks abroad through controls of prudential reports and other statutory returns.

Since Slovenia is the associated member of the European Union, Slovenia's banking supervisors have attended meetings of the sub-committee for the internal market (previously referred as the sub-committee for financial services within the framework of European Commission). They have also taken part in meetings with missions of the World Bank and the International Monetary Fund, and have met with the representatives of international rating organisations and other visitors from foreign countries.

During the period under review, the Bank Supervision Department continued to participate actively in the conferences organised primarily for banking supervisors from Central and Eastern Europe. Senior offices of the Bank Supervision Department were often lecturers at such expert gatherings.

11. LIAISON WITH EXTERNAL AUDITORS

Financial statements prepared by banks operating in Slovenia as at 31 December 1999 for the previous year were audited by four certified audit companies: PriceWaterhouseCoopers d.d. was appointed by most banks, ITEO - Abeceda d.o.o. audited one bank, Deloitte & Touche, d.o.o. audited three banks, and Ernst & Young made a debut in Slovenia and audited three banks. External audit of all Slovenian savings banks except one was carried out by ITEO - Revizija d.o.o. Ljubljana. One savings bank was audited by PriceWaterhouseCoopers d.d.

No objection from independent auditors on financial statements of all banks and savings banks.

All auditors expressed a positive opinion on financial statements of banks and savings banks, which means that in the opinion of external auditors financial statements of Slovenian banks and savings banks give a true and fair view of financial position, operating results, and cash flow in the preceding year. External auditors have the responsibility for forming and expressing their independent opinion on balance sheet, profit and loss account, and cash flow statement, and the management of the respective bank, i.e. savings bank, are responsible to keep adequate accounting records.

A meeting with auditors is held once a year and banking supervisors and auditors get an opportunity to exchange opinions on audited banks and savings banks and auditors' reports. In cases of serious non-compliance or major deficiencies, i.e. problems, identifed in a particular bank or a savings bank, meetings with auditors are organised several times a year. Contacts between the Bank Supervision Department and auditors with regard to pending professional issues arising from the course of daily business are more frequent.

The Bank Supervision Department participates in the development of audit profession through the Slovenian Institute of Auditing and the Internal Audit Board within the framework the Bank Association of Slovenia. It has a proactive role in addressing open accounting issues and in developing accounting standards through the Accountancy Board within the framework of the Bank Association of Slovenia.

II. RESULTS OF OPERATIONS OF BANKS AND SAVINGS BANKS IN 1999 AND THE FIRST HALF OF 2000[8]

1. BANKING SECTOR STRUCTURE

Consolidation of Slovenia's banking sector under way.

From the record high 33 operating banks in Slovenia at the end of 1994, the number of banks gradually decreased over the following years. At the end of 1998, this figure plunged to 24 following three mergers and one liquidation. There was another merger in 1999, but the number of banks at the end of 1999 in comparison with the end of 1998 actually increased by one on the account of the newly incorporated bank and the first branch of a foreign bank. As at 30 June 2000, the number of banks remained the same in comparison with 31 December 1999.

In 1999 M banka d.d., Ljubljana, was taken over by Banka Koper d.d, while the newly established subsidiary of Hypo Alpe Adria banka d.d., Ljubljana, is the first new bank in Slovenia after five years.

Since the Banking Act, which came into force in February 1999, envisages terms and conditions for the opening of branches of foreign banks in Slovenia, the Bank of Slovenia gave green light in June 1999 for the establishment of the first branch of a foreign bank on the territory of Slovenia. Kaerntner Sparkasse AG, Celovec (Klagenfurt), a branch established in Slovenia, was registered at court in September 1999.

In 1999, two new applications for registration as representative offices of foreign banks in Slovenia were reviewed and approved. Thus at the end of 1999, there were nine representative offices operating in Slovenia.

25 banks, 6 savings banks and 68 savings and loan undertakings operated in Slovenia as at 30 June 2000.

As at 31 December 1999 and 30 June 2000, there were 25 operating banks in the Slovenian banking environment. 4 of them are subsidiaries of foreign banks and one is a branch of a foreign bank. Alongside banks, there were also 6 savings banks and 68 savings and loan undertakings.

The number of savings banks in the first half of 2000 as opposed to the end of 1999 remained the same. As of 1 July 2000, the number of savings banks dropped to 5 as a result of the merger between Mariborska hranilnica-posojilnica d.o.o., Maribor, and Delavska hranilnica d.d., Ljubljana. It is likely that the decrease in the number of savings banks will continue in the second half of 2000 following the decision taken on 30 June 2000 at the general meeting of shareholders of Poteza-Hranilnica d.o.o., Ljubljana, to institute regular (voluntary) liquidation. The winding up will become effective as of the date of entry into the competent court registry. In addition, Hranilnica in posojilnica KGP Kočevske, d.d. is on the point of joining Slovenska zadružna kmetijska banka d.d. Ljubljana.

[8] Figures for the first half of 2000, i.e. as at 30 June 2000, are unaudited.

The number of operating savings and loan undertakings decreased by two in 1999, while the number in the first half 2000 remained unchanged in comparison with the end of 1999.

Market share of savings banks and savings and loan undertakings remains small.

As during the past few years, the market share of savings banks and savings and loan undertakings (measured by total assets) at the end of the first half of 2000 was extremely low in comparison with banks. Namely, it amounted to mere 2.0 per cent (in savings banks it was 0.4 per cent, in savings and loan undertakings 1.6 per cent).

Out of 25 operating banks as at 31 December 1999 and 30 June 2000 there were 10 banks owned by domestic shareholders and 5 are either wholly or majority owned (controlled) by foreign shareholders. The remaining 10 banks were controlled by domestic shareholders; however, the share of foreign owners in 6 banks did not exceed 1 per cent. All savings banks are owned by domestic shareholders and are mostly in private hands.

How well developed a country's banking sector is, may be illustrated by the portion of bank total assets in GDP. At the end of June 2000, total assets of banks amounted to approximately 80 per cent of GDP, while total assets of banks together with savings banks accounted for approximately 81 per cent, and the sum of total assets of banks, savings banks and savings and loan undertakings amounted to approximately 82 per cent of GDP.

Table 4: The number of business units and headcount, banks' total assets in GDP

	31 Dec 1995	31 Dec 1996	31 Dec 1997	31 Dec 1998	31 Dec 1999	30 Jun 2000
Number of business units	558	577	590	557	570	
Number of employees	10,137	10,317	10,410	10,394	10,445	
Total assets (in millions of Tolars)	1,497,544	1,729,083	2,022,037	2,350,359	2,687,600	2,942,709*
Total assets/Number of employees (in millions of Tolars)	147.7	167.6	194.2	226.1	257.3	
GDP at current prices (in millions of Tolars)	2,221,459	2,555,369	2,907,277	3,253,751	3,637,437	3,637,437**
Total assets/GDP (in %)	67.4%	67.7%	69.6%	72.2%	73.9%	80.9%

* Total assets include NLB branch in Italy.
** Assessment of GDP at current prices for the whole 2000 totals 4,099,800 million tolars; however, the calculation presented herein is based on GDP for the year 1999.
Source: Bank of Slovenia

2. OPERATIONS OF BANKS AND SAVINGS BANKS

2.1. Operations of banks

2.1.1. Operations of banks in 1999

Banks increased total assets by almost 6% in real terms by end-1999.

Aggregate **total assets** of Slovenian banks as at 31 December 1999 amounted to 2,687.6 billion tolars (audited figures). With regard to the end of 1998, there was a 14.3 per cent nominal rise, i.e. 5.8 per cent growth in real terms. It means that the trend of moderate growth from the past year continued in 1999.

Table 5: Total assets, growth rates and market shares of seven largest banks

Banks	Total Assets (in millions of Tolars)		Nominal Growth (in %)		Market Share (in %)	
	31 Dec 1998	**31 Dec 1999**	**1998/1997**	**1999/1998**	**31 Dec 1998**	**31 Dec 1999**
NLB	648,595	752,343	18.1	16.0	**27.6**	**28.0**
SKB banka	281,184	307,637	16.7	9.4	**12.0**	**11.4**
NKBM	285,029	321,813	19.9	12.9	**12.1**	**12.0**
Banka Koper	137,190	167,905	14.0	22.4	**5.8**	**6.2**
Banka Celje	135,094	155,712	23.7	15.3	**5.7**	**5.8**
Abanka	123,151	149,301	19.5	21.2	**5.2**	**5.6**
Gorenjska banka	108,041	130,310	19.1	20.6	**4.6**	**4.8**
Total - top 7 banks	1,718,284	1,985,022	18.4	15.5	**73.1**	**73.9**
Total - all banks	**2,350,359**	**2,687,600**	**16.2**	**14.3**	**100.0**	**100.0**
NLB Banking Group	829,543	1,041,409	17.6	25.5	35.3	38.7

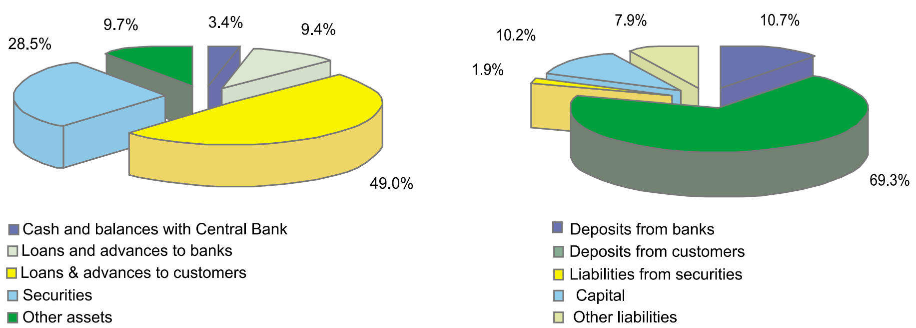
Source: The Bank of Slovenia

In 1999, total assets of almost all banks (20 banks to be exact) increased in nominal and in real terms, while their nominal grow rates ranged from 9.4 to 27.5 per cent. More vigorous growth in total assets, which outpaced growth rates achieved by most banks, was posted by the newly established banks and the branch of the foreign bank. On the other hand, total assets of three banks decreased in real terms.

Market shares of largest banks remain stable.

Over the last six years, the aggregate market share of Slovenia's heavyweight banks measured by unconsolidated total assets remained constant. Since the end of 1994, the market share of the top three banks has been in the range between 51 and 53 per cent of total assets of all banks. The market share held by the five largest banks has been between 62 and 63 per cent, of the seven largest banks between 71 and 74 per cent, and of the top ten banks between 80 and 82 per cent.

Figure 2: Average structure of assets and liabilities of banks as at 31 December 1999



Share of deposits from non-bank sector shrank.

As for the **average structure of total liabilities** in 1999 in comparison with 1998, the share of deposits placed by **non-bank sector** decreased (corporate sector, households, government, other financial institutions, not-for-profit providers of services to households, and non-residents). The decrease from 70 per cent to 69.3 per cent is a result of more sluggish growth in deposits placed by individuals and a decrease in real terms in deposits from the corporate sector, government and non-residents.

That deposits from the corporate sector lost momentum was first obvious in 1997, and the trend continued through 1998 and 1999. The decrease in deposit interest rates in the first quarter of 1999 triggered a fall in nominal terms in deposits from the corporate sector. These deposits did not recover until the end of June 1999 when they reached the level recorded at end of 1998. In the second half of the year 1999, deposits placed by the corporate sector resumed slight growth. In spite of more vigorous growth in the second half of 1999 and the introduction of foreign exchange accounts, overall annual growth remained modest. Namely, these deposits grew in nominal terms by 2.3 per cent, which means a 5.3 per cent decrease in deposits from the corporate sector in real terms.

Deposits from individuals grew by almost 14% in nominal terms in 1999.

In 1999, deposits from households strengthened and accounted for the largest portion of the structure of liabilities to customers other than banks (55.6 per cent deposits placed by non-bank customers, i.e. 38.5 per cent of aggregate total liabilities at the end of 1999). Deposits placed by individuals rose in nominal terms and topped 13.9 per cent, while the same figure over the past years even exceeded a 20 per cent growth. Short-term savings slightly increased in the first quarter and following a slump in April and May, they resumed growth in mid-1999. In the second half of 1999, long-term savings somewhat increased. The maturity structure of funds gathered from individuals deteriorated in 1999 in comparison with 1998 and the share of short-term deposits decreased (from 56.1 per cent at the end of 1998 to 54.1 per cent at the end of 1999). On the other hand, the share of deposits repayable on demand (sight deposits) pencilled in a rise (from 41.8 per cent at the end of 1998 to 42.3 per cent at the end of 1999). Besides, the share of long-term deposits placed by individuals grew from 2.1 per cent to 3.6 per cent mainly in the response of individuals to new forms of long-term savings, such as the national savings scheme for housing purposes.

Foreign exchange deposits from individuals grew by 3.1 per cent in real terms. Namely, savings deposits and short-term time deposits in foreign currency recorded in 1999 a more substantive increase for the first time after 1996. Consequently, the tendency that led to the shrinking of the share of foreign exchange deposits in all deposits placed by individuals slowed down in 1999 after several years of consistent decline. Thus the share of foreign exchange deposits from individuals decreased at the end of 1999 over the end of 1998 by only one percentage point (down to 44.8 per cent at the end of 1999).

In addition to deposits from individuals (citizens), deposits placed by households include deposits from sole traders (entrepreneurs). At the end of 1999, deposits from sole traders accounted for mere 1.8 per cent of deposits from households (as portion of deposits of the non-bank sector). In 1999, deposits of sole traders increased in nominal terms by 34 per cent.

As at 31 December 1999, the structure of other deposits from customers (government, other financial institutions, non-residents, not-for-profit providers of services to households) compared to the figures posted year-on-year, it is obvious that only the share of deposits placed by the government and the share of deposits of non-residents decreased by one percentage point and by a half of the percentage point, respectively. Thus the share of deposits from the government was 11.2 per cent, while the share of deposits of non-residents notched 2.5 per cent at the end of 1999.

Share of deposits from banks increased.

Due to the fall in deposits from customers, banks turned to other banks for **funds** (referred to as **banking sources**). The central bank and foreign banks were important sources of funds for the Slovenian banking sector in 1999 (particulary during summer months) and represented an important stimulus for the growth of the volume of banking operations. The share of deposits from banks grew in the average structure of total liabilities from 9.2 per cent in 1998 to 10.7 per cent in 1999.

The share of liabilities arising from **securities issued** in the average structure of total liabilities at the end of 1999 amounted to 1.9 per cent, and lagged behind the level recorded at the end of 1998 by a half of the percentage point. **Other liabilities** and **capital** maintained a constant share of the average structure of total liabilities (7.9 per cent and 10.2 per cent, respectively).

Table 6: Main items in the balance sheet as at 31 December 1998 and 31 December 1999

	in millions of Tolars			in %	in %
	Amount		Nominal growth		Real growth
	31 Dec 1998	**31 Dec 1999**	**98/97**	**99/98**	**99/98**
Cash and balances with Central Bank	84,696	88,761	14.6	4.8	-3.0%
Loans and advances to banks	227,331	252,615	5.8	11.1	2.9%
Loans and advances to corporate sector	622,200	777,134	25.4	24.9	15.6%
Loans and advances to households	346,016	429,999	29.3	24.3	15.1%
Loans and advances to government	103,799	124,719	50.4	20.2	11.3%
Securities	714,566	708,622	3.6	-0.8	-8.2%
Other assets	251,751	305,750	19.4	21.4	12.5%
Total assets	**2,350,359**	**2,687,600**	**16.2**	**14.3**	5.9%
Deposits from banks	223,738	309,002	9.6	38.1	27.9%
Deposits from corporate sector	386,392	395,257	11.6	2.3	-5.3%
Deposits from households	904,934	1,033,559	20.1	14.2	5.8%
Deposits from government	206,074	208,773	18.4	1.3	-6.2%
Liabilities from securities	57,649	44,755	10.0	-22.4	-28.1%
Other liabilities	315,290	416,973	19.3	32.3	22.5%
Capital	256,281	279,281	12.5	9.0	0.9%
Total liabilities	**2,350,358**	**2,687,600**	**16.2**	**14.3**	5.9%

Source: The Bank of Slovenia

Lending to non-bank sector accounted for almost half of banks' assets.

Turning to the average structure of total assets in 1999, the share of lending to the non-bank sector grew from 44.2 per cent to 49.0 per cent. In the first half of 1999, lending to households enjoyed a vigorous growth, as a result of surging demand of individuals for long-term loans on the eve of the introduction of the value added tax on 1 July 1999. In the second half of 1999, lending to individuals calmed down while short-term borrowing by the corporate sector surged partly spurred by fiscal changes. Nevertheless, growth rates of lending to the corporate sector and individuals in 1999 fell short of the respective figures recorded in 1998. Namely, in 1999 nominal growth rate was 24.9 per cent for corporate and 25.1 per cent for retail lending (1998: 25.4 per cent and 26.6 per cent). Lending activities were buoyant enough and at the end of 1999 in comparison with the end of 1998 both the share of corporate lending and the share of retail lending increased in the average structure of total assets.

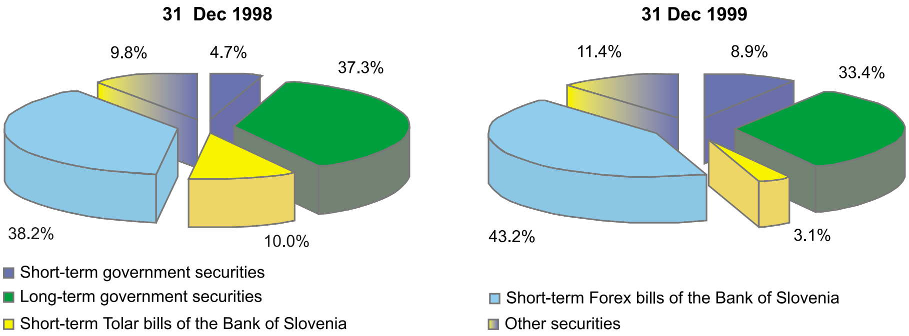
Lending to the government (also referred to as state) accounts for a minor share of loans granted to the non-bank sector. In 1999, these loans preserved a 9 per cent share in lending to the non-bank sector, while due to a rise in short-term lending to other financial institutions, the share of all loans and advances granted to other financial institutions in the structure of lending to the non-bank sector increased from 1.5 per cent at the end of 1998 to 2.4 per cent at the end of 1999.

The share of loans and advances to non-residents in the structure of loans and advances to the non-bank sector was a constant 1.5 per cent share at the end of 1999.

Share of investments in securities dropped at end-1999.

During the past few years, **investments in securities** accounted for over one third of aggregate total assets of banks. At the end of 1999, the share of investments in securities in the average structure of total assets dropped to 28.5 per cent. Bank investments in tolar-denominated bills of the Bank of Slovenia dropped most, but this negative trend was counterbalanced by the rise in the underwriting of foreign currency bills of the Bank of Slovenia.

Figure 3: Structure of bank investments in securities as at 31 December 1998 and 31 December 1999



Source: The Bank of Slovenia

Bills in foreign currency issued by central bank accounted for a lion's share of securities portfolio in all banks.

As at 31 December 1999, foreign currency bills of the Bank of Slovenia accounted for 43.2 per cent of all securities held by banks as opposed to tolar-denominated bills that accounted for mere 3.1 per cent. The share of securities issued by the Republic of Slovenia (government bonds) remained unchanged (42.3 per cent as at 31 December 1999). The share of other securities (bank investments in shares of other banks and other issuers as well as in other securities floated by banks, non-residents, other governments, etc.) grew from 9.8 per cent at the end of 1998 to 11.4 per cent at the end of 1999. The rationale for such a rise mainly lies in more intense underwriting of securities issued by corporate sector towards the end of the year; a move aimed at reducing banks' tax base.

The share of **lending to the banking sector** in the average structure of total assets at the end of 1999 remained practically unchanged with 9.4 per cent with respect to at the end of 1998 when it was 9.3 per cent. During the past few years, the share of **cash in hand and balances with the central bank** has been in the range of 3 per cent, while the share of **other assets** has been around 10 per cent.

Table 7: Maturity structure of deposits from and loans and advances to the non-bank sector

in %

	31 Dec 1998	31 Mar 1999	30 Jun 1999	30 Sept 1999	31 Dec 1999
Demand deposits from non-bank sector	33.3	33.9	37.4	35.4	34.9
Short-term deposits from non-bank sector	57.9	57.7	54.8	56.5	56.7
Long-term deposits from non-bank sector	8.8	8.4	7.8	8.1	8.4
Total deposits from non-bank sector	100.0	100.0	100.0	100.0	100.0
Short-term loans and advances to non-bank sector	57.4	56.4	55.5	56.5	57.2
- Receivables arising from guarantees issued	0.2	0.2	0.2	0.2	0.2
Long-term loans and advances to non-bank sector	42.6	43.6	44.5	43.5	42.8
Total loans and advances to non-bank sector	100.0	100.0	100.0	100.0	100.0

Source: The Bank of Slovenia

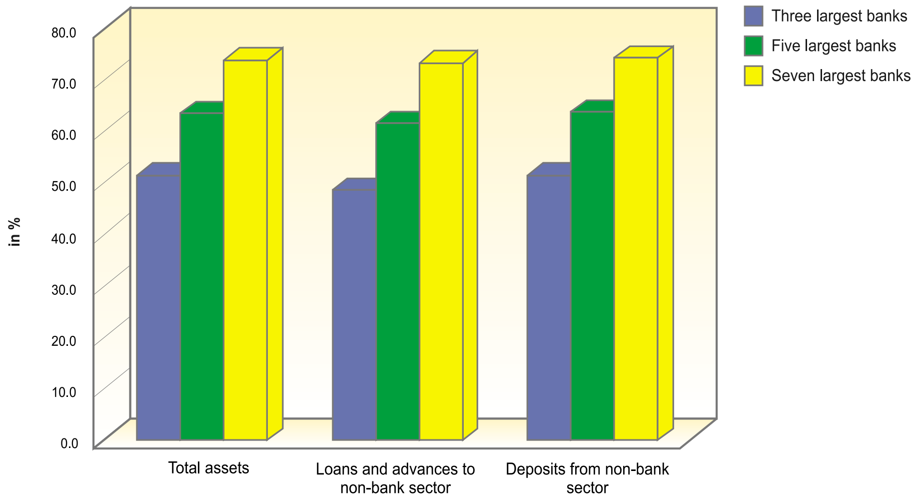
Maturity structure of deposits from non-bank sector improved in second half of 1999.

Maturity structure of deposits placed by the non-bank sector in the first half of 1999 in comparison with the end of 1998 deteriorated due to the increase in demand (often referred to as sight) deposits. The termination of the last interbank agreement on the ceiling put on deposit interest rates was followed by a decrease in interest rates paid on deposit. Furthermore, due to wide-spread anxiety ahead of the introduction of the value added tax, markets were jittery. All these factors led to the impaired quality of savings deposits. In the second half of the year, there was a U-turn and the contractual maturity of deposits placed by the non-bank sector within the framework of short-term funds of the non-bank sector extended (mainly due to a rise in deposits due after 181 days).

In the first half of 1999, the assets side of banks' balance sheets reflected a vigorous growth in long-term lending, predominately driven by strong consumer demand. In the second half of the year, retail lending activities slowed down, and the corporate sector started to borrow more heavily (meaning mostly short-term lending for banks).

The share of **average total liabilities** denominated in foreign currency in average bank total liabilities decreased from 35.8 per cent posted at end of 1997 to 31.5 per cent at the end of 1998, and continued to fall by shedding one percentage point. At the end of 1999, this figure landed at 30.5 per cent. The same trend as observed in the average **share of total assets denominated in foreign currency in aggregate average total assets of banks** that stood at 32.8 per cent at the end of 1997, fell to 30.3 per cent at the end of 1998, and notched 29.6 per cent at the end of 1999. In the first half of 1999, both assets and liabilities denominated in foreign currency grew evenly to be outpaced by the increase in liabilities (also referred to as sources of funds) denominated in foreign currency in the second half of the year. The latter increased by 16.5 per cent during the entire 1999, while assets in foreign currency rose by 16 per cent. Average figures for the year 1999 show that banks had by 3 per cent more liabilities in foreign currency than assets (1998: 4.1 per cent). Consequently, the balance sheet structure of banks did not change significantly, despite unrestricted opening of resident foreign exchange accounts after 1 September 1999.

Figure 4: Share of top three, five and seven banks in total assets, lending to the non-bank sector and deposits from customers as at 31 December 1999



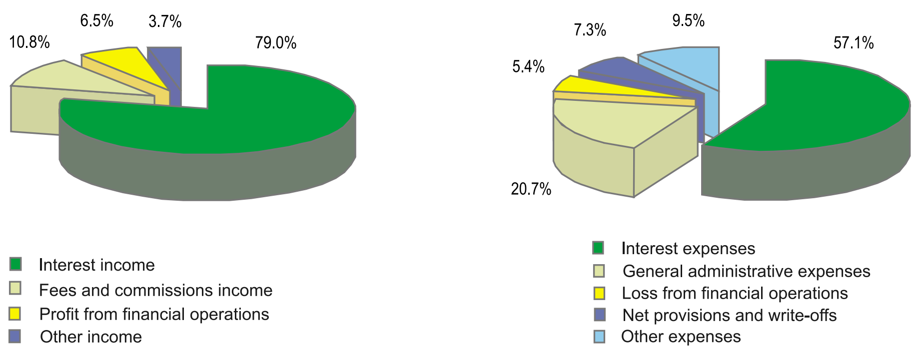
Source: The Bank of Slovenia

Profit generated by banks in 1999 was lower than in 1997 and 1998.

