BANKA
SLOVENIJE

BANK OF SLOVENIA

ANNUAL REPORT

YEAR 2001

Published by:

BANK OF SLOVENIA
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The cut-off date for the data included in this Annual Report was mid-February 2002.

The English edition of the Annual Report of the Bank of Slovenia for 2001 is a translation of the Slovenian original which remains the legal version.

Printed by:
Geodetski inštitut Slovenije, Ljubljana

ISSN 1318-072X

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Overview

The main feature of the past year has been a slowdown in economic activity around the globe. Closely knitted into global trends and largely dependent on foreign trade, Slovenia's economic growth was dampened. Domestic demand remained quite modest for the second year in a row and the past year witnessed a drop in gross fixed capital formation that fell sharper than other components of domestic demand. A slowdown in the economic activity was mirrored in the movements in employment that ground to a halt in the second half of the year. Nevertheless, unemployment continued to move downward for the third consecutive year.

The current account recorded only a small deficit, as a result of modest imports and relatively favourable export results. Exporters managed to make up for the weak demand from Slovenia's traditional trade partners by re-routing exports to the markets of former Yugoslavia and former Soviet Union, hence the regional composition of exports changed in 2001.

Sluggish economic activity and deflated oil prices contributed significantly to lower inflation around the world last year. Price pressures from abroad lost momentum during the second half of 2001 resulting in less vigorous rises in consumer prices; hence in December the annual inflation figure for Slovenia was 7 per cent. The downturn in global commodity prices affected local market prices that started to grow at a higher rate than administered prices.

The year under review was also marked by extensive capital inflows, primarily due to the changeover of the EMU countries when the new euro notes and coins were introduced and as a result of direct investments made by non-residents in Slovenia. Large financial inflows made a considerable impact on movements of monetary aggregates and put pressure on for an appreciation of the tolar. The components above were growing at an exceptionally high rate, particularly fixed-term deposits denominated in tolars and household deposits denominated in foreign currency, but had no direct impact on inflation.

The Bank of Slovenia has reviewed its strategy for guiding monetary policy during the period of converging with the EMU and has adopted a medium-term inflation target: to lower inflation to 4 per cent by the end of 2003. The new strategy envisages the implementation of a monetary policy that rests on two pillars of monetary policy indicators, with money and its components being the indicators comprised in the first pillar. The Bank of Slovenia has pursued a pro-active exchange rate policy, which assists a gradual reduction of inflation and partly reduces the gap between interest rate prevailing on the domestic market and cross-border interest rates.

The use of monetary policy instruments was linked to considerable inflows from abroad and was influenced by the increasing need for sterilisation. Banks that had signed the agreement with the Bank of Slovenia to participate in interventions in foreign exchange markets cooperated and temporarily sold foreign exchange was the most important source of liquidity of the banking system. It was mainly towards the end of 2001 that monetary policy had to address the issue of a burden of large amounts of temporarily purchased foreign exchange and issued tolar bills. By this type of intervention, the Bank of Slovenia neutralised the impact of capital inflows on the exchange rate.

The main feature of the banking sector during the year under review was a rise in the volume of operations handled by the banks that mainly stemmed from the increase in household deposits and the falling interest rate margin and a weaker return on average bank assets. A breakdown of investments made by banks shows that investments in securities gained momentum, particularly when it came to subscribing to bills issed by the Bank of Slovenia and slightly less in the case of loans and advances extended to the non-bank sector.

An important event of 2001 was the 10th anniversary of the monetary independence of Slovenia, which was honoured by the Bank of Slovenia with a celebration, and the issue of commemorative coins.

1. ECONOMIC ENVIRONMENT

1.1. International economic developments

World economy marked by the events of 11 September

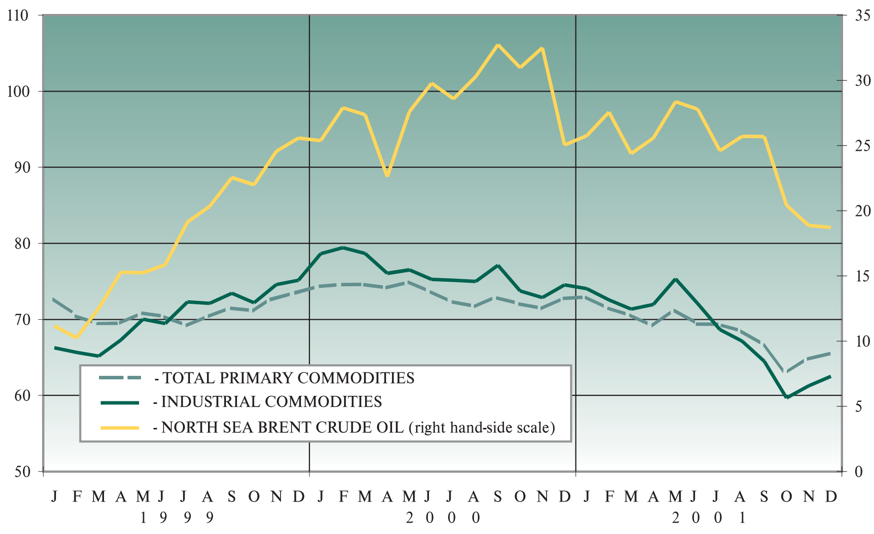
The global economic downturn was the key feature of the year 2001 that will also be remembered for a decline in both inflationary risks and oil prices in the second half of the year. As uncertainty increased, the world economy was additionally handicapped by events in the wake of September 11th in the United States, although a slowdown in economic activity was felt as early as the first half of 2001.

The figure released by the International Monetary Fund set the world economic growth in 2001 at 2.4 per cent following the economic downturn which first started to materialise at the end of 2000 and continued throughout 2001. The terrorist attack in the U.S.A. had a further dampening effect on the economy. Early estimates show that economic growth in the U.S.A. in 2001 tapered off to 1.2 per cent - a considerable fall in comparison with growth in excess of 4 per cent over four consecutive years and a record low growth after the 1991 recession. Preliminary estimates for the EMU for 2001 put growth at 1.5 per cent, falling for the first time since 1996 below 2 per cent. The Japanese economy entered recession in the middle of 2001; overall economic decline was -0.5 per cent. At the end of the year 2001 an economic and financial crisis occured in Argentina.

Slovenia's main trade partners enjoyed lower economic growth

The sluggish economic activity in 2001 did not bypass Slovenia's trade partners. Estimated economic growth in Germany for 2001 was 0.6 per cent, in Italy 1.8 per cent, in Austria 1.1 per cent, and in France 2.0 per cent. All these countries did considerably better in 2000 when their economic growth was around 3 per cent. During the year under review, Slovenia's partners from Eastern Europe were also affected by lower economic growth. Except only Croatia, which remained in 2001 at the 2000 level with a growth rate of approximately 3.7 per cent. Estimates for 2001 place Russia's economic growth at 5.2 per cent and Poland's at 1.2 per cent; both countries lower than 2000.

Chart 1: **Commodity** (1999 = 100) **and oil prices** (North Sea Brent in US$ per barrel) **on the international market**



International trade growth slackened as well

The growth of international trade was lower in comparison to 2000. According to OECD estimates, international trade growth fell from 12.8 per cent in 2000 down to a 0.3 per cent growth in 2001.

A fall in oil prices below US$ 20 per barrel…

Oil prices had hovered around 26 US dollars per barrel until September 11th 2001 when gloomy predictions for world economic growth and consequently slack demand triggered a fall in oil prices that eventually settled at around 20 US dollars per barrel. OPEC members tried to prevent a further fall in oil prices and after lengthy negotiations with selected non-member countries (Russia, Mexico, Norway, Oman and Angola) clinched a deal at the end of December to cut back oil extraction quotas over the following six months. Dollar prices of other commodities fell by 6.5 per cent on average year-on-year, while prices of industrial goods fell 10.1 per cent, and food prices by 3.7 per cent.

… and a slowdown in economic growth led to falling inflation around the globe

Lower oil prices and a downswing in economic growth dampened inflation all over the world. In the U.S.A. and in the EMU countries inflation was going up in the early months of 2001 and reached a peak of around 3.5 per cent in May. Then the trend reversed and inflation started to fall, so at the end of December it reached 1.6 per cent in the U.S.A. and 2.1 per cent in the euro area. Overall, European inflation was very close to the target set by the European Central Bank of 2 per cent. On several occasion as economic growth and inflation faltered, the European and the American central banks each cut back key interest rates. The U.S. Federal Reserve had a more pro-active stance towards the cutting of interest rates and in 2001 it cut back interest rates 11 times, overall by 4.75 percentage points. As a result, the key interest rate of Fed Funds at the end of December stood at 1.75 per cent. The European Central Bank decided to lower interest rates four times, which meant 1.5 percentage points lower over the year. The key refinancing interest rate of the ECB (minimum bid rate) was 3.25 per cent in December. Interest rates in international markets fell in line with the cuts in interest rates set by central banks. The LIBOR interest rate on three-month deposits denominated in US dollars in 2001 averaged 3.78 per cent and on three-month deposits denominated in the euro averaged 4.26 per cent.

Depreciation of the euro against the US dollar

The value of the euro in comparison with the US dollar lost ground until mid-2001. The picture changed when in the second half of the year as the euro gained in strength for some time. The strengthening of the euro could be partially accounted for by the events in the USA but it was short-lived and towards the end of the year, it started to lose value once again. On average, the euro was worth US$0.896 in 2001 and in comparison with the average for 2000 when it was worth US$0.924, it lost 3 per cent of its value.

1.2. Gross domestic product, employment and labour costs

Economic growth in Slovenia cooled after two years

Relatively high economic growth over the past two years when GDP was rising on average by approximately 5 per cent per annum cooled down in 2001 when GDP growth was 3.0 per cent. Value added rose most strongly in the utilities sector: electricity, gas and water supply (up by 6.1 per cent), and public administration (up by 5.2 per cent), financial intermediation (up by 5.3 per cent), and manufacturing (up by 4.4 per cent). Value added declined in mining and construction (-7.1 per cent and -3.5 per cent, respectively). Such a composition of economic growth shows the impact that comparativelly large employment has had in the public sector and major shifts in the financial markets, while in manufacturing activities it is the reflection of strong foreign demand. Exporters were particularly successful in replacing sluggish demand from Slovenia's leading traditional trade partners in the second half of the year in particular by intensifying efforts to export more to the markets of former

Yugoslavia and the former Soviet Union. Domestic demand remained depressed for the second consecutive year. Among the components of domestic spending there was firstly a weakening in investment in the private sector, gross fixed capital formation fell sharply (-3.7 per cent), while there was a sluggish growth in household spending (1.7 per cent) and a rapid rise in government spending (3.2 per cent).

Exports redirected to the markets of former Yugoslavia and the Soviet Union helped to keep up foreign demand

The biggest contribution for economic growth goes to net foreign trade (80 per cent, i.e. 2.5 percentage points). Given the fact that the current account of the balance of payments was near-balanced in 2001, domestic savings were almost sufficient to cover gross investments.

In line with the relatively high value-added growth in manufacturing activities, industrial production was rising as well. Volume growth of industrial production in 2001 topped 2.9 per cent, but the pace of growth started to falter in the second half of the year and at the end of the year growth was practically stagnant. The output volume of capital investment goods showed the strongest rise (8.3 per cent) as opposed to the output of consumer goods that fared less well with a 1.7 per cent growth. Overall inventories increased by 5.6 per cent year-on-year, while intermediate goods rose by a record 10.0 per cent.

Growth in industry was 2.9 per cent

Table 1: **Selected economic indicators**

	1995	1996	1997	1998	1999	2000	2001[1]
Real growth in the gross domestic product[2] in %	4.1	3.5	4.6	3.8	5.2	4.6	3.0
Gross domestic product in USD millions	18,744	18,878	18,208	19,585	20,071	18,122	18,767
Gross domestic product per capita in USD	9,431	9,481	9,163	9,878	10,109	9,105	9,455
Structure of the gross domestic product in % of GDP							
Agriculture, forestry and fishing	3.9	3.8	3.7	3.6	3.2	2.9	2.7
Building- and other industries	32.6	32.7	32.9	33.0	32.6	33.1	32.2
- Manufacturing industry	24.6	24.1	24.3	24.1	24.3	25.2	24.3
Services	48.2	48.4	49.5	49.2	49.5	50.4	51.3
Total value added	84.8	85.0	86.1	85.8	85.3	86.4	86.2
Compensation of employees	57.2	54.8	53.6	52.3	51.8	52.6	52.8
Taxes on production and imports, subsidies excluded	14.9	15.3	14.9	15.4	16.1	15.4	15.6
Gross operating surplus and diverse income	27.9	29.9	31.5	32.4	32.1	32.0	31.6
- Exports of goods and services	55.2	55.8	57.4	56.6	52.5	59.1	60.1
- Imports of goods and services	57.2	56.8	58.3	58.2	56.9	62.7	60.5
Net exports	-2.0	-1.0	-0.8	-1.5	-4.4	-3.6	-0.4
Domestic private consumption	58.5	57.5	56.4	55.7	55.8	54.9	53.1
Public expenditure	20.1	20.1	20.4	20.3	20.2	20.8	20.1
Gross investment	23.3	23.4	24.1	25.6	28.4	27.8	27.2
Active population[3] in thousands	952	942	978	978	959	968	972
The employed and the self-employed	882	875	906	901	886	901	911
The unemployed	70	69	72	77	73	68	61
Unemployment rate (ILO)	7.4	7.3	7.4	7.9	7.6	7.0	6.3
Real growth in the gross salary per employee in %	5.1	5.1	2.4	1.6	3.3	1.6	3.2
Labour productivity growth in %	3.3	4.4	5.1	3.8	4.0	3.5	3.0

1 Data on expenditure structure of GDP and active population for 2001 are estimates of the Institute of the Republic of Slovenia for Macroeconomic Analysis and Development.
2 In constant prices of 1995.
3 Internationally comparable data under the ILO methodology.
Source: The Statistical Office of the Republic of Slovenia and the Institute of the Republic of Slovenia of Macroeconomic Analysis and Development

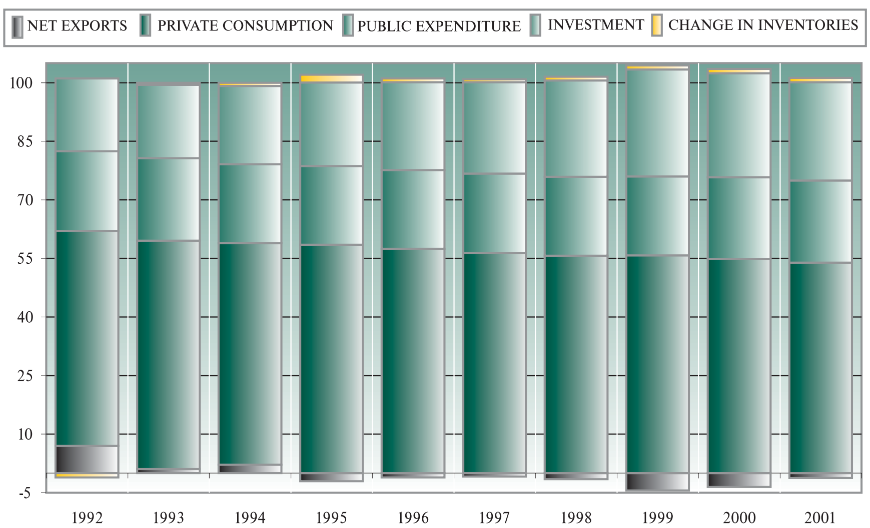
Wages and salaries were rising faster than planned

Wages and salaries outpaced the forecast 2.3 per cent real growth in 2001 owing to fast growth in the beginning of the year. The annual growth rate of wages in 2001 averaged 11.9 per cent or in real terms 3.2 per cent. Real growth in wages paid in the trade sector for the twelve-month period averaged 2.2 per cent and lagged behind productivity growth by 0.9 percentage points. According to the national accounts, the share of compensation of employees due to the rather high growth in wages and salaries and higher employment in 2001 rose again and amounted to 52.8 per cent of GDP (2000: 52.6 per cent). In spite of a weak domestic demand, the cost side of GDP shows that the share of taxes on goods and services hardly changed at all, while the share of import levies fell oncemore. During the year under review, the share of gross business surplus dropped in comparison with the previous year (32.0 per cent of GDP) and amounted to 31.6 per cent of GDP mainly due to lower export demand and rising pressures to cut prices.

Employment downswing in the second half of the year

Overall, the trends witnessed in unemployment in 2001 were positive, following the slowdown experienced in 1999 and the satisfactory movement in 2000. Nevertheless, there was a downturn in the second half of the year particularly in some labour-intensive areas and this trend may not be shortterm. The number of active persons in employment increased in 2001 by 1.4 per cent on average, with employment growth being more vigorous in enterprises and institutions (1.8 per cent) than in the small business sector (0.6 per cent). Employment rose most in the real estate business (7.3 per cent), financial intermediation (3.4 per cent) and in activities related to the public sector (2.8 per cent). With a comparatively high level of activity, employment in the manufacturing sector edged up after a number of flat years (by 1.0 per cent over one-year). The number of employed persons varied considerably from one manufacturing activity to another. On the one hand, some industries were in the doldrums (food-proccessing, textile and paper industries) and on the other, there were activities creating new jobs at a fast rate (primarily in metal processing, furniture and automotive industries). The growth in employment in the services sector (2.6 per cent) was still ahead of the figure of industry (0.8 per cent). The gap between the two narrowed last year in comparison with the previous years. As regards the regional distribution of unemployment, the year 2001 brought no significant changes, since the rate of registered unemployment remained a record high in the Podravska, Pomurska, Savinjska and Posavska regions. An opposite trend was enjoyed by the Central Slovenian and Primorska regions with lower unemployment.

Chart 2: **GDP structure**



Source: The Statistical Office of the Republic of Slovenia and the Institute of the Republic of Slovenia of Macroeconomic Analysis and Development.

Unemployment rates keep falling for the third year in a row

It is estimated that the active population (according to the ILO methodology) rose by four thousand persons in 2001, while there were seven thousand less unemployed persons. As a consequence, after the jump in 1998 when the unemployment rate stood at 7.9 per cent, in 2001 it dropped for the third year in a row and on average amounted to in 6.3 per cent (2000: 7.0 per cent). The critical groups, despite the falling number of people out of work remained those unemployed for a longer period, the young (mainly first-time job seekers), people over 40 years of age and the unemployed with a low level of education. Within the framework of the introduction of a modern employment policy founded on four pillars, the programmes aimed at boosting employability come first, followed by the programmes designed to encourage entrepreneurship, the actions aimed at encouraging flexibility of individuals and corporate entities, and equal opportunities schemes. Over the past few years, funds allocated to the so-called passive employment policy have noticeably declined in response to stricter principles required by the Act on Employment and Insurance in Case of Unemployment promulgated in 1998. The draft bills of the Employment Relations Act and the Collective Employment Agreements Act have been in the parliamentary process for two years. The enactment of the two laws is expected to boost flexibility of the labour market and facilitate "hiring and firing". The negotiations between social partners are unfinished because of opposition to the terms of fixed-term employment, terms of giving notice and severance payments, and the definition of benefits that the trade unions want to see incorporated in the Employment Relations Act instead of in collective employment contracts for particular activities.