Banks' **profit before taxation** was 20.1 billion tolars in 1999. Net revaluation gain amounted to 25.1 billion tolars. A year-on-year comparison of profit before taxation reveals that profit earned by banks in 1999 was lower by 5.8 billion tolars due to a loss incurred by one of major banks in the amount of 5.5 billion tolars (in 1998, banks' profit before taxation totalled 26.0 billion tolars). Four banks were in red figures at the end of 1999 (in 1998 two banks reported losses).

Profit after taxation in 1999 amounted to 10 billion tolars, as opposed to 16 billion tolars earned in 1998.

Figure 5: Structure of income and expenses of banks in 1999



Source: The Bank of Slovenia

After **net interest income** lost momentum in 1998, the figures posted in 1999 decreased by 2.9 per cent in real terms. On the other hand, banks stated 3.4 per cent real rise in **income from fees and commissions**, mainly due to commissions received from payment transactions effected in the country, commissions for administrative services, and fees earned on lending operations. **Net financial operations** (profit from financial transactions reduced for any loss incurred in the course of financial transactions plus gain on securities) jumped by one third in 1999 over 1998 figures. Such strong growth was made possible mainly by higher gains from securities (income from equity investments made by banks, dividends from dealing securities), and income earned on foreign exchange transactions.

Net interest income dropped in real terms in 1999.

In 1999, banks reported lower extraordinary expenses; hence the item **net other** started to fall in real terms. In addition to extraordinary expenses, this item includes extraordinary income, other income from banking operations, as well as revaluation of capital, fixed assets and equity investments. In addition, the item includes other expenses.

Nominal growth in **gross income** pencilled in by banks in the year 1999 in comparison with 1998 remained unchanged (9.8 per cent). Gross income generated by banks was thinner in the portion attributed by net interest income. On the other hand, due to a slight real increase in income from fees and commissions, gross income remained at the 1998 level in real terms. In line with the trend present over the past years, the composition of gross income in 1999 stable slightly changed. Namely, the decrease in the share of net interest and strengthening of the share of net fees and commissions in gross income continued.

Gross income did not change in real terms.

Table 8: Principal items in adjusted profit and loss account in 1998 and 1999

	in millions of Tolars		in %		in %	
	Amount		Share in gross income		Nominal growth	
	1998	**1999**	**1998**	**1999**	**98/97**	**99/98**
Net interest income	90,153	94,770	74.0	70.8	6.7	5.1
Net fees and commissions	30,206	33,726	24.8	25.2	12.2	11.7
Net financial operations	6,691	9,541	5.5	7.1	-10.3	42.6
Net other	-5,162	-4,183	-4.2	-3.1	-32.5	-19.0
Gross income	**121,888**	**133,854**	**100.0**	**100.0**	**9.6**	**9.8**
Operating expenses	77,106	87,318	63.3	65.2	13.5	13.2
- labour costs	38,343	43,701	31.5	32.6	8.4	14.0
Net income	**44,782**	**46,536**	**36.7**	**34.8**	**3.4**	**3.9**
Net provisions and write-offs	-18,806	-26,401	-15.4	-19.7	-15.4	40.4
Profit before taxation	**25,976**	**20,135**	**21.3**	**15.0**	**23.2**	**-22.5**

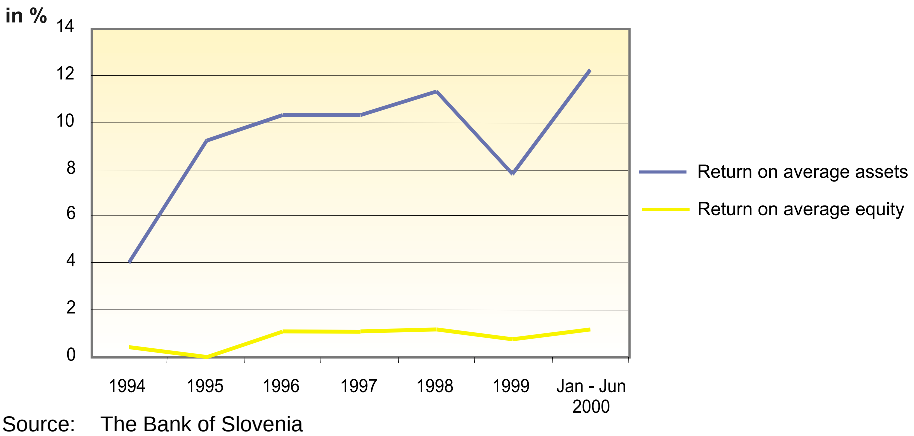
Source: The Bank of Slovenia

Operating expenses, whose nominal growth over the previous years lost momentum, picked up in 1999 in comparison with the year 1998 by 4.8 per cent in real terms. The breakdown of operating expenses in banks shows that **labour costs** grew (in real terms by 5.6 per cent), mostly as a result of swelling expenses for gross wages and salaries, expenses for outcontracted services, expenses for consulting, auditing, accounting as well as other services. The share of gross income earmarked for the coverage of labour costs reached once more one third of gross income (32.6 per cent).

Operating expenses grew by almost 5% in real terms.

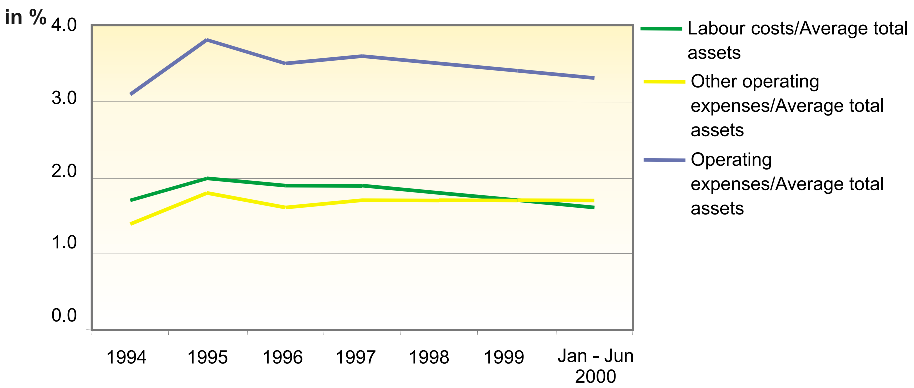
In 1999, banks allocated 26.4 billion tolars to **net provisions** - 7.6 billion tolars more than in the year 1998. The entire increase in net provisions could be attributed to the bank that presented loss at the end of 1999 due to high expenses incurred by making long-term provisions.

Figure 6: Profitability of banks per year



Source: The Bank of Slovenia

Figure 7: Effectiveness of banks per year



Source: The Bank of Slovenia

Interim figures that illustrate ROAA that was in excess of 1 per cent (more specifically, between 1.1 and 1.3 per cent), decreased in December 1999 to 0.8 per cent as a result of additional large provisions earmarked by one of major banks. Similarly, return on average equity (ROAE) that used to be in excess of 10 per cent during the year (between 10.6 per cent and 14.3 per cent) decreased to 7.8 per cent in December 1999.

Operating expenses to average total assets decreased even though operating expenses increased.

Bank efficiency is often measured by using cost-to-assets ratio, i.e. **operating expenses to average assets**[9]. This ratio slightly decreased from 3.5 per cent in 1998 to 3.4 per cent in 1999 due to faster rise in average total assets (in real terms by 7.7 per cent) than the growth rate of operating expenses (in real terms by 4.8 per cent).

Net interest margin, calculated as a ratio between the sum of real and revaluation interest income and average gross interest-bearing assets, after the year 1997 started to slide down and in 1997 amounted to 4.9 per cent, in 1998 it stood at 4.5 per cent, and in 1999 it further decreased by a half of the percentage point to 4.0 per cent. Net interest margin varied enormously from one bank to the other; at the end of 1999, this figure was between 1.3 per cent and 7.3 per cent.

9 Operating expenses include general administrative expenses, depreciation and other expenditures incurred in the course of banking operations (taxes, contributions, subscription/membership fees, etc.).

Interest spread calculated as the difference between average real interest rate charged on loans and advances to and average real interest rate paid on deposits denominted in tolars from the non-bank sector dropped from 3.7 percentage points recorded for the last quarter of 1998, to 3.3 percentage points in the last quarter of 1999.

2.1.2. Operations of banks in the first half of 2000

Real growth in total assets of banks was 4.4% in the first half of 2000.

As at 30 June 2000, aggregate **total assets** of Slovenian banks amounted to 2,928 billion tolars. This figure represents growth in nominal terms by 8.9 per cent in comparison with the end of 1999 (a rise of 240 billion tolars). When consumer price index (CPI) calculated to be 4.3 per cent in the first half of 2000 is taken into account, then total assets increased by 4.4 per cent in real terms.

In 2000, almost all banks (23 banks to be exact) reported a rise in the volume of banking operations both in nominal and in real terms, while above average growth rate during the period under review was posted by 11 banks. Nominal growth rates achieved by these banks ranged between 10.9 and 40.3 per cent, the most intensive growth rate were achieved by two minor banks.

The aggregate **market share** of the three largest banks measured by the size of total assets decreased as at 30 June 2000 in comparison with 31 December 1999 by 1 percentage point to 50.4 per cent. The market share of the seven largest banks also dropped to 73.4 per cent, while the market share of the ten largest banks dropped to 81.9 per cent.

Table 9: Balance-sheet structure and growth rates

in millions of Tolars , in %

	31 Dec 1999		**30 Jun 2000***		**Growth Jun 2000*/Dec 1999**	
	Amount	Share in average assets	Amount	Share in average assets	Nominal	Real
Loans and advances to banks	252,615	9.4	293,165	9.6	16.1	11.3
Loans and advances to customers	1,388,440	49.0	1,500,557	51.1	8.1	3.6
- corporate sector	777,134	27.3	857,452	28.8	10.4	5.8
- households	429,999	15.1	462,087	15.9	7.5	3.0
- government	124,719	4.5	118,563	4.3	-4.9	-8.9
Securities	708,622	28.5	751,148	26.3	6.0	1.6
Other assets	337,923	13.1	382,766	13.0	13.3	8.6
Total assets	**2,687,600**	**100.0**	**2,927,635**	**100.0**	**8.9**	**4.4**
Deposits from banks	309,002	10.7	322,469	11.2	4.4	0.1
Deposits from customers	1,859,009	69.3	2,007,504	68.7	8.0	3.5
- corporate sector	395,257	15.0	398,781	13.9	0.9	-3.3
- households	1,033,559	38.5	1,159,810	39.4	12.2	7.6
- government	208,773	7.8	215,150	7.2	3.1	-1.2
Capital and subordinated liabilities	305,112	10.8	317,951	11.0	4.2	-0.1
Other liabilities	214,477	9.2	279,711	9.1	30.4	25.0
Total liabilities	**2,687,600**	**100.0**	**2,927,635**	**100.0**	**8.9**	**4.4**

* Figures do not include NLB branch in Italy.
Source: The Bank of Slovenia

Deposits from corporate sector continued to decrease.

In real terms decrease in deposits placed by the **corporate sector** and the government during the first six months of the year 2000 was the principle reason for a decrease in deposits from customers. Deposits from customers shrank by 0.6 percentage point to 68.7 per cent of average total liabilities. The unfavourable trend of movements in deposits from the corporate sector also affected the decrease in their share in the average structure of total liabilities (13.9 per cent of average total liabilities). Another look reveals primarily a decrease in deposits denominated in domestic currency, while deposits denominated in foreign currency grew (75.1 per cent growth). The principal source of funds for banks – deposits – are still funds from **households**, which grew faster than total assets. Namely, their share in the structure of total liabilities grew by almost one percentage point and reached a 39.4 per cent portion of average total liabilities. Deposits from the **government** fluctuated considerably from one month to another, and their share in the structure decreased slightly in the first half of 2000. On the other hand, deposit maturity structure improved over the same period mostly owing to deposits with longer maturity.

To make up for the decrease in deposits from customers, banks often resorted to borrowing within the framework of **banking sector**, and the bulk of fresh funds come from borrowing abroad - liabilities to foreign banks. Part of the rise in deposits from banks arises from syndicated loans – a move mostly resorted to by banks owned by domestic shareholders. The banks wholly-owned or controlled by foreign shareholders accounted for the rest. Borrowing from the central bank hit record high in March 2000 when the nominal level of the Bank of Slovenia lending totalled 41,0 billion tolars, and then it started to fall. In the first half of 2000, only few major banks with balance sheet in excess of 100 billion tolars decided to use instruments of the central bank at a larger scale.

In spite of the fact that the volume of **securities issued** in the first half of 2000 has been modest, there are signs that this will change and banks are poised to raise funds by issuing **securities** (primarily long-term registered bonds) and by resorting to **subordinated debt instruments** (as part of supplementary capital - tier II).

Lending to non-bank sector accounted for over one half of average total assets of banks.

Lending to the non-bank sector accounted for the largest portion of **average structure of total assets**. Thus the share of loans and advances to customers at the end of June 2000 jumped from 49 per cent to 51.1 per cent. This increase in the structure of banks' assets was predominately caused by intensive growth in loans and advances granted to the **corporate sector** (in the case of three banks this figure dropped in nominal terms). Growth rate of corporate lending at the end of June 2000 was stronger than growth rate reported for total assets of the system. Thus the share of corporate lending grew by 1.5 percentage points and topped 28.8 per cent of average total assets. Since after lending to **households** slowed down in the second half of 1999, retail lending continued to be "business as usual" in the first six months of 2000. Vigorous activity in retail lending did have an impact on boosting the share of this type of loans in the average structure of total assets (15.9 per cent) due to more intensive long-term lending. There has been an absolute decrease within the framework of lending to the non-bank sector in the case of loans to the **government** (short-term portion). The share of this type of lending dropped to 4.3 per cent of average total assets. The highest lending growth rate within the non-bank sector was reported in the segment of loans and advances to other **financial institutions** (21.2 per cent). On the other hand, the share of lending to other financial institutions in the structure of total assets remained comparatively small (between 1.2 and 1.4 per cent of total assets).

Banks had over 45% of securities in bills of the Bank of Slovenia.

Investments in **securities** in the first half of 2000 accounted for 26.3 per cent of average total assets. Since growth in this segment was rather sluggish, the share of investments in securities at the end of June (in comparison with end-December 1999) was lacklustre – the share decreased by 2.2 percentage points in comparison with December 1999. The bulk of securities portfolio comprised bills of the Bank of Slovenia (more than 45 per cent); however, the downward trend in holdings of tolar-denominated bills of the Bank of Slovenia that started a year ago continued. This trend was counterbalanced by a rise in bills denominated in foreign currency. A look at the structure of securities portfolio reveals that government securities ranked second right after bills of the Bank of Slovenia (between 41.7 per cent and 43.9 per cent). In the first half of 2000, there has been a rather strong increase in government securities (growth topped 9.8 per cent) and this growth was most pronounced in the segment of short-term treasury bills (3-, 6- and 12-month treasury bills). As for securities with long-term maturity periods, bonds issued with the aim to replenish the government budget were most frequent (3-, 5- and 10-year bonds). As regards investments in other securities in the first half of 2000, no significant movements have taken place. However, the share of other securities in securities portfolio was in excess of 10 per cent.

Growth in loans and advances to the **banking sector** in the first half of 2000 outpaced growth rate in total assets of the system (16.1 per cent as opposed to 8.9 per cent), and it affected the increase in the share in average structure of total assets (9.6 per cent). The rise is to be grossly attributed to short-term time deposits in foreign currency abroad.

Table 10: Maturity structure of loans and advances to and deposits from customers

in millions of Tolars, in %

	31 Dec 1999		31 Mar 2000		30 Jun 2000		Growth Jun 2000/Dec 1999	
	Amount	Share	Amount	Share	Amount	Share	Nominal	Real
Short-term loans and advances	794,357	57.2	811,554	56.6	859,192	57.3	8.2	3.7
Long-term loans and advances	594,083	42.8	622,021	43.4	641,364	42.7	8.0	3.5
Total loans and advances	**1,388,440**	**100.0**	**1,433,575**	**100.0**	**1,500,557**	**100.0**	**8.1**	**3.6**
Demand deposits	648,265	34.9	654,805	34.0	699,423	34.8	7.9	3.4
Short-term deposits	1,055,074	56.7	1,099,036	57.0	1,127,404	56.2	6.9	2.5
Long-term deposits	155,669	8.4	172,923	9.0	180,677	9.0	16.1	11.3
Total deposits	**1,859,008**	**100.0**	**1,926,764**	**100.0**	**2,007,504**	**100.0**	**8.0**	**3.5**

Source: The Bank of Slovenia

Maturity structure of sources of funds improved at the start of 2000.

The maturity structure of liabilities (sources of funds) to the non-bank sector over the first six months of 2000 improved owing to a higher share of long-term deposits and deposits repayable in more than 90 days. As for the rise in long-term deposits, the most significant contribution was made by deposits placed by individuals, deposits from the corporate sector followed suit, and the same was reported for deposits from the government and other financial institutions. Due to a slow down in growth of short-term deposits in comparison with the entire non-bank sector, their share at the end of June 2000 was somewhat below the level recorded at the end of 1999. Nevertheless, the maturity structure within short-term deposits was better with longer maturity owing to a rise in deposits with maturity over 181 days. The fact that deposits decreased in absolute terms at the end of June 2000 over December 1999 in the non-bank sector was most evident in the case of short-term deposits repayable within 30 days. On the assets side, there were no major changes with regard to the **maturity structure of loans and advances** to the non-bank sector in the first half of the year 2000. Maturity mismatch, i.e. exceeding long-term sources with short-term ones was rather stable and was in the range of one third. The breakdown of individual sectors shows that the trend, which started in 1999 persisted in the first half of 2000. Namely, the corporate sector was keen to obtain short-term financing, while the retail sector (households) showed more interest in obtaining long-term lending.

Shares of average foreign exchange assets and liabilities started to increase.

Both **assets and liabilities denominated in foreign currency** outpaced assets and liabilities in domestic currency in the first half of 2000. The share of **average foreign exchange liabilities**, which was falling during the previous reporting period, grew in the first half of 2000 to 31.9 per cent of average total liabilities. Deposits placed by individuals did most in absolute terms to increase this figure. Retail deposits were followed by deposits from the corporate sector, while deposits from non-residents, from the banking sector and subordinated liabilities lagged behind and had lesser influence. Also the share of **average foreign exchange assets** grew at the end of June 2000 to 30.8 per cent of average total assets. The rise of these items was attributable to a surge in short-term time deposits placed with the banking sector, followed by investments in securities issued by the Bank of Slovenia, and lending to the corporate sector.

Table 11: Principal items in adjusted profit and loss account of banks and the structure in % of gross income

in millions of Tolars, in %

	Jan - Jun 1999		Jan - Jun 2000		Growth Jun 2000/Jun 1999	
	Amount	Share in gross income	Amount	Share in gross income	Nominal	Real
Net interest income	44,092	70.4	59,217	77.4	34.3	22.4
Net fees and commissions	16,761	26.7	18,280	23.9	9.1	-0.6
Net financial operations	3,054	4.9	2,033	2.7	-33.4	-39.3
Net other	-1,282	-2.0	-3,034	-4.0	136.7	115.7
Gross income	**62,626**	**100.0**	**76,497**	**100.0**	**22.1**	**11.3**
Operating expenses	41,420	66.1	45,543	59.5	10.0	0.2
- labour costs	20,958	33.5	22,645	29.6	8.0	-1.5
Net income	21,205	33.9	30,954	40.5	46.0	33.1
Net provisions and write-offs	-7,776	12.4	-14,288	18.7	83.7	67.5
Profit before taxation	**13,430**	**21.4**	**16,666**	**21.8**	**24.1**	**13.1**

Source: The Bank of Slovenia

Profit generated by banks in the first half of 2000 exceeded figures for the same period in 1999.

Profit of all banks in the first half of 2000 amounted to 16.7 billion tolars (net revaluation in the amount of 19.2 billion tolars). This figure is by 24.1 per cent, i.e. by 3.2 billion tolars higher than in the same period in 1999. With the exception of three minor banks, all banks made profit in the first half of 2000. Gross income in the amount of 76.5 billion tolars was at half-year higher by 13.9 billion tolars, i.e. rose by 22.1 per cent. These strong figures were generated mostly by **net interest income**, which in turn was a consequence of significantly higher consumer prices in the first half of 2000 as opposed to the same period of 1999. Consequently, the share of interest income as a percentage of total income grew to 80.3 per cent, **net interest margin** over a year's period increased from 4.0 per cent to 4.6 per cent. Somewhat lower was the performance reported by banks in the segment of **net financial operations** during the first six months of 2000 due to unfavourable movements in the capital market, banks had to deduct higher expenses in relation to valuation of securities. The ratio between growth rates in gross income and operating expenses remains favourable, i.e. **operating expenses**

in the first half of 2000 increased at the pace lagging behind gross income growth. Consequently, in the first half of 2000 a smaller portion of gross income was earmarked for the coverage of operating expenses. During the first half of 2000 operating expenses to average assets decreased from 3.4 per cent to 3.3 per cent, even though this more favourable indicator is primarily a result of stronger growth in average total assets and not a result of falling operating expenses. In comparison with interim figures for 1999, banks in the first half of 2000 made by 6.5 billion tolars more **net provisions** and for this purpose they allocated 18.7 per cent of gross income. ROAA and ROAE in the first half of 2000 was higher than over the same period of 1999. In addition to three banks that reported losses, below ROAA (below 1.2 per cent) was posted by 11 banks; on average, ROAA was in the range between 0.3 per cent and 3.0 per cent.

Table 12: Key banking ratios

in %

	Jan - Jun 1999	Jan - Dec 1999	Jan - Jun 2000
Return on average assets	1.11	0.79	1.19
Return on average equity	10.90	7.80	12.20
Net interest margin	4.00	4.00	4.60
Operating expenses/Average total assets	3.40	3.40	3.30

Source: The Bank of Slovenia

2.2. Operations of savings banks

2.2.1. Operations of savings banks in 1999

Aggregate assets of operating six savings banks at the end of 1999 amounted to 11.0 billion tolars. In comparison with 1998 figures when aggregate total assets of all savings banks grew in real terms, in the course of 1999 total assets of two savings banks decreased in real terms. Growth in aggregate total assets of operating savings banks slowed down (16 per cent growth in nominal terms, i.e. 7.4 per cent growth in real terms) and converged with growth in total assets of banks. At the same time, savings banks maintained a modest share of the Slovenian banking environment: the two largest savings banks accounted for over one half (55 per cent), and the three largest savings banks accounted for a 74.1 per cent share of the market covered by all savings banks.

There are considerable differences between savings banks.

There are considerable differences between savings banks both in terms of size and balance-sheet structure. As opposed to banks where deposits placed by the corporate sector shrank in real terms in 1999, corporate deposits placed with savings banks grew strongly; hence the average share of deposits from the corporate sector in the average structure of total liabilities grew by six percentage points (to 22.4 per cent) by the end of 1999. Fast growth of deposits from the corporate sector was followed by a strong rise in deposits from households due to the increase in deposits from individuals (growth of 45 per cent in real terms). Deposits from households represented second significant source of funds (liabilities) in the structure of total liabilities by accounting for 22 per cent of average total liabilities at the end of 1999. The share of deposits from the banking sector in the average structure of total liabilities ranged below 10 per cent throughout 1999.

For savings banks households sector is the most important on the assets side.

Funds gathered by savings banks were mostly channelled to loans and advances granted to households (mostly to individuals). Loans and advances to households increased by 20.2 per cent over 1999 in real terms). Thus loans to households at the end of 1999 accounted for over two thirds of total assets. On the other hand, the share of lending to the banking sector and the share of lending to the corporate sector shrank in 1999: at the end of 1999 loans and advances to banks were below 9 per cent, while corporate lending was below 11 per cent in the average structure of total assets. Four savings banks invested in bills of the Bank of Slovenia every month in 1999; nonetheless, the share of these investments in 1999 in comparison with their share at the end of 1998 was cut by half (to 1.5 per cent of total assets).

Due to the high level of long-term lending to individuals, the share of long-term loans and advances reported by savings banks at the end of 1999 rose to a half of all loans and advances to the non-bank sector (to a 49.7 per cent share of lending to the non-bank sector).

In 1999, in relation to gathered funds, the maturity structure of deposits from customers improved. The portion of demand (sight) deposits was lower in savings banks than in banks in the past as well, but it went down further and landed at 4.3 per cent of deposits from customers, while the share of long-term deposits grew to 21.2 per cent of all deposits from customers at the end of 1999.

All savings banks had profit in 1999.