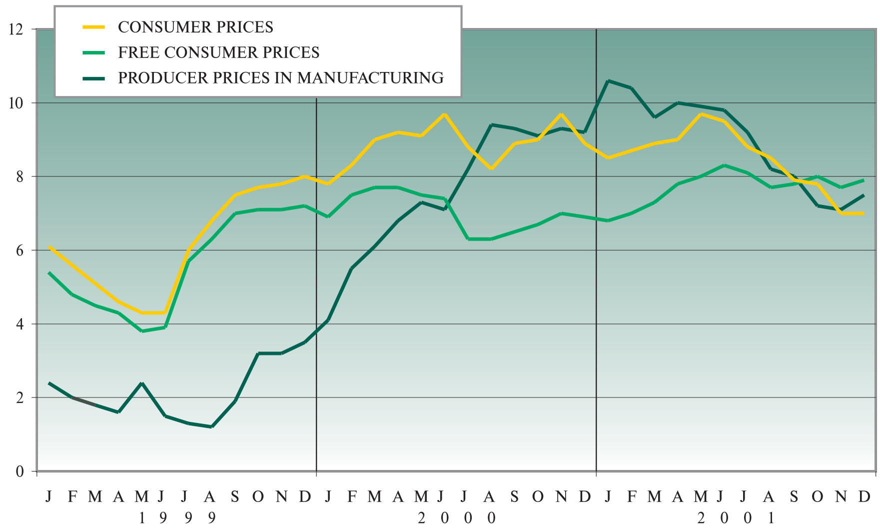
1.3. Prices

Growth in consumer prices at the end of 2001 amounted to 7.0 per cent

During the first half of 2001, the annual rate of consumer prices rose from 8.5 per cent in January to 9.7 per cent in May. Then consumer prices started to ease. The growth in consumer prices in 2001 amounted to 7.0 per cent (December - December), i.e. 8.4 per cent when measured as the average inflation for the year 2001 in comparison with 2000.

Inflationary pressures grew in the corporate sector at the start of 2001; first was a rise in prices of oil products, which started in summer 1999 and then with the

Chart 3: **Prices** (annual growth rates in %)



Source: The Statistical Office of the Republic of Slovenia and the Bank of Slovenia

The early months of 2001 saw inflation pressures in the corporate sector…

… then the pressure started to ease off

import prices aggregate. Consumer prices were also indirectly affected by the prices of domestic producers. Those ever-increasing inflationary pressures were reflected on accelerated growth in market prices and core inflation indicators. At mid-year, the growth in import prices gradually cooled. World oil prices started to fall in July but this did not produce an immediate effect on oil prices in Slovenia due to the Government's decision to raise excise duties. Nevertheless, cross-border price pressures started to weaken. This was reflected in prices of imports, and also in price indices of manufacturers in industry. Industrial producer prices increased in 2001 by 7.5 per cent (as opposed to 2000 when this rise was 9.2 per cent).

Lower prices of oil products helped curb the rise in administered prices

The increase in administered prices remained a modest 3.6 per cent in 2001 (2000: 19.9 per cent) and was mainly the result of low prices of oil in world markets in the second half of the year. Oil products were cheaper in the domestic market by 5.4 per cent (as opposed to 2000 when oil prices rose by 32.7 per cent). Administered prices excluding oil products increased in 2001 by 10.5 per cent (2000: 12.4 per cent), while other prices went up by 7.9 per cent (2000: 6.9 per cent).

1.4. Balance of payments

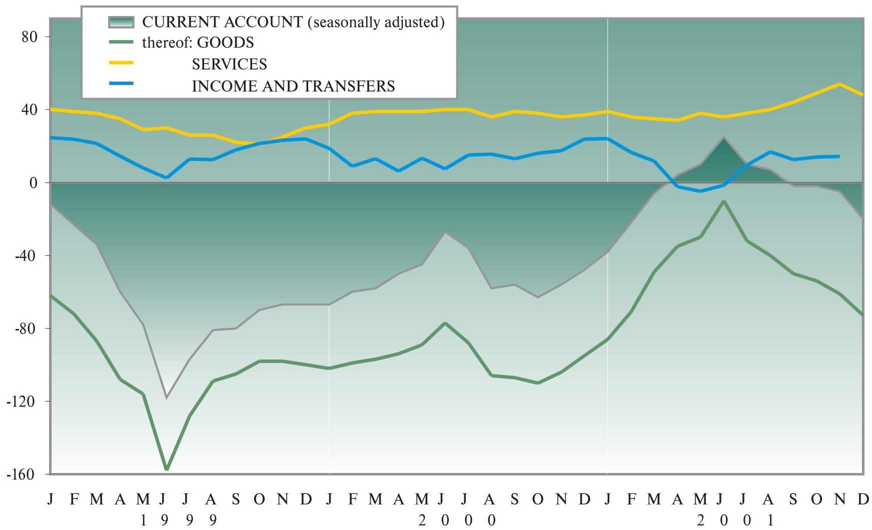
Lower deficit in current account transactions…

In 2001, Slovenia had a current account deficit arising from cross-border transactions of US$67 million or 0.4 per cent of the estimated GDP figure. The reduction in the deficit on the current account is in comparison with 2000, when this figure stood at US$611 million, primarily the result of modest domestic consumption and favourable export movements, and less a consequence of a rise in the surplus in services created by rising exports and imports services. The surplus arising from transfers on the capital and financial account was also larger, whereas the revenue account fared worse due to a heavier burden of interest payments.

… largely from a better trade balance…

Slovenia's deficit in foreign trade was US$893 million in 2001, i.e. 4.8 per cent of the GDP estimate, and in comparison with 2000 up by more than 3 percentage points. Exports of goods amounted to US$9,252 million, and in terms of the current exchange rate for the US dollar, it was a rise of 6.0 per cent year-on-year. Imports of goods amounted to US$10,145 million in 2001 and exceeded 2000 imports by 0.3 per cent. The fact that the dynamics of growth in exports outpaced the growth in

Chart 4: **Balance of payments current account** (seasonally adjusted, in US$ million)



Source: The Statistical Office of the Republic of Slovenia; estimates made by the ARC of the Bank of Slovenia imports was shown by a higher level of imports being covered by exports – up from 86.3 per cent to 91.2 per cent. Favourable export movements coupled with low import growth lowered the trade deficit and hence boosted the impact of the foreign trade balances to economic growth.

Real growth in exports of goods was lower than indicated by figures denominated in US dollars, while imports were slightly higher. Export-import prices denominated in US dollars keep changing due to the changes in the composition of trade by currency and the exchange ratios between the dollar and other currencies as well as non-dollar denominated prices of goods. In 2001, the share of the US dollar in the currencies composition of exports decreased only slightly (from 10.4 per cent to 10.3 per cent). Marked changes happened on the import side where the decline was just over two percentage points (from 17.9 per cent to 15.7 per cent). The share of imports denominated in US dollars was more volatile than the share of exports denominated in US dollars, since imports are more frequently and more strongly affected by the changes in the prices of raw materials and oil, both of which are commonly quoted in US dollars on the world commodity exchanges. The bulk of the components of trade are the currencies of the euro zone, the minor share in the range of 5.0 per cent refers to all other convertible currencies. By being almost flat in comparison with a year earlier, the rise in the value of the US dollar against the euro zone currencies contributed in 2001 to a fall in the value of trade expressed in dollars. However, this decline on the imports side was comparatively higher on imports since the share of the US dollar in the currency composition of imports dwindled more (-3.8 per cent) than on the exports side (-3.0 per cent). By disregarding the relations among currencies, the prices of goods increased by 3.9 per cent and 3.8 per cent on the exports and imports sides, respectively. The real growth (in terms of quantity) in exports of goods in 2001 went up by 5.1 per cent, and in visible imports by 0.4 per cent.

The currencies of euro zone account for the bulk of trade

Slovenian terms of trade slightly improved following two worsening years in a row

After two consecutive worsening years, the Slovenian terms of trade slightly improved in 2001. This turnaround by 0.9 per cent (-5.1 per cent a year earlier) was largely a consequence of favourable developments in the second half of the year when lower oil prices and the halt in the depreciation of the euro against the US dollar entirely checked the growth in import prices. In comparison with the average for 2000, the export prices denominated in dollars increased by 0.8 per cent, and dollar-denominated import prices fell by 0.1 per cent over the same period. Just above three-quarters of the change for the whole year in terms of trade could be accounted for by changes in exchange rates. As an illustration of the argument, the increase in the value of the US dollar in comparison with the euro was mirrored in a fall of Slovenian dollar-denominated export prices that averaged 3.0 per cent annually, while import prices declined by 3.8 per cent.

Changed composition of imports of goods by economic purpose

The movements in the composition of domestic spending also affected the change in the composition of imports of goods according to economic purposes. A glance at the components of imports show that the share of capital investment goods declined (down from 16.2 per cent to 15.4 per cent), while the share of imports of raw materials increased (to 59.3 per cent) and imports of consumer goods were up (to 25.3 per cent). In contrast with imports, investments grew faster than other items on the export side, and for the second year in a row this item had a 7.8 per cent annual growth rate. Raw materials ranked next in growth (6.5 per cent) and exports of consumer goods after that (4.7 per cent). The share of exports of raw materials rose from 52.8 per cent to 53.0 per cent, investments grew from 10.4 per cent to 10.5 per cent, while only the share of exports of consumer goods declined from 36.9 per cent in 2000 to 36.4 per cent in 2001. The balance of trade flows showed a reduction in imports of raw materials and investments, both items declined by approximately 20.0 per cent in comparison with 2000; the surplus in consumer goods strengthened again last year by 11.6 per cent at US$ 800 million.

Growing market shares of Slovenian exporters in EU markets

According to preliminary figures, export competitiveness measured by the share that Slovenian exporters have in the markets of the European Union improved in 2001. This share rose most strongly in Austria and Germany, and declined in Italy, while the Croatian market has hardly changed over the past few years. After a strong reduction in 1999, the share of exports from Slovenia going to the market of the Russian Federation once again increased and is approaching the value achieved before the financial crisis of 1998.

Deeper changes in the regional structure of trade regarding exports than imports

The regional composition of Slovenia's foreign trade has been changing over recent years in a more accelerated way on the export than on the import side. Due to the strengthening of exports to the markets of the countries of former Yugoslavia and the Soviet Union after 1999, the proportion of exports to the EU Member States started to reduce at the same time and in 2001 stood at 62.2 per cent - are lowest level since 1992. There was practically no change in the share of imports from the countries of the European Union - down from 67.8 per cent in 2000 to 67.7 per cent last year. The order of the EU Member States, which have accounted for more than a half of Slovenia's trade, remained unchanged. Among the trading partners Germany was in the top position (exports 26.2 per cent, imports 19.2 per cent), Italy second (12.5 per cent and 17.7 per cent), followed by Austria (7.5 per cent and 8.3 per cent) and France (6.8 per cent and 10.6 per cent). The main feature of trade with this group of countries is that in 2001, the share on the export side

Table 2: **Regional composition of foreign trade** (in millions of US dollars)

	EXPORTS			IMPORTS			TRADE BALANCE		
	1999	2000	2001	1999	2000	2001	1999	2000	2001
European Union (15)	**5,650**	**5,580**	**5,758**	**6,945**	**6,856**	**6,863**	**-1,295**	**-1,276**	**-1,106**
Austria	622	656	693	805	833	844	-183	-177	-151
France	491	619	628	1,100	1,043	1,079	-609	-424	-451
Italy	1,176	1,188	1,158	1,686	1,761	1,793	-511	-574	-635
Germany	2,627	2,376	2,428	2,072	1,918	1,949	555	457	480
CEFTA	**622**	**692**	**741**	**851**	**920**	**967**	**-229**	**-228**	**-226**
Czech Republic	159	151	168	281	252	249	-122	-101	-81
Hungary	145	168	157	267	294	315	-123	-125	-158
Poland	190	226	242	111	138	144	79	89	98
EFTA	**112**	**125**	**120**	**239**	**213**	**172**	**-127**	**-88**	**-52**
Non-European OECD members	**379**	**391**	**347**	**613**	**608**	**591**	**-234**	**-217**	**-244**
USA	258	270	244	293	299	297	-34	-30	-53
South Corea	8	13	11	104	73	63	-96	-59	-52
Countries of the former Yugoslavia	**1,296**	**1,364**	**1,564**	**572**	**594**	**540**	**724**	**769**	**1,024**
Bosnia and Herzegovina	363	374	397	56	58	62	308	316	335
Croatia	671	688	799	444	448	404	227	240	395
FR of Yugoslavia	85	143	236	36	41	47	49	102	188
Countries of the former USSR	**213**	**281**	**410**	**201**	**263**	**323**	**12**	**18**	**88**
Russian Federation	129	191	281	159	231	281	-30	-40	0
Other countries	**274**	**300**	**313**	**661**	**662**	**689**	**-387**	**-362**	**-376**
TOTAL	**8,546**	**8,732**	**9,252**	**10,083**	**10,116**	**10,145**	**-1,537**	**-1,384**	**-893**

Source: The Statistical Office of the Republic of Slovenia; the data for 2001 are preliminary figures.

reduced and increased on the imports side. The deficit with the Member States of the European Union was US$1,106 million, less by US$170 million than in 2000.

The biggest deficit for the second consecutive year was recorded with Italy (US$635 million), followed by France (US$451 million) and Austria (US$151 million). Nevertheless, Slovenia has had a relatively high surplus in the trade of goods with Germany over several years; during the year under review, it was US$480 million and above the 2000 figure by US$23 million.

Rapid growth in trade with the republics of former Yugoslavia…

For the second year in a row, trade with the countries of former Yugoslavia grew at an above-average rate. Measured in US dollars, it rose by 5.2 per cent and 14.7 per cent in 2000 and 2001 respectively. The growth in exports to the F.R. Yugoslavia was fastest and is expected to continue over the next few years as normalization of economic relations follow after being absent for a long time.

The modest increase in imports from the Federal Republic of Yugoslavia may be a limiting factor for trade between the two countries. Slovenian companies exported in 2001 goods in the value of US$ 236 million. Croatia remained the most important trading partner from the group of countries of former Yugoslavia as it accounted for half of Slovenia's exports to this group (US$799 million) and three quarters of imports from these countries (US$404 million). The surplus generated through trade with the countries in the region increased in 2001 by US$255 million to US$1,024 million being only US$82 million lower than the deficit incurred in trade with the countries of the European Union.

…and huge surplus in trade with the countries of former Soviet Union

During the year under review, the surplus generated in the trade of goods with the republics of the former Soviet Union was US$88 million, four times more than the average of the preceeding two years, but still falling short of the surplus generated in 1998 (US$114 million).

The trade in goods with CEFTA countries exceeded average growth, exports 7.1 per cent and imports 8.1 per cent. The deficit from the trade with this group of countries was US$226 million and has not in the main changed over the last three years. Slovenia's surplus in trade with Poland amounted to US$98 million for 2001, while a fast-increasing deficit with Hungary rose to US$158 million.

Trade in services continued to grow

In 2001, the trade in services continued to grow. Exports of services in comparison with 2000 rose by 6 per cent and imports by 2 per cent in real terms, the surplus was US$501 million – up by US$65 million year-on-year.

Tourism and transport contributed to the increased surplus with US$37 million and US$42 million, respectively. Aggregate receipts generated by tourism in 2001 totalled US$995 million, and attained a 7-per-cent real rise. Payments for tourism grew at a more moderate rate - by 3 per cent in real terms and in the year totalled US$518 million. The surplus from tourism was up from US$440 million to US$477 million.

Transport services did well in the second half of the year, with increased exports on the one hand and decreased imports on the other, and recorded a net positive balance of US$181 million (a year earlier: US$138 million). Construction services showed a higher surplus than in 2000, partly as a result of the growth in exports, even more so due to lower imports. Among the services, which are generally imported, the imports of communications services and the imports of patents, licences and copyrights edged higher with the overall volume of imports up by US$60 million. The services with high deficit figures - business and technical services - were in the red for 2001 with a deficit of US$90 million. This group of services showed a growth in imports of 9 per cent and a rise in exports of as much as 16 per cent (both in dollar-denominated values).

Preliminary figures show that profits of foreign investors amounted to US$134 million

In 2001, net inflows of income stemming from employment remained at approximately the same level in real terms as a year earlier and amounted to US$156 million. Expenses from capital as in previous years net outflows with a deficit of US$231 million – US$47 million more than in 2000. As external assets and liabilities went up, both income and expenses from capital increased. Income from capital, largely on foreign exchange reserves of the Bank of Slovenia and commercial banks, were in dollars higher by 27 per cent (US$63 million). Capital expenses increased by approximately the same percentage (26 per cent), but the absolute increase was higher (US$110 million). Preliminary figures for 2001 indicate that profits generated by foreign investors amounted to US$134 million (up in US$ by 3.9 per cent), being composed of one third of distributed and other two thirds of undistributed, that is reinvested profit. The latter has been added to the amount of last year's foreign direct investment. The remaining part of expenditure paid from capital, which is largely interest accrued on the external debt and reached US$395 million, was 36 per cent more than the year 2000.

Current account transfer flows continued to rise throughout 2001 with inflows up by 14 per cent and outflows by 16 per cent. The surplus rose from US$116 million in 2000 to US$128 million.

Table 3: **Balance of payments** (in millions of US dollars; preliminary figures for 2001)

	1996	1997	1998	1999	2000	2001
A. CURRENT ACCOUNT	**31**	**11**	**-147**	**-783**	**-611**	**-67**
- in % of GDP	**0.2%**	**0.1%**	**-0.8%**	**-3.9%**	**-3.4%**	**-0.4%**
1. Goods	-825	-776	-789	-1,245	-1,139	-622
2. Services	633	630	492	364	436	501
2.1. Transport	73	97	131	142	139	181
2.2. Travel	638	669	530	415	440	477
- thereof: exports	1,240	1,187	1,088	954	961	995
2.3. Other	-78	-136	-169	-193	-143	-157
3. Income	132	39	28	-24	-25	-75
3.1. Labour income	210	179	179	174	160	157
3.2. Investment income	-78	-140	-151	-199	-184	-231
4. Current transfers	91	118	122	123	116	128
B. NET FINANCIAL INFLOWS	**871**	**666**	**347**	**650**	**1,072**	**1,647**
- in % of GDP	**4.6%**	**3.7%**	**1.8%**	**3.2%**	**5.9%**	**8.7%**
1. The State: Government bonds [1]	163	184	113	365	224	187
Other (including loans)	-69	-27	-20	16	128	-9
2. Bank of Slovenia	129	-9	-51	-51	12	-9
3. Private sector:						
3.1. Direct investment from abroad [2]	129	335	248	181	176	442
3.2. Portfolio investment from abroad [2]	68	92	6	-3	25	10
3.3. Commercial loans	-294	-339	-428	-335	-179	-210
3.4. Loans from abroad	529	357	294	754	820	606
- Banks [1]	291	-15	41	257	277	126
- Enterprises	238	372	253	497	542	480
3.5. Other (together with all outflows)						
- Households	37	151	89	-223	1	691
- Banks, enterprises	186	-156	33	-80	-176	-108
4. Statistical error	-5	77	62	27	43	47
C. FOREIGN EXCHANGE RESERVES (increase (-))	-902	-678	-200	132	-461	-1,580
1. Bank of Slovenia	-587	-1,287	-112	126	-196	-1,282
2. Banks	-315	610	-88	6	-265	-298

1 The transactions effected by domestic banks involving government bonds are deducted.
2 The data between September 1996 and February 1997 are estimated under the unchanged aggregate of direct and portfolio investments.

Source: Bank of Slovenia.

Net financial inflows in 2001 totalled US$1,647 million or 8.7 per cent of the GDP estimate. In comparison with the past few years, there were less debt-related and more equity-related inflows, this figure being 42 per cent of overall financial net inflows. This is a result of the migration of foreign currency cash from individuals to banks upon the changeover to euro notes and coins.