In 1999, **all savings banks reported profit**. Thus profit earned by all savings banks before taxes amounted to 181.5 million tolars, while profit after taxes amounted to 141 million tolars. Profit before taxes was in 1999 by 141.4 million tolars higher than in 1998. Savings banks managed in 1999 to preserve the amount of gross income in real terms (real rise was 1.5 per cent) mainly due to a rise in net fees and commissions (in real terms it grew by 4.2 per cent), while earnings from net interest income in real terms was at the level for net interest income in 1998. This stronger operating result in 1999 is attributable to lower amounts set aside for net provisions in 1999 (49.6 million tolars) with respect to 1998 (172.2 million tolars), while one savings bank in 1999 released more provisions than it had made. Profitability deteriorated in most savings banks at the end of 1999: ROAA of individual savings banks amounted at the end of 1999 between 0.4 per cent and 2.4 per cent, and averaged 1.7 per cent.

As a result of curbed growth in operating expenses incurred by savings banks (real growth of 1.8 per cent) and more moderate growth in labour costs (real growth of 2.8 per cent), in 1999 the ratio between operating expenses and average total assets dropped (5.0 per cent) and the ratio between labour costs and average total assets also fell (2.4 per cent). Despite some encouraging signs, these ratios still exceed the comparable figures posted by banks (3.4 per cent and 1.7 per cent, respectively).

Net interest margins earned by savings banks were thinner.

Net interest margin in savings banks continued to fall and in 1999 it decreased in comparison with 1998 by a half of the percentage point (down to 5.1 per cent). Nevertheless, this figure still exceeded net interest margin earned by banks (4.0 per cent).

In comparison with banks, savings banks paid and charged deposit and lending interest rates in excess of industry-wide figures, although there is a downward trend. In the last quarter 1999, real lending interest rate charged by savings banks was 8.3 per cent as opposed to 5.8 per cent charged by banks, real deposit interest rate paid by savings banks was 4 per cent (banks 2.5 per cent). Due to the difference between lending interest rates charged by savings banks and comparable interest rates charged by banks, interest spread earned by savings banks of 4.3 percentage points exceeds interest spread in banks (3.3 percentage points).

2.2.2. Operations of savings banks in the first half of 2000

Aggregate **total assets** of savings banks as at 30 June 2000 amounted to 12.0 billion tolars, and this figure represented an 8.8 per cent nominal rise, i.e. a rise by 969 million tolars[10] in comparison with the end of 1999. The **market share** held by savings banks in the entire banking sector still remained modest (0.4 per cent), the two largest savings banks held a 55.4 per cent market share in aggregate total assets of savings banks.

A comparison between the **structure of liabilities** (sources of funds) with the situation in 1999 indicates that the share of deposits from households increased to 26.2 per cent of average total liabilities. Therefore, retail deposits once again represented the most significant sources of funds, while the share of deposits from the corporate sector, which in 1999 grew strongly, over the first half-year of 2000 slightly decreased to 21.4 per cent. On the other hand, the share of deposits from the banking sector remained practically unchanged (9.7 per cent of average total liabilities). Not-for-profit providers of services to households accounted for a hefty portion of liabilities (sources of funds) in savings banks with a share in total liabilities of just above 19 per cent.

During the first six months of 2000, **lending** to households was intense (growth in retail lending of 22.4 per cent); hence the share of retail lending in the average structure of total assets rose to 73 per cent. The trend of falling loans and advance to the banking and corporate sector experienced in 1999 continued also in the first half of 2000 with shares in the average structure of total assets below 10 per cent. The share of investments in securities in the average structure of total assets of savings banks was relatively small, and it decreased further in the first half of 2000 to 2 per cent. Two savings banks opted for intensive channelling of their assets in government securities, while investments in securities of the central bank decreased.

As for gathered funds, the **maturity structure** of deposits from customers improved; a fall in the share of short-term deposits (72.6 per cent) was compensated by an increase in the portion of long-term deposits that rose to 23.2 per cent of all deposits from customers. Due to strong long-term lending to households, the share of long-term loans soared to over a half of all loans to the non-bank sector.

In the first half of 2000, all savings banks operated with **profit** and together generated 99.8 million tolars in profit. This figure is by 32 per cent lower than the figure posted at mid-1999. Unlike net interest earned by banks, **net interest income** earned by savings banks in the first half of 2000 were lower even in nominal terms than a year before, while more favourable results were posted in the **net fees and commissions** item (fees and commissions earned

10 As at 30 June 2000, there were 6 operating savings banks. The smallest savings bank has been excluded from information given herein since as at 30 April 2000 it transferred all its operations to one of the banks, and on 30 June 2000 it passed a Decision to institute voluntary winding up (liquidation) and is waiting for the competent court to make entry into the register.

Return on average assets in savings banks remained at the level of 1999.

on lending operations). As opposed to 1999, savings banks made additional provisions in the first half of 2000 in the amount of 31 million tolars (a 7.9 per cent share of their gross income). Growth in **operating expenses** was less vigorous in comparison with average assets and had an impact on achieving a more favourable ratio (annual decrease from 5.0 per cent to 4.5 per cent). In the case of net interest margin, the downward trend continued and in a year's time plunged from 5.4 per cent to 4.4 per cent. With 1.7 per cent, ROAA remained at the level of the year 1999.

3. CREDIT RISK

For banks operating in Slovenia, credit risk is generally recognised as the most significant exposure. Since 30 June 1999, banks disclose credit risk in line with the criteria laid down in the Decree on the Classification of On- and Off-Balance Sheet Items of Banks and Savings Banks (Official Gazette of the Republic of Slovenia, No. 32/99). The said Decree supersedes the Decree of the same description enacted in December 1996 and amended in July 1998. The requirements laid down in the new Decree do not differ significantly from the provisions contained in the »old« one.

After the entry into force of the Banking Act, the Decree on Large Exposure of Banks and Savings Banks (Official Gazette of the Republic of Slovenia, No. 32/99), was issued. Large exposure means exposure banks or savings banks to a client, which adds up to or exceeds 10 per cent of the bank's capital[11]. The sum of all large exposure shall not exceed 800 per cent of capital, while maximum exposure to a single client shall not exceed 25 per cent of the bank's capital. Aggregate large exposure was in each bank considerably below statutory requirements, while only four banks reported positions where 25 per cent limit on exposure to groups of related counterparties occured as at 30 June 2000. Three banks reported positions where the 20 per cent limit on exposure to connected counterparties occurred (counterparties, which are directly or indirectly controlled by bank, i.e. counterparties which are connected with reporting bank by being parent undertaking indirectly or directly).

Banks calculate credit risk on the basis of claims classified in groups graded from A to E.

Banks assess credit risk in line with criteria for the classification of claims in groups (also reffered to as categories) that range from A to E[12]. These criteria effective from the end of 1992 when only past-due amounts were taken into account, became more stringent in 1993 and remained in force without modifications until the end of 1996. As from 1 January 1997, more comprehensive criteria started to apply. The methodology that was used between 1993 and 1996 was built upon creditworthiness of clients (counterparties). Nevertheless, it was allowed under certain circumstances to classify assets collateralised by pledging moveable and immovable property in the best class - group A - irrespective of the borrower's creditworthiness. As from January 1997, claims collateralised by pledging property may be ranked only one group higher than the ranking based on the assessment of the borrower's creditworthiness would have been. In order to mitigate the effect of these more stringent criteria on loan portfolios of banks and savings banks, a gradual approach (phasing in) was adopted to give them some breathing space. Thus banks and savings banks were allowed time to comply with the requirement for earmarking additional provisions by the end of 1997.

11 In the 1999 Banking Act reffered to as own funds.

12 A = standard, B = watch, C = substandard, D = doubtful, E = loss.

In spite of gloomy prospects, loan portfolios did not deteriorate at the end of 1997. A number of banks had taken appropriate steps to implement more stringent classification criteria ahead of the effectiveness of the relevant Decree. Namely, banks and savings banks started to classify claims on their respective counterparties exclusively on the basis of the assessment of their creditworthiness (despite the fact that collateral came in all kinds and forms), and the share of bills issued by the Bank of Slovenia increased (bills of the Bank of Slovenia are classified in group A).

Share of performing assets was approximately 95%.

Over the last four years, the quality of loan portfolio of banks has not changed significantly. The share of performing assets (claims classified in groups A and B) has ranged between 94 and 95 per cent over the past years (the share of non-performing assets has been between 5 and 6 per cent), while the share of bad assets (claims classified in D and E groups) has been between 3 and 4 per cent.

At the end of 1999, performing assets of banks (including on- and off- balance sheet items) amounted to slightly higher figure than a year before - 94.8 per cent (0.2 percentage point more than at the end of 1998) and did not change until the end of June 2000. This increase was balanced by a decrease in the share of non-performing assets (groups C, D and E), which dropped by 0.2 percentage point from 5.4 per cent to 5.2 per cent.

Table 13: Classification of on- and off-balance sheet items in banks

in %

Group	31 Dec 1993	31 Dec 1994	31 Dec 1995	31 Dec 1996	31 Dec 1997	31 Dec 1998	31 Dec 1999	30 Jun 2000
A	81.1	86.1	89.4	89.5	90.1	89.6	88.5	88.2
B	6.6	5.7	4.8	4.2	4.4	5.0	6.3	6.6
C	4.7	2.5	1.9	2.4	2.3	2.1	2.0	2.2
D	3.2	2.6	2.1	2.2	1.8	1.8	1.5	1.4
E	4.3	3.1	1.8	1.6	1.4	1.5	1.7	1.6

Source: The Bank of Slovenia

Table 13a: Classification of clients without taking into consideration first-class and other eligible collateral

in millions of Tolars, in %

Group	31 Dec 1997		31 Dec 1998		31 Dec 1999		30 Jun 2000	
	Net exposure	Share	Net exposure	Share	Net exposure	Share	Net exposure	Share
A	1,945,493	84.8	2,158,695	79.2	2,550,830	82.0	2,597,148	76.2
B	170,301	7.4	306,372	11.2	344,322	11.1	386,082	11.3
C	72,320	3.2	110,956	4.1	79,535	2.6	187,601	5.5
D	55,694	2.4	67,945	2.5	64,516	2.1	140,551	4.1
E	50,173	2.2	83,010	3.0	70,477	23.0	97,282	2.9
Total	**2,293,981**	**100**	**2,726,979**	**100**	**3,109,680**	**100**	**3,408,664**	**100**

Source: The Bank of Slovenia

If collateral was excluded, the share of performing assets would be 87.5%.

If only the criterion of creditworthiness assessed for the respective counterparty was to be taken into account (without taking into account various forms of collateral that could improve the classification) then as at 30 June 2000, 76.2 per cent of claims was classified in group A (5.8 percentage points less than as at 31 December 1999). If different forms of collateral are taken into account, the share of standard claims (group A) is higher by 12 percentage points. 11.3 per cent of claims got a place in group B (0.3 percentage points more than at the end of 1999), and 12.5 per cent were non-performing assets (groups C, D and E - 5.5 percentage points more than at the end of 1999).

Net aggregate (on- and off-balance sheet) exposure to credit risk as at 31 December 1999 amounted to 3,109.7 billion tolars, as at 30 June 2000 this figure was 3,408.7 billion tolars, which represents 9.6 per cent nominal growth with respect to the end of 1999.

Together with suspended income, exposure as at 31 December 1999 amounted to 3,168.8 billion tolars (2,600.2 billion tolars in risk-adjusted on-balance sheet assets and 568.5 billion tolars in risk-adjusted off-balance sheet items), as at 30 June 2000 this figure was 3,475.2 billion tolars (2,842.3 billion tolars in risk-adjusted on-balance sheet assets and 633 billion tolars in risk-adjusted off-balance sheet items).

The highest growth rate for net aggregate exposure in 1999 was reported in groups B in E (in nominal terms this rise was by 43.2 per cent and 26.3 per cent, respectively, while the average rise was 14 per cent); in the first half of 2000, assets classified in groups C and B grew most vigorously (by 19.9 per cent and 14.2 per cent, respectively).

Value adjustments and provisions made exceeded prudential requirements.

In 1999, the volume of adjustments and provisions also increased, and at the end of 1999 notched a 30.5 per cent rise over the end of 1998. The scope of adjustments and provisions grew in the second half of 1999 due to the increase in adjustments and provisions made for claims classified in group A as a result of the effectiveness of the Decree on Establishing Specific Provisions of Banks and Savings Banks (Official Gazette of the Republic of Slovenia No. 32/99). Under this Decree, general provisions made for claims classified in group A (pursuant to the 1993 Decree on the Amount and Manner of Establishment of Provisions for Potential Losses of Banks and Savings Banks) under the new Decree shall be included in specific provisions for credit (and country) risk. The volume of adjustments and provisions made as at 30 June 2000 with regard to 31 December 1999 increased by 9.4 per cent. The volume of adjustments and provisions made is still in the excess of mandatory limits.

Table 14: Review of bank exposure per groups and adjustments and provisions

in millions of Tolars

Group	Aggregate Exposure	Adjustments, Provisions	Aggregate Exposure	Adjustments, Provisions	Aggregate Exposure	Adjustments, Provisions	Aggregate Exposure	Adjustments, Provisions
	31 Dec 1997		31 Dec 1998		31 Dec 1999*		30 Jun 2000*	
A	2,067,463	1,325	2,442,371	683	2,751,937	16,790	3,006,665	19,483
B	100,241	11,772	137,094	15,613	196,315	22,479	224,225	24,995
C	53,040	17,386	56,335	16,780	63,123	18,553	75,710	22,385
D	40,352	27,925	50,155	30,774	46,511	27,225	47,358	28,190
E	32,885	32,877	41,023	41,035	51,794	51,789	54,706	54,647
TOTAL	2,293,981	91,285	2,726,979	104,885	3,109,680	136,835	3,408,664	149,700

* Including specific provisions for claims classified in group A
Source: The Bank of Slovenia

The share of bad and doubtful assets in gross total assets grew as at 31 December 1999 as opposed to 31 December 1998 (from 10.9 per cent to 11.6 per cent). The same happened with the share of value adjustments in gross total assets of banks (from 6.1 per cent to 6.3 per cent). As at 30 June 2000, both the share of bad and doubtful assets in gross total assets and the share of value adjustments in gross total assets grew slightly (to 11.9 per cent and 6.4 per cent, respectively). The coverage of bad and doubtful assets by value adjustments as at 31 December 1999 in comparison with 31 December 1998 fell by 1.5 percentage points and notched 54.6 per cent, and by the end of June 2000 in comparison with the end of 1999 it shaded additional 0.5 percentage point. On the whole, bad and doubtful assets were well secured in line with the principles of safe and sound banking operations.

Bad and doubtful assets were sufficiently covered with revenue.

The volume of bad and doubtful on-balance sheet assets of banks grew faster in 1999 than the aggregate volume of banking operations. Between 31 December 1998 and 31 December 1999, growth rate reported for bad and doubtful on-balance sheet assets was 22.5 per cent, while growth rate of the volume of banking operations was 14.4 per cent. In the first half of 2000, bad and doubtful on-balance sheet assets increased by 11.6 per cent, while the volume of banking operations grew by 8.9 per cent.

The structure of aggregate on- and off-balance sheet exposure of banks per type of activity at the end of June 2000 did not undergo major changes in comparison with the end of 1999. The bulk of assets was still invested in financial intermediation[13] (15.9 per cent), despite the fact that their share in gross aggregate exposure decreased over the last two years and a half (at the end of 1998, it stood at 18.2 per cent, at mid-year 1999 it was 17.5 per cent, and at the end of 1999 it was only 15.8 per cent). Lending to processing industries took the second place with 13.5 per cent of gross aggregate exposure (the said share has remained unchanged over the past few years and has been in the region of 14 per cent). The breakdown of processing industries shows that most borrowers came from chemical and metal- processing industry, as well as machine building. Exposure to public administration[14], defence and compulsory social security ranked third and at mid-2000 accounted for 12.8 per cent of all assets at the end of June 2000. Loans and advances to borrowers classified as trade and repair of motor vehicles stood at 11.2 per cent (this share has been growing for six years in a row), loans and advances to borrowers classified as real estate and business services followed suit (5.3 per cent), lending to borrowers in transport, warehousing and communications came next with 4.9 per cent, etc.

Approximately three fourths of all lending (74.3 per cent) comprised amounts due from corporate customers and sole traders (entrepreneurs), followed by amounts due from individuals (citizens) with 14.7 per cent, while amounts due from non-residents as at 30 June 2000 accounted for 11 per cent of all on- and off-balance sheet exposure.

Three quarters of all exposure of banks was in companies and sole traders.

Over the last two years, the share of performing assets of savings banks ranged between 94 in 95 per cent (balances as at year-end), while non-performing assets ranged between 5 and 6 per cent. The only significant year-on-year change in 1999 was a rise in the share of assets classified in group A, while assets in group B shrank. At the same time, the respective shares of assets classified in groups C in D decreased, while assets classified in group E increased. At the end of June 2000, as much as 92.6 per cent of all classified

13 Activities classified as financial intermediation also comprise claims on the Bank of Slovenia, which as at 31 December 1999 accounted for 61.7 per cent (30 June 2000: 60.4 per cent) of aggregate exposure associated with financial intermediation.

14 This group comprises government securities.

on-balance sheet assets and off-balance sheet items was classified in group A (the trend of assets rising in group A has continued since 1996, while the portion of assets classified in group B has been decreasing). At the end of 1999, savings banks resorted for the first time to the classification of assets that takes into account different kinds of collateral and the asset classification on the basis of creditworthiness. Until the end of 1998, as opposed to banks, savings banks took into account only the criterion of creditworthiness of their clients. More stringent criteria applicable to the classification of assets from 1997 did not impair the quality of loan portfolio of savings banks over a two years' time.

Savings banks started to classify loans and advances by taking into account collateral.

Table 15: Classification of on- and off-balance sheet items of savings banks

in %

Group	31 Dec 1993	31 Dec 1994	31 Dec 1995	31 Dec 1996	31 Dec 1997	31 Dec 1998	31 Dec 1999	30 Jun 2000
A	89.8	91.6	86.2	85.8	88.7	88.6	91.4	92.6
B	5.9	4.1	7.2	6.3	6.5	5.5	3.9	2.9
C	1.0	2.2	3.4	3.7	1.3	1.8	1.3	1.5
D	0.3	0.5	1.3	2.3	1.8	2.3	1.0	0.7
E	3.0	1.6	1.9	1.9	1.7	1.9	2.3	2.3

Source: The Bank of Slovenia

Net total exposure of savings banks, which as at 31 December 1999 amounted to 10.4 billion tolars (when suspended income is included, this figure was 10.6 billion tolars) with respect to 31 December 1998 increased by 13.6 per cent in nominal terms; by the end of June 2000, net aggregate exposure rose further by 10.9 per cent to 11.5 billion tolars.

The volume of adjustments and provisions made by savings banks in 1999 grew by 18.8 per cent, in the first six months of 2000 by 6.7 per cent.

4. COUNTRY RISK

In accordance with the Decree on the Classification of On- and Off-balance Sheet Items of Banks and Savings Banks (Official Gazette of the Republic of Slovenia, No. 32/99), banks are obliged to include country risk in amounts due from non-residents. Country risk has been defined as exposure to potential losses associated with the borrower's country. Banks must make provisions to act as a buffer against this kind of exposure at least in the amount stipulated by the Bank of Slovenia on the basis of risk assessments made for designated countries.

Banks are not required to make provisions against potential losses due to country risk for the following:

1. Claims on non-residents with contractual maturity up to 6 months,
2. Claims on branches of investment-grade foreign banks[15],
3. Claims secured with standard (first-class) collateral[16], and
4. Claims collateralised with joint and several guarantee issued by a blue-chip domestic counterparty.

Exposure to non-residents was 10.5% of aggregate exposure.

Aggregate exposure of banks to non-residents counterparties has been growing slightly since the year 1997 and as at 30 June 2000 it amounted to 364.1 billion tolars. It was the first time that it exceeded the record high achieved in 1996¸ when this type of exposure amounted to 318.7 billion tolars. Gross aggregate exposure to non-residents (on-balance sheet and off-balance sheet items) increased as at 30 June 2000 in comparison with 31 December 1999 by 25.1 per cent and accounted for 10.5 per cent of aggregate on- and off-balance sheet exposure of banks (3,475.2 billion tolars as at 30 June 2000).

Largest exposure was to counterparties from the EU.

Banks are most exposed to counterparties from the European Union. As at 30 June 2000, as much as 76.7 per cent of aggregate exposure to non-residents represented exposure to counterparties from the European Union (279.2 billion tolars). Growth rate of exposure to counterparties from the EU was by the end of June 2000 at the level much higher than the entire growth rate in 1999 (28 per cent in comparison with 5.7 per cent growth in nominal terms in 1999). The growth exposure do counterparties from the EU has been increasing over the years, while banks were most exposed to counterparties from Germany, Austria, Great Britain, France, and Italy.

Exposure to counterparties from the republics of former Yugoslavia stated as at 30 June 2000 was below the average growth rate of aggregate exposure to non-residents (with respect to 31 December 1999), and it amounted to mere 8.8 per cent (average growth was 25.1 per cent). The opposite trend was obvious in the case of counterparties from the EFTA countries – following the last year's 20 per cent drop in exposure to this segment, this year's exposure has increased by 33.6 per cent (exposure to counterparties from Switzerland heads the list).

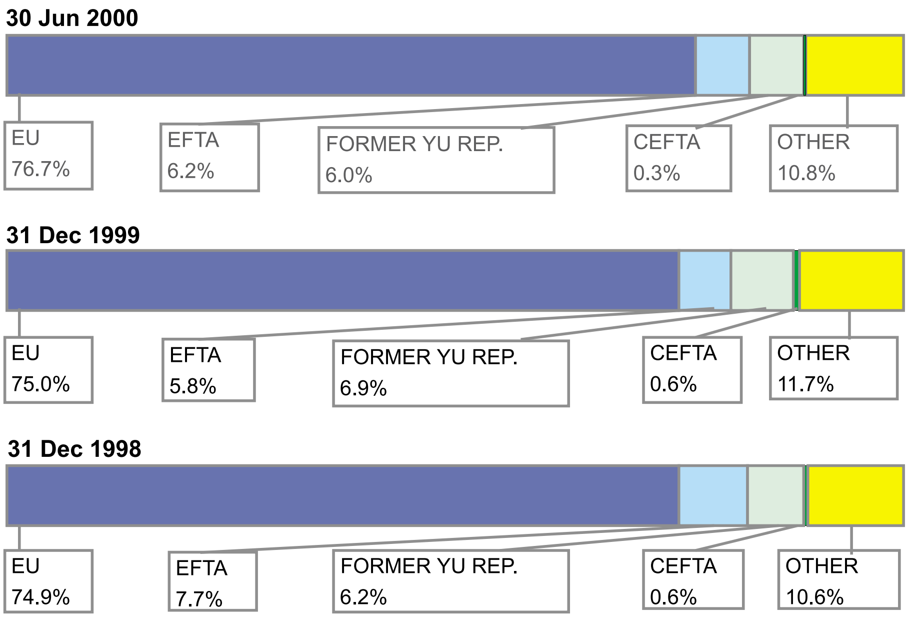
[15] Investment-grade refers to ratings awarded by Moody's (Baa3 or better), Standard & Poor's, Fitch, Thomson Financial BankWatch (BBB- or better).

[16] First-class collateral comprises bank deposits, readinly available for settlement of claims, securities issued by the Republic of Slovenia, the Bank of Slovenia, EEA countries and comparable OECD countries, and irrevocable guarantees payable on first demand issued by authorised local and foreign investment-grade banks, and gilt-edged debt securities issued by banks tradeable in financial markets (excluding subordinated and negotable securities) and irrevocable guarantee of the Slovene Export Corporation and the Republic of Slovenia.

Exposure to counterparties from the CEFTA countries has been decreasing and at the end of June 2000 it dropped below the level stated at the end of 1997.

As for the exposure of Slovenian banks to other countries at the end of June 2000, the bulk of exposure was to counterparties from the USA (32.9 billion tolars or 9 per cent of aggregate exposure to non-resident counterparties). The Russian Federation (CIS) followed suit with 3.6 billion tolars or less than 1 per cent of exposure to non-residents and Ukraine with 1.4 billion tolars (0.4 per cent of gross aggregate exposure).

Figure 8: Exposure of banks to foreign counterparties



Source: The Bank of Slovenia

Savings banks do not engage in international payment services and cross-border credit operations; hence they are not exposed to country risk.

5. OPERATIONAL RISK

Operational risk is becoming more important.

The issue of operational risk has become more important over the past few years and is addressed by most banking regulators, standard-setters, as well as banks. Although this type of risk escapes a "cut-and-dry" definition, it belongs to the group of most significant risk exposures in banking industry. It is generally accepted that this type of risk arises from distortions in internal controls function and troubled corporate governance. The key factor in monitoring and controlling risks is bank management and internal controls systems. It is significant that operational risk is generally cumulative with other kinds of risk exposure – market and credit risks for instance. Most banks are in the initial phase of addressing problems associated with operational risk and there is lack of formal risk management systems in this field. Consequently, the most common practice is to apply experimental methods. Factors that aggravate the situation as far as operational risks are concerned may be described as internal: the quality of internal audit, the scope and scale of banking operations, the number of transactions, the scale and nature of misjudgements made, etc.). It should be noted that the correlation between factors and the scope of operational risks is not known; hence it is not possible to measure operational risks. It is beyond any doubt that effective internal controls systems and internal audit make up the risk monitoring and control system, which is to be enhanced by other forms of risk management such as system limit on the basis of risk factors, collateralisation, adequate provisioning level, etc. The Banking Act addresses the issue of operational risks in Article 26 when responsibilities of management are elaborated on. Supervisory authorities have not addressed the issue in detail, so as to be able to issue comprehensive methodologies for measuring operational risks. It is accounted for by the issue of quantitative limits remaining unresolved. It is to be expected that the issue of operational risks will soon be dealt with, and initiatives for the inclusion of this type of risk in the system of capital adequacy requirements have also been given. The Bank Supervision Department intends to pay due attention to operational risks both through on-site examinations and by means of drafting adequate legislation.