Net financial inflows were over 8 % of the estimated GDP…

The bulk of financial inflows entered the country through the private sector, while the government borrowed abroad 50% less than in 2000. In 2001 the government issued Eurobonds twice: first in February when with an additional 100 million euros it supplemented the issue from the year 2000, and second in April with a new issue of Eurobonds in the amount of 450 million euros.

… and mainly entered the country through the private sector

Eurobonds from 1996 came to maturity in August in the amount of US$325 million. By taking into account the transactions involving government bonds and net repayment of foreign loans in the amount of US$9 million, Slovenia's debt to foreign creditors rose in 2001 by US$178 million net (2000: US$352 million).

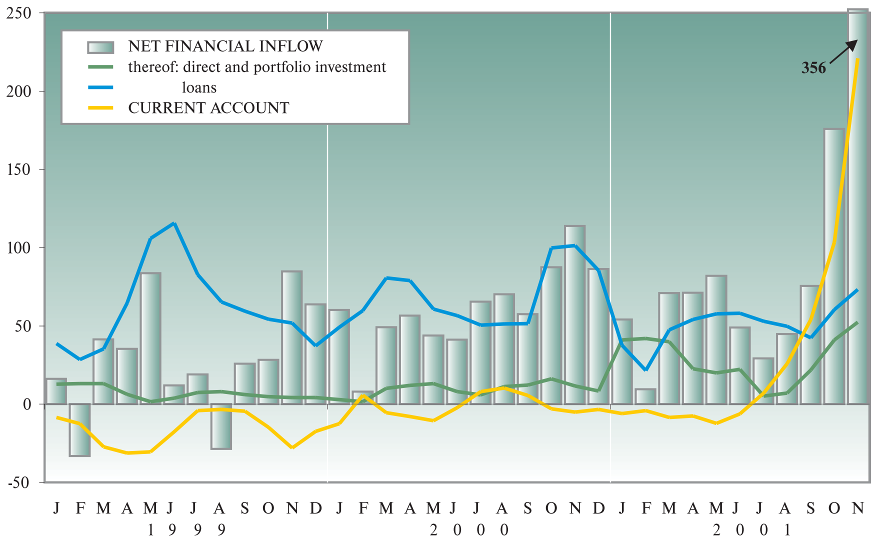
Net inflows into the private sector rose from US$666 million in 2000 to US$1429 million in 2001. Almost one half of this kind of inflows in 2001 were inflows of foreign cash through the household sector (estimated at US$691 million), which citizens placed with the banking system upon the changeover to the euro. If this extraordinary inflow were excluded, the net inflows into the private sector would be slightly above the previous figures but would not exceed 4 per cent of the GDP estimate.

Almost a half of net inflows in private sector was effected through households when euro cash was introduced

In 2001, inward foreign direct investment totalled US$442 million, two-and-a-half times that in 2000. The majority of foreign investment was made in telecommunications and banking and the number and volume of the remainder and smaller investments went up as well. With the net amount of US$10 million, portfolio investments made by non-residents were more modest than before (US$25 million), and the decline of importance in equity investments made by foreign investors indicates that there is a long-term interest of foreign investors in the purchase of participationa in Slovenian companies.

Foreign direct investment jumped to two-and-a-half times that of 2000

Chart 5: **Current account of the balance of payments**
(in millions of US dollars, moving average 3)



Source: Bank of Slovenia.

Most Slovenian outward direct investment went to the markets of former Yugoslav republics

After of the changes of the political framework and the promise of economic recovery in the countries, which originate from the territory of former Yugoslavia, investments made by the Slovenian companies in those areas picked up. The value of Slovenian outward direct investment amounted to US$104 million in 2001 with predominantly an almost three-quarter share in former Yugoslav republics.

Downswing in cross-border financing for Slovenian companies

Financing of enterprises by borrowing abroad reduced in comparison with a year earlier by US$62 million to US$480 million, the share of foreign financing in aggregate corporate financing after a sharp upturn in 2000 (to 44 per cent) last year declined to 35 per cent. Enterprises borrowed less abroad and the maturity structure of financing changed with the share of short-term loans increasing, financing traditionally provided in the past by the domestic banks. Domestic banks borrowed abroad in 2001 substantially less than in the two previous years - net US$126 million (as opposed to US$277 million in 2000). As regards assets which are amounts owed by foreign parties, net granted commercial loans remained the most important item in 2001, and for the year under review amounted to US$210 million, 31 million dollars more than a year earlier. Lending to enterprises abroad amounted to US$23 million net.

A greater corporate tendency towards short-term cross-border borrowing in 2001 lifted slightly the share of short-term debt during the year under review (to 3 per cent of aggregate debt), although the bulk of the debt at the end of the year was repaid; hence the share of short-term borrowing slipped back (1.9 per cent). The average maturity of new lending was cut down from 7 years and 7 months in 2000 to 7 years and 4 months in 2001. The average indexed interest rate charged on new lending was 5.5 per cent, two percentage points below the respective figure in 2000.

Aggregate foreign exchange reserves of the Bank of Slovenia and banks went up by US$1,578 million

Cross-border transactions pushed up aggregate foreign exchange reserves of the Bank of Slovenia and banks by US$1,578 million in 2001. The balance of foreign exchange reserves at the end of the year topped US$5,738 million or US$1,362 million more than at the end of 2000. The smaller rise in reserves, arising from the cross-border transactions was affected by the changes favouring the US dollar (US$216 million).

Table 4: **Slovenia's external debt** (balance at year-end in millions of US dollars)

	1997	1998	1999	2000	2001
Total external debt	4,123	4,915	5,400	6,217	6,717
1. Short-term debt	135	110	117	99	126
in % of the total debt	3.3	2.2	2.2	1.6	1.9
2. Long-term debt	3,988	4,805	5,283	6,118	6,591
- public and public-guaranteed	2,014	2,326	2,451	2,665	2,710
- private non-guaranteed	1,974	2,479	2,832	3,453	3,881
External debt/GDP in %	22.6	25.0	26.9	34.2	35.7
External debt/exports in %	39.4	44.2	51.3	58.1	59.5
Debt servicing in GDP	5.6	7.6	5.0	6.6	9.7
Debt servicing in exports	9.8	13.4	9.6	11.1	16.1
Interest servicing in GDP	1.3	1.2	1.3	1.6	1.9
Interest servicing in exports in %	2.2	2.1	2.4	2.8	3.1
Foreign exchange reserves/external debt in %	106.2	97.3	76.2	70.4	85.4
Foreign exchange reserves/short-term debt by maturity*	1.18	1.39	1.14	1.05	1.56

* All gross cross-border liabilities except equity with maturity within the next 12 months.
Source: Bank of Slovenia.

Since the proportion of inflows other than of debt nature (direct investment and inflows through households) was significant, a large portion of inflows did not result in increasing Slovenia's external debt. Against this background, new net borrowing added US$782 million, one half less than the increase in foreign exchange reserves. Slovenia's external debt (year-end stock) was US$6717 in 2001 million after a rise of US$500 million.

The currency composition at the end of 2001 shows that 85.1 per cent of external debt was denominated in the euro, 8.1 per cent in US dollars and 6.8 per cent in other currencies. The share of the US dollar stood at 13.3 per cent in July and sharply dropped in August after redeeming bonds denominated in US dollars.

Slovenia remains among the countries with low debt

Standard indicators of the burden of external debt still rank Slovenia among low debt countries, particularly measured by the indicators that weigh debt servicing by export capability of the private sector. The only indicator that placed Slovenia in 2000 among the countries with the medium-level of debt is the share of external debt in GDP. This figure increased in 2001 by 1.5 percentage points.

In comparison with external liquidity and the possibility that the government could find itself in liquidity difficulties, the burden imposed by external liabilities has been significantly alleviated. The level of Slovenia's foreign exchange reserves was at the end of 2001 56 per cent above that considered necessary to ensure repayment of all pending and contingent liabilities to non-residents over the next 12 months, taking into aacount short-term commercial loans and deposits from non-residents (gross short-term debt by maturity).

1.5. Public finance

Government budget enacted in May

The country's general elections held late in 2000 postponed the adoption of the 2001 budget to early May 2001. Consequently, the so-called temporary financing was still being implemented. The beginning of the fiscal year was marked by the temporary financing and also by the transfer of a portion of unsettled liabilities from the year 2000 in the amount of 23 billion tolars to the year 2001. A landmark event in the general government area was the launch of the privatisation of the two biggest state-owned banks, Nova Ljubljanska banka and Nova Kreditna banka Maribor and proceeds from the sale are expected to come in over the next two years. The government also sold at the end of the year a licence for the new generation of UMTS mobile telephony and realised 22 billion tolars. In time well ahead of the new fiscal year.the budget for the next two years was adopted.

Preliminary figures show general government deficit at 63 billion tolars or 1.4 per cent of GDP

In 2001, the general government deficit as indicated on the basis of preliminary estimates was 63 billion tolars or 1.4 per cent of GDP, and remained in line with the Government's plan. The general government deficit is composed of four areas of public finance: the government budget, municipality budgets, the Fund of the Pension and Disability Insurance Institute of Slovenia, and the Health Insurance Institute of Slovenia (both solely in compulsory insurance). Local government budgets and the Pension and Disability Insurance Institute ended the fiscal year with a surplus, while the state budget and Health Insurance Institute with deficits.

Among general government revenue, the sharpest growth in taxes on personal income and corporate profits

According to provisional estimates, total general government revenue in 2001 amounted to 1,967 billion tolars or approximately 43.3 per cent of GDP, and total general government expenditure to 2,030 billion tolars or 44.7 per cent of GDP. Both items slightly exceeded the figures planned by the government. As regards the major components of general government revenue, personal income taxes and corporate income tax were the items that reached real growth of approximately 6.0 per cent and generated an inflow in the amount of 358 billion tolars in 2001. Social security contributions with a lower growth of 3,6 per cent in real terms accounted for an inflow of 621 billion tolars in 2001. Domestic taxes levied on goods and services, which related primarily to value-added tax and excise duties, achieved a 3.0 per cent real growth and an inflow of 673 billion tolars. Just, as in preceding years, January income from VAT and excise duties in 2001 was allocated to budgetary revenue for 2000, while January revenues from VAT and excise duties in 2002 were allocated to budgetary revenues for 2001. This lag in revenues is expected to be levelled off in 2002, so that the revenues in 2002 will not feature added January revenues from VAT and excise duties from 2003 and will impact with a higher deficit in 2002.

Among general government expenditure wages rose most

As regards general government expenditure, early estimates show that expenditures on wages and allowances in state administration and public institutions showed the fastest growth (8.6 per cent in real terms) totalling 456 billion tolars in 2001. Expenditure on purchases of goods and services grew more slowly (5.8 per cent in real terms) and by the end of the year under review amounted to 385 billion tolars. Transfers to households, of which pensions accounted for the greater pat, rose in real terms by 3.6 per cent and amounted to 821 billion tolars.

As regards the lending and repayments account in 2001, net inflows totalled 13 billion tolars, an increase in comparison with a year earlier when this figure amounted to 5 billion tolars. Almost the whole of the inflow is a consequence of net repayment of a loan to the government, albeit there was still no substantial privatisation flow in 2001.

The government issued new and redeemed mature Eurobonds

The financing account of all four general government funding areas showed in 2001 approximately 73 billion tolars in net debt. The key feature was that net borrowing at home (53 billion tolars) was higher than net cross-border borrowing (20 billion tolars). The Republic of Slovenia raised funds by issuing government bonds (93 billion tolars), by means of loans it reduced debt by 20 billion tolars net. Other events in relation to the issuance of government bonds were the issues and redemption of Eurobonds, the commencement of the issue of one-month Treasury bills and the start of trading in Treasury bills in the secondary market. In 2001, the government first increased in February the issue of Eurobonds from 2000 by 100 million euros, and then in April it launched a new issue in the amount of 450 million euros. The repayment of the principal of the Eurobonds issued in 1996 in the amount of 325 million went abroad when it fell due in August and accounted for a major outflow. Amongst domestic bonds, a one-month Treasury bill was underwritten for the first time in the month of May and its issued quota amounted to 2 billion tolars on the commencement date, while at the end of the year it reached 5 billion tolars. In mid-December, trading in Treasury bills in the secondary market commenced.

The debt of the Republic of Slovenia as at 31 December 2001 amounted to 1,229 billion tolars, approximately one half of the debt was to domestic sectors, another half to foreign creditors. Only 18 per cent of the debt stems from borrowing, the rest refers to securities issued by government.

2. MONETARY POLICY

2.1 Monetary policy objective and money supply

Shift from M3 to two pillars of monetary policy indicators

The Bank of Slovenia Act gives the Bank of Slovenia operational responsibility for securing the stability of the domestic currency and the overall liquidity of domestic and cross-border payments. A Commitment to lower inflation to the level maintained by the EU Members States remained the definitive aim of the Bank's monetary policy strategy. With the long-term inflation targeting policy, the broad monetary aggregate M3 has been used as the intermediate monetary policy objective since 1997. The inter-link between monetary policy and M3 on the one hand and M3 and price stability as the ultimate monetary policy objective on the other is long-term. Hence the Bank of Slovenia also deploys other indicators for continuous monitoring and management of monetary policy. Since November 2001 when a new framework for the monetary policy pursued by the Bank of Slovenia was adopted, the steering of monetary policy takes into account two pillars (see Box 1). The first pillar takes account of the quantity of money in circulation, that is a group of explanatory indicators, while the second one takes into consideration the indicators that supplement information about economic health as well as those that indicate expansion or restriction of monetary policy.

Box 1: **Intermediate monetary policy target and new monetary policy framework of the Bank of Slovenia**

The Governing Board of the Bank of Slovenia adopted on 30 January 2001 an intermediate monetary policy target for the year 2001 having the following features: M3 monetary aggregate annual growth in the range between the average for the last quarter of 2000 and the last quarter of 2001, namely in the 11% to 17% band. The assumption for meeting the set monetary policy target was real GDP growth of 4.0% p.a., general government deficit up to 1.3% of GDP, i.e. public finance expenditure being 42.8% of GDP, and growth in real wages and salaries of up to 2.5%. As regards currency stability, the Bank of Slovenia declared a commitment to matching the conditions proclaimed by the Government in relation to inflation in 2001.

Furthermore, the Bank of Slovenia made the assumption that inflationary pressures and inflation would depend mainly on domestic factors - more specifically on general wage growth, as well as on the administered prices policy implementation. The background to the assumptions of the Bank of Slovenia was a commitment by social partners to being moderate and reasonable when negotiating wage policy. The Bank of Slovenia continued to subscribe to the policy of concern for the stability of the domestic currency while creating the conditions necessary to equalize the costs of financing at home and abroad, and to set up conditions for adequate money supply in Slovenia.

The actual annual growth in M3 measured as explained above, was 23.9%. This percentage was by 6.9 percentage points above the ceiling of the intermediate target. Having reviewed the results, the Governing Board of the Bank of Slovenia concluded at its session held on 28 February 2002 that monetary policy pursued in 2001 was in line with the endorsed guidelines, whereas the excess over the target ceiling was attributable to the movements in the balance of payments.

In line with Slovenia's convergence with the European Union, the Bank of Slovenia in November 2001 reframed its strategy of steering monetary policy in the period of moving nearer to the EMU. At the same time the medium-term inflation target of lowering inflation to 4% by the end of 2003 was adopted. Growth in broad monetary aggregate M3 as the catalyst to the process will decline in the course of 2002 to between 12% and 18% and between 9% and 15% in 2003. The new strategy establishes that the implementation of monetary policy rests on two pillars. The first pillar is composed of the quantity of money in circulation, that is a group of underlying indicators such as the banking system liquidity, short-term interest rate movements, the composition of monetary aggregates, and banks' credit activity. The second monetary policy pillar takes into account a broader spectrum of information, the indicators being the balance of payments, cross-border interest rates and interest rate difference, foreign exchange rate, wages and growth in administered prices.

Assumptions taken into account when drafting monetary policy

For the purpose of monetary policy planning in 2001, the Bank of Slovenia took into account the parameters stemming from the macro-fiscal scenario and the premises for drafting the budget of the Republic of Slovenia for 2001 and 2002. These parameters were an annual GDP growth rate of 4.0%, annual growth in real net wages of 2.5%, government sector deficit of 1.3 % of GDP, and public finance expenditure of 42.8% of GDP.

Actual performance different from anticipated

As regards the domestic economy, performance was different from analysts expectations made in early 2001. The latest projections indicate that during the year under review, economic growth was below the estimate and the current account balance was level most of the time owing to favourable foreign demand and lower imports but still ending the year with a minimal deficit. Capital inflows were unexpectedly stronger, and with the balanced current account financing the current deficit, international foreign exchange reserves, increased and exerted pressure to appreciate the tolar.

Inflation decreased but it was higher than expected

Inflation measured by consumer prices was 7.0% in December 2001 and it was higher than expected due to the increase in prices of food (10.8%) and services (8.1%). Non-administered prices increased by 7.9% as opposed to a 3.6% rise by administered prices.

Government sector deficit curbed at the 2000 level

The government sector deficit is estimated to have reached 1.4% of GDP - slightly above the projected figure. The principal reason for exceeding the projected deficit was in modest domestic spending and consequently flatter revenue from taxes on goods and services (down by 2.0% in real terms).

Foreign exchange rate policy

Within the framework of the set objectives, the Bank of Slovenia aided the growth in exchange rates for foreign currencies by making possible a lowering of inflation and partial closing of the interest rate gap between domestic and foreign interest rates. Since September, the Bank of Slovenia has also responded to changes in the foreign exchange market by sending signals setting the highest selling and the lowest buying exchange rates, and thus it backed growth in market exchange rates. At the end of October, the Bank of Slovenia signed with banks an annex to the agreement on participation in interventions of the Bank of Slovenia in the foreign exchange markets and set both the refinancing interest rate and interest rate for investments made with the Bank of Slovenia.

Table 5: **Base money supply** (in billions of tolars)

	As at 31 December			Quarterly changes in 2001				
	1999	**2000**	**2001**	**I**	**II**	**III**	**IV**	**Total**
1. Net foreign assets	633.5	742.0	1122.2	31.2	174.7	-1.0	175.3	380.2
2. Foreign-currency domestic liabilities	-334.3	-394.0	-490.0	-14.5	-100.9	46.7	-27.2	-96.0
- foreign currency bills	-310.4	-358.3	-458.8	-19.8	-21.3	-39.0	-20.4	-100.5
- foreign currency deposits by the Budget	-23.9	-35.7	-31.2	5.2	-79.7	85.7	-6.8	4.5
3. Net foreign-currency assets (1+2)	**299.2**	**348.0**	**632.3**	**16.7**	**73.8**	**45.7**	**148.1**	**284.3**
4. Time deposits by the Budget	**0.0**	**0.0**	**-19.9**	**0.0**	**-13.8**	**11.4**	**-17.5**	**-19.9**
5. Loans to banks	**22.0**	**6.8**	**0.5**	**3.0**	**4.8**	**-8.6**	**-5.6**	**-6.3**
6. Tolar bills	**-27.4**	**-6.9**	**-125.9**	**-6.7**	**-22.5**	**-46.0**	**-79.1**	**-154.3**
7. Other, remaining net liabilities	**-83.2**	**-132.3**	**-225.9**	**-17.1**	**-31.7**	**-2.2**	**-7.4**	**-58.3**
8. Net Tolar assets (4 to 7)	**-88.6**	**-132.4**	**-371.3**	**-20.7**	**-63.3**	**-45.3**	**-109.5**	**-238.8**
9. Base money (3+8)	**210.5**	**215.6**	**261.0**	**-4.0**	**10.6**	**0.4**	**38.5**	**45.4**
- bank reserves	79.4	87.4	103.2	2.3	-1.8	2.6	12.8	15.8
- other sight deposits	6.2	8.4	15.6	0.2	1.3	-0.5	6.3	7.3
- cash in circulation	125.0	119.8	142.1	-6.5	11.0	-1.7	19.5	22.3

Source: Bank of Slovenia - excluding accrued interest and discounts.