6. LIQUIDITY RISK

6.1. Compliance with mandatory reserves and foreign exchange minimum

All banks and savings banks held mandatory reserves and foreign exchange minimum in line with statutory requirements.

In 1999, all banks except for one were compliant on a monthly basis with the **mandatory reserve requirement**, whereas all **savings banks** were compliant with this requirement and held mandatory reserves. Each month during the first half of 2000, all banks and savings banks adhered to the requirements regarding mandatory reserves. The percentage of compliant banks in the first half of 2000 was 103.8 per cent, while savings banks achieved 141.9 per cent.

Reserves maintained by banks in 1999 exceed the calculated amount of mandatory reserves by 3.2 per cent on average. In the first half of 2000, the calculated amount of mandatory reserves was generally exceeded by 4.0 per cent on average.

Since January 1999, banks have been calculating **foreign exchange minimum** on the basis of the new methodology. Foreign exchange minimum shall be computed in relation to savings of individuals in foreign currency, tolar-denominated savings with covenants included, and holdings of non-residents in foreign currency[17]. Banks are required to maintain at least 60 per cent of foreign exchange minimum invested in bills of the Bank of Slovenia that are denominated in foreign currency.

At the end of 1999, all banks except for one were compliant with the requirement to maintain foreign exchange minimum, while as at 30 June 2000, all banks exceeded the mandatory foreign exchange minimum. Foreign exchange minimum grew from 362.3 billion tolars at the end of 1998 to 446.6 billion tolars at the end of December 1999. By 30 June 2000, foreign exchange minimum increased to 507.3 billion tolars. For some years banks have reported mandatory foreign exchange minimum well in excess of the statutory threshold

[17] Foreign exchange minimum amounts to 100 per cent of demand deposits, 95 per cent of deposits due within three months, 75 per cent of deposits due between three months and one year, and 35 per cent of deposits due after one year.

(by 23.3 per cent at the end of 1998, by 12.1 per cent at the end of 1999 and by 18 per cent at the end of June 2000).

6.2. Short-term planning of tolar liquidity flows and maturity structure

Although banks are expected to have funds necessary for maintaining optimum liquidity, the Bank of Slovenia exercises ongoing supervision of daily cash flows on the basis of mandatory planning aimed at maintaining tolar liquidity flows. Banks are required to submit these plans (statutory returns) to the Bank of Slovenia for the current and the following day.

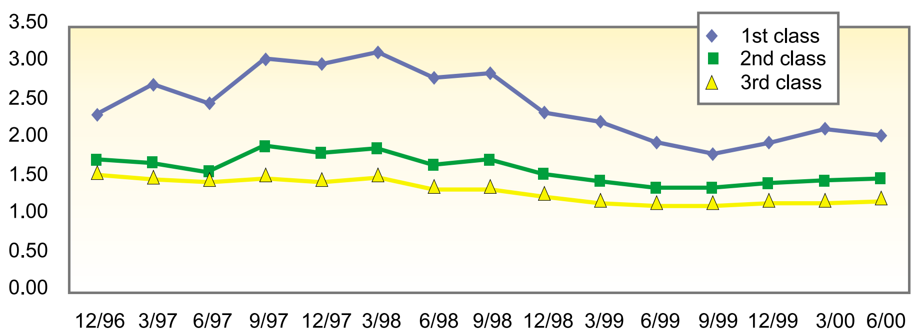
As opposed to savings banks, banks fulfilled statutory requirements to adjust maturity of assets and liabilities.

In accordance with the Decree on the Required Adjustment of the Maturity Structure between Assets and Liabilities (Official Gazette of the Republic of Slovenia No. 40/99), which elaborates on ratios between liabilities and assets of banks to be maintained in individual groups (referred to as classes), banks and savings banks were required to hold assets at least in the amount of liabilities held in respective classes[18]. All banks complied with this requirement as at 31 December 1999 and 30 June 2000. As for savings banks, they encountered more difficulties in their efforts to be compliant and they fell short of target as at 31 December 1999 and as at 30 June 2000. On average, not in a single class did savings banks succeed in covering assets with liabilities, i.e. avoid mismatch.

Since the first quarter of 1998, banks have been reducing maturity mismatch; namely, the level of liabilities that matched assets in individual groups fell to record low in the third quarter of 1999, when the coverage achieved in the second and third group came close to the mandatory minimum (under the Decree it is a 100 per cent coverage), while in the first class at the end of June 1999 the coverage dropped below 200 per cent for the first time. In September 1999 the coverage hit the bottom at 183 per cent.

Ratios achieved in all three classes as at 30 June 2000 in comparison with 31 December 1999 slightly improved, while an increase was realised mainly within the framework of first-class assets (assets classified as highly liquid and clean bills of the Bank of Slovenia and government securities). Thus as at 30 June 2000, the ratio for assets in the first class was 2.07, in the second class 1.48, and in the third class 1.24.

Figure 9: Adjustments of the maturity structure between assets and liabilities



Source: The Bank of Slovenia

[18] The Decree has introduced 1st, 2nd and 3rd class of assets and sources of funds classified on the basis of maturity.

6.3. Secondary liquidity

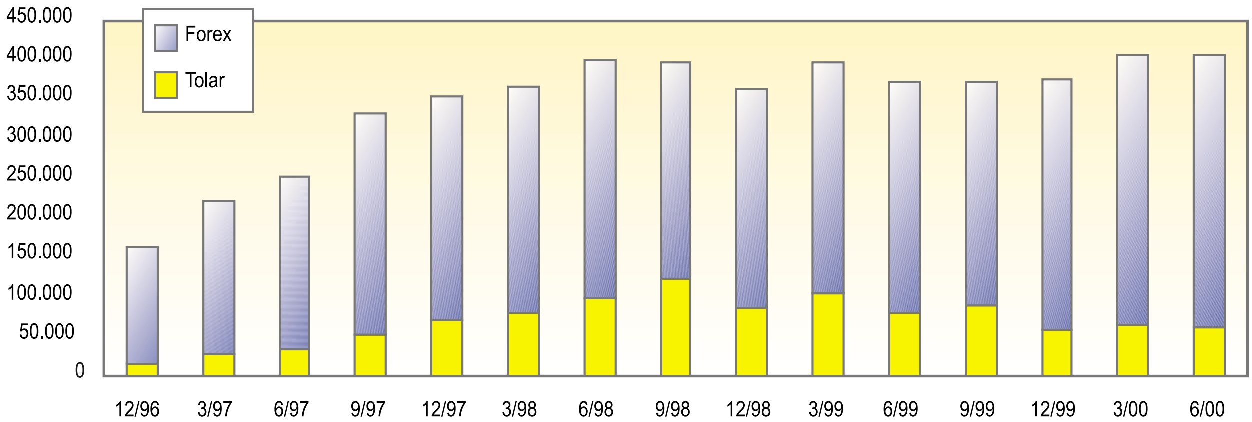
Secondary liquidity[19] is composed of investments in securities issued by the Bank of Slovenia and the Republic of Slovenia in domestic and foreign currencies. A bank's portfolio composed of such securities serves as a liquidity safety net for the respective bank. These assets may be pledged as collateral when banks apply for bridge-over loans in cases of liquidity problems. Banks may also obtain other liquidity loans from the Bank of Slovenia against these assets, i.e. securities.

Secondary liquidity of banks increased in absolute terms but dropped with respect to total assets.

With 163.8 billion tolars at the end of 1996, secondary liquidity of **banks** was rather low but then it started to improve in nominal terms and was at its peak at the end of June 1998 when it stood at 401.5 billion tolars. At that point the trend reversed, and secondary liquidity ratio fluctuated until the middle of 1999 when it recovered and reached a new peak at the end of June 2000 with 405.8 billion tolars. The rationale for these developments is that banks stepped up investments in assets composed of bills of the Bank of Slovenia and government securities in foreign currency.

On the other hand, secondary liquidity of banks in relation to total assets has been decreasing for the fourth year in a row, i.e. since the end of 1997 when secondary liquidity amounted to 17.5 per cent of total assets, this percentage dropped to 14 per cent at the end of 1999 and by June 2000, it decreased by additional 0.2 percentage point. Thus at the end of June 2000, secondary liquidity accounted for 13.8 per cent of total assets held by the banking system. During all these years under review, foreign exchange secondary liquidity accounts for the major portion of aggregate secondary liquidity (at the end of June 2000, this percentage was 84.9 per cent; hence secondary liquidity in tolars was only 15 per cent).

Figure 10: Secondary liquidity of banks (in millions of tolars)



Source: The Bank of Slovenia

Secondary liquidity of **savings banks** amounted to 602.4 million tolars at the end of June 1998 and in the second half of 1998 started to fall. In 1999, secondary liquidity fluctuated until the second half of 1999 when this figure plunged and at the end of 1999 it amounted to 164.5 million tolars. Until June 2000, secondary liquidity in savings banks decreased to 133.3 million tolars (1.1 per cent of total assets) due to a drop in investments in securities issued by the central bank.

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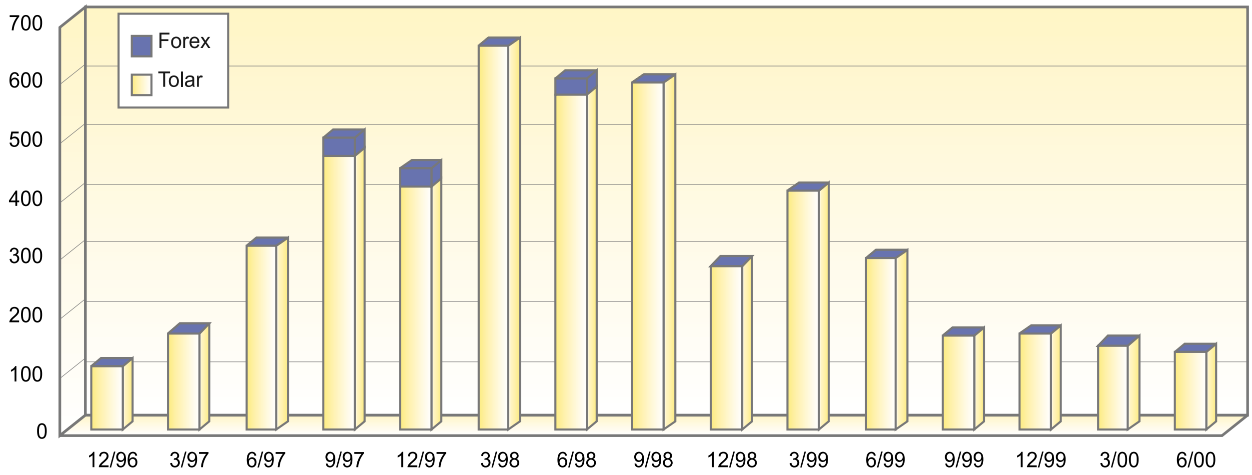
19 Secondary liquidity is composed of bills of the Bank of Slovenia both in tolars and in foreign currency, as well as treasury bills and bonds of the Republic of Slovenia.

Savings banks held only securities denominated in tolars.

Unlike banks, savings banks do not have foreign exchange secondary liquidity; hence, savings banks hold as instruments of secondary liquidity mostly or entirely tolar-denominated securities.

Figure 11: Secondary liquidity of savings banks (in millions of tolars)



Source: The Bank of Slovenia

6.4. Concentration of depositors

Statutory returns for thirty largest depositors of banks indicate that banks still depend heavily on a handful of heavy weight depositors. A high degree of dependence on a few depositors increases liquidity risk, especially if maturity dates on which such deposits fall due are not evenly spread.

Exposure to thirty largest depositors remained unchanged with respect to year-end.

Concentration on the side of the deposit base varies from one bank to the other. The share of top thirty depositors in deposits of the entire banking system (excluding banks and private individuals) was at the end of December 1999 by 0.6 percentage point lower year-on-year (52 per cent), while until 30 June 2000, this share grew slightly (by 0.1 percentage point).

7. SOLVENCY RISK

Until the year 1995, the capital adequacy ratio[20] in the Slovenian banking system was rising in response to the requirements laid down by the Bank of Slovenia for higher capital that banks had to achieve in order to be licensed for certain types of banking operations. After 1995, when capital adequacy ratio posted by **banks** reached a record high of 21.5 per cent, it started to go down. The downward trend continued mostly due to faster growth of risk-adjusted assets (risk-weighted assets) than capital growth (regulatory capital or own

[20] In accordance with the Banking Act, capital adequacy ratio is the ratio between bank capital (in the 1991 Law on Banks and Savings Banks referred to as regulatory capital, in the 1999 Banking Act reffered to as own funds) and risk-adjusted assets (in the Law on Banks and Savings Banks referred to as risk-weighted assets) plus other risks ad justed items. Capital adequacy ratio must at all times be at least 8 per cent.

funds). Thus capital adequacy ratio of Slovenian banks amounted to 14 per cent as at 31 December 1999. As at 30 June 2000, capital adequacy ratio continued to slide down and amounted to just 13.6 per cent (even less than the minimum recorded in 1993, when capital adequacy ratio started to go up).

Capital adequacy ratio decreased due to new methodology.

The lower capital adequacy ratio is mainly a result of changes in the methodology prescribed for reporting on capital adequacy that converges with European directives. Bank capital (own funds), composed of core (tier I) and supplementary (tier II) capital[21] decreased considerably in comparison with 31 December 1998 when the »old« methodology was still used. In accordance with the new Decree on the Calculation of Own Funds, Capital Requirements and Capital Adequacy Ratio of Banks and Savings Banks (Official Gazette of the Republic of Slovenia, No. 32/99), supplementary capital (tier II) does not include provisions for claims on counterparties classified in group A, while profit for the current year (up to the amount of 50 per cent after deductions for taxes and other levies), is included in core (tier I) capital provided that the amount of the profit stated has been confirmed by a certified auditor. Another novelty is that item “intangible long-term assets” is deducted from capital.

Turning to risk-adjusted assets[22], they continued to grow (growth rate as at 30 June 2000 in comparison with risk-adjusted assets as at 31 December 1999 was 9.9 per cent). Coupled with lower capital, risk-adjusted assets further reduced capital adequacy ratio. The most important changes with regard to the old methodology used for risk-weighted assets are more strict weighting of exposure to other banks, inclusion of derivative financial instruments, and more strict weighting of assets secured by property (lower index only applies for loans secured by real estate).

In accordance with the Banking Act and the Decree on the Calculation of Own Funds, Capital Requirements and Capital Adequacy Ratio of Banks and Savings Banks, the calculation of capital adequacy ratio also includes other risks adjusted items; therefore, banks in savings banks reported for the first time as at 30 June 2000 on foreign exchange risks-adjusted items, which on the reporting date totalled 48.1 billion tolars for all Slovenian banks.

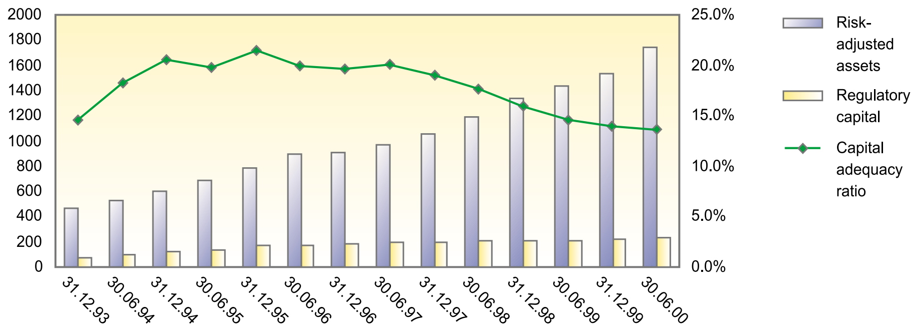
Wide range of capital adequacy ratios in banks.

Capital adequacy ratio differs from one bank to another. At the end of June 2000, the lowest figure was capital adequacy ratio was 9 per cent, while the highest was as much as 35.4 per cent.

21 For the purpose of calculating capital (own funds), the sum of core (tier I) capital and supplementary (tier II) capital is reduced by deducting certain items.

22 Risk-adjusted assets is the sum of book balances of all on- and off-balance sheet items, decreased by specific provisions earmarked for those items and weighted in line with credit risks.

Figure 12: Movements in risk-adjusted total assets[23] and capital (in billions of tolars) and capital adequacy ratio (in %) from 31 December 1999 to 30 June 2000

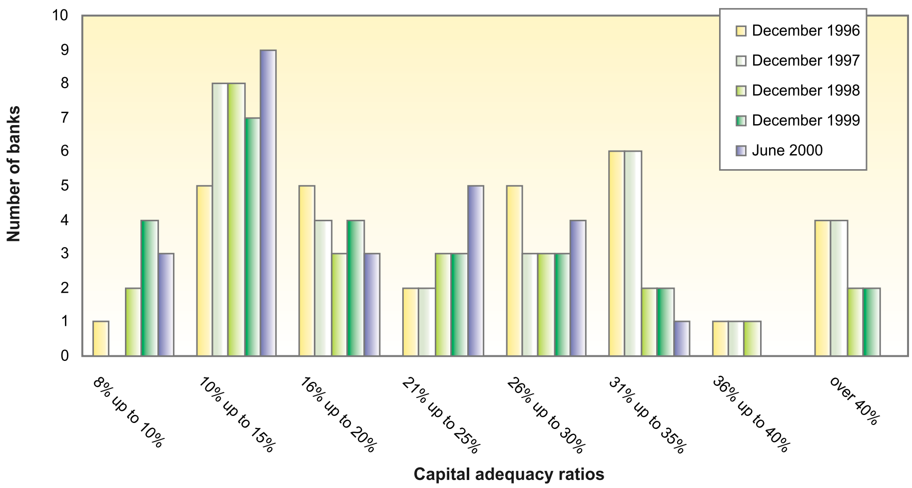


Source: The Bank of Slovenia

Number of banks in the group where capital adequacy ratio is the lowest continued to rise.

If all banks operating in Slovenia are classified in groups on the basis of capital adequacy ratios, it is clearly demonstrated that there has been a rise in the number of banks in groups with the lowest capital adequacy ratios and flattening of the groups where banks boasting higher capital adequacy ratios were classified. Thus at the end of June 2000, three banks had capital adequacy ratio between 8 and 10 per cent, nine banks were in the bracket where capital adequacy ratio was between 11 and 15 per cent, twelve banks had capital adequacy ratio between 16 in 30 per cent, while the remaining bank has capital adequacy ratio in excess of 31 per cent.

Figure 13: Distribution of banks in terms of capital adequacy ratio



Source: The Bank of Slovenia

For the purpose of analysing movements in the number of banks in each group over the years, changes in the total number of banks have to be taken into account (there were 25 banks as at 30 June 2000).

[23] As from 30 June 2000, the amount of risk-adjusted assets is higher by items adjusted for currency risk.

As opposed to banks, capital adequacy ratio reported by **savings banks** increased to 14.4 per cent in 1999 and exceeded capital adequacy ratio achieved by banks for the first time. Until this latest development, banks used to lead the way - at the end of 1998, capital adequacy ratio reported by savings banks was 13.4 per cent. At the end of 1999, capital adequacy ratio reported by savings banks was in the range of 8.1 per cent (as a consequence of the implementation of the new methodology for the calculation of capital adequacy ratio with effectiveness on 20 August 2000) and as much as 50.3 per cent (the span as at 30 June 2000 was between 7.9 per cent and 15.9 per cent).

8. CURRENCY RISK

8.1. Bank exposure to currency risk

Foreign currency mismatch

Banks posted short foreign exchange position in foreign exchange sub-balance sheet.

As in previous years, **banks** reported again at the end of 1999 short position in foreign currency (also referred to as foreign exchange position) in the so-called foreign-exchange sub-balance. As at 31 December 1999, the foreign exchange sub-balances in banks stated by 35.3 billion tolars more foreign exchange liabilities than assets, which means that this kind of banks' net exposure increased again by 12 per cent at the end of 1999 – the first rise after the year 1998, when foreign exchange position plunged from 51.8 billion tolars to 31.4 billion tolars.

The structure per currency in the foreign exchange sub-balance sheet was as follows: out of the total amount of 813.9 billion tolars in foreign exchange assets (claims), there was as much as 477.9 billion tolars (58.7 per cent) denominated in euro, 149.2 billion tolars (18.3 per cent) denominated in US dollars, while other claims (23 per cent) were denominated in other currencies. On the liabilities side, there was 32.2 per cent of liabilities denominated in euro, 17.4 per cent was denominated in US dollars and 50.4 per cent was denominated in other currencies.

The Decree on Mismatch between Assets and Liabilities of Banks in Foreign Currency (Open Foreign Currency position) (Official Gazette of the Republic of Slovenia, No. 37/99), which became effective in May 1999 superseded the Decree bearing the same name and promulgated in accordance with the Law on Banks and Savings Banks. Under the new Decree, short or long position in foreign currency must not exceed 20 per cent of bank capital[24] daily, while average monthly open position of banks in foreign currency must not exceed 10 per cent of capital of the respective bank.

Open foreign exchange position of all banks computed in accordance with the said Decree, as at 31 December 1999 represented 5 per cent of banks' capital (at 30 June 2000, this figure increased to 6.4 per cent).

24 Also reffered to as regulatory capital or own funds.

Mismatch in transactions with foreign currency clause

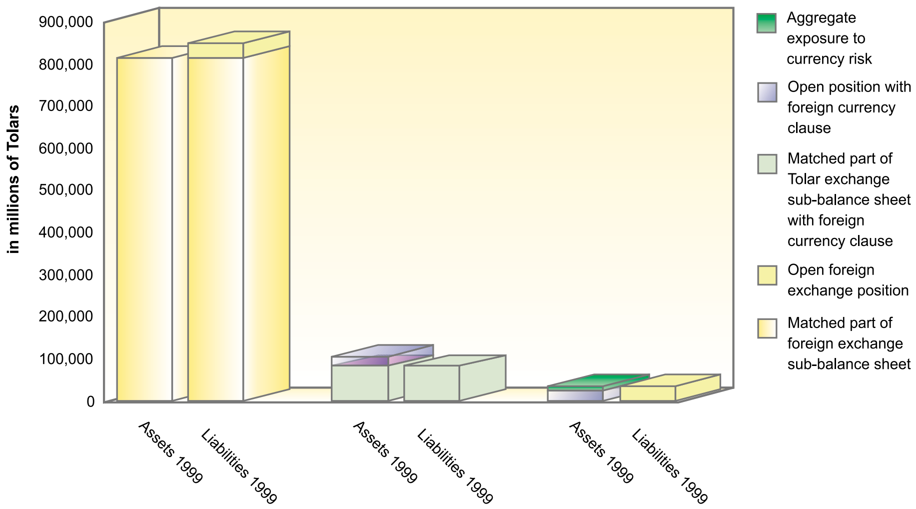
Banks reported long foreign exchange position in relation to tolar sub-balance sheet with foreign currency clause: items on the assets side exceeded by 23.9 billion tolars items on the liabilities side. In comparison with 1998 when the surplus amounted to 31.4 billion tolars, it means a 23.9 per cent decrease in long foreign exchange position in tolar sub-balance sheet with foreign currency clause.

Aggregate exposure to currency risk

Aggregate net exposure to currency risk increased in banks.

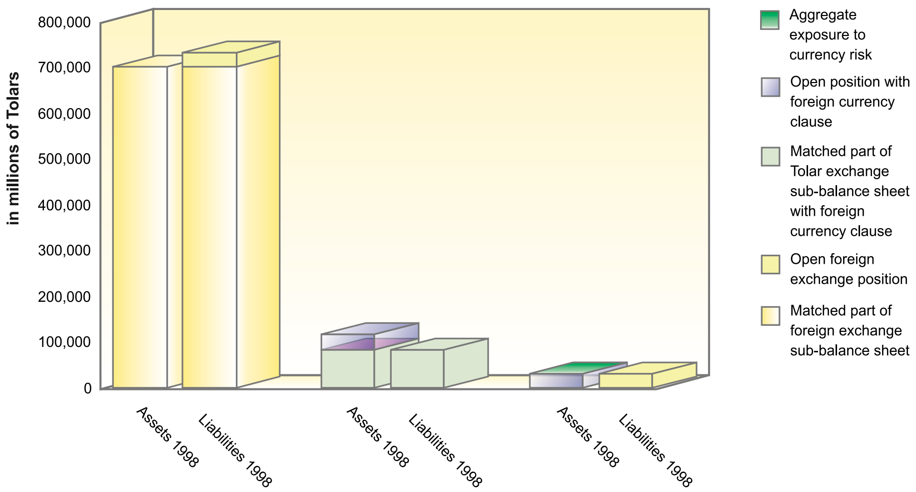
Aggregate net exposure to foreign currency risk takes into account both foreign currency mismatch and mismatch that arises from transactions including foreign currency clause. Aggregate net exposure of Slovenian banks to currency risk as at 31 December 1999 was short and amounted to 11.4 billion tolars, while since 1998 it had been only 27.6 million tolars. This means that there was a shift of aggregate net exposure with respect to the position at the end of 1998.

Figure 14: Exposure of banks to currency risk as at 31 December 1999



Source: The Bank of Slovenia

Figure 15: Exposure of banks to currency risk as at 31 December 1998



Source: The Bank of Slovenia

8.2. Exposure of savings banks to currency risk

Foreign currency mismatch in savings banks

Unlike banks, **savings banks** carried long foreign exchange position and as at 31 December 1999 posted assets (claims) in foreign currency in the amount of 10.8 million tolars and no liabilities in foreign currency. As at 31 December 1998, savings banks carried assets in foreign currency in the amount of 10.2 million tolars and no liabilities in foreign currency.

Mismatch in transactions with foreign currency clause

As for the tolars sub-balance sheet with the foreign currency clause, the situation reported by savings banks was at opposite ends compared to the situation reported by banks, since as at 31 December 1999, savings banks reported short position in foreign currency (short foreign exchange position). Liabilities in tolars with foreign currency clause exceeded assets (claims) denominated in tolars with foreign currency clause by 11.9 million tolars. With regard to 31 December 1998 when liabilities with foreign currency clause exceeded assets (claims) by 24.7 million tolars, the difference amounted to 12.8 million tolars.

Aggregate exposure to currency risk

Unlike banks, savings banks managed to reduce foreign currency mismatch.

Aggregate exposure to currency risk (foreign exchange mismatch and mismatch arising from operations involving foreign currency clause) reported by savings banks as at 31 December 1999 amounted to 1.1 million tolars. As opposed to 31 December 1998, when net exposure to currency risk amounted to 14.5 million tolars (short position), aggregate exposure of savings banks to currency risk at the end of 1999 was almost balanced. To summarise, the trend noticeable in relation with savings banks and developments associated with banks diverged in this segment.

9. RISKS ASSOCIATED WITH INFORMATION TECHNOLOGY SYSTEMS

With the introduction of computerised information systems in banks and savings banks, these institutions have acquired tools for serving their customers better, to step up quality and provide in-depth expertise within shorter time limits, i.e. when required. Risks brought along by information technology are not necessarily new to banking systems managers, but they come in all shapes and colours and their disguise makes them difficult to spot. Hence bank management may find themselves in a tight corner when faced with this type of risk and tension rises. The role of the Bank Supervision Department within the framework of the Bank of Slovenia is to focus efforts and deploy supervisory and surveillance resources needed to identify these risks, sound the alarm, and to resort to supervisory mechanisms (measures), which banking supervisors pass on to bank management with the aim of minimising their adverse effects.

These risks are:

- risk of losing information and/or data,
- integrity (comprehensiveness) of information and/or data (errors of entry and processing errors),
- risk of losing income,

- incorrect, i.e. inadequate reporting,
- impaired, i.e. lost competitive advantage,
- decreased, i.e. lost privacy,
- reduced productivity,
- disturbances in business cycle,
- loss of confidence of staff (users) in the course of process implementation,
- inadequate reliance on automated systems,
- new aspects of funds protection, and
- violations of laws and regulations and other requirements posed by regulators.

Risks are reflected in events (unpleasant ones) that may occur as one-off event or frequently. Furthermore, these events are associated with small or large losses, i.e. consequence. These events may be classified in four groups:

- marginal (trivial) –one-off events causing small losses,
- concerning – frequent events causing small losses,
- significant –one-off events causing large losses,
- critical – frequent events causing large losses.

In the light of the nature and scope of unpleasant events, it is quite natural that bank management addresses individual risks and strives to control them. Certain risks are associate with a particular function and as such they cannot be removed (inherent risks), while others are volatile and change in certain circumstances. Such risks may be restrained by implementing adequate controls.

9.1. Risks management models – management information systems and internal controls systems

Need to control IT risks has driven large banking systems and professional associations to work out models designed to deal with this issue.

Over the past few years, exigency of bank management to manage risk (certain risks go undiscovered for some time before they are properly address, while others are regulatory monitored and coped with by implementing control systems) has driven large banking systems on the one hand and professional associations on the other to pool resources and define what best practice in this area would be. The purpose of all these efforts has been to set up such controlling systems that would ensure effective controls that would not stifle growth of businesses. Another guideline in that process has been a desire of those who steer the banking ship and represent corporate governance (persons who actually run credit institutions: depositors through general meeting of shareholders, members of supervisory and management boards) to design a “yardstick” and measure performance of executive and senior managers appointed to fulfil their business goals. By using the “yardstick” one expects to define expectations and hence minimise the possibility of conflicts between directors – senior management over meeting target values.

Controlling frameworks that serve to manage business systems comprise COSO (1992 USA), CoCo (1995 Canada), Cadbury (1992 London, initiated by Financial Reporting Council, London Stock Exchange), King Report (1994 South Africa) as well as a wide range of standards and guidelines, including those issued by professional associations in the field of audit. A controlling framework such as COSO (a report of joint working bodies) was issued by the Committee of Sponsoring Organisation of Threadway which is composed of the representatives of the American Institute of CPA, American Accounting Association, Institute of Internal Auditors, Institute of Management Accountants, Financial Executive Institute. The Report addresses controlling environment, risk management, activities in the ambit of controlling, dissemination of information and reporting and it outlines different roles of individuals (management, executive directors, internal audit) in the process of running banks.

The role of the controlling environment is of key importance and it has the following elements:

- organisational forms and structures,
- awareness of people of controls and their purpose,
- personal, ethical and operational features of individuals,
- rules, principles, philosophy and operational management styles,
- assignment of authorisations and responsibilities,
- attention paid by top management levels to requirements and guide lines laid down by owners (directors), other connected counterparties and public.

Prepared by the Information Control Audit and Control Foundation, COBIT (Control Objectives for Information and Related Technology) falls within the scope of documents, which identify the limits of controlling. If the mission of all these documents is to promote best practice in operations and controlling, they are a measure or a benchmark used to make comparison with a given environment. Such documents also mean a treasury chest of knowledge for managers as executives who implement processes, since they contain information relevant for risk management and effective and prudent resource management. COBIT exceeds similar papers by its scope and sophistication – it builds on the findings presented in previous reports drawn up primarily for top management. Furthermore, it also elaborates guidelines for conducting audit.

COBIT defines key points in four domains (planning and organisation, acquisition and implementation, provision of services and maintenance and monitoring) 34 processes for which criteria are defined in the light of resources deployed (human resources, applications, technology, technical facilities – centres and data). These criteria are set in line with targets for the control function (effectiveness, capability, confidentiality, comprehensiveness, availability, convergence and reliability). These processes are used to define significant goals of controlling. Due to such approach, COBIT is not only a manual for controllers of information systems, but also a tool for earmarking of internal controls.

Banks shall abide by Slovenian standard PSIST BS 7799.

The Bank of Slovenia is particularly vigilant when it comes to safety of information systems. The Governing Board of the Bank of Slovenia addressed issues in this area and in May 2000 adopted a decree which requires banks to abide by the Slovenian standard PSIST BS 7799 – code of professional secrecy – when carrying out operating activities. The Bank of Slovenia intends to check if banks are compliant with the standard within the framework of ongoing examinations.

III. DEVELOPMENTS RELATED TO BANKING LEGISLATION AND PAYMENT SYSTEMS REFORM

In 1999 and the first half of 2000, the Bank Supervision Department focused efforts on the preparation of secondary legislation in line with the Banking Act. The Banking Act became effective on 20 February 1999, only three weeks after the entry into force of the EU-Slovenia Europe Agreement.

Republic of Slovenia requests transitional period for deposit-guarantee scheme and savings and loan undertakings.

In February 1999, the issue of free movement of services was on the table in the preliminary phase of legislation screening. In the second half of 1999, Slovenia's negotiation positions were submitted to the European Union for Chapter 3: Freedom to provide services accompanied by additional clarifications to the negotiating position. The Republic of Slovenia has stated its readiness to adopt the acquis communaitaire of the European Union for freedom to provide services, but it requested two transitional periods for full alignment to be completed after the expected accession of the European Union.

The first transitional period requested by the negotiation team of the Republic of Slovenia refers to savings and loan undertakings established prior to the effectiveness of the Banking Act (20 February 1999). Under the said request, savings and loan undertakings shall be granted a two-year transitional period after the date of Slovenia's full-fledged membership of the European Union (i.e. until 31 December 2004) to meet capital requirements and other standards associated with safe and sound banking operations, which are laid down in the directives of the European Union. The second transitional period has been requested by the Republic of Slovenia for the protection of the level and scope of domestic deposit-guarantee scheme for deposits with banks for a three-year period counting from the day when Slovenia is expected to join the European Union until 31 December 2005.

1.1. TRANSITIONAL PERIOD FOR SAVINGS AND LOAN UNDERTAKINGS

In the past, savings and loan undertakings in the Republic of Slovenia were established in accordance with a special law on savings and loan undertakings, which was promulgated back in 1969, and in 1990 was superseded by the present law. For the foundation of savings and loan undertakings there was no threshold for initial capital, and as for terms and conditions of operations conducted by savings and loan undertakings, they were set at founders' discretion. The law stipulates that founders are jointly and severally liable for savings deposits and all liabilities of savings and loan undertakings. Only in the case where a savings and loan undertaking obtains a bank guarantee, a subsidiary guarantee of the Republic of Slovenia also covers deposits secured in this way. Savings and loan undertakings, which are members of the Association of Savings and Loan Undertakings, are obliged to hold a liquidity reserve with the Association in the amount of at least 5 per cent of demand (sight) deposits for the purpose of providing funds to members who encounter liquidity problems.

The core purpose of business activities carried out by savings and loan undertakings is to gather savings deposits from private individuals (mostly farmers) with the aim of injecting funds back into the sector by granting loans to its founders – co-operatives and citizens. Due to the limited scope of banking operations, savings and loan undertakings feature mostly as local community services.

At the end of June 2000, there were 68 savings and loan undertakings in Slovenia. Most of them were established within the framework of agriculture and forestry co-operatives and are members of the Association of Savings and Loan Undertakings – also set up as a savings and loan undertaking. As at 30 June 2000, total assets of all savings and loan undertakings in Slovenia amounted to 48.8 billion tolars – approximately the size of a medium-sized bank operating in the v Republic of Slovenia. As for the share of savings and loan undertakings in aggregate total assets of the Slovenian banking sector (banks, savings banks, and savings and loan undertakings), savings and loan undertakings as at 30 June 2000 accounted for a 1.6 per cent share (mere 1.2 per cent of GDP). Figures show that savings and loan undertakings are small-scale institutions that serve a narrow circle of customers.

The Banking Act takes into account the fact that savings and loan undertakings are specific. On the other hand, there is no doubt that savings and loan undertakings are by nature credit institutions. As credit institutions, they will have to abide by the provisions laid down in European directives valid for credit institutions. In accordance with the Second Banking Directive, the Banking Act stipulates that both savings banks and savings and loan undertakings must hold minimum capital in the amount of 186 million tolars. The transitional period in the duration of five years (after the entry into force of the Banking Act) for savings and loan undertakings should give savings and loan undertakings breathing space to pool resources necessary to comply with the requirement that sets the minimum capital and other provisions laid down in the Banking Act, which refer to risk management and safe and sound banking operations.

Savings and loan undertakings will be fully compliant with provisions of Banking Act by February 2004.

In December 1999, the Bank of Slovenia promulgated the Decree on the Bringing of the Operation of Savings and Loan Undertakings into Line with the Provisions of the Banking Act. Under this Decree, savings and loan undertakings are to meet provisions laid down in the Banking Act referring to credit institutions gradually, so as to be fully compliant by February 2004. This means that savings and loan undertakings, which intend to comply with the provisions, have to increase »capital« by 31 December 2001 so as to hold at least one half of the mandatory minimum for initial capital. Afterwards, savings and loan undertakings are to step up capital step-by-step in order to meet the target figure by 31 December 2003 and be complaint with the mandatory minimum for initial capital in the amount of 186 million tolars. As from that date, savings and loan undertakings must also meet mandatory capital adequacy ratio and abide by limits set in relation to exposure to a single counterparty or a group of related counterparties, as well as limits in respect of aggregate amount of large exposures. The Decree also highlights the requirements to assess creditworthiness of counterparties in relation to loan portfolio, to make provisions for credit and other risks, as well as prudential reporting to the Bank of Slovenia.

Steps necessary to instigate compulsory liquidation of those savings and loan undertakings, which have failed to comply by February 2004, will be duly taken.

1.1. DEPOSIT-GUARANTEE SCHEME

Deposit-guarantee scheme will come into force on 1 January 2001.

Under the Banking Act, the new deposit-guarantee scheme[25] will enter into full force and effect on 1 January 2001 and will be implemented in line with standards and practices outlined in the Decision[26] on Deposit-Guarantee Scheme (Official Gazette of the Republic of Slovenia, No. 61/00). Since the Slovenian legislative framework has to be fully aligned with the acquis, the Decree has been drawn up to incorporate meaningfully the provisions laid down in the European Directive on Deposit-Guarantee Schemes (Directive 94/19/EC).

The most important features of the deposit-guarantee scheme, which derive from the Banking Act and are different from the »old« deposit-guarantee scheme are summarised below:

- Guarantee of the Republic of Slovenia has been replaced by guarantees issued by banks and savings banks,
- The amount of guarantee per individual depositor has been set at 3.7 million tolars at the beginning of instigating bankruptcy of a bank,
- Deposit guarantee has been extended to include deposits of small-sized legal entities,
- The Banking Act explicitly lists which depositors and their deposits have been excluded from the deposit-guarantee scheme in accordance with the Directive.

Participation in the deposit-guarantee scheme is compulsory for all banks, savings banks and savings and loan undertakings authorised by the Bank of Slovenia, as well as branches of banks with the registered office outside the territory of the Republic of Slovenia, provided they are partly or fully included in the host country deposit-guarantee scheme. Thus banks and branches of foreign banks which have joined the scheme guarantee for the payment of deposits covered by the scheme. Since liquid funds are needed to pay out guaranteed deposits, banks and savings banks are obliged to invest in short-term securities of the Bank of Slovenia or the Republic of Slovenia at least 2.5 per cent of the balance of accounts containing guaranteed deposits placed with the respective bank or a savings bank as at the last day of the preceding half-year period.

The Decision (Decree) on the Deposit-Guarantee Scheme promulgated in June 2000 addresses the following issues:

- Defining detailed conditions and procedures for earmarking funds needed in order to pay out guaranteed deposits,
- The method of calculating the amount of liquid assets and more details about securities held for the purpose of maintaining liquid funds required for the payment of guaranteed deposits, and
- Responsibilities of banks with regard to reporting.

Guaranteed deposit amounts to 3.7 million tolars including interest.

The amount of guaranteed deposits refers to balances of deposits placed by an individual depositor up to the amount of 3.7 million tolars, and it includes accrued interests computed until the day of the institution of bankruptcy proceedings in the respective bank.

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25 Also referred to as deposit insurance scheme and deposit protection scheme.

26 Also referred to as Decree on Deposit-Guarantee Scheme.

For the purpose of the deposit-guarantee scheme, a deposit means aggregate balance of all claims of a depositor in line with:

- Contract on keeping a current or giro account,
- Savings deposits,
- Cash deposits,
- Certificates of deposit, bills if issued as registered securities (excluding registered bonds and other registered debt securities).

Netting arrangements in line with Bankruptcy Act are applied to calculate guaranteed deposits.

The amount of guaranteed deposits included tolar-denominated claims as well as claims denominated in foreign currency. Deposits placed by sole traders (entrepreneurs) and deposits placed by these depositors in the capacity of natural persons (individuals) are treated as deposits placed by one depositor. For the purpose of calculating guaranteed deposits, the netting principle applies as laid down in the Bankruptcy Act. In other words, the amount of deposits is reduced by the bank's claims on the depositor, and the netted deposit is guaranteed up to the amount of 3.7 million tolars. In the case of a joint account, the share of each depositor is taken into account when calculation is made for each depositor and, unless stipulated otherwise, funds in such an account are distributed amongst depositors in equal shares.

The deposits listed below are excluded from the deposit-guarantee scheme:

- Bearer's deposits,
- Deposits placed by other banks and other financial institutions,
- Deposits placed within the framework of money-laundering operations,
- Deposits placed by governments, central banks, and local governments/communities,
- Deposits placed by members of the bank's management and supervisory board and their family members,
- Deposits placed by the respective bank's shareholders who have at least a 5-per-cent stake,
- Deposits placed by legal entities connected with the respective bank,
- Deposits placed by members of the bank's management and supervisory board of legal entities connected with the respective bank and shareholders who have more than 5 per cent stake and their family members,
- Subordinated deposits, and
- Deposits placed by legal entities classified as large and medium-sized companies under the Company Act.

Another novelty is obligation to keep depositors informed.

Another significant novelty introduced by the Decision (Decree) is the obligation to keep depositors informed, since the new deposit-guarantee scheme brings substantive changes in comparison with the existing government-backed, full-coverage for all deposits from private individuals. On the one hand, guarantee has been extended to other counterparties as well, but on the other hand, limits have been set both on the amount and the circle of eligible deposits and depositors. Therefore, it is essential that depositors are duly and timely informed on the new system by banks. The Decision (Decree) requires that banks shall post noticeable and comprehensible information in relation to the deposit-guarantee scheme. Banks are also obliged to inform depositors on the possibility that the amount guaranteed under the deposit-guarantee scheme may be exceeded in the case of a merger between banks, and depositors shall be informed about their rights.

Deposit-guarantee scheme starts to function when the Bank of Slovenia institutes bankruptcy procedure.

The deposit-guarantee scheme is activated when the Bank of Slovenia issues a decision to instigate bankruptcy procedure (this shall take place shortly or no later than 21 days after the day when officers of the Bank of Slovenia confirm that the bank in question has not paid to depositors upon request funds, which have become due and shall be repaid upon depositors' request). After the competent court has ruled that a bankruptcy procedures shall be instituted, the Bank of Slovenia shall release a public notice to depositors, while the bank under the bankruptcy procedure and the receiving bank shall no later than within 10 days establish balances on all guaranteed deposits. Depositors will be paid guaranteed deposits no later than three months after the start of the bankruptcy procedure, when the Bank of Slovenia must provide liquid funds for the receiving bank to effect payments. A depositor may dispose with the deposit only after making a deposition that by accepting the guaranteed deposit, he/she withdraws the claim filed in the course of the bankruptcy procedure and does not fall in the group of persons excluded from the guarantee.

The Bank of Slovenia computes stakes or portions to be provided in order to settle liabilities of banks for guaranteed deposits in conformity with information and data from the latest prudential reports submitted by banks on balances of guaranteed deposits prior to bankruptcy of the respective bank. The amount treated as the amount of guaranteed deposits is the amount established on the basis of the final list of guaranteed, i.e. insured deposits issued by the receiver (bankruptcy administrator) and the Bank of Slovenia. The Bank of Slovenia shall send to every bank a notification, i.e. a decision, to pay in its portion of funds required to effect the payment of guaranteed deposits. The notification shall also include the deadline for making the payment and this deadline shall not exceed the period of three months after the commencement of bankruptcy. Banks may honour their obligations by selling short-term securities held as instruments of secondary liquidity, but they may also use other sources. The maximum amount an individual commercial bank shall pay within one financial year is 3.2 per cent of guaranteed deposits placed with the respective bank.

As from the day the Republic of Slovenia becomes a full-fledged member of the European Union, deposits placed with a branch of the bank from a Member State will be guaranteed in line with the deposit-guarantee scheme effective in the country where the bank has its registered seat of office. Slovenian regulators will recognise the deposit-guarantee scheme in place in a Member State is on a par with Slovenia's scheme. However, a branch of a foreign bank may opt to join the deposit-guarantee scheme effective in the Republic of Slovenia for supplementary cover, should it decide to do so. In that case, a bilateral agreement will be made between the Bank of Slovenia and the manager of the deposit-guarantee scheme of the respective Member State, and adequate rules and procedures are defined with respect to paying out guaranteed, i.e. insured deposits. Before Slovenia's accession, the Bank of Slovenia may at its discretion rule that one of the requirements for the establishment of a branch of a foreign bank is for the branch to join the deposit-guarantee scheme effective in the Republic of Slovenia, or it may renounce this requirement when the deposit-guarantee scheme of the home country is assessed to provide adequate protection.

2. ALIGNMENT WITH THE ACQUIS COMMUNAUTAIRE IN THE BANKING SECTOR AND SECONDARY LEGISLATION

Legislative framework for banking sector of the Republic of Slovenia is almost fully aligned with the acquis.

Legislation in the field of freedom to provide services has been addressed in the course of negotiations between the Republic of Slovenia and the European Union. Banking, insurance, securities market and investment funds, as well as non-financial services particularly in the field of banking have reached a high level of alignment with the legislative framework of the EU. Slovenia will be ready to adopt the legal framework of the European Union (acquis communautaire) by 31 December 2002 at the latest. The two exceptions mentioned before require adequate transitional periods.

In 1999 and the first half of 2000, a number of by-laws were promulgated by the Bank of Slovenia staff in accordance with the mandate to pass secondary legislation given to the Bank of Slovenia in the Banking Act. The by-laws that regulate supervisory and surveillance issues related to banking operations carried out by banks and savings banks and adopted in accordance with the provisions laid down in the Banking Act, are presented hereunder in the chronological order that follows the publication of the respective by-law in the Official Gazette of the Republic of Slovenia.

Decree on the Calculation of Own Funds, Capital Requirements and Capital Adequacy of Banks and Savings Banks

The Decree elaborates on the method of calculation of capital (own funds) and minimum capital requirements to be compliant with by banks and savings banks so as to safeguard solvency and cushion risks in the course of ordinary banking business. Under this Decree, capital requirements in connection with credit and currency risk, as well as for exceeding limits imposed on capital holdings in non-financial institutions, have been set forth. Capital requirements put in place in regard of currency risk came into force on 30 June 2000. Banks and savings banks are required to calculate the amount of own funds and capital requirements on regular basis and report to the Bank of Slovenia at least quarterly.

Decree on Large Exposure of Banks and Savings Banks

In terms of this Decree, banks and savings banks shall take appropriate steps to contain risks associated with excessive concentration of credit exposure. Prudential limits are set in order to restrict banks' exposures to single borrower or groups of related borrowers, and to other members of the group. Additionally, the Decree defines large exposure and caps aggregate large exposure with regard to the bank's own funds (capital).

Decree on the Classification of the On-Balance Sheet Assets and Off-Balance Sheet Items of Banks and Savings Banks

The Decree stipulates methods for monitoring and assessing credit and country risks to which banks and savings banks are exposed in the course of ordinary business activities. In addition to detailed criteria for the classification of on- and off-balance sheet items on the basis of the degree of risk associated with each item, the Decree also stipulates rules for the assessment of potential losses, suspension of income, and keeping of credit files.

Decree on Establishing Specific Provisions of Banks and Savings Banks

The Decree lays down the amount and the method for earmarking specific provisions against losses associated with credit and country risks. Under the Decree, banks and savings banks shall make provisions for other risks to which they are exposed in the course of ordinary banking operations. Since banks and savings banks assume risks when providing services, a portion of earnings shall be set aside as a safety net.

Decree on the Implementation of Article 127 of the Banking Act

In line with Article 127 of the Banking Act, banks shall report on certain significant facts and circumstances arising in the course of banking operations. The Decree elaborates on the contents of reports to be submitted in accordance with Article 127 of the Banking Act. In addition, it also stipulates how these reports shall be prepared and determines deadlines for their submission.

Decree on Mismatch between Assets and Liabilities of Banks in Foreign Currency (Open Foreign Exchange Position)

The Decree stipulates that a bank authorised to engage in foreign exchange operations shall calculate on daily basis its open position in foreign currency as a part of its risk-containment practice. Short or long position in foreign currency (also referred to as open foreign exchange position) shall not exceed 20 per cent of the respective bank's own funds daily, while the average monthly open position shall not exceed 10 per cent of the bank's own funds.

Decree on Books of Account and Annual Report and Accounts of Banks and Savings Banks

The Decree stipulates the format of the chart of accounts and the type and format of financial statements for banks, outlines the contents of the annual report and accounts, elaborates on the methodology for the valuation of items presented in the book of accounts, and describes the preparation of financial statements. The detailed contents of monthly and other prudential reports and other statutory returns with balances on the respective bank's accounts, as well as the deadlines for their submission, are addressed by the Decree.

Decree on the Minimum Scope and Content of Audit and Auditor's Report

The Decree defines the form and the minimum scope and content of external auditor's examination and the report on audit. Audit of banking operations of banks and savings banks comprises the audit of the annual report and the consolidated annual report prepared in accordance with the Decree on Books of Account and Annual Report and Accounts of Banks and Savings Banks and the supplement stipulated under this Decree. The appointed external auditor shall focus on and describe in the report in detail financial statements, any changes in capital, provisions and write-offs, consolidation effects, compliance with risk management rules, internal audit function, keeping of books of account, the quality of the information system, adequacy and comprehensiveness of notifications and reports submitted to the Bank of Slovenia, the valuation of on- and off-balance sheet items, and the reporting bank's accounting policies.