Gradual rise in interest rates in the first half and decline in the second half of 2001

The Bank of Slovenia with a rise in interest rates during the first six months of 2001 supported a restrictive adjustment of monetary policy and it thus responded to the continued trend of high inflation. The Bank was decreasing its interest rates in the second half of 2001 in response to rising pressures on the foreign exchange market and the shrinking base interest rate prompted by declining inflation.

Further rationalisation of instruments of the Bank of Slovenia

The Bank of Slovenia also made efforts for rationalisation and greater transparency of its instruments during the year 2001. Already at the beginning of 2001 the Bank discontinued euro- and dollar-denominated bills with maturity of 180, 270 and 360 days. In addition, the Bank discontinued 2-day tolar-denominated bills – they were replaced by an overnight deposit facility – and 12-day tolar-denominated bills and a 3-day liquidity loan facility, which the banks could tap into against pledging those bills as collateral.

21.4% increase in the base money

The issuance of base money in 2001 flowed from foreign exchange transactions, primarily by using the instrument of a foreign exchange swap. The Bank of Slovenia withdrew base money net by tolar-denominated transactions, largely by issuing tolar-denominated bills. Base money increased by 45.4 billion tolars. Nearly half (49.1%) of the increase in base money came from the increase in cash in circulation, 34.8% from the increase in reserves of commercial banks, and the rest came from demand deposits with the Bank of Slovenia.

Issuance of base money through foreign exchange transactions

Annual growth rates of base money and its two most important components after a decline for almost two years in a row (since VAT was introduced in 1999) resumed growth in 2001, being at a high mainly at the end of the year. On average, base money increased at 8.5% per annum, cash in circulation went up by 7.2%, reserves of commercial banks increased by 8.2% and demand deposits with the Bank of Slovenia jumped by 27.5%.

Table 6: **M3 supply: consolidated balance sheet of the monetary system**
(in billions of tolars)

	As at 31 December			Quarterly changes in 2001				
	1999	**2000**	**2001**	**I**	**II**	**III**	**IV**	**Total**
1. Net foreign assets	**702.0**	**811.2**	**1,241.2**	**76.7**	**163.4**	**-43.2**	**233.1**	**430.0**
2. Domestic assets	**1,753.3**	**2,047.8**	**2,404.4**	**96.6**	**78.9**	**88.7**	**92.3**	**356.6**
Public sector: bonds	300.9	326.5	376.0	27.7	23.4	7.1	-8.8	49.5
loans	127.2	152.5	168.2	-1.2	-12.1	10.4	18.6	15.7
Enterprises : securities	77.2	90.8	114.3	1.1	2.7	6.9	12.7	23.4
loans*	809.0	983.0	1,209.5	62.4	53.6	47.3	63.2	226.5
Households: loans*	438.9	495.0	536.4	6.6	11.3	17.0	6.6	41.5
3. Securities issued	**-63.9**	**-79.2**	**-113.6**	**-4.6**	**-10.2**	**-11.1**	**-8.5**	**-34.4**
4. Foreign currency deposits by the Budget	**-23.9**	**-35.7**	**-31.2**	**5.2**	**-79.7**	**85.7**	**-6.8**	**4.5**
5. Other, remaining net assets	**-454.4**	**-537.9**	**-624.1**	**-50.2**	**-36.5**	**-10.8**	**11.3**	**-86.2**
6. M3 (1 to 5)	**1,912.9**	**2,206.2**	**2,876.7**	**123.7**	**116.0**	**109.3**	**321.5**	**670.5**
- foreign currency deposits with banks	497.8	663.6	922.3	61.9	36.4	24.3	136.1	258.6
7. M2	**1,415.1**	**1,542.6**	**1,954.4**	**61.9**	**79.5**	**85.0**	**185.4**	**411.8**
- time deposits with banks	890.9	970.6	1,261.7	80.3	20.2	96.8	93.7	291.0
- time deposits with the Bank of Slovenia	0.0	0.0	19.9	0.0	13.8	-11.4	17.5	19.9
- savings deposits	124.5	148.0	170.7	2.8	10.5	-0.7	10.1	22.7
8. M1	**399.8**	**424.0**	**502.2**	**-21.3**	**35.1**	**0.3**	**64.1**	**78.2**
- sight deposits with banks	268.6	295.8	344.4	-14.9	22.7	2.5	38.4	48.6
- sight deposits with the Bank of Slovenia	6.2	8.4	15.6	0.2	1.3	-0.5	6.3	7.3
- cash in circulation	125.0	119.8	142.1	-6.5	11.0	-1.7	19.5	22.3

* Methodological changeover with regard to lending to enterprises and households in 1999.
Source: Bank of Slovenia.

The monetary aggregate M3 in 2001 increased by 670.5 billion tolars of which almost half was in the last quarter (321.5 billion tolars). The pace of M3 annual growth was accelerating throughout the year and peaked in December with 27.1%.

Strong growth in tolar and foreign exchange deposits

Money aggregate M1 increased on average at 9.5% per annum and was highest in December (16.9%). Since the fastest growth was posted by the components of M3 above transaction money (tolar-denominated time deposits and foreign exchange deposits), high growth in M3 did not produce a direct impact on inflation. The M3 multiplier (between M3 and base money) rose in 2001 from 10.7 to 11.9. The M2 multiplier followed suit by rising from 7.7 to 8.4, while the M1 multiplier remained stable as in preceding years (2000: 1.97; 2001: 1.99).

M3 growth was still strongly influenced by growth in the foreign exchange component. Nonetheless its impact with regard to the tolar-denominated component reduced except in the month of December. Foreign exchange deposits in 2001 contributed to the increase of M3 39%, tolar-denominated time deposits grew by 43%; the remaining part referred to tolar-denominated demand deposit and cash in circulation. Within items consisting of the tolar-denominated time deposits, the deposits with medium-term maturity enjoyed the strongest growth: from 181 days to 1 year rose by 51.2%, and from 91 to 180 days up by 40.2%. Deposits with shorter maturity with agreed maturity of up to 30 days increased by 13.5% and deposit with agreed maturity of between 31 and 90 days rose by 15.6%. There was also a marked growth in long-term deposits - deposits with agreed maturity of over 1 year went up by 32.5%. Due to a fast growth of time tolar deposits that outpaced other components of M3, agreed maturity of tolar-denominated deposits became longer in 2001 (by 7.5 days).

The formation of M3 relied more on net foreign assets than domestic investments

The vigorous growth of M3 was largely prompted by considerable inflows from abroad and the sale of foreign cash and exchange offices at the end of the year under review. Excess supply of foreign exchange resulted in broad money M3 being formed more from net foreign assets than from domestic investments. Net foreign assets increased by 430.0 billion tolars; hence 64% of M3 came from net foreign assets.

Investments of the monetary sector made in 2001were moderate although above the figures a year earlier and amounted to 356.6 billion tolars, of which 70% was invested in the corporate sector, 18% in government, and 12% in households. In comparison with a year earlier, investments in government securities increased and in 2001 were twice as large as in 2000. The annual rate of banks' investments was steady throughout the year under review with rates ranging between 16.5% and 18.0%.

Growth in loans of domestic banks cooled

Aggregate loans granted to the domestic non-bank sector amounted to 283.7 billion tolars in 2001 and accounted for 80% of all investments made by domestic banks. As regards the sectoral breakdown, lending to enterprises amounted to 226.5 billion tolars (80%), 41.5 billion tolars (15%) was lent to households, and lending to government stood at 15.7 billion tolars (5%). Enterprises borrowed more at home than abroad. Thus enterprises borrowed 65% out of the total amount of 349.9 billion tolars in financing granted (home and abroad). The composition of domestic corporate lending shows that the share of long-term tolar loans increased most with the annual growth rate rising from 7.7% in December 2000 to 20.8% in December 2001. Indebtedness of households, which has cooled since the introduction of value-added tax, in the second half of 2001 became steady at an annual rate of around 8.5%. Rather than turning to domestic banks for financing, during the year under review the government opted to issue securities in the amount of 49.5 billion tolars.

2.2. Interest rates

Banks adjusted lending and deposit interest rates to inflation

Inflation rates grew between January and May 2001 (8.5% to 9.7%) and then started to reduce towards the end of the year (7.0%), and banks adjusted lending and deposit interest rates with the minimum time lag possible. In 2000 real interest rates on fixed-term deposits up to 90 days were negative (using CPI as a deflator), but there was a reverse in 2001 and only interest rates on deposits placed for the period of up to 30 days during the first half were negative.

The mid-year rise in the annual inflation rate up to May 2001 influenced the monthly base interest rate (TOM), which in the summer months was at its peak of 10.2% p.a., then fell to 7.3% at the year-end. Consequently, the base interest rate generally recognised as the index factor averaged 8.6% in 2001 and the average annual inflation 8.4%.

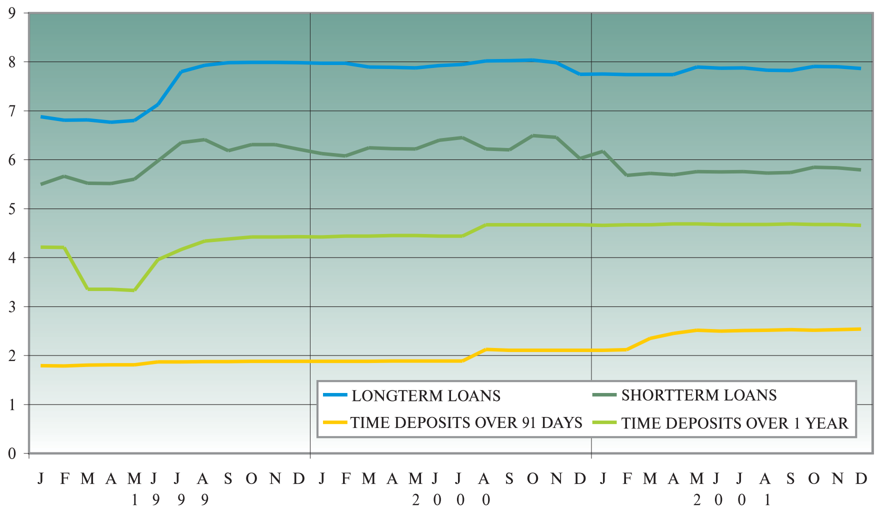
Steeper slope of the time structure of interest rates

At a monthly level, the base interest rate (TOM) ranged between 0.8% and 0.6%, although at the annual level this figure fluctuated more as a result of a different number of days in a month (between 7.3% and 10.2%). This fluctuation largely followed the dynamics of nominal lending and deposit interest rates, although adjustment was more pronounced in the case of short-term nominal interest rates than for the long-term rates. Short-term lending interest rates dropped by 3.0 percentage points during the year under review, while interest rates charged on long-term lending declined by 2.6 percentage points. Therefore, the slope of the time structure of lending interest rates increased. The average nominal interest rate on short-term loans and advances at the end of the year under review stood at 13.5%, i.e. 6.0% over the base interest rate (TOM), and on long-term loans it was 15.7%, i.e. 7.9% over the base interest rate.

Higher interest rates above the base rate on time deposits …

As regards deposit interest rates, there was a lesser reduction in rates compared to lending rates. From December 2000 to December 2001, the nominal interest rate on time deposits with agreed maturity between 91 days and up to one year fell by 2.2 percentage points and on deposits with maturity between 31 days to 90 days this drop was 2.4 percentage points. With a 2.7 percentage point reduction the interest rate paid on long-term deposits (over 1 year) was the most pronounced. Thus the curve of time composition of deposit interest rates, unlike the curve illustrating lending interest rates, was more flat. Nevertheless, it has to be taken into account that TOM fell by 2.6 percentage points and consequently all interest rates over TOM

Chart 6: **Average interest rate bank** (over TOM, in % per annum)



Source: Bank of Slovenia.

on time deposits with the exception of long-term ones slightly increased. The most pronounced changes by banks were during the first quarter of the year as the result of the fact that the recommendations on deposit interest rates made by the Bank Association of Slovenia expired at the end of 2000. It was in December 2000 that the first banks ceased to observe the recommendations when setting its short-term interest rates on deposits placed by legal entities and the trend gained momentum during the first months of 2001 also for other forms of deposits. A cooling of the rise of deposit interest rates was influenced by greater inflows stemming from the sales of equity holdings of non-residents. At the end of 2001, the average interest rate on time deposits with maturity between 31 and 90 days was 1.1% over the base interest rate (8.5% nominal), on time deposit with maturity between 91 days and 180 days it was 2.5% over base (10.0%), on time deposits with maturity between 181 days to one year it was 3.4% over base (11.0%) and for time deposit with agreed maturity over one year 4.7% over the base (12.3%).

… and lower interest rates on foreign exchange deposits

In 2001, interest rates on foreign exchange deposits with banks declined in line with cross border movements in interest rates. Interest rates on foreign exchange fixed-term of over one year decreased last year by 1.4 percentage points (from 3.6% to 2.2%) and on demand foreign exchange deposits dropped by 0.2 percentage points (from 0.9% to 0.7%). In addition to the falling interest rates on deposits denominated in foreign currency the falling rate of growth in the foreign exchange rate followed and it affected the decrease in the yield rate on foreign exchange deposits. Consequently, the average rate of return on fixed-term deposits denominated in euros over one year was 7.8%, and clearly lagged behind the return as the same type of tolar-denominated deposits during the year 2001 which averaged 12.8%.

Strong influence of events in foreign currency markets and monetary policy of the Bank of Slovenia on interest rates

During the first months of 2001, the movement of TOM determined fluctuations in interest rates in the wider money market i.e. market for the Treasury bills of the Republic of Slovenia, and less so the fluctuations in the interbank interest rate on loans with maturity of up to 30 days. As regards the remaining period, a significant factor in setting interest rates was the volume of foreign exchange inflows and the management of exchange rate policy. The interest rate in the interbank money market in the first half of the year under review was in the range between 7.2% and 7.7%, after which it started to fall for the rest of the year until it settled at the level of 4.7%. The behaviour of the interbank interest rate partly changed starting from October 2001, with the amended agreement on the participation of banks in the

Table 7: **Interest rates of the Bank of Slovenia and the money market**
(monthly average balances in 2001, in % annualised)

	Repurchase agreements		Lombard loan	Bank of Slovenia Tolar bills		Money market	Treasury bills			IRIF
	7 days	2 months	1 day	60 days	270 days	up to 30 days	3 months	6 months	12 months	
January	10.75	11.38	11.00	10.00	11.00	7.19	11.21	11.49	11.83	8.56
February	10.60	11.50	11.00	10.00	11.00	7.49	11.32	11.49	11.83	9.52
March	11.22	11.46	11.00	10.63	-	7.27	11.30	11.49	12.33	8.56
April	11.37	11.45	12.00	11.00	-	7.56	11.51	12.28	12.33	8.86
May	11.18	11.32	12.00	11.00	-	7.47	11.36	12.28	12.71	8.56
June	11.03	11.16	12.00	11.00	11.50	7.74	11.40	11.89	12.71	10.18
July	11.00	11.03	12.00	11.00	11.50	7.53	11.40	11.89	12.91	9.84
August	11.00	11.13	12.00	11.00	11.50	6.82	11.14	12.29	12.91	8.56
September	11.00	11.03	12.00	11.00	11.50	6.73	10.93	12.29	12.28	8.86
October	11.00	11.03	12.00	11.00	11.50	6.47	10.66	11.44	12.28	7.30
November	11.00	11.03	12.00	9.06	12.00	5.86	9.73	11.44	11.20	7.55
December	11.00	11.03	12.00	8.35	10.47	4.74	8.54	8.78	11.20	7.30

Source: Bank of Slovenia.

interventions of the Bank of Slovenia in the foreign exchange market and new interest rate on seven-day repo agreements was signed. As a consequence, the Bank of Slovenia also set the refinancing (minimum bid) interest rate at 8.25% – and it dropped to 7.75% early in November – and interest rate on investments with the Bank of Slovenia in the amount of 6.25% (it was also reduced in November by 0.5 of a percentage point). The movements in the interbank interest rate did not depend any longer on the bid rate at auctions of foreign exchange bills of the Bank of Slovenia (repo DBZ), but on the situation on the foreign exchange market and consequently the liquidity of the banking system.

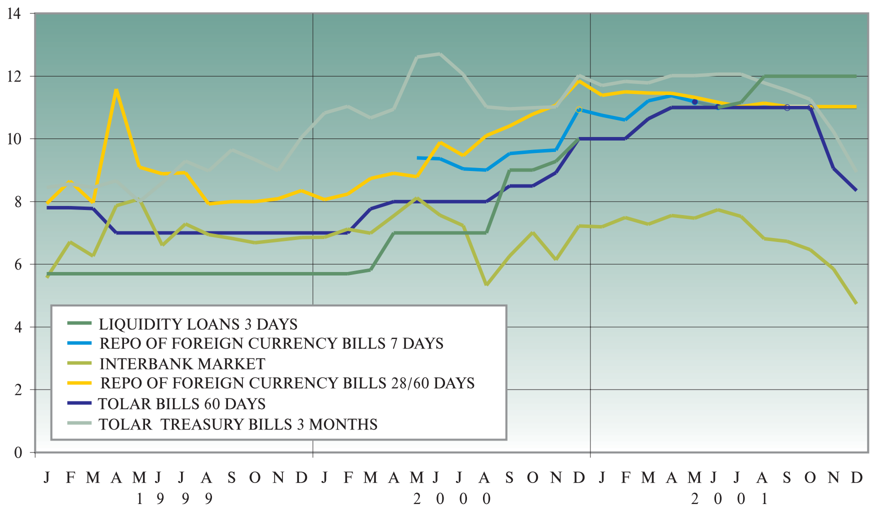
The interest rates of the Bank of Slovenia were raised in the first half of the year under review…

In the first half of the year 2001, the Bank of Slovenia raised its interest rates in line with its commitment to the pursuit of restrictive monetary policy. In April, the discount and Lombard interest rates went up by one percentage point to 11.0% and 12.0%, respectively. A month earlier, the minimum interest rate at auctions for seven-day and two-month repo bills denominated in foreign currency went up to 11.0%. As in the case of the instruments of the base money supply, the Bank of Slovenia also increased during the first half of 2001 the interest rate on tolar-denominated bills, on two- and twelve-day bills by 1.5 percentage points, for 60-day tolar-denominated bills by one percentage point. In June, when the open tender to subscribe for 270-day tolar bills was resumed after four months, the relevant interest rate was increased by 0.5 of a percentage point to 11.5%.

… and decreased in the second half

In the second half of 2001, when the annual inflation rate began to reduce high capital inflows continued and the Bank of Slovenia first cut the interest rates at the end of October and at the beginning of November for tolar-denominated bills, and for the overnight deposit facility, which was available to banks for the first time in July. The interest rates on twelve-day tolar-denominated bills were cut from 8.5% to 7.0% and on six-day bills from 11.0% to 9.0%. At the end of 2001 there was another cut in interest rates on 60-day tolar-denominated bills to 8.0%. The yield on 270-day tolar bills, which since November have been offered for sale at regular auctions, fell to 8.9% at the end of the year.

Chart 7: **Interest rates of the Bank of Slovenia and the money market**
(monthly average above base interest rate, in % per annum)



Source: Bank of Slovenia.