Decree on the Required Adjustments of the Maturity Structure between Assets and Liabilities

The Decree requires banks and savings banks to match the maturity structure of assets and liabilities. Therefore, the Decree classifies assets in three groups on the basis of maturity and stipulates the ratio between assets and liabilities with different maturities.

Decree on the Detailed Method fot the Calculation of Liabilities, Claims and Holdings for the Purpose of Determining Net Indebtedness

The Decree lays down guidelines for the calculation of net indebtedness of a bank's or a savings bank's counterparty. Net indebtedness in excess of the prudential limit is regarded as one of the reasons standing in the way to the appointment of such a net debtor to the supervisory board of the respective bank, i.e. the savings bank.

Decree on Determining and Prudential Reporting on Value of Holdings of Banks and Savings Banks in Non-Financial Institutions and Investments in Tangible Fixed Assets

The Banking Act sets a ceiling on equity investments banks and savings banks have in non-financial institutions and caps investments in tangible fixed assets. The value of a bank's aggregate investments in equity capital of non-financial institutions shall not be in excess of 60 per cent of the bank's capital, while a single investment in a particular non-financial institutions may not exceed 15 per cent of the bank's capital. Aggregate value of investments in land, buildings, business equipment and equity capital of non-financial institutions shall not exceed the bank's capital. Banks are required to report on these investments on a quarterly basis. Any overshot limits in non-financial institutions capital holdings shall have adequate capital coverage.

Decree on the Annual Fee and Lump-Sum Charger for Prudential Supervision

The Decree stipulates the amount of annual fee charged by the Bank of Slovenia to banks and savings banks for prudential supervision, as well as lump-sum charges (also referred to as remuneration) for procedures carried out by the Bank of Slovenia. The amount of annual fee is levied in proportion to the bank's respective risk-adjusted assets. Remuneration shall be paid by the respective bank in the case when a corrective measure is imposed. The amount is computed by multiplying the number of hours the Bank's examiners have actually used to carry out the examination of banking operations of the bank in question with the examiner's hourly fee.

Decree on Minimum Requirements for Obtaining Authorisation for the Provision of Banking and Other Financial Services and Documents to be Attached to Application[27]

The Decree lists staffing, technical and organisational terms and conditions to be fulfilled by the applicant-requesting authorisation to provide bankingservices.

27 Also referred to as Decree on the Laying Down of the Terms and Conditions to be Complied with by Banks and Saving Banks in order to Perform Banking and the Other Financial Services and on the Laying Down of the Documentation on the basis of which it may be Determined wheather a Company will be able to Carry Out the Activities which are the Object of its Application for an Authorisation.

Attachments to be enclosed to the application serve to prove that the applicant has staff, technical and organisational capabilities to provide banking services and are listed in the Decree.

Decree on Minimum Scope of Documents to be Submitted by a Foreign Bank with Application to Establish a Branch[28]

The Decree lists documents to be attached to the application for the authorisation to establish a branch of a foreign bank. The listed documents serve to prove that the branch has staff, technical and organisational capabilities to provide banking services.

Decree on the Notification of the Intended Disposal of Shares

Under the Decree, any person on the point of disposing of shares that would result in reducing the holding below the limit for which the respective shareholder has obtained an authorisation from the Bank of Slovenia, shall notify in writing the Bank of Slovenia in advance.

Decree on the Conditions to be Met by Credit Intermediary

The Decree highlights terms and conditions to be compliant with if a bank is disposed to authorise a credit intermediary for lending and other banking operations, as well as reporting requirements (information furnished to the Bank of Slovenia with regard to credit intermediary).

Decree on the Bringing of the Operation of Savings and Loan Undertakings into Line with the Provisions of the Banking Act

Savings and loan undertakings are to meet provisions laid down in the Banking Act referring to credit institutions gradually, so as to be fully compliant by February 2004.

Decree on the Supervision of Banks and Savings Banks on a Consolidated Basis

Banks, which control or have a holding in one or more other banks, other financial institutions or companies for ancillary banking services are subject to consolidated supervision. Such banks shall comply with the minimum capital requirements on a consolidated basis, the capital adequacy requirement, limits set with regard to exposure of the entire group to a single counterparty or groups of related counterparties, and they shall observe restraints imposed on equity investments in non-financial institutions. Adequate internal audit department shall be set up with the aim of ensuring transparent and comprehensive information essential to effective consolidated supervision.

Decision (Decree) on Deposit-Guarantee Scheme

Key points introduced in line with the Decree are presented in a separate section of this Report.

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28 Also referred to as Decree on the Determing of the Documentation Serving as a Basis of Assessment of a Foreign Bank,s Branch Capacity to Perform the Services which are the Object of the foreign Bank,s Application for an Authorisation to Establish a Branch Office.

Instructions for Preparation of Reports on Major Depositors

The Instructions stipulate that banks shall report on a monthly basis on deposits of thirty largest depositors. In addition to the amount of the respective deposit placed by an individual depositor, the report shall include data on the currency in which the deposit was made, initial and maturity date in case of time deposits, the method of accruing interest, and the interest rate applied.

Instructions for the Implementation of the Decree on the Classification of On-Balance Sheet Assets and Off-Balance Sheet Items as well as of the Decree on Establishing Specific Provisions of Banks and Savings Banks

The Instructions prescribe the content, form and manner of compliance and submission of prudential reports on the classification of on- and off-balance sheet items and specific provisions made by banks and savings banks. Banks are obliged to submit these reports quarterly.

Instructions for Preparation of Reports on Movements in Tolar Liquidity

In accordance with the Instructions, banks shall report on a daily basis on expected flows of tolar-denominated funds for the current and the following business day, as well as on expected inflows and outflows for five largest depositors. Banks are to plan inflows and outflows in tolars in compliance with standards and principles of prudent banking. In other words, banks may include only inflows that can be reasonably expected to be effected on the due date, whereas outflows shall include all liabilities that fall due on a particular day.

Instructions for Calculation of Some Common Interest Rates on Deposits from Non-Bank Sector and Loans to Non-Bank Sector

The Instructions stipulate that banks and savings banks shall calculate on a quarterly basis certain significant lending and deposit interest rates classified on the basis of maturity and shown separately for the banking and the non-bank sector. In addition, deposits and loans and advances in domestic currency that earn base interest rate or that have been contracted with foreign currency clause have to be separated within each sector.

Instructions for Restructuring Claims of Banks and Savings Banks

The Instructions define which assets are eligible for restructuring, methods to be applied for the purpose of restructuring, and accounting standards and policies used in the process of restructuring and asset valuation. The Instructions elaborate on making provisions, write-offs, as well as suspending income, and classifying claims into different groups in case of a change in lending conditions. Write-offs and provisioning in case of the reduction of some claims are also addressed. In addition, the Instructions stipulate the method of valuation of tangible fixed assets and financial assets or a combination of both kinds of assets acquired for partial or full claim settlement. In this regard, the Instructions define write off, provisioning and suspension of income. The Instructions also stipulate the procedure to be followed when in the course of debt restructuring, a third party takes over the debt of the original borrower.

Instructions for Implementation of the Decree on Books of Account and Annual Report and Accounts of Banks and Savings Banks

The Instructions stipulate the methodology for the preparation of financial statements (balance sheet and profit and loss account) of banks and savings banks.

Instructions for Preparation of 10-Day Reports on Bank Accounts

The Instructions elaborate on the methodology for the preparation of reports submitted every ten days. These reports contain entries made by banks with regard to loans granted to and deposits accepted from the non-bank sector. Banks prepare such reports on 10th, 20th and the last day in a month.

Instructions for Submitting Monthly Reports on Balances on Banks' Accounts

The Instructions determine the content, the manner in which the statutory return is filled in, the form and the submission procedure, as well as the checking of the data on the book balances of accounts of banks and savings banks.

3. REFORM OF PAYMENT SYSTEMS AND CASH DISTRIBUTION REFORM

3.1. Payment Systems

Payment systems reform continue.

In 1999, consolidation of operation of the Real Time Gross Settlement System and the Giro Clearing, as well as preparations for the commencement of the transfer of accounts of legal entities from the Agency for Payments to banks took place. In addition, the payment systems reform - a joint project of the Bank of Slovenia, the Ministry of Finance, the Agency for Payments, commercial and savings banks, and the Bank Association of Slovenia - continued.

Consolidation of the Real Time Gross Settlement and the Giro Clearing

Consolidation of operations carried out in the ambit of both infrastructure systems has been focused on credit and debit transactions on giro accounts of legal entities with the Agency for Payments in the RTGS and the Giro Clearing system. By shifting payment transactions from the Agency for Payments these two payment systems, the volume of payment orders handled by the Agency dropped and the number of employees had to be adequately reduced. The process lasted from March 1999 to May 2000, and the Agency for Payments addressed the redundancy issue.

Preparations for the transfer of accounts of legal entities to commercial banks

The climax of the payment systems reform and its ultimate goal is to transfer accounts of legal entities and payments effected on their behalf and for their account of the Agency for Payments into the banking environment. As the payment systems reform went on, the following step was to launch pilot training for banks designed to equip them with knowledge and skills required for holding accounts of legal entities. The milestones of the pilot training programme for banks were put in place and large and medium-sized legal entities were selected for the participation in the pilot project:

- Accounts of legal entities are still kept with the Agency for Payments and the Agency continues to effect payments;
- Banks keep only the so-called shadow transaction account of legal entities;

- Legal entities establish business relations with a commercial bank and start to submit payment orders to the bank and receive statements of the account from the respective bank;
- Banks submit payment orders to the Agency for Payments on behalf and for the account of legal entities and are responsible for the correctness of payment orders submitted.

The checklist of goals identified within the framework of the pilot project is given below:

- Banks will be capable of handling accounts of legal entities including full-fledged payment and other associated services made on behalf and for the account of their clients,
- Banks will acquire know-how and skills necessary essential for the migration of accounts of legal entities to banks (the learning process is to involve both sides: banks and legal entities),
- All banks will be ready to start to take over accounts of legal entities on the same day,
- The ability of all banks to provide payment services will be re-examined/evaluated against relevant benchmarks.

Key objective of the payment systems reform is to transfer accounts of legal entities from the Agency for Payments to commercial banks.

In line with the documents drafted by the Bank of Slovenia, the Ministry of Finance and the Agency for Payments, the Government of the Republic of Slovenia has adopted the decision on gradual transfer of accounts of legal entities to commercial banks. The actual commencement date for the migration of accounts of legal entities will be proposed by the Bank of Slovenia and approved by the Ministry of Finance and the Board of the Agency for Payments. In accordance with operating plans for the take-over of accounts from the Agency for Payments, banks will gradually take over accounts of their depositors over seven quarters (banks are to prepare operating plans for each quarter and specify which legal entities are scheduled for the account transfer in a particular quarter), from the date of the commencement of the accounts transfer until the scheduled completion date on 30 September 2001. The initial delay in the commencement of the migration will be compensated over the following quarterly periods.

In accordance with the third paragraph of Article 73 of the Agency for Payments Act, criteria for the transfer of accounts of legal entities to banks have been laid down and endorsed by the Governor of the Bank of Slovenia and the Minister of Finance. Whether a bank is to be authorised to take over accounts of legal entities will depend on its compliance with the requirements set out in formal and technical criteria. A task force of the Bank of Slovenia has already examined organisational, technical and human resources banks have in place for the transfer of accounts of legal entities from the Agency for Payments to banks.

Establishment of central transaction account registry

Bank of Slovenia keeps central transaction accounts registry.

For the purpose of providing technical support to banks in the course of the migration of accounts of legal entities from the Agency for Payments into the banking environment, the Bank of Slovenia has set up a central transaction accounts registry. The registry serves as a master database with data on transaction accounts of legal entities kept with banks. In the first phase, only accounts of legal entities and sole traders are in the central transaction accounts registry, whereas transaction accounts of individuals will be eventually logged on as the payment systems reforms continues.

The central transaction accounts registry has been put in place in order to ensure regularity of payment transactions through the control of transaction accounts. At the same time, the registry will serve as a source of information and data on holders of accounts. Such information will be available to institutions duly authorised under law to get insight into the data kept in the registry.

Single treasury account

An essential segment of the project undertaken with the aim of overhauling the payment systems are also activities in connection with the opening of the single treasury account in the Bank of Slovenia. The project was launched at the end of 1998 and called for co-ordinated efforts of both the Ministry of Finance and of the Bank of Slovenia. The project was successfully completed by opening the single treasury account (STA) in June 1999.

Payment Operations Act

Bill of a new law on payment transactions is in the pipeline.

The pace of the payment systems reform gained momentum in 1999 when efforts to complete a draft of the new law on payment transactions intensified. Under the guidance of the Ministry of Finance, a team composed of the representatives of the Ministry of Finance, the Agency for Payments and of the Bank of Slovenia. The draft was eventually amended on the basis of comments and proposals of the Agency for Payments and the Bank of Slovenia, but suggestions submitted by other ministries, the Legislation Office of the Government the Republic of Slovenia, as well as remarks given at the sessions of relevant parliamentary committees for the Corporate Sector and the Government Committee for State and Public Affairs have also been meaningfully incorporated. The Government of the Republic of Slovenia has submitted the bill of the Payment Operations Act to the National Assembly for the so-called second reading.

The bill essentially covers two basic parts. The first part of the bill addresses issues in connection with payment services: direct relationship between participants in payment systems and consequences which arise as the result of these relations, and payment systems as a publicly recognised institutional infrastructure. The second part of the bill addresses issues in connection with the transfer of payment transactions in accordance with agreed procedures and methods for the completion of this transfer to be stipulated by the Ministry of Finance and the Bank of Slovenia. The bill also deals with the method of operations of the Agency for Payments during the transitional period and sets the time limit for the winding up of banking operations provided by the Agency. For the purpose of ensuring continuity of all tasks and responsibilities conferred upon the Agency for Payments, the bill also stipulates the establishment of the Agency for Public Records and Services and the Bureau for Public Payments. The former is a public institution with a mandate to provide statistical analysis of payment operations, while the latter will operate within the framework of the Ministry of Finance responsible for the procurement of information on public revenue and expenditures and for payment instructions which debit and/or credit the single treasury account with the Bank of Slovenia.

3.2. Cash Distribution Reform

Migration of cash payment transactions to banks addresses both direct and indirect supply of banks with banknote and the transfer of incoming and outgoing payment transactions from the Agency for Payments to banks.

Banknote distribution is organised by the Bank of Slovenia through depots set up by commercial banks as contractual providers of this type.

The Bank of Slovenia is responsible for the distribution of banknotes through a system of contractual depots run by commercial banks – depositories - where banknotes are kept.

As from 1 July 1999, there are eight depots of banknotes in Slovenia operating at different locations in the ambit of seven commercial banks – depositories and one depot (vault) for coins. The depots are exclusively intended for the supply of banks with banknotes.

For the purpose of running the depot network, a software application has been installed in the Bank of Slovenia and in each depository bank. Thus all changes in total balance and per each denomination are promptly recorded. A computer system – BSNet – is used for the exchange of messages between the depositor (the Bank of Slovenia) and the depository as well as between depository and banks, while payments are effected through the Real Time Gross Settlement system and the S.W.I.F.T. network following standard procedures.

In line with commitment to curb costs, only one depot for coins has been set up, and the supply channel for coins is independent from the distribution channel for banknotes. By setting up a depot (vault) for coins, all aspects of banking operations involving coins have been upgraded including the organisational, technical, logistics and security infrastructure.

As from 30 September 1999 when the transitional period expired, banks and savings banks have been supplied with cash from the depots of banknotes and from the depot (vault) for coins. Thus the project launched in the Bank of Slovenia for the distribution of banknotes and coins to banks was successfully completed.

A joint working group composed of the representatives of the Agency for Payments of the Republic of Slovenia, commercial banks and the Bank of Slovenia has drafted a model for the migration of cash operations effected on behalf and for the account of legal entities to commercial banks. The milestones envisaged test periods for the following transactions:

- the migration of incoming cash payments made by legal entities to banks was successfully completed on 28 February 1999 and the transaction was incorporated in routine operating activities of banks, and
- the migration of outgoing cash payments made by legal entities to banks was completed on 1 September 1999 and the transaction was incorporated in routine operating activities of banks.

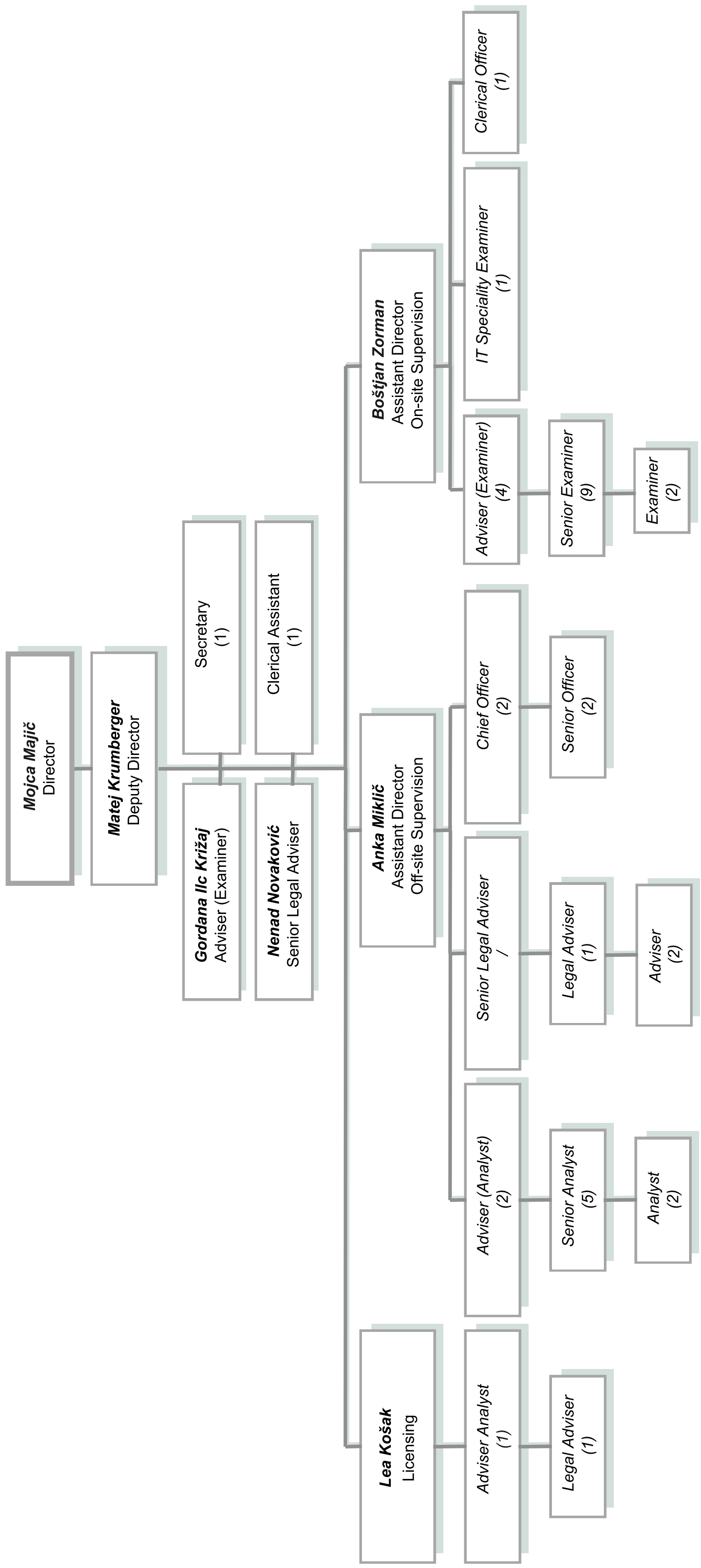
Prepared by: Bank Supervision Department
(Gordana Ilc Križaj and co-workers) and
Payments Systems and Banknote Department
(Reform of Payment Systems)

Samo Nučič
Deputy Governor

Mojca Majič, M.A.
Director
Banking Supervision

APPENDIX 1

ORGANISATIONAL STRUCTURE OF THE BANK SUPERVISION DEPARTMENT AS AT 30 SEPTEMBER 2000



APPENDIX 2

TOTAL NUMBER OF BANKS AND SAVINGS BANKS AND OWNERSHIP STRUCTURE

1. Number of operating banks and savings banks

	31 Dec 1992	31 Dec 1993	31 Dec 1994	31 Dec 1995	31 Dec 1996	31 Dec 1997	31 Dec 1998	31 Dec 1999	30 Jun 2000
Banks [1]	30	32	33	31	29	28	24	25	25
Savings banks	15	13	11	8	7	6	6	6	6

2. Number of banks with majority foreign share [2]

	31 Dec 1992	31 Dec 1993	31 Dec 1994	31 Dec 1995	31 Dec 1996	31 Dec 1997	31 Dec 1998	31 Dec 1999	30 Jun 2000
Banks [1]	2	5	6	6	4	4	3	5	5

3. Number of banks with majority state share [3]

	31 Dec 1992	31 Dec	31 Dec 1994	31 Dec 1995	31 Dec 1996	31 Dec 1997	31 Dec 1998	31 Dec 1999	30 Jun 2000
Banks	1	3	3	3	3	3	3	3	3

1 Foreign branch established in 1999 included.

2 Foreign-owned stake over 50%; all savings banks are owned by domestic shareholders.

3 State ownership over 50%; Poštna banka Slovenije d.d. (Slovenian Post Office Bank) is included in the figures. From the establishment until 31 December 1994 fully owned by PTT company, from 1 January 1995 to 20 December 1996 fully owned by the Republic of Slovenia, since 21 December 1996 owned by Pošta Slovenije d.o.o., Maribor (established by the Republic of Slovenia).

APPENDIX 3

TOTAL ASSETS AND OFF-BALANCE SHEET ITEMS OF BANKS AND SAVINGS BANKS

4. Total assets

in billions of Tolars

	31 Dec 1993	31 Dec 1994	31 Dec 1995	31 Dec 1996	31 Dec 1997	31 Dec 1998	31 Dec 1999	30 Jun 2000 [1]
Banks	937.2	1,183.4	1,497.5	1,729.0	2,022.0	2,350.4	2,687.6	2,927.6
Savings banks	2.1	2.7	4.4	5.1	7.2	9.5	11.0	12.0

4.a. Growth rate of total assets

in %

	31 Dec 1993	31 Dec 1994	31 Dec 1995	31 Dec 1996	31 Dec 1997	31 Dec 1998	31 Dec 1999	30 Jun 2000 [1]
Banks	49.3	26.3	26.5	15.5	16.9	16.2	14.3	8.9
Savings banks	-19.2	28.6	63.0	15.9	41.2	31.9	15.8	9.1

5. Risk-weighted off-balance sheet items[2]

in billions of Tolars

	31 Dec 1993	31 Dec 1994	31 Dec 1995	31 Dec 1996	31 Dec 1997	31 Dec 1998	31 Dec 1999	30 Jun 2000 [1]
Banks	288.7	292.5	347.0	338.9	382.6	503.7	568.5	632.9
Savings banks	0.059	0.004	0.027	0.122	0.036	0.093	0.088	0.120

5.a. Growth rate of risk-weighted off-balance sheet items

in %

	31 Dec 1993	31 Dec 1994	31 Dec 1995	31 Dec 1996	31 Dec 1997	31 Dec 1998	31 Dec 1999	30 Jun 2000 [1]
Banks		1.3	18.6	-2.3	12.9	31.7	12.9	11.3
Savings banks		-93.2	575.0	351.9	-70.5	158.3	-5.5	36.6

1 Figures excluding NLB Branch in Italy. Figures as at 30 June 2000 are unaudited.

2 Off-balance sheet items include guarantees, letters of credit, endorsed and accepted bills of exchange, irrevocable commitments and other.

APPENDIX 4

LENDING OF BANKS AND SAVINGS BANKS TO CUSTOMERS AND DEPOSITS FROM CUSTOMERS

6. Lending to non-banks

in billions of Tolars

	31 Dec 1993	31 Dec 1994	31 Dec 1995	31 Dec 1996	31 Dec 1997	31 Dec 1998	31 Dec 1999	30 Jun 2000[1]
Banks	347.3	416.4	607.9	725.6	862.4	1,108.8	1,388.4	1,500.6
Savings banks	1.4	1.9	3.2	4.0	5.2	7.1	8.8	10.3

6.a. Growth rate of lending to non-banks

in %

	31 Dec 1993	31 Dec 1994	31 Dec 1995	31 Dec 1996	31 Dec 1997	31 Dec 1998	31 Dec 1999	30 Jun 2000[1]
Banks	53.5	19.9	46.0	19.4	18.9	28.6	25.2	8.1
Savings banks	-12.5	35.7	68.4	25.0	30.0	36.5	23.9	17.0

7. Deposits from non-banks

in billions of Tolars

	31 Dec 1993	31 Dec 1994	31 Dec 1995	31 Dec 1996	31 Dec 1997	31 Dec 1998	31 Dec 1999	30 Jun 2000[1]
Banks	492	712.6	916.6	1,169.4	1,412.2	1,667.7	1,859.0	2,007.5
Savings banks	1.6	1.7	2.8	3.2	4.6	6.0	7.7	8.6

7.a. Growth rate of deposits from non-banks

in %

	31 Dec 1993	31 Dec 1994	31 Dec 1995	31 Dec 1996	31 Dec 1997	31 Dec 1998	31 Dec 1999	30 Jun 2000[1]
Banks	64.1	44.8	28.6	27.6	20.8	18.1	11.5	8.0
Savings banks	-27.3	6.3	64.7	14.3	43.8	30.4	28.5	11.7

[1] Figures as at 30 June 2000 are unaudited.