Interest rates on Treasury bills also declined

The new regular weekly offer of one-month Treasury bills launched in May 2001 was yet another step towards boosting the development of Slovenia's money market. From the launch of the offer until the end of 2001¸ the interest rate declined from 10.1% to 7.4%. As with one-month bills, other Treasury bills with different maturities had the highest interest rates in July and August. The interest rate on three-month Treasury bills at that time reached 11.4%, six-month Treasury bills 12.3% and twelve-month Treasury bills 12.9%. Following the introduction of 270-day tolar-denominated bills available for sale at auctions, the bid rates of yield for the residual maturity period for specific maturity bands of Treasury bills fell to the lowest value during the year. As a consequence, at end-December 2001, the interest rate on three-month Treasury bills was 8.5%, on six-month Treasury bills 8.8% and on twelve-month Treasury bills 11.2%.

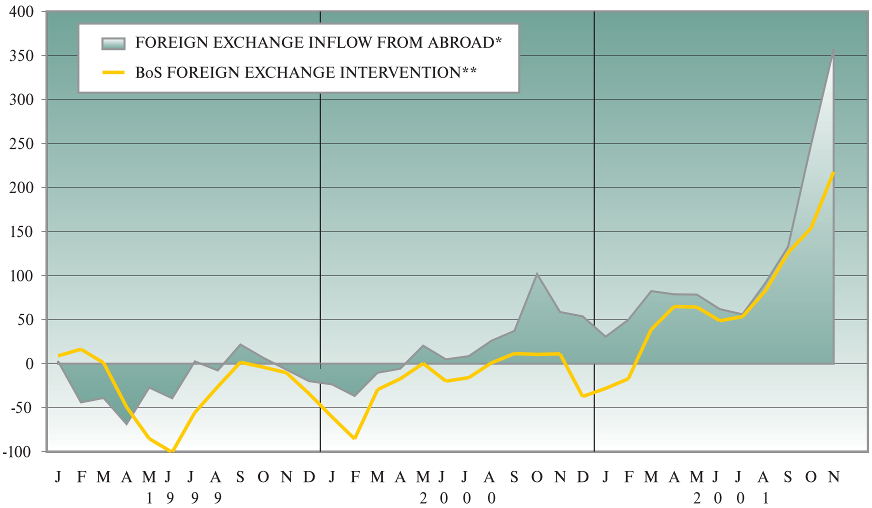
2.3. Foreign exchange market and foreign exchange rate

In the system of managed floating exchange rate, the fluctuations of foreign exchange rate depend mainly on supply and demand for foreign exchange and the interventions the central bank.

Strong balance-of-payment inflows

Supply and demand in the foreign exchange market is largely determined by movements in the balance of payments and decisions taken by domestic entities as to what form their investments should have. In 2001, net financial inflow in Slovenia totalled as much as US$ 1,647 million (8.7% of the GDP estimate), the deficit on the current account of the balance of payments was US$ 67 million. Therefore, the foreign exchange reserves the banks maintain with the Bank of Slovenia rose by US$1,580 million. The inflows channelled through direct investment totalled US$ 442 million and were outweighed by the inflows of foreign cash through households totalling US$691 million. Substantial direct investments are a consequence of the sale of equity holdings to non-residents.

Chart 8: **Foreign exchange flows***
(in millions of US dollars on a monthly basis; moving average 3)



* Inflows from the rest of the word without direct inflows from abroad to the Bank of Slovenia (interests, etc. and reduced by net payments from foreign exchange government account).

Source: Bank of Slovenia.

Excess foreign exchange supply in foreign currency markets

By the end of 2001, foreign exchange supply exceeded demand for foreign exchange in the spot foreign exchange market by 1,857 million euros. The lowest net inflows in this market were in the first quarter of the year when the monthly average was 59 million euros, while the highest inflows were recorded in the second and the third quarter when their respective monthly average was 225 million euros. The banks sold 955 million euros in foreign exchange more than they purchased in the futures foreign exchange market. During the first quarter the net sale of foreign exchange by banks in that market was 162 million euros, while in the second and third quarters it totalled 852 million euros. In the last quarter the banks purchased in the futures foreign exchange market more foreign exchange than they sold. Exchange offices sold to August 28 million euros more in foreign currency cash than they bought. Due to the changeover of the EMU countries to euro notes and coins, the net purchase of foreign cash since September to the end of the 2001 totalled as much as 271 million euros. The aggregate net inflow in the foreign exchange and exchange market thus in the entire 2001 totalled 1,145 million euros.

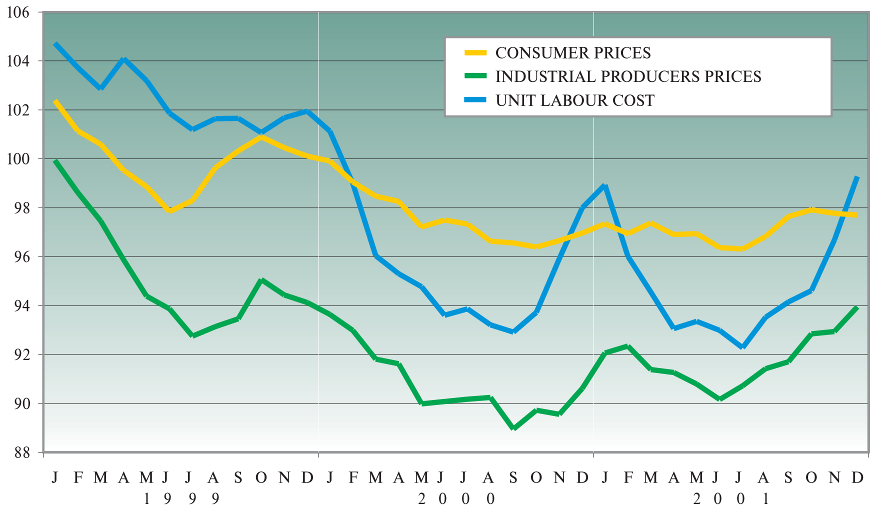
The Bank of Slovenia addressed the mismatch in the foreign exchange markets within the framework of the set targets and monetary policy guidance, and supported growth in the foreign exchange rate, which enabled a gradual decrease in inflation and partial closing of the interest spread between domestic and cross-border interest rates.

Comprehensive interventions of the Bank of Slovenia in foreign exchange markets

In line with the aforementioned approach, the Bank of Slovenia was a net seller of foreign exchange at the beginning of last year, and a net buyer from March onwards. Thus in January and February it sold net to the banks 21.7 billion tolars in foreign exchange, while from March to December it purchased net 251.5 billion tolars in foreign exchange. For the majority of transactions of the purchase and sale of foreign exchange the Bank provided a facility in the form of a temporary purchase, i.e. temporary sale of foreign exchange under an agreement to sell, i.e. purchase within 7 days - a repurchase (repo).

The growth in the euro exchange rate was rather brisk during the first quarter and on average amounted to in 0.5% per month. Under the pressure of a large excess supply of foreign exchange, during the second and the third quarters the rate of growth in the foreign exchange rate diminished and in September reached just under 0.2%. Since then the Bank of Slovenia has intervented in the foreign exchange markets;

Chart 9: **Real effective tolar exchange rate** (1995=100)



Source: Bank of Slovenia.

which increased the pace of the growth in the foreign exchange rate. The average monthly increase over the last quarter of 2001 totalled approximately 0.3%. In 2001, the increase in the exchange rate for the euro in the foreign exchange market was 4.4 per cent. The fluctuations in the exchange rate for the euro in exchange offices more or less followed the fluctuations of the euro exchange rate in the foreign exchange market; the annual increase totalled 4.6%. The official rate for the euro rose 2001 by 4.8%, the official exchange rate for the US dollar increased by 5.1%. The nominal effective traded-weighted exchange rate increased by 4.3%.

Real appreciation of the tolar

The tolar depreciated in real terms during the first half of the year under review and appreciated in the second half-year. Cumulative real appreciation of the tolar in 2001 was 0.7%, measured by the ratio between foreign and domestic consumer prices, and by 1.3%, measured by relative unit labour costs. With 3.7% the strongest appreciation of the tolar was in terms of producer prices.

2.4. Instruments used

An overview of the instruments of monetary policy and exchange rate policy was made on the basis of the definition of the structural positions in the money market for Slovenia. Consistent with this definition, there are instruments of monetary policy, instruments of exchange rate policy, and prudential measures. The instruments of buying and selling of foreign exchange are classified under the instruments of exchange rate policy despite restricted autonomy of net assets denominated in foreign currency. Instruments of exchange rate policy which are found in the

Table 8: **Use of instruments of monetary policy and exchange rate policy** (in millions of tolars)

	Balance	Average daily balance per quarter in 2001				Balance
	12/31/00	I.	II.	III.	IV.	12/31/01
Monetary policy instruments						
Lending facilities	112	468	1,313	395	165	75
Lombard loans	0	357	325	87	46	0
Liquidity loans	0	0	897	217	43	0
Other*	112	111	91	91	75	75
Repurchase agreements	6,299	7,572	4,843	2,672	377	0
Reserves of banks and saving banks		88,653	92,001	93,032	97,688	
Required		85,452	89,006	91,413	95,293	
Excess reserves		3,201	2,995	1,620	2,395	
Bank of Slovenia Tolar bills	6,946	8,829	30,955	53,980	107,282	125,777
Overnight deposit facility	0	0	0	3,196	7,116	35,372
Government time-deposits received	0	0	7,686	6,008	5,959	19,896
Exchange rate policy instruments						
Temporary purchase of foreign exchange	15,535	9,410	43,143	82,818	168,139	262,012
Temporary sale of foreign exchange	213	3,827	183	44	0	0
Memo:						
Bank of Slovenia foreign-currency bills	357,633	374,962	395,381	427,079	451,092	461,857
Foreign exchange minimum	569,696	591,541	623,322	659,230	684,473	697,901

* Long-term selective loan, granted before monetary independence.
Source: Bank of Slovenia; excluding accrued interest and discount.

balance sheet of the Bank of Slovenia are coupled with the description of the instruments, which otherwise are not reflected in the balances, but do affect the exchange rate, as well as credit activity of banks'. These instruments are conditioning, or signalling exchange rates, open foreign exchange positions, foreign exchange minimums, maturity ladders and restrictions on capital flows.

Monetary Policy Instruments

During the year under review, the excess in the structural position in the money market was growing steadily due to massive monetisation of foreign exchange inflows. The inflows were stronger and monetisation faster than was the case when Slovenia enjoyed larger capital inflows in the 1997 - 1998 period.

The use of monetary policy instruments was influenced by the increasing need for sterilisation. Repurchase operations involving buying of foreign exchange with a 7-day maturity remained the most important source of liquidity throughout the year under review, whereas loans and repurchase operations with bills denominated in foreign currency did not have an important role, even though the Bank of Slovenia made them available.

The use of monetary policy instruments affected by an ever-increasing need for sterilisation

Lending facilities

Against the background of a massive monetisation of foreign exchange, lending facilities provided by the Bank of Slovenia in 2001 were a less important monetary policy instrument in the second half of the year. On average, the balance of outstanding lending facilities during the year under review totalled 0.6 billion tolars (2000: 0.7 billion tolars). The volume of lending was at its highest in the April-June period.

Massive monetisation of foreign exchange resulted in the banks requiring less loans and…

Lombard loans were available to the banks until the middle of May on the basis of an open tender as a lending facility due in five (calendar) days at the interest rate of one percentage point above the discount rate. In mid-May, the Bank of Slovenia shortened the maturity of Lombard loans to one business day. In July the Bank also changed the methodology for setting the interest rate for this loan, so that the interest rate is not directly pegged to the discount rate, but is determined by issuing a decision on the Lombard interest rate and the interest rate charged for overnight deposits. The percentage of withdrawn loan funds of the amount of pledged securities (Bank of Slovenia bills denominated in foreign currency and Treasury bills) totalled 5%. In 2001, banks mostly tapped into loans in January and April, the average outstanding balance was 203.8 million tolars.

Liquidity loans primarily serve as instruments for balancing short-term tolar-denominated liquidity of the banking system. In 2001, the average outstanding balance of liquidity loans totalled 289.3 million tolars (2000: 190 million tolars). The banks only tapped into liquidity loans backed by tolar bills.

Liquidity loans backed by tolar bills were granted to banks against pledging 12-day tolar bills, for three working days. In December, the Bank of Slovenia revoked its open market tender for underwriting tolar bills with that maturity and thus cancelled the possibility of tapping into such a type of loans.

Overnight liquidity loans were the subject of tenders of the Bank of Slovenia when there was a need to manage the interbank interest rate or in the case of a mismatch between demand and supply in the interbank money market. The Bank of Slovenia offered loans on the evening interbank market, even though in 2001 no auction was staged for overnight liquidity loans.

Liquidity loans of last resort is a lending facility available to banks for the purpose of obtaining funding against pledging securities on the basis of the open market tender at a lawfully set penal interest rate. In 2001, the banks did not require this type of lending facility.

Bills purchased under agreement to sell

...the balance of temporary purchase of bills at the end of the year under review was zero

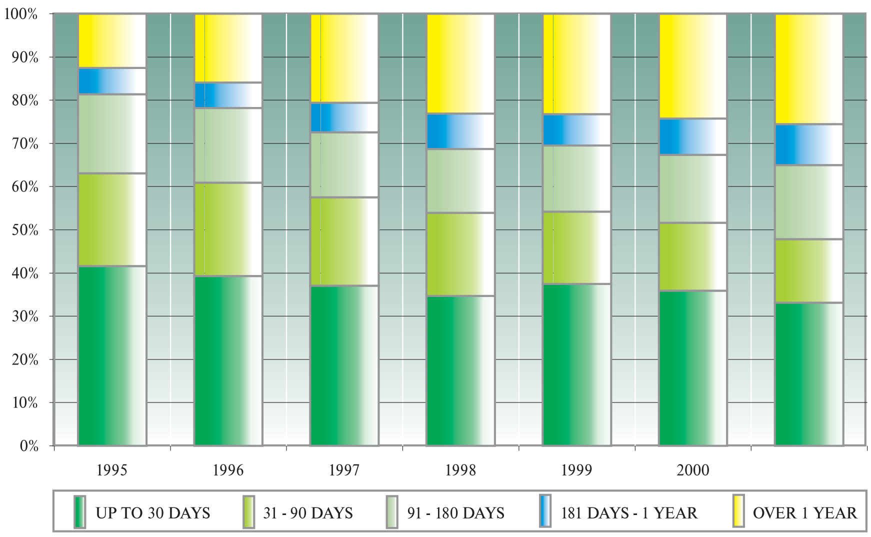
Within the framework of its open market operations, the Bank of Slovenia made available every day in 2001 a repurchase facility for bills denominated in foreign currency for seven days and twice-monthly repurchase facility for bills denominated in foreign currency for 60 days. By means of repurchase operations with shorter maturity, the Bank of Slovenia enables the banks to steer liquidity within the relative month, while through repurchase operations with longer maturity the Bank balances the long-term base money supply. Due to a considerable level of repurchase operations involving foreign exchange and the resulting high level of liquidity, in 2001 the situation of this instrument declined: on average it was increasing by March, then the trend was reversed and in November it reached at zero.

Mandatory reserve

Mandatory reserves to be maintained by banks and savings banks, including savings and loan undertakings are to be calculated on all tolar-denominated deposits, received loans and advances and issued securities, whose holders come from the non-bank sector. The rate of mandatory reserves shall be determined with regard to maturities of liabilities (deposits): 12% on demand and time deposit with agreed maturity of up to 30 days, 6% on time deposit with maturity of between 31 and 90 days, 2% on time deposits between 91 and 180 days, and 1% on time deposit with maturity between 181 days to one year. Deposits placed for the period over one year do not attract any mandatory reserves.

Since December 1998, the balance on the settlement account and cash balances (held with direct participants in the real time gross settlement system - the RTGS), i.e. the balance on the special account for mandatory reserves and cash balances (held with indirect participants in the RTGS) shall be regarded as the funds for

Chart 10: **Average composition tolar deposits**



Source: Bank of Slovenia.

mandatory reserves. The funds held in settlement, that is the special account earn interest at the one-per-cent annual interest rate, but only up to the amount of the calculated mandatory reserves for the preceding month. Since December 2000, the banks participating in the national housing savings scheme can cover the entire portion of liabilities arising from payments made within the framework of the national housing savings scheme by subscribed 60-day tolar-denominated bills issued by the Bank of Slovenia.

The base of mandatory reserves increase, average rate declined

The mandatory reserve base increased in 2001 by 25% (as opposed to 11.7% a year earlier) and in December 2001 it amounted to 1907.0 billion tolars. The calculated reserves (at prescribed rates in relation to maturity of deposits) rose by 7.2% to 97.6 billion tolars in December 2001. The average rate of mandatory reserves on all tolar-denominated deposits declined by 0.3 percentage points year-on-year and reached 5.3%, as a consequence of a change to the composition of this group of deposits. The average rate of reserves, calculated for deposits of up to one year, also dropped and on average reached 7.1% (2000: 7.5%). The achieved reserves on average exceeded liabilities by 2.8% (2000: 3.7%), of which the banks had on average the lowest excess reserves and the savings banks had the highest. The entities obliged to comply must have every day in their settlement, that is the special account, funds in the amount of at least 50% of liabilities carried in the previous month, which they may use for overnight liquidity against a payment for a charge at a penal interest rate.

Overshooting of mandatory reserves more modest than in 2000

Tolar bills

Only bills with maturity of 60 and 270 days

Tolar bills are dematerialised registered securities provided to the banks by the Bank of Slovenia. In 2001, the Bank of Slovenia narrowed the offer of tolar bills. As a continuing facility only tolar bills with a maturity of 60 days are still available. At mid-February, the Bank of Slovenia terminated the option to subscribe 270-day bills on the basis of an open tender and made it available again in June but it failed to attract any substantial interest. In November this instrument was introduced at regular twice-monthly auctions. In July the Bank of Slovenia discontinued tolar-denominated bills with maturity of 2 days and replaced them with an open offer for overnight deposits, in December it discontinued tolar-denominated bills with a maturity of 12 days.

The balance in tolar bills strongly increased in 2001 due to wide-scope monetisation of foreign exchange: from 7 billion tolars to 161 billion tolars at the end of 2000 and the end of 2001 respectively (including overnight deposits).

Overnight deposits

The Bank of Slovenia offered for the first time to banks and savings banks in July 2001 the possibility to place a time deposit over night. This is a standing facility, which enables banks and savings banks to place with the Bank of Slovenia their excess liquidity. The applicable interest rate is set by the Governing Board of the Bank of Slovenia by issuing a resolution on Lombard interest rates and overnight deposit interest rates, and represents the floor for the interbank overnight interest rate.

Overnight deposit highly popular

Due to sound liquidity the balance of overnight deposits gained momentum and peaked in December with 35.4 billion tolars. The maximum daily balances coincided with the closing dates for the periods when mandatory reserve requirements had to be met (26^{th} of the month). Having introduced overnight deposits, excess reserves of the banking system on average reduced.

One-month Treasury bill and deposit of the Ministry of Finance

The Bank of Slovenia signed an agreement with the Ministry of Finance in April 2001 stipulating coordination between the two institutions on developing the money market (see Box 7). The purpose of the agreement is the development of the money market which is founded upon a security – one-month Treasury bills underwitten by the Ministry of Finance in co-operation with the Bank of Slovenia. Under the accord the Ministry of Finance undertakes to invest in the Bank of Slovenia the proceeds of sale, i.e. subscription of one-month Treasury bills and may dispose of those funds for balancing budget liquidity.

In the course of the introduction of one-month Treasury bills, more specifically during the first two months, the Ministry of Finance in line with the agreement did not draw down the deposit, and from July it was free to draw down these funds on the basis of a monthly plan, that is by pre-arrangement. The deposit earns interest at an interest rate equal to the interest rate adopted at the auction.

Exchange rate policy instruments

The Bank of Slovenia influences the foreign exchange rate by different instruments. It buys and sells outright and on a temporary basis, foreign exchange and thus fits the offer to the demands of the foreign exchange market. Within the framework of the Agreement on the Participation of Banks in Interventions on the Foreign Currency Markets (see Box 2) it signals the exchange rate and sets the possible band for exchange rates, observed by the banks when concluding deals with other parties.

Purchase and sale of foreign exchange

In 2001, the Bank of Slovenia sold foreign exchange to banks and also purchased from them on the basis of offers addressed to all banks, and through instruments on

Table 9: **Purchase and sale of foreign exchange**

	2000		2001	
	EUR millions	SIT billions	EUR millions	SIT billions
Outright purchase of foreign exchange	**217.4**	**44.2**	**89.6**	**19.2**
Payment transactions and other operations for the State	217.4	44.2	89.6	19.2
Outright sale of foreign exchange	**285.3**	**57.6**	**210.2**	**45.7**
For the purchase of foreign currency bills	245.0	49.3		
Outright sale of foreign exchange to contractual banks			73.8	15.8
Payment transactions and other operations for the State	40.3	8.3	136.4	29.9
Temporary purchase and repurchase of foreign exchange	**2,271.2**	**471.9**	**18,424.5**	**4,053.6**
Temporary purchase under contract - two months	18.5	3.7		
Temporary purchase under contract - one week	1,727.6	359.0	18,180.5	4,001.4
Repurchase of foreign exchange (standing facility)				
Repurchase under contract - one week	525.1	109.2	244.0	52.2
Temporary sale and reverse sale of foreign exchange	**2,218.6**	**460.5**	**17,318.2**	**3,808.6**
Temporary sale under contract - one week	526.1	109.4	243.0	52.0
Reverse sale under contract - one week	1,654.5	343.5	17,075.2	3,756.6
Reverse sale under contract - two months	38.0	7.6		

Source: Bank of Slovenia.

the basis of the agreement on the participation in the interventions in the market of foreign currency and the annex to the agreement. Buying and selling of foreign exchange was also conducted so as to be able to effect cross-border payment operations for budgetary purposes and on the basis of other transactions carried out on behalf of the government.

Sales of foreign exchange to the Bank of Slovenia under repurchase agreement were the most important source of liquidity for the banking system

Purchases of foreign exchange made by the Bank of Slovenia were the most significant source of liquidity for the banking system in 2001. The Bank of Slovenia purchased from the banks and the government 4,073 billion tolars and sold 3,854 billion tolars in foreign exchange. The net cumulative issuance of tolars from foreign exchange transactions amounted to 218,5 billion tolars.

Amongst **outright transactions,** the Bank of Slovenia sold foreign exchange to banks, and the final sale was concluded on the basis of a seven-day temporary sale in the countervalue of 15.8 billion tolars in January and February.

Box 2: **Contractual participation in interventions in the foreign exchange markets**

At the beginning of 2000, the Bank of Slovenia signed an agreement with banks to act jointly in the foreign exchange market with the aim of facilitating the implementation of exchange rate policy so as to achieve the objective of a gradual decrease in inflation and reducing the interest spread between domestic and cross-border interest rates. The participation of the signatories builds upon the following mechanisms:

- During the intervention, the Bank of Slovenia sets the lowest buying and the highest selling exchange rates that the contracting banks must apply when agreeing deals to buy or sell foreign currency in the foreign exchange market, by setting the base rate along with the highest margins. At any other time when the Bank of Slovenia does not set the exchange rate, the banks decide on buying and/or selling rates at their discretion.
- The Bank of Slovenia makes available to the contracting banks a standing facility to purchase/sell foreign exchange for a 7-day period under the repurchase agreement (a 7-day repo). Repurchase operations are concluded at the base exchange rate and during the periods when no base rate has been specified, the average market rate shall apply.

The agreement on banks' participation was signed in March 2000 by 22 out of 25 operating banks. The Bank of Slovenia invited the banks in October 2001 to sign an annex to the basic agreement to enable the Bank of Slovenia to set expenses related to refinancing operations provided to the banks by the Bank of Slovenia. Consequently, the new contractual co-operation does not only influence the exchange rate, but also provides one of the elements for setting interest rates. The Bank of Slovenia has invited the banks, which did not sign the agreement when it was offered to them for the first time to join in by signing the basic agreement and the annex. The amended agreement has been signed by 20 out of 21 banks.

The annex modifies some of the provisions set out in the basic agreement and elaborates on the measures in relation to oversight of the banks' risk management and control. The changes refer to the following:

- By playing a pro-active role in setting the interest rate on repurchase operations involving foreign exchange, the Bank of Slovenia will get more room to decide on the scale of foreign exchange monetisation, i.e. it will obtain a broader control over the volume of the base money. This price has an effect on the proportion between interest-bearing foreign exchange and tolar-denominated banks' assets that may be refinanced with the Bank of Slovenia. This is how the transmission mechanism of interest rates, which requires a developed money market in order to be more effective, becomes meaningful.
- Since by making refinancing available the Bank of Slovenia assumes liquidity risk the signatories of the agreement are exposed to, it is no longer reasonable to split in two parts the requirement to set aside assets in appropriate currency separately for foreign exchange and tolars savings. Therefore, a single maturity ladder shall apply to these banks with two bands for the adjustment between assets and liabilities, namely from 0 to 30 days and from 0 to 180 days.

The contracting banks are required to ensure a higher degree of transparency of operations in the foreign exchange market; hence the banks are obliged to announce on the web site of the Bank of Slovenia the exchange rates at which they are prepared to buy and sell the euro to legal entities.

As regards **temporary transactions** in foreign currency, the amount went up year-on-year mostly due to purchases; this increase was a result of large foreign exchange inflows and strong excess in supply of foreign exchange in the foreign exchange market. As a consequence, the sale of foreign exchange under the repurchase agreement was not as important as in 2000. Overall, the Bank of Slovenia bought 4,001 billion tolars in foreign exchange and sold 52 billion tolars within the framework of its repurchase operations, and after taking into account the reverse operations, the base money supply increased by 245.0 billion tolars.

Sending signals and setting exchange rates

Agreement-based participation in interventions in the foreign exchange markets

The Bank of Slovenia resorts to the mechanisms of setting exchange rates under the agreement on the participation of banks in interventions in the foreign exchange markets. By setting exchange rates, the signals are transmitted by the central bank into a broader financial and real sector. The Bank of Slovenia responded to the pressures to boost the value of the tolar due to excess supply on foreign exchange markets by settling on interventions as a tool for setting the pace of rate growth. Since mid-September, the Bank has intervened in the foreign exchange market by setting the base rate and hence limiting also the highest selling and the lowest buying rate so as to encourage the closing of the interest rate spread between domestic and foreign interest rates.

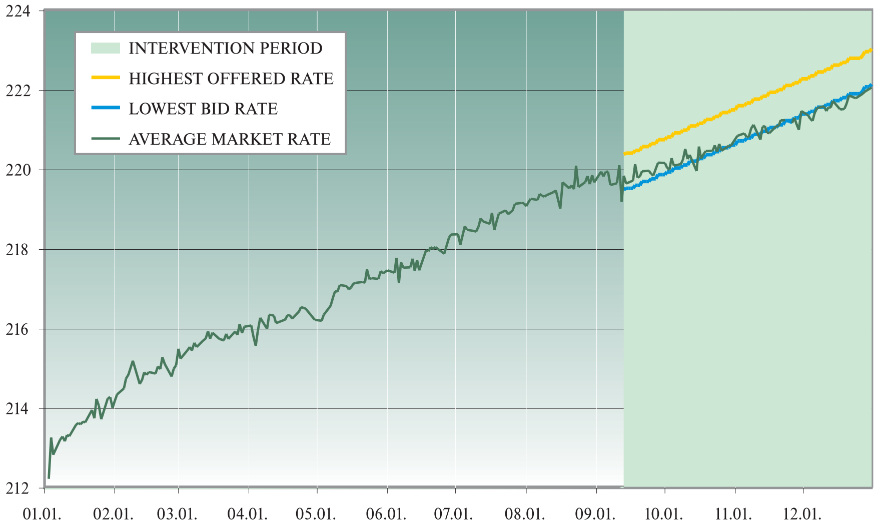
Prudential measures

Bills denominated in foreign currency

More modest array of bills denominated in foreign currency

In 2001, the Bank of Slovenia narrowed the array of bills denominated in foreign currency, and in February it abolished bills with maturity of over 120 days (180, 270 and 360 days). Bills denominated in foreign currency have been issued as short-term, transferable, registered, non-serial and dematerialised securities since January 1992 and the Bank sells them as a standing facility. The bills are paid in at a discount in the euro or US dollars. The Bank of Slovenia tunes the interest rate paid on the bills to the relevant interest rates prevailing in cross-border money markets.

Chart 11: **Exchange rates in the foreign exchange market during interventions**
(tolars/euros)



Source: Bank of Slovenia.

Bills denominated in foreign currency are used by the banks as a basis for tapping into most lending facilities made available by the Bank of Slovenia. The banks may pledge them to collateralise a Lombard loan or for repurchase operations of the Bank of Slovenia, and they may also serve as a collateral for liquidity and short-term loans with assets stemming from the bills eligible to be pledged as collateral for the deal made.

The largest part of the demand for bills denominated in foreign currency was in 2001 linked to the regulation on foreign exchange minimums, which stipulates that banks must hold at least 60% of the calculated liabilities in bills denominated in foreign currency with agreed maturity of up to and including 120 days. The banks also subscribed to bills denominated in foreign currency for the purpose of complying with the tolar and foreign currency maturity ladder.

Box 3: **Balancing cross-border capital flows**

The European Agreement on the Association between the Republic of Slovenia and the European Communities and their Member States allows for restrictions related to short-term capital flows during the transitional four-year period. On the other hand, direct investments flows are generally unrestricted. Back in 1999, the Government made a commitment in the relevant common negotiating position that the legislative framework of the Republic of Slovenia concerning free capital flows will be gradually harmonised with the *acquis communautaire* in place in the European Union no later than by the date of the country's accession to the EU.

The lifting of the last restrictions on foreign direct investment currently in place in specific sectors is subject to the promulgation of relevant legislation. Pending bills in the final stage of parliamentary procedure will amend the laws, which have kept lottery and other similar games off-limits for non-residents. Furthermore, new legislation in relation to investment funds management, investigation and security services, as well as the exploitation of natural resources is expected to be drafted shortly.

As from the promulgation of the new Foreign Exchange Act in 1999, the Bank of Slovenia has fully liberalised borrowing abroad and has kept in a place few controls that refer to short-term capital flows. In response to the calls voiced by the European Union that Slovenia shall complete the liberalisation of capital account before accession to the European Union and no later than upon accession and that a detailed time frame for the elimination of the remaining restrictions concerning capital flows shall be prepared, including target dates and interim steps for the full current account liberalisation, the Bank of Slovenia is committed to complying with the full-scope easing of few effective restrictions, *viz.*:

- With effect from 1 January 2001, the Bank of Slovenia cut back the period after which a non-resident does not have to pay the premium on the right to purchase foreign exchange from one year to six months; with effect from 1 July 2001, it made another step towards full capital account liberalisation. Namely, the Bank of Slovenia liberalised purchases of non-residents in the domestic capital market, while it left in place the obligation to pay the premium for the purchase of the right to purchase foreign exchange from the Bank of Slovenia in the amount of the balance maintained on the custody account applicable to non-residents purchasing in the money market and the purchases of investment coupons of those mutual funds in the Republic of Slovenia, which operate by the rules that allow to the mutual fund in question to invest over 60% of all mutual fund's assets in money market instruments. During the third and the fourth quarter of 2001, the premium on the balances on non-resident custody accounts was 0.2%.

With effect from 1 January 2002 the restriction referred to in the previous paragraph that limited purchases of non-residents in the domestic money market was lifted; hence non-residents may subscribe for and pay, i.e. buy and sell securities in the Republic of Slovenia without restraint.

- The Bank of Slovenia abolished with effect from 1 July 2001 the restrictions on opening of current and deposit accounts abroad for legal entities; while other sectors may as a rule open accounts abroad solely with the authorisation of the Bank of Slovenia. This constraint is due to be lifted by the full-fledged membership of the Republic of Slovenia of the European Union.
- With effect from 1 July 2001 the limits on residents purchase of securities abroad, which stipulated that residents may (except for securities issued by the OECD countries and international financial institutions, and the securities rated at least AA by no less than two recognised international rating agencies) purchase other securities only through a stock exchange, which is member of the International Federation of Stock Exchanges (FIBV), and through member of the stock exchange authorised for trading in securities, have been lifted.

As of 1 January 2002, transfers of domestic and foreign cash into the country and out of the country are fully liberalised. Therefore, cash can be brought into and out of the country under the terms and in accordance with the procedure laid down in the Money Laundering Prevention Act.

In December 2000, the average amount of subscribed bills denominated in foreign currency was 360.5 billion and it increased to 457.6 billion tolars in December 2001, an annual increase of 27%.

A special liquidity loan with the participation of banks

The 6th agreement was concluded with 21 commercial banks in 2001 to provide a stand-by facility for managing liquidity. The banks, signatories to the agreement, are entitled to a remuneration of 1.5% of their agreed state of readiness. There was no need in the course of 2001 to trigger the mechanism with the contracting banks.

Foreign exchange minimum and foreign exchange maturity ladder

For the purpose of ensuring overall liquidity of outward payments and fulfilling liabilities arising from foreign exchange deposits of residents and non-residents, the banks' foreign exchange and liquid foreign-exchange investments abroad shall on a daily basis be sufficient to meet the foreign exchange minimum.

In 2001 the methodology for the calculation of foreign exchange minimums remained unchanged. In April 2001 banks submitted for the first time also a statutory return on foreign exchange liquidity in accordance with the Decree on the Foreign Exchange Maturity Ladder, promulgated in September 2000. The Bank of Slovenia promulgated in October 2001 a Decree on the Narrowest Range of Liquidity the Banks Shall Have to Meet with effect from 1 January 2002 and thus standardised monitoring of banks' liquidity in tolars and foreign currency.

In 2001, the foreign exchange minimum was increased from 570 billion tolars in January to 698 billion tolars in December 2001, and namely by 96 billion tolars arising from foreign exchange deposits of domestic natural persons, by 12 billion tolars arising from the balances on the foreign exchange non-resident accounts and by 19 billion tolars arising from the balances on the foreign exchange accounts of domestic legal entities. The highest excess over the foreign exchange minimum was recorded at the end of February 2001 when it totalled 27.6%, as opposed to the end of September 2001 when the percentage of excess over the threshold was at its lowest (15.0 %).

Banks complied with the prescribed foreign exchange minimum in 2001 with net credits on accounts denominated in foreign currency placed with cross-border banks and international financial institutions, net balances of short-term claims to domestic or cross-border banks denominated in foreign currency, with foreign currency cash and cheques, short-term claims on the Bank of Slovenia denominated in foreign currency, Bank of Slovenia bills denominated in foreign currency, and investments in gilt-edged foreign debt securities. The banks were obliged to comply with at least 60% of foreign exchange minimum by subscribing to bills issued by the Bank of Slovenia denominated in foreign currency.

Open foreign exchange position of banks

As a safeguard against foreign exchange risk, the banks which carry out operations involving foreign means of payment are obliged to calculate each day their open foreign exchange position, which shall not exceed 20% of the bank's capital (own funds), while the bank's average monthly open foreign exchange position shall not exceed 10 % of capital (own funds). This position does not include tolar-denominated assets and off-balance items.

In line with the amendments to the Decision on Capital Adequacy of Banks and Savings Banks and in the wake of the implementation of the requirement for daily reporting to the Bank of Slovenia also in line with the Decree on the Narrowest Liquidity Range which the Bank Shall Have to Ensure, the Decree on Open Foreign Currency Position of Banks shall become null and void with effect from 30 June 2002.

The aggregate open foreign exchange position of banks as at 31 December 2001 was short with foreign exchange liabilities exceeding foreign exchange assets by 6,362 million tolars or 2.3% of overall banks' capital. A short open foreign exchange position was posted by 16 banks at the end of the year under review, as opposed to 5 banks, which reported a long open foreign exchange position.

Supervision of implementation of monetary policy measures

Supervisory oversight exercised by the Bank of Slovenia includes the examination of the implementation of monetary policy measures, as well as the terms and conditions stipulated in relation to its open market operations. By applying a combination of off- and on-site supervision of banks, savings banks and savings and loan undertakings the central bank discharges its responsibilities in accordance with Article 50 of the Bank of Slovenia Act and the Decision on Supervision of the Implementation of Measures and the Measures against Banks and Savings Banks. Off-site supervision is an ongoing process where analysts sift through statutory returns and other documents that banks and savings banks submit to the Bank of Slovenia. In addition, there are on-site supervisory visits conducted by the examiners of the Bank of Slovenia at set intervals or on an *ad hoc* basis. On such occasions the examiners look into the books of account and other documentation in the bank or a savings bank in question. If minor cases of non-compliance are revealed and provided that such shortcomings do not violate monetary policy regulations, the Bank of Slovenia warns the non-complying bank, savings bank and/or a savings and loan undertaking in writing or by phone that it is in breach of regulations and asks for a clarification and requires a corrective action.

Most cases of non-compliance related to mandatory reserves and foreign exchange position

In 2001, the findings reached on the basis of off- or on-site examinations of banks and savings banks were noted down in 30 protocols (2000: 28) of which non-compliance was revealed through off-site supervision in 14 banks, one in a savings bank and 8 in savings and loan undertakings. It was eventually decided to conduct on-site examinations in 7 banks and the findings of the examiners were minuted in 7 protocols. During the year under review, no on-site examinations were conducted in savings banks and savings and loan undertakings. Most cases of non-compliance were a failure to maintain mandatory reserves and conformity with the regulatory amount of foreign exchange positions. In response to non-compliance with monetary policy regulations, 11 rulings were issued to non-compliant banks and 7 rulings were addressed to savings and loan undertakings specifying the respective corrective measure to be taken. In 10 banks, one savings bank and one savings and loan undertaking the examination was completed by issuing a ruling to ending the control proceedings. In six banks the breach concerned the contractual relationship for exchange operations; hence three banks were notified in writing of the measure taken against them. As regards the other three banks, the proceedings were ended. The most common measures are the prohibition to purchase securities from the Bank of Slovenia, the prohibition to participate in the bids organised by the Bank of Slovenia, and the payment of the penal charge for failing to meet the mandatory reserve requirement.

During the year under review, 12 cases of non-compliance were revealed through off-site supervision of banks' foreign exchange operations. Three such cases were detected in relation to the compliance with the requirements concerning open foreign exchange positions, and the non-compliant banks had to pay interest to the Bank of Slovenia at a penal rate, while in two cases the banks fell short of the mandatory amount to be subscribed in bills denominated in foreign currency. The sanction in the latter case was to prohibit the banks from purchasing tolar-denominated bills issued by the Bank of Slovenia for ten days. The Bank of Slovenia resolved that the proceedings were to end, and in six cases the proceedings against the non-compliant banks are still going on.

Within the framework of prudential oversight of exchange operations, the Bank of Slovenia conducted 43 examinations of contractual exchange offices in 2001 and on the basis of the findings the Bank issued 28 rulings ending the control proceedings of exchange operations. Six motions to instigate the proceedings on the basis of a violation were filed with the Foreign Exchange Inspectorate of the Republic of Slovenia, seven authorisations for carrying out exchange operations were suspended for a determined period of time pending another review when the effects of corrective actions (if any) will be validated.