APPENDIX 5

TOTAL ASSETS AND MARKET SHARE OF SLOVENIAN BANKS

in millions of Tolars / in %

	Banks	Total Assets				Market Shares			
		31 Dec 1997	31 Dec 1998	31 Dec 1999	30 Jun 2000[1]	31 Dec 1997	31 Dec 1998	31 Dec 1999	30 Jun 2000[1]
1	Nova Ljubljanska banka d.d. Ljubljana	549,225	648,595	752,343	813,447[2]	27.2	27.6	28.0	27.8[2]
2	Nova Kreditna banka d.d. Maribor	237,654	285,029	321,813	348,631	11.8	12.1	12.0	11.9
3	SKB d.d. Ljubljana	241,010	281,184	307,637	312,969	11.9	12.0	11.4	10.7
4	Banka Koper d.d. Koper	120,299	137,190	167,905	187,082	5.9	5.8	6.2	6.4
5	Abanka d.d. Ljubljana	103,055	123,151	149,301	174,363	5.1	5.2	5.6	6.0
6	Banka Celje d.d. Celje	109,246	135,094	155,712	169,350	5.4	5.7	5.8	5.8
7	Gorenjska banka d.d. Kranj	90,706	108,041	130,310	144,472	4.5	4.6	4.8	4.9
8	Dolenjska banka d.d. Novo mesto	64,675	77,476	87,574	91,804	3.2	3.3	3.3	3.1
9	Bank Austria Creditanstalt d.d. Ljubljana	49,808	83,379	83,633	88,964	2.5	3.5	3.1	3.0
10	Pomurska banka d.d. M. Sobota, Bs NLB	51,426	55,936	62,138	67,231	2.5	2.4	2.3	2.3
11	Krekova banka d.d. Maribor	40,092	50,868	57,811	60,843	2.0	2.2	2.2	2.1
12	Banka VIPA d.d. Nova Gorica	43,378	49,446	54,114	57,259	2.1	2.1	2.0	2.0
13	Poštna banka Slovenije d.d. Maribor	24,927	37,500	47,811	56,139	1.2	1.6	1.8	1.9
14	Probanka d.d. Maribor	29,434	34,204	40,982	46,977	1.5	1.5	1.5	1.6
15	SZKB d.d. Ljubljana	29,263	36,930	41,552	43,010	1.4	1.6	1.5	1.5
16	Koroška banka d.d. Sl. Gradec, Bs NLB	29,351	33,493	38,013	42,439	1.5	1.4	1.4	1.4
17	Banka Domžale d.d. Domžale, Bs NLB	27,852	32,967	38,023	41,414	1.4	1.4	1.4	1.4
18	Banka Velenje d.d. Velenje, Bs NLB	27,505	32,395	37,343	39,612	1.4	1.4	1.4	1.4
19	Volksbank-Ljudska banka d.d. Ljubljana	17,149	19,730	24,311	28,361	0.8	0.8	0.9	1.0
20	Banka Zasavje d.d. Trbovlje, Bs NLB	19,921	26,157	25,976	28,081	1.0	1.1	1.0	1.0
21	S I B d.d. Ljubljana	20,137	21,249	24,595	26,199	1.0	0.9	0.9	0.9
22	Factor banka d.d. Ljubljana	13,450	14,913	17,490	22,280	0.7	0.6	0.7	0.8
23	Hypo Alpe Adria banka d.d. Ljubljana			10,392	18,008	0.0	0.0	0.4	0.6
24	Banka Societe Generale d.d. Ljubljana	10,649	11,205	9,568	13,426	0.5	0.5	0.4	0.5
25	Kaerntner Sparkasse, Branch office			1,254	5,274	0.0		0.0	0.2
26	Banka Creditanstalt d.d. Ljubljana	31,232				1.5			
27	M banka d.d. Ljubljana, Bs Banke Koper	13,501	14,227			0.7	0.6		
28	UBK banka d.d. Ljubljana, Bs SKB	12,511				0.6			
29	Hmezad banka d.d. Žalec, Bs Banke Celje	11,481				0.6			
30	Hipotekarna banka d.d. Brežice	3,099				0.2			
	Total	**2,022,036**	**2,350,359**	**2,687,600**	**2,927,635**	**100.0**	**100.0**	**100.0**	**100.0**

1 Figures as at 30 June 2000 are unaudited.

2 Figures do not include NLB branch in Italy.

APPENDIX 6

BALANCE SHEET OF SLOVENIAN BANKS

in millions of Tolars

Item. No.	Balance Sheet Designation		DESCRIPTION	31 Dec 1994	31 Dec 1995	31 Dec 1996	31 Dec 1997	31 Dec 1998	31 Dec 1999	30 Jun 2000[1]
1.	A.	I.	Cash in hand and balances with Central Bank	39,602	58,786	58,475	73,888	84,696	88,761	98,058
2.	A.	II.	Government securities and other bills eligible for discount by Central Bank	0	0	0	0	0	0	0
3.	A.	III.	Loans and advances to banks and savings banks	248,059	253,566	309,936	214,874	227,331	252,615	293,165
4.	A.	IV.	Loans and advances to customers	417,233	607,884	725,610	862,406	1,108,798	1,388,440	1,500,557
5.	A.	V.	Investment securities	316,257	387,411	449,161	628,059	615,876	584,586	618,332
6.	A.	VI.	Securities held for dealing purposes	20,686	27,293	29,436	61,563	98,690	124,036	132,816
7.	A.	VII.	Investments in non-associated companies	16,400	16,082	15,996	15,650	16,173	25,096	27,533
8.	A.	VIII.	Investments in associated companies	6,727	10,022	11,499	16,168	31,479	34,743	35,639
9.	A.	IX.	Intagible assets	974	1,350	2,311	3,625	5,011	8,912	9,037
10.	A.	X.	Tangible fixed assets	49,403	56,748	60,877	73,223	77,863	92,606	94,417
11.	A.	XI.	Subscribed capital unpaid	1,262	0	0	0	0	0	0
12.	A.	XII.	Own shares	5,235	3,486	3,231	2,421	2,026	2,195	2,207
13.	A.	XIII.	Other assets	55,997	65,063	53,266	56,529	67,979	70,809	98,980
14.	A.	XIV.	Prepayments and accrued income	5,587	9,854	9,287	13,629	14,437	14,802	16,894
			TOTAL ASSETS	**1,183,423**	**1,497,544**	**1,729,083**	**2,022,037**	**2,350,359**	**2,687,600**	**2,927,635**
15.	P.	I.	Deposits and borrowings from banks and savings banks	205,836	236,602	213,852	204,084	223,738	309,002	322,469
16.	P.	II.	Deposits and borrowings from customers	712,624	916,608	1,169,449	1,412,196	1,667,695	1,859,009	2,007,504
17.	P.	III.	Liabilities evidenced by paper	20,782	45,066	37,082	52,418	57,649	44,755	54,684
18.	P.	IV.	Other liabilities	16,871	24,316	18,726	22,827	22,595	24,025	49,222
19.	P.	V.	Accruals and deferred income	55,098	65,402	56,920	66,547	79,958	91,937	114,832
20.	P.	VI.	Provision for liabilities and charges	30,172	32,905	35,518	36,218	42,443	49,258	55,702
21.	P.	VII.	General banking risks	0	0	0	0	0	4,502	5,272
22.	P.	VIII.	Subordinated liabilities	0	0	0	0	0	25,831	35,181
23.	P.	IX.	Subscribed capital	48,963	56,695	56,789	60,385	54,925	58,765	64,178
24.	P.	X.	Share premium account	6,696	10,094	8,420	7,720	7,681	9,029	7,778
25.	P.	XI.	Reserves	67,363	68,129	72,891	77,512	94,882	98,490	97,605
26.	P.	XII.	Capital revaluation adjustment	18,596	31,203	44,580	62,338	76,154	92,633	102,869
27.	P.	XIII.	Net profit or loss brought forward	65	-447	1,127	4,393	6,578	10,292	15,883
28.	P.	XIV.	Net profit or loss for the financial year	358	10,971	13,729	15,398	16,061	10,073	-5,544
			TOTAL LIABILITIES	**1,183,423**	**1,497,544**	**1,729,083**	**2,022,037**	**2,350,359**	**2,687,600**	**2,927,635**
29.	B.		OFF-BALANCE SHEET ITEMS (B.1. - B.3.)	402,723	509,513	489,456	615,597	758,145	942,196	1,040,580
			Total assets - average of the year [2]	1,060,858	1,324,570	1,640,467	1,879,618	2,184,297	2,541,098	2,822,701
			Number of banks	33	31	29	28	24	25	25

1 Figures as at 30 June 2000 are unaudited.

2 Calculated as average balance at month-end.

COMPOSITION OF THE BALANCE SHEET OF BANKS

as % of total assets at month-end

Item. No.	Balance Sheet Designation		DESCRIPTION	31 Dec 1994	31 Dec 1995	31 Dec 1996	31 Dec 1997	31 Dec 1998	31 Dec 1999	30 Jun 2000 [1]
1.	A.	I.	Cash in hand and balances with Central Bank	3.3	3.9	3.4	3.7	3.6	3.3	3.3
2.	A.	II.	Government securities and other bills eligible for discount by Central Bank	0.0	0.0	0.0	0.0	0.0	0.0	0.0
3.	A.	III.	Loans and advances to banks and savings banks	21.0	16.9	17.9	10.6	9.7	9.4	10.0
4.	A.	IV.	Loans and advances to customers	35.3	40.6	42.0	42.7	47.2	51.7	51.3
5.	A.	V.	Investment securities	26.7	25.9	26.0	31.1	26.2	21.8	21.1
6.	A.	VI.	Securities held for dealing purposes	1.7	1.8	1.7	3.0	4.2	4.6	4.5
7.	A.	VII.	Investments in non-associated companies	1.4	1.1	0.9	0.8	0.7	0.9	0.9
8.	A.	VIII.	Investments in associated companies	0.6	0.7	0.7	0.8	1.3	1.3	1.2
9.	A.	IX.	Intagible assets	0.1	0.1	0.1	0.2	0.2	0.3	0.3
10.	A.	X.	Tangible fixed assets	4.2	3.8	3.5	3.6	3.3	3.4	3.2
11.	A.	XI.	Subscribed capital unpaid	0.1	0.0	0.0	0.0	0.0	0.0	0.0
12.	A.	XII.	Own shares	0.4	0.2	0.2	0.1	0.1	0.1	0.1
13.	A.	XIII.	Other assets	4.7	4.3	3.1	2.8	2.9	2.6	3.4
14.	A.	XIV.	Prepayments and accrued income	0.5	0.7	0.5	0.7	0.6	0.6	0.6
			TOTAL ASSETS	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**
15.	P.	I.	Deposits and borrowings from banks and savings banks	17.4	15.8	12.4	10.1	9.5	11.5	11.0
16.	P.	II.	Deposits and borrowings from customers	60.2	61.2	67.6	69.8	71.0	69.2	68.6
17.	P.	III.	Liabilities evidenced by paper	1.8	3.0	2.1	2.6	2.5	1.7	1.9
18.	P.	IV.	Other liabilities	1.4	1.6	1.1	1.1	1.0	0.9	1.7
19.	P.	V.	Accruals and deferred income	4.7	4.4	3.3	3.3	3.4	3.4	3.9
20.	P.	VI.	Provision for liabilities and charges	2.5	2.2	2.1	1.8	1.8	1.8	1.9
21.	P.	VII.	General banking risks	0.0	0.0	0.0	0.0	0.0	0.2	0.2
22.	P.	VIII.	Subordinated liabilities	0.0	0.0	0.0	0.0	0.0	1.0	1.2
23.	P.	IX.	Subscribed capital	4.1	3.8	3.3	3.0	2.3	2.2	2.2
24.	P.	X.	Share premium account	0.6	0.7	0.5	0.4	0.3	0.3	0.3
25.	P.	XI.	Reserves	5.7	4.5	4.2	3.8	4.0	3.7	3.3
26.	P.	XII.	Capital revaluation adjustment	1.6	2.1	2.6	3.1	3.2	3.4	3.5
27.	P.	XIII.	Net profit or loss brought forward	0.0	0.0	0.1	0.2	0.3	0.4	0.5
28.	P.	XIV.	Net profit or loss for the financial year	0.0	0.7	0.8	0.8	0.7	0.4	-0.2
			TOTAL LIABILITIES	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**
29.	B.		OFF-BALANCE SHEET ITEMS (B.1. - B.3.)	34.0	34.0	28.3	30.4	32.3	35.1	35.5

[1] Figures as at 30 June 1999 are unaudited.

APPENDIX 8

PROFIT AND LOSS ACCOUNT OF BANKS

in millions of Tolars

	1994	1995	1996	1997	1998	1999	Jan - Jun 2000 [1]
1. Interest income	136,038	242,324	266,484	293,258	280,785	300,353	206,346
2. Interest expense	101,244	183,615	183,790	208,746	190,632	205,583	147,128
3. Net interest income	34,794	58,709	82,694	84,512	90,153	94,770	59,217
4. Net other income	9,284	14,291	9,430	16,926	20,437	26,173	10,548
- net fees and commisions	11,695	19,736	23,627	26,923	30,206	33,726	18,280
- net financial transactions	7,194	8,386	-886	7,462	6,691	9,541	2,033
- other income [2]	-9,605	-13,832	-13,310	-17,460	-16,460	-17,094	-9,766
5. Gross income (3+4)	44,078	73,000	92,124	101,438	110,590	120,944	69,765
6. General administrative expenses	28,151	42,280	50,293	58,111	65,808	74,408	38,811
- labour costs	1,921	26,911	31,843	35,361	38,343	43,701	22,646
7. Net income (5-6)	15,927	30,720	41,831	43,327	44,782	46,536	30,954
8. Net provisions and write-offs	-11,253	-16,962	-23,489	-22,240	-18,806	-26,401	-14,288
9. Profit before taxation (7-8)	4,673	13,759	18,342	21,087	25,976	20,134	16,666
10. Taxation	243	1,487	2,550	5,747	9,915	10,085	
11. Profit after taxation (9-10)	4,430	12,271	15,792	15,340	16,061	10,049	16,666

1 Figures for the period Jan - Jun 2000 are unaudited.

2 Other income = other operating profit + extraordinary income - depreciation and amortization - other operating expense - revaluation of capital, fixed assets and capital investments - extraordinary expense.

APPENDIX 9

COMPOSITION OF THE PROFIT AND LOSS ACCOUNT OF BANKS

as % of average total assets

		1994	1995	1996	1997	1998	1999	Jan - Jun 2000 [1]
1.	Interest income	12.8	18.3	16.2	15.6	12.9	11.8	7.3
2.	Interest expense	9.5	13.9	11.2	11.1	8.7	8.1	5.2
3.	Net interest income	3.3	4.4	5.0	4.5	4.1	3.7	2.1
4.	Net other income	0.9	1.1	0.6	0.9	0.9	1.0	0.4
	- net fees and commisions	1.1	1.5	1.4	1.4	1.4	1.3	0.6
	- net financial transactions	0.7	0.6	-0.1	0.4	0.3	0.4	0.1
	- other income [2]	-0.9	-1.0	-0.8	-0.9	-0.8	-0.7	-0.3
5.	Gross income (3+4)	4.2	5.5	5.6	5.4	5.1	4.8	2.5
6.	General administrative expenses	2.7	3.2	3.1	3.1	3.0	2.9	1.4
	- labour costs	0.2	2.0	1.9	1.9	1.8	1.7	0.8
7.	Net income (5-6)	1.5	2.3	2.5	2.3	2.1	1.8	1.1
8.	Net provisions and write-offs	-1.1	-1.3	-1.4	-1.2	-0.9	-1.0	-0.5
9.	Profit before taxation (7-8)	0.4	1.0	1.1	1.1	1.2	0.8	0.6
10.	Taxation	0.0	0.1	0.2	0.3	0.5	0.4	0.0
11.	Profit after taxation (9-10)	0.4	0.9	1.0	0.8	0.7	0.4	0.6

1 Figures for the period Jan-Jun 2000 are unaudited.

2 Other income = other operating profit + extraordinary income - depreciation and amortization - other operating expense - revaluation of capital, fixed assets and capital investments - extraordinary expense.

APPENDIX 10

ITEMS FROM THE PROFIT AND LOSS ACCOUNT IN BANKS' INCOME

in %

		1994	1995	1996	1997	1998	1999	Jan - Jun 2000[1]
	% of gross income							
1.	Net interest income	78.9	80.4	89.8	83.3	81.5	78.4	84.9
2.	Net non-interest income	21.1	19.6	10.2	16.7	18.5	21.6	15.1
	- net fees and commissions	26.5	27.0	25.6	26.5	27.3	27.9	26.2
	- net financial transactions	16.3	11.5	-1.0	7.4	6.1	7.9	2.9
	- other	-21.8	-18.9	-14.4	-17.2	-14.9	-14.1	-14.0
3.	General administrative expenses	63.9	57.9	54.6	57.3	59.5	61.5	55.6
	labour costs	4.4	36.9	34.6	34.9	34.7	36.1	32.5
4.	Net income[2]	36.1	42.1	45.4	42.7	40.5	38.5	44.4
5.	Net provisions and write-offs	-25.5	-23.2	-25.5	-21.9	-17.0	-21.8	-20.5
6.	Profit before taxation	10.6	18.8	19.9	20.8	23.5	16.6	23.9
7.	Taxation	0.6	2.0	2.8	5.7	9.0	8.3	
8.	Profit after taxation	10.1	16.8	17.1	15.1	14.5	8.3	23.9
	% of net income							
1.	Net provisions and write-offs	-70.7	-55.2	-56.2	-51.3	-42.0	-56.7	-46.2
2.	Profit before taxation	29.3	44.8	43.8	48.7	58.0	43.3	53.8
3.	Taxation	1.5	4.8	6.1	13.3	22.1	21.7	
4.	Profit after taxation	27.8	39.9	37.8	35.4	35.9	21.6	53.8

1 Figures for the period Jan - Jun 2000 are unaudited.

2 Net income = Gross income - general administrative expenses

APPENDIX 11

RATIOS IN THE SLOVENIAN BANKING INDUSTRY

in %

		31 Dec 1994	31 Dec 1995	31 Dec 1996	31 Dec 1997	31 Dec 1998	31 Dec 1999	30 Jun 2000 [1]
I. Capital adequacy	1. Regulatory capital / Risk-weighted assets	20.5	21.5	19.7	19.0	16.0	14.0	13.6
	2. Core capital / Risk-weighted assets	17.8	19.5	18.2	17.6	15.6	14.0	13.2
II. Asset quality	1. Value adjustments / Bad and doubtful claims	52.7	51.0	58.4	59.2	56.1	54.6	54.1
	2. Bad and doubtful claims / Gross assets	12.0	11.0	10.3	9.4	10.9	11.6	11.9
III. Profitability	1. Net interest margin[2]	3.7	4.9	5.6	4.9	4.5	4.0	4.6
	2. Return on average assets	0.4	1.0	1.1	1.1	1.2	0.8	1.2
	3. Return on average equity	4.0	9.2	10.3	10.3	11.3	7.8	12.2
	4. Net provisions and write-offs / Net income	70.7	55.2	56.2	51.3	42.0	56.7	46.2
IV. Liquidity	1. Average liquid assets / Average demand deposits	21.5	21.7	17.7	23.4	26.8	25.9	24.3
	2. Average demand deposits / Average total liabilities (equity excl.)	27.7	28.6	28.8	28.7	27.1	28.1	27.6
V. Operating expenses	1. Labour costs / Average total assets	1.7	2.0	1.9	1.9	1.8	1.7	1.6
	2. Net non-interest income / Operating costs	42.2	44.2	29.7	39.4	41.2	44.8	37.9

1 Figures for the period ended 30 June 1999 are unaudited.

2 Net interest margin is calculated as the ratio between net interest income (real and revaluation interest) and average gross interest - bearing assets.

APPENDIX 12

NON-PERFORMING ON- AND OFF-BALANCE SHEET ITEMS IN BANKS

Non-performing on- and off-balance sheet items

All banks	31 Dec 1994	31 Dec 1995	31 Dec 1996	31 Dec 1997	31 Dec 1998	31 Dec 1999	30 Jun 2000[1]
Non-performing assets[2] (in millions of Tolars)	91,638	80,169	104,118	107,969	126,651	141,702	157,285
Non-performing assets / Total assets	8.1%	5.8%	6.4%	5.6%	5.7%	5.6%	5.7%
Non-performing assets and off-balance sheet items[3] (in millions of Tolars)	115,837	101,603	124,386	126,240	147,514	161,428	177,774
Non-performing assets and off-balance sheet items / Total assets and off-balance sheet items	8.2%	5.8%	6.2%	5.5%	5.4%	5.2%	5.2%

Bad on- and off-balance sheet items

All banks	31 Dec 1994	31 Dec 1995	31 Dec 1996	31 Dec 1997	31 Dec 1998	31 Dec 1999	30 Jun 2000[1]
Bad assets[4] (in millions of Tolars)	62,026	55,402	64,315	64,120	81,545	88,227	91,091
Bad assets / Total assets	5.5%	4.0%	4.0%	3.3%	3.7%	3.5%	3.3%
Bad assets and off-balance sheet items[5] (in millions of Tolars)	80,723	68,560	76,921	73,246	91,179	98,306	102,064
Bad assets and off-balance sheet items / Total assets and off-balance sheet items	5.7%	3.9%	3.8%	3.2%	3.3%	3.2%	3.0%

1 Figures as at 30 June 2000 are unaudited.

2 Non-performing assets are defined as all on-balance sheet items classified in groups C (substandard), D (doubtful) and E (loss).

3 Non-performing assets and off-balance sheet items are defined as all on- and off-balance sheet items classified in groups C (substandard), D (doubtful) and E (loss).

4 Bad assets are defined as all on-balance sheet items classified in groups D (doubtful) and E (loss).

5 Bad assets and off-balance sheet items are defined as all on- and off-balance sheet items classified in groups D (doubtful) and E (loss).