3. BANKING SECTOR

Very high growth in the volume of banks' operations in 2001

The main feature of Slovenia's banking business in 2001 was a markedly high growth in volume of operations driven by the growth in household deposits prompted by the euro cash changeover. The impact of high net financial inflows of foreign exchange (the inflows under cross-border financing, inflows from citizens, foreign direct investment) which exceeded 8% of GDP (2000: 5.9%) on the banks' results was equally strong. The take over of three banks by the largest bank in Slovenia increased further the level of concentration in the banking sector. The average composition of liabilities shows that the share of household deposits increased, while the share of government deposits dropped. As regards the average composition of assets, the share of assets the banks had invested in securities rose, mostly securities issued by the central bank as the *de minimis* foreign exchange limit was raised and the withdrawal of excess liquidity stemming from excess foreign exchange supply by tolar-denominated instruments of the Bank of Slovenia. Over the past two years loans and advances to non-financial institutions have been rising quite strongly, whilst the growth rate of household lending has been falling. In spite of a number of cuts in interest rates of central banks abroad, and moderate growth in the tolar exchange rate that contributed to lower expenses incurred by cross-border borrowing, and with conditions prevailing in the domestic market, in contrast with 2000 non-financial institutions borrowed in 2001 more heavily in the domestic market than abroad. Banks in Slovenia reported modest profits before tax for 2001 following a high loss of one major bank. In the composition of gross income the share of net interest as the most stable source of earnings declined as opposed to growth in the share of net financial business that edged up. Lower interest margins in 2001 were more felt than past years and so the reduction from 1997 continued. Likewise, the interest spread narrowed in 2001. The narrower interest spread was a consequence of strengthening of deposit rates and declining lending interest rates. During the year 2001, the banks' control of operating costs was firmer than over previous years. The decline in capital adequacy across the banking system was first observed in 1996 and continued throughout 2001. Capital adequacy decreased by 1.7 percentage points to 11.8%.

3.1. The banking sector structure

As at 31 December 2001, there were 21 operating banks in Slovenia, including four subsidiaries of foreign banks and one branch of a bank incorporated outside Slovenia. In addition, three savings banks and 45 savings and loan undertakings were present.

The consolidation of the Slovenian banking sector continued in 2001 and partiularly quickened in the last quarter of 2001 when three banks – Dolenjska banka d. d., Pomurska banka d. d., Murska Sobota, and Banka Velenje d. d. Velenje joined Nova Ljubljanska banka d. d. Ljubljana, and SKB banka d. d. Ljubljana absorbed Banka Societe Generale Ljubljana d. d.

Table 10: **The ownership structure of the banking sector**
(in % of equity capital)

	31-Dec-2000	31-Dec-2001
Non-residents	12.0%	15.4%
Central government	36.8%	37.3%
Other domestic persons	51.2%	47.3%

Source: Bank of Slovenia.

BOX 4: **Deposit Guarantee Scheme**

Effective from 1 January 2001, the Deposit Guarantee Scheme in place in the Republic of Slovenia is a system to guarantee deposits placed with banks and savings banks and transposes the provisions laid down in Directive 94/19/ES. The Deposit Guarantee Scheme covers all banks and savings banks authorised by the Bank of Slovenia and branches of foreign banks (hereinafter: the banks). Savings and loan undertakings will be eligible for membership of the Scheme once they have completed the harmonisation with the relevant provisions of the Banking Act, that is they have been authorised by the Bank of Slovenia.
The ceiling amount of a guaranteed deposit is 4,200,000 tolars per depositor or EUR 18,969 at the exchange rate effective on 31 December 2001.According to the reporting requirements prescribed by the Bank of Slovenia, the banks report to the Bank of Slovenia on a semi-annual basis on the balances of guaranteed deposits and the compliance with the obligation to invest in securities so as to have ready access to liquid assets required to effect payments of guaranteed deposits.
The received returns show that aggregate retail and corporate deposits (excluding deposits of banks and general government) placed with banks and savings banks amounted to 2,113.1 billion tolars, of which 49.5%, i.e. 1,045.8 billion tolars was in guaranteed deposits. All holders of guaranteed deposits (individuals and small corporate clients) with banks and savings banks number 2,006,377. Among these holders of deposits only 4.3% or 82,588 do not have fully guaranteed deposits. The portion, which is not guaranteed or the excess of deposits above the guaranteed amount in this group of depositors totals 586,9 billion tolars. Overall, the purpose, that the mission of the Deposit Guarantee Scheme has been met - to provide a safety net for the majority (in terms of their number) of small depositors whose deposits are fully covered in case a bank files for bankruptcy.
It should be noted that 376.6 billion tolars in deposits are excluded from the Scheme by virtue of law (medium and large legal persons, persons connected with the bank, and other particular cases when the Scheme does not provide a shelter as provided for under the European Directive). In addition, the share of "old" deposits, that is deposits placed by individuals prior to the effectiveness of the Banking Act - before 20 February 1999 - and guaranteed by the government until the contract expires, fell visibly. The amount for this group is 3.8 billion tolars, and this is a negligible amount given the volume of all deposits from individuals.
The data referring to the guaranteed deposits are used as a basis for the calculation of liabilities of banks and savings banks to comply with mandatory investments of banks and savings banks in securities (set to 2.5% of guaranteed deposits pursuant to the Decree on the Deposit Guarantee Scheme) and for the calculation of the amount of the largest potential annual burden on the bank in the amount of 3.2% of guaranteed deposits.

Box 5: **The report on the privatisation procedure in NLB and NKBM**

The Government of the Republic of Slovenia adopted a programme of privatisation of both banks on 31 May 2001. The two basic aims of privatisation are:

- To strengthen effectiveness and competitiveness of the banks and the banking system;
- To achieve a price that will bring the Government sufficient money to alleviate the burden of public debt.

The programme of privatisation of **NLB** envisages the sale of a 48% share of the bank's capital, so that at the completion of that phase as to leave the Republic of Slovenia the owner of 25% + 1 share. Within the framework of this phase, shares will be sold to the following groups of investors: 34% to key investors and 14% to well-informed portfolio investors. The Government endorsed the amendment to the privatisation programme on 13 December 2001 (referring to the part that brings for sale a 14% share to well-informed portfolio investors in combination with a 15% recapitalisation of NLB; both actions to be eventually executed once the 34% share has already been sold to a key investor). The deadline for the submission of binding tenders was 31 December 2001. Negotiations with potential key investors have begun and will probably end in April 2002.
For the privatisation of **NKBM**, the Government intends to sell a 65% share minus one share. The terms and conditions of sale have to provide for the possible sell off also of the remaining Government share and of both funds (KAD and SOD, which hold a 5% share of the bank each), and other options such as buyout and sale rights have to be examined. On 16 July 2001 the invitation for expressing interest to buy NKBM was announced in the domestic and foreign media. By 7 December 2001, binding offers were received complete with draft terms and conditions of sale. Negotiations with bidderrs terminated at the end of the stipulation of conditions and in March 2002 the privatisation of NKBM was stopped.

In 2001 four fewer banks than a year earlier

The number of banks fell by four between the end of 2000 and the end of 2001, while the number of savings banks remained unchanged. As regards the count of savings and loan undertakings, it fell because of a number of mergers with the Association of Savings and Loan Undertakings (14), transfers of assets and liabilities to other credit institutions (3), as well as one bankruptcy and one case of a voluntary winding-up.

Loan and savings undertakings forced to comply with the Banking Act

The number of savings and loan undertakings greatly decreased because of the harmonisation requirements set out in the Banking Act. The Bank of Slovenia gave the savings and loan undertakings time to comply with the requirements to provide at least half of the prescribed initial capital by 31 December 2001, i.e. 110 million tolars. Since most savings and loan undertakings were unable to comply with this condition, they entered into the agreements for amalgamation, that is the transfer of operations to other credit institutions. In addition to the mergers already carried out, the majority of savings and loan undertakings still in business (more than 30) will join the Association of Savings and Loan Undertakings or other banks by the end of 2003.

The market share held by the savings banks and savings and loan undertakings (in terms of total assets) has been extremely low in comparison with banks – as at 31 December 2001 these institutions accounted for only a 2 per cent share of the market (savings banks: 0.4%, savings and loan undertakings: 1.6%).

5 out of 21 banks at year-end controlled or wholly-owned by foreign shareholders

Out of 21 banks operating as at 31 December 2001, there were seven banks wholly owned by domestic shareholders and five wholly or majority owned by non-resident owners. The remaining nine banks were majority owned by domestic owners, and the share of non-resident shareholders in six banks was in the range of 1%. All savings banks were in the hands of domestic shareholders and largely in private hands.

The banks operating in Slovenia are largely in private ownership with the exception of the top two banks (in terms of total assets) - Nova Ljubljanska banka (hereinafter NLB) and Nova Kreditna banka Maribor (hereinafter NKBM), which became state-owned when their rehabilitation started, and Slovenska investicijska banka d.d. (Slovenian Investment Bank.) with a 14.4 per cent equity holding of the Republic of Slovenia. Poštna banka Slovenije d. d. (Post Office Bank of Slovenia) is indirectly in state ownership.

Table 11: **Granted and rejected authorisations to banks and savings banks**

	Authorisation requested*	2000		2001	
		granted	rejected	granted	rejected
1.	Authorisation to provide banking services	25	0	0	0
2.	Authorisation to provide other financial services	194	1	10	1
3.	Authorisation to a foreign bank to set up a branch in Slovenia	0	0	0	0
4.	Authorisation for merger/acquisition of a bank or a savings bank	2	0	4	0
5.	Authorisation to a foreign bank to set up a representative office	0	0	2	0
6.	Approval to a shareholder to acquire a qualifying holding	9	0	6	1
7.	Authorisation to members of management board	25	2	7	0
	Total	255	3	29	2

* Among the above authorisations, there were 31 new authorisations issued by the Bank of Slovenia to banks and savings banks for the taking up and pursuit of other financial services, while banks and savings banks obtained other authorisations pursuant to the decisions of the Bank of Slovenia concerning the compliance with the relevant provisions laid down in the Banking Act.

Source: Bank of Slovenia.

3.2. Review of performance of banks and savings banks

Operations of banks

High growth in total assets of Slovenian banks

According to unaudited annual figures, **total assets** of all Slovenian banks amounted to 3,948 billion tolars as at 31 December 2001 (not including figures for a branch in Trieste). Total assets increased in 2001 by 23.7% (15.6% in real terms), thus setting the highest effective real growth of the volume of operations over the past five years. High growth was a reflection of that in household deposits, which was most prominent during the last two months of 2001, due to the changeover to euro notes and coins.

In 2001, total assets of all banks (20 banks and one branch of a bank incorporated outside Slovenia) increased. In nominal terms, the growth rates ranged between 14.7% and 109.4%.

The largest bank's market share continued to grow

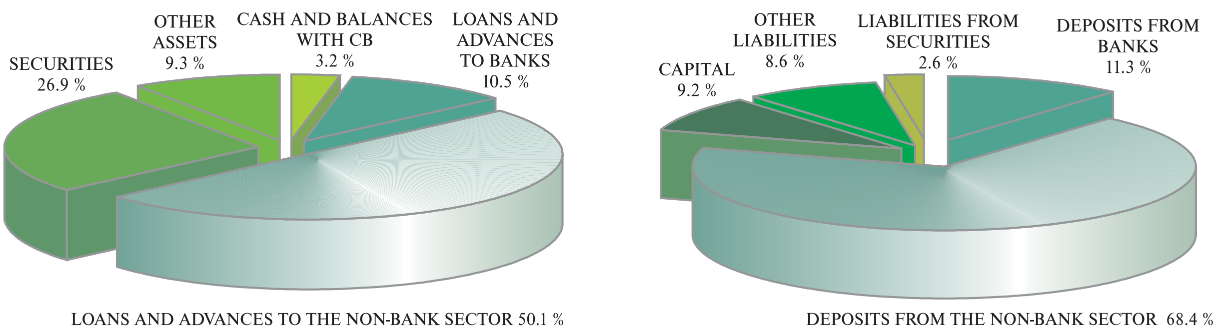
The high concentration of banks in the Slovenian banking system increased in 2001, due to the strengthening of the market share held by the largest bank. The market share held by Slovenia's top bank at year-end 2001 totalled 34.6% (2000: 28.8%) and its combined share with three subsidiaries topped 38.5%. The market share of the three largest banks, which between 1994 and 2000 ranged between 50.4% and 53%, rose to 56.2% at the end of 2001. The market share of the seven largest banks that had between 71% and 73.9% of total assets of all banks between 1994 and 2000, rose to 79.9% in 2001. The market share of the top ten banks reached 86.9% at the year-end.

Table 12: **Total assets and market shares of the largest banks**

	Total assets in SIT millions		Nominal growth in %		Market share in %	
	31-Dec-00	31-Dec-01	2000/1999	2001/2000	31-Dec-00	31-Dec-01
NLB *	918,828	1,367,996	22.1	48.9	28.8	34.6
NKBM	368,109	463,093	14.4	25.8	11.5	11.7
SKB banka	323,353	389,061	5.1	20.3	10.1	9.9
Banka Koper	188,133	255,358	26.0	35.7	5.9	6.5
Banka Celje	198,310	243,961	18.1	23.0	6.2	6.2
Abanka	185,182	226,470	18.9	22.3	5.8	5.7
Gorenjska banka	159,137	206,840	22.1	30.0	5.0	5.2
Aggregate total assets - top 7 banks	2,341,054	3,152,779	17.9	34.7	73.3	79.9
Aggregate total assets - all 25 banks	3,192,792	3,948,262	18.8	23.7	100.0	100.0

* Figures as at 31 December 2001 exclude the branch of NLB in Italy.
Source: Bank of Slovenia

Chart 12: **Average structure of banks' assets and liabilities** (31-Dec-2001)



Source: Bank of Slovenia.

The share of household deposits and issued securities in average total liabilities strengthened

As regards the average **structure of liabilities** in 2001, the share of deposits from the non-bank sector remained hardly changed in comparison with 2000. The structural share of deposits from the general government declined (down by 1.9 percentage points) and deposits from non-financial institutions lost 0.4 percentage points. On the other hand, the structural share of household deposits strengthened (up by 2 percentage points) due to more vigorous growth in foreign exchange deposits at the year-end. The share of issued securities in average liabilities also went up by 0.7 percentage points. The share of deposits from the banking sector in 2001 remained unchanged year-on-year, whereas the share of capital decreased by 0.6 percentage points.

Liabilities of banks to the non-bank sector (customers) increased greatly in 2001 (up by 28% compared to 16.1% in 2000). The real growth rate of deposits placed by the non-bank sector (19.6%) was well above the growth rates achieved during the period 1998–2000 when the figures ranged between 3.2% and 10.9%. Such a high growth rate came as a consequence of the strong growth in foreign exchange household deposits during the last quarter of 2001. During the year under review, the share of deposits from the non-bank sector in average total liabilities was 68.4% (2000: 68.6%).

More vigorous growth in deposits from non-financial institutions…

The growth in deposits from non-financial institutions (17,1%) was up compared to 2000 (11.8%) and was more pronounced in the tolar-denominated segment than in the foreign exchange one. In 2001, demand and time deposits with agreed maturity between 91 days and 1 year enjoyed the best growth. In spite of higher figures, the share of deposits from non-financial institutions in average total liabilities decreased to 13.5%.

and households…

After vigorous growth of household deposits in 2000, the year 2001 showed even higher figures. The achieved real growth rate (26,9%) was well ahead of the growth rates between 1998 and 2000 (5.8% to 14.9%). The rise in household deposits was in comparison with previous years particularly strong in the tolar-denominated segment (time deposits of over 91 days to 1 year) and in the foreign exchange segment (deposits repayable on demand). Their share in average total liabilities increased to 41.7% (2000: 39.7%).

… and a downswing in deposits placed by the government

Since deposits placed by the government fell by 11.5% primarily due to lower obligations under the New Finance Agreement, the share of this item in average total liabilities in 2001 decreased to 5%. The movement in deposits from other financial institutions was in contrast with the movements in the government deposits. This item went up in 2001 by 40.4% (2000: 8.6%); hence their share in average total liabilities rose to 5.5%.

Table 13: **Maturity structure of deposits from and lending to the non-bank sector** (in %)

	31-Dec-00	31-Mar-01	30-Jun-01	30-Sep-01	31-Dec-01
Demand deposits of nonbanks	33.6	32.4	33.0	31.5	34.3
Shortterm deposits of nonbanks	57.6	58.9	58.5	60.1	58.0
Longterm deposits of nonbanks	8.8	8.7	8.5	8.3	7.7
Total deposits of nonbanks	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**
Shortterm loans to nonbanks	57.8	58.3	58.7	59.0	56.9
Longterm loans to nonbanks	42.1	41.6	41.2	40.9	43.0
Claims from guarantees issued	0.1	0.1	0.2	0.2	0.1
Total loans to nonbanks	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**

Source: Bank of Slovenia.

Liabilities to cross-border banks still the largest liability item carried by domestic banks

Liabilities to banks increased in 2001 by 10.2% - less than in past years. The whole increase arises from higher liabilities to cross-border banks, but it still remained below the figures in 1999 and 2000 (despite the fact that in 2001 foreign banks invested heavily in equity capital of Slovenian banks). Liabilities to cross-border banks, which accounted at year-end for 71.7% of aggregate liabilities to banks (2000: 67.7%), continued to be the most important sub-item of liabilities to banks. The share of these liabilities in average total liabilities practically stayed the same in 2001 (11.2% compared to 11.1% in 2000).

Investments in securities gained momentum in 2001

During the year 2001, the banks showed a preference for the issuance of cheaper securities with shorter maturity that have no characteristics of a subordinated debt rather than for the issuance of instruments, which have the characteristics of a subordinated debt. **Liabilities arising from issued securities** increased in 2001 by 59.9%. The banks generally opted for the issuance of short-term and long-term securities. The share of liabilities arising from issued securities in the average structure of liabilities went up from 1.9% to 2.6% in 2001. Given the growth in **capital** compared to the growth in total assets in the year 2001 there was a decline in the share of capital in average total liabilities from 9.8% to 9.2%.

As regards the **structure of assets,** the share of investments in securities increased (up by 1.2 percentage points) and loans and advances to the banking sector (up by 0.3 percentage points) in 2001 due to a fall in the share of loans and advances to the non-bank sector (down by 1 percentage point). The downward trend was mainly caused by a fall in lending to households (down by 1.4 percentage points), while the share of loans and advances to non-financial institutions increased (by 0.8 percentage points).

Lending to the banking sector up and to the non-bank sector down…

A steady rate of growth in lending to non-financial institutions throughout the year under review reached 23.1%, being above the 2000 rate of growth of 20.9%. The achieved real growth rate in lending to non-financial institutions after 1999 (7.1%) reflects an ever-increasing orientation of banks towards crediting this sector in 2000 (11%) and 2001 (15.1%). Borrowing by households increased in 2001 by 7.7% (2000: 12.5%). The effective real growth rate in loans and advances to households after the record high 1999 (34.5%), due to the introduction of value added tax fell in 2000 and 2001 to 3.3% and 0.7%, respectively. While loans and advances to individuals stayed at the 1999 level in real terms, loans and advances to sole traders fell in real terms. The rates of growth in lending to other financial institutions in 2001 went down to 16.4%, this figure being considerably below 91.8% in 1999 and 30% recorded in 2000. Loans and advances granted to the government in 2001 showed in a 5.4% growth - a drop in comparison with the previous year (21%), since the government substituted borrowing from banks and tapped into fresh funds by issuing securities (Treasury bills and bonds). This trend was consistent with lending to non-residents that declined by 18.4% and to non-profit institutions serving households that fell by 30.9%.