APPENDIX 13

STRUCTURE OF AGGREGATE (ON- AND OFF-BALANCE SHEET) EXPOSURE OF BANKS PER TYPE OF ACTIVITY

in millions of Tolars, in %

ACTIVITY	31 Dec 1994	Share	31 Dec 1995	Share	31 Dec 1996	Share	31 Dec 1997	Share	31 Dec 1998	Share	31 Dec 1999	Share	30 Jun 2000 [1]	Share
A. CORPORATE SECTOR	**1,070,587**	**74.6**	**1,289,088**	**72.8**	**1,436,658**	**71.3**	**1,753,786**	**75.3**	**2,117,982**	**76.3**	**2,381,241**	**75.1**	**2,583,472**	**74.3**
1. Agriculture, hunting and forestry	10,054	0.7	12,195	0.7	13,413	0.7	13,614	0.6	15,796	0.6	17,821	0.6	16,521	0.5
2. Fishing	174	0.0	187	0.0	220	0.0	280	0.0	303	0.0	300	0.0	280	0.0
3. Mining and quarrying	541	0.0	956	0.1	4,496	0.2	5,518	0.2	4,831	0.2	6,590	0.2	5,987	0.2
4. Manufactoring	193,658	13.5	259,851	14.7	278,894	13.8	302,348	13.0	377,898	13.6	426,675	13.5	470,824	13.5
4.1. Manufacture of food products; beverages and tobaco	15,395	1.1	23,893	1.3	24,341	1.2	31,023	1.3	48,596	1.8	57,656	1.8	61,632	1.8
4.2. Manufacture of textiles and textile products and manufacture of leather products	25,584	1.8	31,086	1.8	31,859	1.6	34,769	1.5	39,207	1.4	44,360	1.4	46,875	1.3
4.3. Manufacture of wood and wood products and manufacture of paper and paper products	30,377	2.1	33,378	1.9	35,694	1.8	37,457	1.6	41,553	1.5	47,539	1.5	53,123	1.5
4.4. Manufacture of chemical, chemical products and man made fibres	29,344	2.0	45,667	2.6	48,004	2.4	52,341	2.2	77,025	2.8	79,666	2.5	97,470	2.8
4.5. Manufacture of basis metals and fabricated metal products and manufacture of machinery and equipment	43,925	3.1	55,794	3.2	63,317	3.1	69,831	3.0	79,806	2.9	99,738	3.1	111,187	3.2
4.6. Manufacture of electrical and optical equipment	20,929	1.5	29,169	1.6	31,225	1.5	31,374	1.3	40,357	1.5	44,829	1.4	47,726	1.4
4.7. Manufacture of transport equipment	20,123	1.4	30,498	1.7	31,612	1.6	31,818	1.4	35,450	1.3	33,604	1.1	31,796	0.9
4.8. Manufacture of furniture, manufacturing not elswhere classified and recycling	7,981	0.6	10,366	0.6	12,842	0.6	13,735	0.6	15,906	0.6	19,283	0.6	21,016	0.6
5. Electricity, gas and water supply	49,846	3.5	57,932	3.3	57,859	2.9	61,325	2.6	109,237	3.9	111,774	3.5	98,611	2.8
6. Construction	27,527	1.9	31,900	1.8	35,953	1.8	51,297	2.2	75,817	2.7	102,762	3.2	110,315	3.2
7. Wholesale and retail trade; repair of motor vehicles, personal and household goods	90,941	6.3	135,477	7.6	165,200	8.2	205,612	8.8	266,753	9.6	347,658	11.0	387,511	11.2
8. Hotels and restaurants	6,603	0.5	11,940	0.7	16,360	0.8	21,481	0.9	27,567	1.0	38,642	1.2	41,169	1.2
9. Transport, storage and communications	66,466	4.6	55,126	3.1	64,817	3.2	70,177	3.0	108,571	3.9	150,082	4.7	169,617	4.9
10. Public administration and defence; compulsory social security [2]	147,834	10.3	290,770	16.4	317,261	15.7	351,583	15.1	368,947	13.3	415,733	13.1	444,242	12.8
11. Health and social work	4,929	0.3	5,690	0.3	5,968	0.3	6,458	0.3	8,087	0.3	8,882	0.3	9,228	0.3
12. Education	520	0.0	535	0.0	884	0.0	1,186	0.1	1,278	0.0	2,468	0.1	2,764	0.1
13. Other community, social and personal service activities	3,005	0.2	4,913	0.3	7,187	0.4	8,784	0.4	13,238	0.5	19,185	0.6	21,336	0.6
14. Financial intermediation [3]	323,964	22.6	250,557	14.1	299,621	14.9	480,186	20.6	504,997	18.2	501,882	15.8	552,599	15.9
15. Real estate, leasing and business activities	73,835	5.1	87,675	5.0	98,135	4.9	109,081	4.7	146,913	5.3	168,075	5.3	185,528	5.3
16. Other items	70,690	4.9	83,384	4.7	70,391	3.5	64,857	2.8	87,749	3.2	62,711	2.0	66,939	1.9
B. PRIVATE INDIVIDUALS	**117,555**	**8.2**	**200,425**	**11.3**	**259,148**	**12.9**	**309,334**	**13.3**	**381,693**	**13.8**	**468,858**	**14.8**	**510,494**	**14.7**
C. NON-RESIDENTS	**247,672**	**17.2**	**281,591**	**15.9**	**319,057**	**15.8**	**266,124**	**11.4**	**275,728**	**9.9**	**318,680**	**10.1**	**381,256**	**11.0**
TOTAL (A+B+C)	**1,435,814**	**100.0**	**1,771,104**	**100.0**	**2,014,864**	**100.0**	**2,329,244**	**100.0**	**2,775,403**	**100.0**	**3,168,778**	**100.0**	**3,475,222**	**100.0**

1 Figures as at 30 June 1999 are unaudited.
2 Public administration also comprises securities issued by the government.
3 Financial intermediation includes also claims on the Bank of Slovenia.

APPENDIX 14

BANKS AND SAVINGS BANKS IN SLOVENIA AS AT 30 SEPTEMBER 2000

I. BANKS

Banks authorised by the Bank of Slovenia to provide banking services and other financial selected services, which have adjusted their operations with Article 240 of the Banking Act (Official Gazette of the Republic of Slovenia - 7/99):

ABANKA D.D. LJUBLJANA
1517 LJUBLJANA
Tel.: +386 1 471 81 00
Fax: + 386 1 432 51 65

BANK AUSTRIA CREDITANSTALT D.D., LJUBLJANA
Wolfova 1
1000 LJUBLJANA
Tel.: +386 1 477 76 00
Fax: +386 1 251 29 77

BANKA CELJE D.D.
Vodnikova 2
3000 CELJE
Tel.: +386 3 543 10 00
Fax: +386 3 548 35 11

BANKA KOPER D.D.
6502 KOPER
Tel.: +386 5 665 11 00
Fax: + 386 5 639 74 51

BANKA SOCIETE GENERALE LJUBLJANA D.D.
Trg republike 3
1000 LJUBLJANA
Tel.: +386 1 200 16 00
Fax: + 386 1 426 32 83

BANKA VELENJE D.D., VELENJE
BANČNA SKUPINA NOVE LJUBLJANSKE BANKE
Rudarska 3
3320 VELENJE
Tel.: +386 3 899 52 00
Fax: + 386 3 586 94 81

BANKA VIPA D.D.
Kidričeva 7
5000 NOVA GORICA
Tel.: +386 5 338 50 00
Fax: +386 5 302 85 16

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DOLENJSKA BANKA D.D., BANČNA SKUPINA NOVE LJUBLJANSKE BANKE
Seidlova cesta 3
8000 NOVO MESTO
Tel.: +386 7 331 65 00
Fax: +386 7 332 11 13

FACTOR BANKA D.D.
Železna 16
1000 LJUBLJANA
Tel.: +386 1 431 11 36
Fax: +386 1 432 80 66

GORENJSKA BANKA, D.D., KRANJ
Bleiweisova cesta 1
4000 KRANJ
Tel.: +386 4 208 40 00
Fax: +386 4 202 15 03

HYPO ALPE-ADRIA-BANK D.D., LJUBLJANA
Trg Osvobodilne fronte 12
1000 LJUBLJANA
Tel.: +386 1 300 44 00
Fax: +386 1 300 44 01

KOROŠKA BANKA D.D., SLOVENJ GRADEC,
BANČNA SKUPINA NOVE LJUBLJANSKE BANKE
Glavni trg 30
2380 SLOVENJ GRADEC
Tel.: +386 2 884 91 11
Fax: +386 2 884 23 82

KREKOVA BANKA D.D. MARIBOR
Slomškov trg 18
2000 MARIBOR
Tel.: +386 2 229 31 00
Fax: + 386 2 252 35 02

NOVA KREDITNA BANKA MARIBOR D.D.
2505 MARIBOR
Tel.: +386 2 229 22 90
Fax: +386 2 252 43 33

NOVA LJUBLJANSKA BANKA D.D., LJUBLJANA
1520 LJUBLJANA
Tel.: +386 1 425 01 55
Fax: +386 1 425 03 31

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POMURSKA BANKA D.D., MURSKA SOBOTA,
BANČNA SKUPINA NOVE LJUBLJANSKE BANKE
Trg zmage 7
9000 MURSKA SOBOTA
Tel.: +386 2 515 14 00
Fax: +386 2 515 42 68

PROBANKA D.D.
Gosposka ulica 23
2000 MARIBOR
Tel.: +386 2 252 05 00
Fax: +386 2 252 48 17

SKB BANKA D.D. LJUBLJANA
1513 LJUBLJANA
Tel.: +386 1 433 21 32
Fax: +386 1 231 45 49

SLOVENSKA INVESTICIJSKA BANKA, D.D., /DELNIŠKA DRUŽBA/, LJUBLJANA
Čopova 38
1101 LJUBLJANA
Tel.: +386 1 426 11 81
Fax: +386 1 426 20 95

SLOVENSKA ZADRUŽNA KMETIJSKA BANKA D.D., LJUBLJANA
Kolodvorska 9
1000 LJUBLJANA
Tel.: +386 1 472 71 00
Fax: +386 1 472 74 05

VOLKSBANK - LJUDSKA BANKA D.D.
Miklošičeva 30
1000 LJUBLJANA
Tel.: +386 1 431 10 09
Fax: +386 1 431 22 63

BANKA DOMŽALE D.D., DOMŽALE,
BANČNA SKUPINA NOVE LJUBLJANSKE BANKE
Ljubljanska cesta 62
1230 DOMŽALE
Tel.: +386 1 724 53 00
Fax: +386 1 721 68 21

BANKA ZASAVJE D.D., TRBOVLJE,
BANČNA SKUPINA NOVE LJUBLJANSKE BANKE
Trg revolucije 25c
1420 TRBOVLJE
Tel.: +386 3 562 12 33
Fax: +386 3 562 61 93

A bank with a license for all domestic commercial banking operations (except for personal foreign currency deposits, for nonresidents' custody accounts, for non-residents' accounts, if not current or giro accounts of foreign banks and financial institutions dealing in international payments with foreign banks) and for cross-border payments with international postal payment instruments:

POŠTNA BANKA SLOVENIJE D.D.
Vita Kraigherja 5
2000 MARIBOR
Tel.: +386 2 228 82 00
Fax: +386 2 228 82 10

Banks licensed under the Constitutional Law:

KREDITNA BANKA MARIBOR D.D.
Trg republike 3
1000 LJUBLJANA
Tel: +386 1 476 30 03

LJUBLJANSKA BANKA D.D., LJUBLJANA
Trg republike 3
1000 LJUBLJANA
Tel.: +386 1 476 30 03

Branch office:

KAERNTNER SPARKASSE AG, CELOVEC,
PODRUŽNICA V SLOVENIJI
Dunajska 63
1000 LJUBLJANA
Tel.: +386 1 309 23 99
Fax: +386 1 309 23 97

NOVA LJUBLJANSKA BANKA banking group consists of the following banks:

NOVA LJUBLJANSKA BANKA D.D., LJUBLJANA,
BANKA DOMŽALE D.D., DOMŽALE, BANČNA SKUPINA NOVE LJUBLJANSKE BANKE,
BANKA VELENJE D.D., VELENJE, BANČNA SKUPINA NOVE LJUBLJANSKE BANKE,
DOLENJSKA BANKA D.D., BANČNA SKUPINA NOVE LJUBLJANSKE BANKE,
KOROŠKA BANKA D.D. SLOVENJ GRADEC, BANČNA SKUPINA NOVE LJUBLJANSKE BANKE,
POMURSKA BANKA D.D., MURSKA SOBOTA, BANČNA SKUPINA NOVE LJUBLJANSKE BANKE,
BANKA ZASAVJE D.D., TRBOVLJE, BANČNA SKUPINA NOVE LJUBLJANSKE BANKE.

APPENDIX 14

II. SAVINGS BANKS

Savings bank authorised by the Bank of Slovenia to provide banking services and other financial selected services, which have adjusted its operations with Article 240 of the Banking Act[1]:

DELAVSKA HRANILNICA D.D. LJUBLJANA
Dalmatinova 4
1000 LJUBLJANA
Tel.: +386 1 300 02 00
Fax: +386 1 300 02 20

LLT HRANILNICA IN POSOJILNICA D.D., MURSKA SOBOTA
Staneta Rozmana 11/a
9000 MURSKA SOBOTA
Tel.: +386 2 527 18 00
Fax: +386 2 527 18 00

Savings banks, which have not adjusted its operations with Article 240 of the Banking Act:

HRANILNICA LON D.D., KRANJ
Bleiweisova 2
4000 KRANJ

Tel.: +386 4 280 07 77
Fax: +386 4 201 13 37

HRANILNICA IN POSOJILNICA KGP KOČEVSKE, D.D.[2]
Roška cesta 8
1330 KOČEVJE

Tel.: +386 1 895 37 77
Fax: +386 1 895 37 77

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1 As of 1 July 2000, Mariborska hranilnica-posojilnica d.o.o., Maribor joined Delavska hranilnica d.d., Ljubljana. In addition, the decision was taken on 30 June 2000 at the general meeting of shareholders of Poteza-Hranilnica d.o.o., Ljubljana, to institute regular (voluntary) liquidation. The winding up will become effective as of the date of entry into the competent court registry.

2 Hranilnica in posojilnica KGP Kočevske, d.d. is on the point of joining Slovenska zadružna kmetijska banka d.d. Ljubljana.

APPENDIX 14a

REPRESENTATIVE OFFICES OF FOREIGN BANKS IN SLOVENIA AS AT 30 SEPTEMBER 2000

1. Cassa di Risparmio di Trieste
2. Cassa di Risparmio di Udine
3. Die Kärntner Sparkasse
4. European Bank for Reconstruction and Development
5. Magyar Külkereskedelmi Bank Rt.
6. LHB Internationale Handelsbank
7. Raiffeisen Zentralbank Österreich
8. Bank für Kärnten und Steiermark
9. Bank für Arbeit und Wirtschaft

APPENDIX 15

CHANGES IN LEGAL STATUS OF SLOVENIAN BANKS AND SAVINGS BANKS FROM JANUARY 1991 TO JUNE 2000

I. BANKS

Name	Type of change	Date of change
	MERGERS AND ACQUISITIONS	
Ljubljanska banka Komercialna banka Nova Gorica d.d., Nova Gorica	Taken over by Nova Kreditna banka Maribor d.d.	30 Dec 1994
E banka d.d. Maribor	Taken over by Nova Ljubljanska banka d.d., Ljubljana	12 Jan 1995
Ljubljanska banka Posavska banka d.d., Krško	Taken over by Nova Ljubljanska banka d.d., Ljubljana	01 Apr 1996
Banka Noricum d.d. Ljubljana	Taken over by Banka Celje d.d.	19 Dec 1996
Hmezad banka d.d. Žalec	Taken over by Banka Celje d.d.	30 Sep 1998
Banka Creditanstalt d.d. Ljubljana	Taken over by Bank Austria d.d.	02 Nov 1998
UBK banka d.d. Ljubljana (bančna skupina SKB)	Taken over by SKB banki d.d. Ljubljana	30 Dec 1998
M banka d.d. Ljubljana	Taken over by Banka Koper d.d.	01 Oct 1999
	BANKRUPTCIES AND LIQUIDATIONS	
Komercialna banka Triglav d.d. Ljubljana	Liquidation proceedings commenced	05 Jul 1996
	Bankruptcy proceedings commenced	27 Dec 1996
Hipotekarna banka d.d. Brežice	Liquidation proceedings commenced	02 Dec 1998
	Bankruptcy proceedings commenced	19 Apr 2000

II. SAVINGS BANKS

Name	Type of change	Date of change
	MERGERS AND ACQUISITIONS	
HIP Fiba d.d. Koper	Taken over by Abanka d.d. Ljubljana	30 Dec 1994
Hranilnica Magro d.d. Grosuplje	Taken over by Hranilnica Lon d.d., Kranj	21 Aug 1995
Hranilnica Hmezad Agrina d.o.o. Žalec	Taken over by Komercialna banka Triglav d.d. Ljubljana	03 Jul 1996
HIP Val d.o.o. Izola	Taken over by Komercialna banka Triglav d.d. Ljubljana	04 Jul 1996
Hranilnica Hipo d.d. Domžale	Taken over by Ljubljanska banka – Banka Domžale d.d., Domžale	14 Mar 1997
Mariborska hranilnica – posojilnica d.o.o. Maribor	Taken over by Delavska hranilnica d.d., Ljubljana	30 Jun 2000
	BANKRUPTCIES AND LIQUIDATIONS	
Kranjska hranilnica in posojilnica Ljubljana d.d., Ljubljana		
Štajerska hranilnica d.d., Maribor		
Alea d.d. hranilnica Ajdovščina		
Mestna hranilnica d.o.o., Krško		
Hranilnica in posojilnica Tilia d.o.o. Novo mesto	Wound up	11 Nov 1997

APPENDIX 16

LEGISLATION REGARDING REGULATION OF BANKING SUPERVISION

1. **Law on the Bank of Slovenia**
(Official Gazette of the Republic of Slovenia/I, No. 1/91)

2. **Banking Act**
(Official Gazette of the Republic of Slovenia, No. 7/99)

3. **Law on Savings and Loan Undertakings**
(Official Gazette of the Republic of Slovenia, Nos. 14/90, 30/90, 17/91, 55/92, 66/93, 7/99)

4. **Law on Banks and Savings Banks**
(Official Gazette of the Republic of Slovenia, Nos. 1/91, 38/92, 46/93, 45/94, 7/99) –superseded by the 1999 Banking Act except for Article 79.

5. **Law on the Agency of the Republic of Slovenia for Insurance of Deposits Gathered by Banks and Savings Banks** (Article 12)
(Official Gazette of the Republic of Slovenia/I, Nos. 1/91, 7/99)

6. **Decree on Supervision of Operating Activities of Banks and Savings Banks**
(Official Gazette of the Republic of Slovenia, Nos. 55/92, 89/98)

7. **Decree on the Calculation of Own Funds, Capital Requirements and Capital Adequacy of Banks and Savings Banks**
(Official Gazette of the Republic of Slovenia, No. 32/99)

8. **Decree on Large Exposure of Banks and Savings Banks**
(Official Gazette of the Republic of Slovenia, No. 32/99)

9. **Decree on the Classification of the On- and Off-balance Sheet Items of Banks and Savings Banks**
(Official Gazette of the Republic of Slovenia, No. 32/99)

10. **Instructions for Implementation of the Decree on the Classification of the On- and Off-balance Sheet Items of Banks and Savings Banks**
(issued on 10 May 1999)

11. **Instructions for Restructuring Claims of Banks and Savings Banks**
(issued on 20 May 1999)

12. **Decree on Establishing Specific Provisions of Banks and Savings Banks**
(Official Gazette of the Republic of Slovenia, No. 32/99)

13. **Decree on the Implementation of Article 127 of the Banking Act**
(Official Gazette of the Republic of Slovenia, Nos. 32/99, 89/99)

14. **Decree on Books of Account and Annual Report and Accounts of Banks and Savings Banks**
(Official Gazette of the Republic of Slovenia, Nos. 39/99, 50/99, 63/99)

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15a. **Instructions for Implementation of the Decree on Books of Account and Annual Report and Accounts of Banks and Savings Banks – methodology for the preparation of balance sheet including detailed items**
(issued on 27 May 1999, amended on 22 June and 27 July 1999)

15b. **Instructions for Implementation of the Decree on Books of Account and Annual Report and Accounts of Banks and Savings Banks – methodology for the calculation of ratios**
(issued on 21 Jan 2000)

16. **Instructions for Submitting Monthly Reports on Balances on Banks' Accounts**
(issued on 27 May 1999)

17. **Instructions for Preparation of 10-Day Reports on Bank Accounts**
(issued on 3 September 1999)

18. **Decree on the Minimum Scope and Content of Audit and Auditor's Report**
(Official Gazette of the Republic of Slovenia, No. 39/99)

19. **Decree on the Detailed Method for the Calculation of Liabilities, Claims and Holdings for the Purpose of Determining Net Indebtedness**
(Official Gazette of the Republic of Slovenia, No. 42/99)

20. **Decree on Determining and Prudential Reporting of Value of Holdings of Banks and Savings Banks in Non-financial Institutions and Investments in Tangible Fixed Assets**
(Official Gazette of the Republic of Slovenia, No. 42/99)

21. **Decree on the Required Adjustments of the Maturity Structure between Assets and Liabilities**
(Official Gazette of the Republic of Slovenia, No. 40/99)

22. **Instructions for Preparation of Monthly Reports on Effective Proportion between Assets Graded as First, Second and Third Class**
(issued on 10 March 1999, amended on 21 July 1999)

23. **Decree on Granting Special Liquidity Loans in Co-operation with Banks**
(Official Gazette of the Republic of Slovenia, Nos. 25/97, 37/98, 31/99)

24. **Instruction for Preparation of Reports on Major Depositors**
(issued on 25 March 1999)

25. **Instructions for Preparation of Reports on Movements in Tolar Liquidity**
(issued on 20 May 1999)

26. **Decree on the Provision of Integral Data on Balances on Customer Accounts of Banks and Savings Banks**
(Official Gazette of the Republic of Slovenia, No. 85/98)

27. **Instructions for Calculation of Some Common Interest Rates on Deposits from Non-Bank Sector and Loans to Non-Bank Sector**
(issued on 20 May 1999)

28. **Decree on Mismatch between Assets and Liabilities of Banks in Foreign Currency (Open Foreign Currency Position)**
(Official Gazette of the Republic of Slovenia, No. 37/99)

29. **Decree on the Bringing of the Operation of Savings and Loan Undertakings into Line with the Provisions of the Banking Act**
(Official Gazette of the Republic of Slovenia, No. 109/99)

30. **Decree on the Supervision of Banks and Savings Banks on a Consolidated Basis**
(Official Gazette of the Republic of Slovenia, No. 109/99)

31. **Decree on Minimum Requirements for Obtaining Authorisation for the Provision of Banking and Other Financial Services and Documents to Be Attached to Application**
(Official Gazette of the Republic of Slovenia, Nos. 109/99, 52/2000)

32. **Decree on Minimum Scope of Documents to Be Submitted by a Foreign Bank with Application to Establish a Branch**
(Official Gazette of the Republic of Slovenia, Nos. 109/99, 52/2000)

33. **Decree on the Notification of the Intended Disposal of Shares**
(Official Gazette of the Republic of Slovenia, No. 109/99)

34. **Decree on the Conditions to be Met by Credit Intermediary**
(Official Gazette of the Republic of Slovenia, No. 110/99)

35. **Decision (Decree) on Deposit-Guarantee Scheme**
(Official Gazzete of the Republic of Slovenia, No. 61/2000)

36. **Recommendations for Trading Activities in Banks**
(issued in April 1997)

37. **Recommendations for Capital Management in Banks**
(issued in October 1998)

38. **Recommendations for Credit Risk Management in Banks**
(issued in October 1998)

39. **Recommendations for Liquidity Risk Management in Banks**
(issued in October 1998)

40. **Recommendations for Currency Risk Management in Banks**
(issued in October 1998)

41. **Recommendations for Internal Control Systems in Banks**
(issued in October 1998)

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42. **Operational Risk Management, Basel Committee on Banking Supervision**
(issued in September 1998)

43. **Enhancing Bank Transparency, Basel Committee on Banking Supervision**
(issued in September 1998)

44. **Decree on Tariffs for Services Rendered by the Bank of Slovenia**
(Official Gazette of the Republic of Slovenia, Nos. 23/91, 3/92, 44/92, 3/94, 4/94, 5/94, 73/94, 27/98, 76/98, 19/99, 27/99, 53/99, 61/99, 78/99, 90/99, 59/2000)

45. **Decree on the Annual Fee and Lump-sum Charges for Prudential Supervision**
(Official Gazette of the Republic of Slovenia, No. 42/99)

46. **Code of Practice on the Co-operation between Supervisory Authorities**
(Official Gazette of the Republic of Slovenia, No. 55/99)

47. **Instructions for Setting Criteria Regarding Other Financial Services**
(Official Gazette of the Republic of Slovenia, No. 55/99)

APPENDIX 17

RATINGS OF SLOVENIAN BANKS AND SLOVENIA AS AT 30 SEPTEMBER 2000

Fitch IBCA

Rated banks	Short-term rating	Long-term rating	Individual rating	Support
Nova Ljubljanska banka	F2	BBB+	C	2
Nova Kreditna banka Maribor	F3	BBB	C/D	2
SKB				4
Banka Koper	F3	BBB-	C/D	4
Banka Celje	F3	BBB	C	4
Abanka	F3	BBB-	C/D	4
Gorenjska banka	F3	BBB	C	4

Country	Long-term rating in foreign currency	Long-term rating in domestic currency	Short-term rating
Slovenia	A	AA	F1

Moody's

Rated banks	Bank deposits - short-term	Bank deposits - long-term	Financial strength
Nova Ljubljanska banka	P-2	Baa2	D+
Nova Kreditna banka Maribor	P-2	Baa2	D+
SKB banka	P-3	Baa3	D+

Country	Long-term government bonds in foreign currency	Long-term government bonds in domestic currency
Slovenia	A3	Aa3

Standard & Poor's

Rated banks	Short-term counterparty rating	Long-term counterparty rating: Foreign currency	Long-term counterparty rating: Domestic currency	Outlook
Nova Ljubljanska banka	A-3	BBB-	BBB-	stable
Nova Kreditna banka Maribor			BB-pi	
Banka Koper			B-pi	
Banka Celje			BB-pi	
Abanka			B-pi	
Gorenjska banka			BB-pi	

Country	Outstanding sovereign rating: Foreign currency	Outstanding sovereign rating: Local currency
Slovenia	A/Stable/A-1	AA/Stable/A-1+

Thomson Financial BankWatch

Rated banks	Short-term rating	Senior debt rating	Intra-country issuer rating
Nova Ljubljanska banka	LC-1	A-	IC-B
Nova Kreditna banka Maribor	LC-1	BBB	IC-B/C
SKB banka	LC-1	BBB+	IC-B
Banka Celje	LC-2		IC-C
Abanka	LC-2		IC-C

Country	Sovereign rating
Slovenia	A-

Capital Intelligence

Rated banks	Short-term rating	Long-term rating	Support	Outlook
Nova Ljubljanska banka	A 2	BBB+	2	positive
Nova Kreditna banka Maribor	A 2	BBB-	2	stable
SKB banka	B	BB+	3	stable
Banka Koper	A 3	BBB-	4	stable
Banka Celje	A 3	BBB-	3	stable
Abanka	B	BB+	4	stable
Gorenjska banka	A 3	BBB-	4	stable

Country	Long-term rating	Short-term rating
Slovenia	A-	A2