… the share of long-term lending also up

The composition of loans and advances to customers other than banks by maturity has been gradually changing over the past five years in favour of long-term lending. Therefore, the ratio between short-term and long-term loans at year-end 1995 was 59:41 compared to 2001 when it was 57:43. During the year , short-term lending increased by 14.4%, long-term lending by 18.7%. The real growth rates indicate a steady decline in the growth of short-term loans and advances, whilst growth in long-term lending recovered in 2001 after flagging in 1999 and 2000. The growth of loans and advances denominated in foreign currency with a 21.0% rise achieved in 2001 was below the relative figures for 2000 and 1999 (31.4% and 34.4% respectively). The share of investments in securities in average total assets was up in 2001 after a drop in 1999 (4.9 percentage points) and 2000 (2.8 percentage points) owing to underwriting of bills issued by the Bank of Slovenia (up 1.2 percentage points to 26.9%). The composition of securities held by banks at year-end shows the largest portion of securities of the Bank of Slovenia (52.7%), followed by government-issued securities whose share in 2001 decreased to 34.8% in spite of a new issues of Treasury bills, and other securities with 12.5%.

Bills of the Bank of Slovenia headed the list of investments in securities

Investments in securities in 2001 increased by 39.8%, with investments in the Bank of Slovenia bills rising most (up 59.9%), both in foreign currency due to the higher foreign exchange minimum and tolar-denominated – the strengthening of these items was most prominent in the second half of the year under review and reflects the policy pursued by the Bank of Slovenia to withdraw excess liquidity by deploying tolar-denominated instruments. Investments in government securities increased of 18.8% in 2001 most with investments in short-term securities (Treasury bills). Investments in other securities (shares/stocks, bonds, securities of non-resident issuers, governments, etc.) increased by 35% especially with shares (stocks) and securities of non-resident issuers.

A 7.5% increase in investments in the banking sector

In 2001, investments in the banking sector rose by 7.5%, particularly when denominated in foreign currency. A break down of the average assets shows that the share of investments channelled into the banking sector grew from 10.2% in 2000 to 10.5% in 2001. The composition of investments in banks hardly changed during the year under review; hence at year-end tolar-denominated investments accounted for 16.7%, and investments denominated in foreign currency accounted for 83.3% of the item in question (2000: 16.5% and 83.5%, respectively).

At year-end, the share of cash on hand and balances on accounts with the central bank accounted for a rather high share in aggregate total assets with 5.2% (overnight deposits).

Decline in the share of average liabilities denominated in foreign currency

Excess supply of foreign exchange in the foreign currency markets was the source of a continuous pressure on the tolar exchange rate to appreciate. The lagging behind of the growth rate of the base interest rate (TOM), was more pronounced than in 2000, and was translated into the falling **share of average foreign exchange liabilities in the aggregate average liabilities carried by banks.** This figure remained within the average for the year 2001 (33.9%), however it was by 1.2 percentage points above the figure for 2000. The average share of foreign exchange assets in banks' average assets was with 33.1% in 2001 up by 1.5 percentage points year-on-year. The banks had on average in 2001 by 2.5% more foreign-exchange liabilities than assets.

Table 14: **Classification of on- and off-balance sheet items of banks, value adjustments and provisions** (amounts in millions of tolars)

	31-Dec-2000					31-Dec-2001				
	Aggregate exposure			Value adj., provisions		Aggregate exposure			Value adj., provisions	
	in the amount of	%		in the amount of	%	in the amount of	%		in the amount of	%
A	3,264,439	87.4	(83,9)	24,106	14.4	3,910,113	86.6	(82,3)	28,991	13.7
B	277,864	7.4	(9,5)	30,728	18.3	363,536	8.1	(10,6)	38,014	18.0
C	77,144	2.1	(2,6)	20,726	12.4	92,655	2.1	(2,7)	24,181	11.4
D	58,682	1.6	(2,0)	33,743	20.1	66,766	1.5	(1,9)	37,005	17.5
E	58,352	1.6	(2,0)	58,351	34.8	83,888	1.9	(2,4)	83,485	39.4
Total	3,736,480	100.0		167,654	100.0	4,516,958	100.0		211,676	100.0

Note: Percentages in brackets do not take into account claims on the Bank of Slovenia and the Republic of Slovenia.
Source: Bank of Slovenia.

To curb excessive concentration of credit exposure to a single client and a group of connected clients is generally considered to be a key element of credit risk management. Enacted in 2001, modifications and amendments to the Banking Act in addition to large exposure limits of 25% and 20% introduced a 10% limit in exposures to persons in a special relationship with a bank as stipulated in Article 83 of the Banking Act. The sum of large exposures at the banking system level as at 31 December 2001 totalled 208.6% of capital (own funds). The limit set at 10% of capital (own funds) on exposures to the clients in a special relationship with a bank was exceeded by 13 banks. The deadline for compliance with the limit expires on 3 August 2004.

The composition of the banks' loan portfolio as at 31 Dec 2001 was slightly changed with the share of the A group falling by 0.8 percentage point and the B group expanding which was worse than at the end of 2000. On the one hand the share of the A group in the aggregate exposure of the banking sector without taking into account claims on the Bank of Slovenia and the Republic of Slovenia dropped in 2001, and on the other hand the share of groups B and E increased.

Due to the stronger growth in the volume of bad and doubtful assets (28.3%) than in the growth of total assets (23.7%), the share of bad and doubtful assets in gross assets increased from 13.1% to 13.3%, as well as the share of value adjustments in banks' gross total assets (up from 6.5% to 6.6%) as at 31 December 2001 with respect to the end of 2000.

Exposure incurred by banks to a single client increased

Aggregate exposure to credit risk carried by the banks as at 31 December 2001 was 4,516.9 billion tolars (composed of 3,696.8 billion tolars in on-balance sheet and 820.1 billion tolars in off-balance sheet asset items). Exposure to a single client increased in comparison with the end of 2000 by 14% to 137.4 million tolars. The share of collected assets as opposed to written-off assets for the year under review was 85.5% (2000: 47.5%).

Table 15: **Principal balance sheet items carried by banks**

	Amount in millions of tolars		Nominal growth, in %		Real growth, in %
	31-Dec-00	31-Dec-01	2000/1999	2001/2000	2001/2000
Deposits with Central bank	98,631	206,224	11.1	109.1	95.4
Loans to banks	364,388	391,643	44.3	7.5	0.4
Loans to nonbanks	1,636,557	1,902,286	17.9	16.2	8.6
- loans to enterprises	939,660	1,156,722	20.9	23.1	15.0
- loans to households	483,789	521,135	12.5	7.7	0.7
- loans to government	150,921	159,075	21.0	5.4	-1.5
Securities	793,180	1,109,110	11.9	39.8	30.7
Other assets	300,036	338,998	20.4	13.0	5.6
Total assets	**3,192,792**	**3,948,262**	**18.8**	**23.7**	**15.6**
Liabilities to banks	399,712	440,586	29.4	10.2	3.0
Liabilities to nonbanks	2,157,509	2,761,126	16.1	28.0	19.6
- liabilities to enterprises	441,787	517,219	11.8	17.1	9.4
- liabilities to households	1,293,711	1,756,177	25.2	35.7	26.9
- libilities to government	171,202	151,533	-18.0	-11.5	-17.3
Libilities from securities	69,405	110,996	55.1	59.9	49.5
Other liabilities	250,556	295,894	28.1	18.1	10.4
Capital	315,611	339,660	13.0	7.6	0.6
Total liabilities	**3,192,792**	**3,948,262**	**18.8**	**23.7**	**15.6**

Source: Bank of Slovenia.

The methodology for calculating asset and liability matching changed

Secondary liquidity of banks at year-end 2001 amounted to 701.1 billion tolars. The share of secondary liquidity in total assets went up in 2001 (after a three-year decline) as banks subscribed to more Bank of Slovenia bills - up from 13.7% to 17.8%. All banks complied with the mandatory criteria in relation to matching maturity of liabilities and assets (as prescribed in the Decree on the Required Adjustment of the Maturity Structure of Assets and Liabilities in the first half of 2001. When the Decree on the Tolar Maturity Ladder came into force in July 2001, the methodology for the calculation of the liquid-asset requirements changed. Due to the new methodology, five banks did not meet the prescribed liquidity ratios in the second half of 2001 but the number of complying banks was going up towards the end of the transitional period. In October the methodology was changed again to implement a uniform calculation of liquidity ratios in the tolar-denominated and foreign exchange part, and the banks, which had signed the agreement with the Bank of Slovenia, could achieve compliance with the prescribed liquidity ratios with the combined tolar and foreign exchange part combined. As at 31 December 2001, the achieved liquidity ratio for the period between 0 and 30 days was 0.97 and between 0 and 180 days the ratio was 1.03. Ten banks failed to meet the prescribed liquidity ratio and the transitional period was due to expire on 1 July 2002.

Higher concentration of depositors was typical of smaller banks

As regards collecting of deposits, the downward trend in the concentration of deposits from thirty largest depositors seen in the past years has reversed. The share of the thirty largest depositors (excluding loans and advances to banks and deposits from natural persons) in deposits from the banking system increased in 2001 from 48.5% at year-end 2000 to 51% at year-end 2001, largely due to the fact that the share of the two largest depositors went up. Smaller banks were typically associated with fewer depositors. In the largest banks, the share of the thirty largest depositors in all deposits has ranged between 38% and 44%, while in smaller banks this figure has been between 70% and 86%. Liquidity risk is mitigated by the fact that the share of household deposits in the funds gathered from the non-bank sector remains high. Over the past five years this item has increased from 53.3% to 63.6% at year-end 1997 and 2001, respectively. Time dispersion of the deposits from the thirty largest depositors in 2001 broadly remained the same; at year-end 2001 the deposits with residual maturity of up to 90 days accounted for 46.1% and the deposits with the residual maturity of up to 1 year accounted for 74.0% of all deposits placed by these depositors.

Table 16: **Principal items carried by banks in the profit and loss accounts**

	Amount in millions of tolars		Share in %		Nominal growth in %	
	2000	2001*	2000	2001	2000/1999	2001/2000
Net interest income	123,298	116,789	72.6	68.3	30.1	-5.3
Net fees and comissions	37,858	41,368	22.3	24.2	12.3	9.3
Net financial operations	13,355	19,096	7.9	11.2	40.0	43.0
Net other	-4,666	-6,141	-2.7	-3.6	11.5	31.6
Gross income	**169,845**	**171,111**	**100.0**	**100.0**	**26.9**	**0.7**
Operating expenses	100,041	111,205	58.9	65.0	14.6	11.2
- labour expenses	49,085	53,317	28.9	31.2	12.3	8.6
Net income	**69,804**	**59,906**	**41.1**	**35.0**	**50.0**	**-14.2**
Net provisions and net write-offs	37,233	44,553	21.9	26.0	41.0	19.7
Profit before tax	**107,037**	**15,353**	**19.2**	**9.0**	**61.8**	**-52.9**
Profit after tax	**19,951**	**1.883**	**11.7**	**1.1**	**98.5**	**-90.6**

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

Modest banks' profit due to a high loss incurred by a major bank

Banks earned in 2001 15.4 billion tolars in **profit before tax** including the gain from revaluation of 30.2 billion tolars. In comparison with a year earlier, the generated profit was lower by 17.2 billion tolars, that is by 52.9%. It was the lowest over the past six years as the consequence of a high loss of one major banks (setting aside additional funds to accommodate the requirements related to the classification of the parent bank). By excluding the high loss incurred by the bank in question, profit before tax earned by the banking system in 2001 was 34.9 billion tolars. Profit after tax for 2001 totalled 1.9 billion tolars (2000: 19.9 billion tolars).

Falling share of net interest in the gross income structure…

Net interest earned in 2001 was 116.8 billion tolars. After a strong rise in net interest recorded in 2000 (by 30.1%, in real terms by 19.5%), net interest earned in 2001 declined by 6.5 billion tolars (by 5.3%, in real terms by 11.5%) due to falling revaluation interest. **Net fees and commissions** amounted to 41.4 billion tolars in 2001. In comparison with 2000, this item increased by 9.3% (by 2.1% in real terms) driven mainly by fees and commissions earned by providing payment operations in the country and on intermediary and agency deals. The year under review was highly favourable for banks in the segment of **net financial transactions**, since they earned 19.1 billion tolars - this figure being by 5.7 billion tolars, 43% more than the figure in 2000, primarily due to valuation of investment securities and securities held for dealing purposes as quotations for securities went up. The item referred to as net other (other income from operations, extraordinary income and expenses, and revaluation of capital) in 2001 amounted to -6.1 billion tolars. In comparison with 2000 this item rose by 31.6% due to the increase in extraordinary expenses (payments of taxes and loss incurred by selling fixed assets).

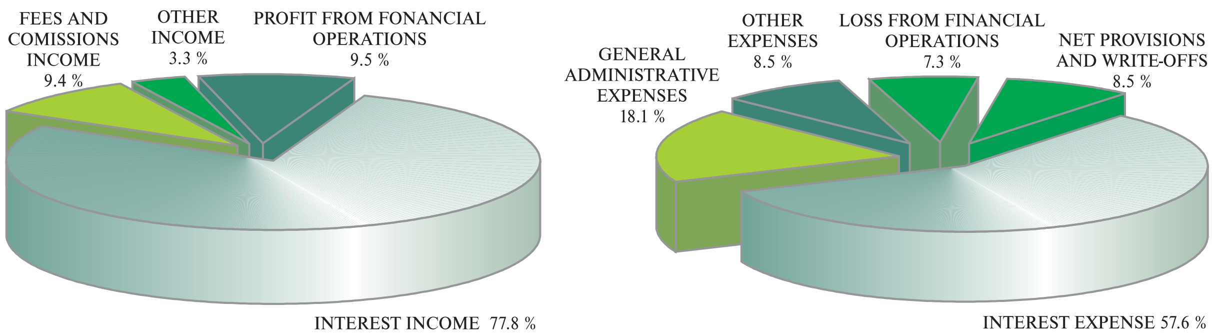
… and the rising share of net fees and commissions, and net financial transactions

Gross income (income before tax) earned by the banks in 2001 totalled 171.1 billion tolars and due to a fall in net interests year-on-year it rose only by 0.7% (in real terms it decreased by 5.9%). As regards the composition of this item, the share of net interest dropped (from 72.6% to 68.3%) in comparison with 2000, and the share of net fees and commissions grew (from 22.3% to 24.2%) followed by net financial operations (from 7.9% to 11.2%).

11.2% rise in operating costs…

Operating costs in 2001 were 111.2 billion tolars. In comparison with 2000 it rose by 11.2%, meaning in real terms up by 3.9%. The real growth rate of operating costs indicates that in 2001 banks managed to control expenses more effectively than during the period 1998–2000 when the real growth rates ranged between 4.9% and 6.6%. The proportion of operating costs to gross income increased in 2001, due to sluggish growth of gross income and went from 58.9% to 65% and the proportion of staff costs from 28.9% to 31.2%. A faster growth in the volume of operations than the growth in operating costs resulted to a fall in operating costs (from 3.4% to 3.1%), as well as in staff expenses (from 1.7% to 1.5%) on average assets.

Chart 13: **The composition of banks' income and expense** (in 2001)



Source: Bank of Slovenia.

Given the stagnant gross income, the growth in operating costs was reflected on **net income** earned (59.9 billion tolars), which was by 14.2% below the 2000 figure when the growth rate was a record high. The fall in real net income is a continuation of reduced earnings in 1998 and 1999 interrupted by the a recovery in 2000 when income figures went up in real terms due to a sharp rise in net interest.

…by 14.2% lower net income and…

The banks set aside 44.6 billion tolars in **net provisions** in 2001 or 7.3 billion tolars (19.7%) more than a year earlier. The share of provisions in the composition of allocation of gross income in 2001 was 26.0% (2000: 21.9%).

… 19.7% more in net provisions

Net revaluation gain or loss in the amount of 30.2 billion tolars was in 2001 by 8.4 billion tolars (21.8%) below the 2000 figure and reflects the reduction in »inflation profit« earned by banks in 2001.

Return on average assets earned by banks in 2001 totalled 0.4% - the lowest over the past seven years. During the period between 1995 and 2000, profit ranged between 0.8% and 1.2% of average assets. By disregarding the loss made by one bank in 2001, the banks' return on average assets in 2001 was 1.1%.
Return on average equity was 4.8% in 2001 or 11.9% when disregarding the bank with a loss.

Lower return on average assets…

Table 17: **The composition of revaluation result of banks' operations**
(in millions of tolars)

	1999	2000	2001
Net revaluation gain or loss	25,073	38,626	30,208
Net revaluation interest	35,081	51,539	40,686
- reval. income [1]	182,013	286,269	251,063
- reval. expense [2]	146,932	234,731	210,377
Net other	-10,008	-12,912	-10,478
- reval. income (fixed assets, capital investments, other)	10,050	13,450	10,193
- reval. expense (capital, other)	20,058	26,362	21,671
Capital revaluation adjustment	19,041	25,112	20,664
Foreign exchange trading gain or loss	-57	-2,056	-403
Gain or loss on contracts with foreign currency clause	202	274	382

1 Arising from FX gains, granted tolar-denominated loans/deposits with/without foreign currency clause, arising from securities.
2 Incurred by FX losses, by taking loans/deposits, by issuing securities, by assuming tolar-denominated liabilities with currency clause.
Source: Bank of Slovenia.

Table 18: **Banks' key performance ratios**

	31-Dec-99	**31-Dec-00**	**31-Dec-01**
Return on average assets	0.8	1.1	0.4 (1.1)
Return on average equity	7.8	11.3	4.8 (11.9)
Net interest margin	4.0	4.5	3.6 (3.7)
Labour cost/average assets	1.7	1.7	1.5 (1.5)
Other operating expenses/Average assets	1.7	1.7	1.6 (1.6)

Note: Values in the brackets exclude the bank, which incurred a high loss.
Source: Bank of Slovenia.

... and lower interest margin

Interest margin calculated as the ratio between net interest and average gross interest-bearing assets whose trend since 1997 has been downward (except in 2000), declined by 1 percentage point in 2001 to 3.6%. By disregarding the figures of the bank that was in loss in 2001, the net interest margin earned by Slovenia's banking system in 2001 was 3.7%. Interest margins varied quite differently from one bank to another in 2001 - between 1.1% and 6.9%.

Interest spread calculated as the difference between average annual nominal deposit and lending interest rate on tolar-denominated investments, that is assets from the non-bank sector, was down in the last quarter of the 2001 review in comparison with the last quarter of 2000 by 1.5 percentage points (down from 6.4 percentage points to 5 percentage points), contributed to by the strengthening of deposit interest rates and lower lending interest rates.

Banks' capital calculated in accordance with the Regulation on Capital Adequacy of Banks and Savings Banks totalled 275.5 billion tolars as at 31 December 2001, of which core capital amounted to 260.4 billion tolars. **Capital adequacy** across the banking system was 11.8% (at year-end 2000: 13.5%).

3.3. Operations of savings banks

There were three operating savings banks in Slovenia in 2001. The aggregate assets of the three savings banks at year-end amounted to 15.2 billion tolars and this figure was by 23.5% higher year-on-year. Therefore, the share of savings banks in the Slovenian banking community remained modest (0.4%). Nevertheless, there were major differences in the size and composition of their balance sheet items.

Households deposits accounted for the largest portion of liabilities of savings banks ...

Deposits of households have remained the most significant source of funding in the composition **of liabilities** carried by the savings banks. In 2001, this item increased by 35.7%, and their share in average total liabilities of the savings banks also rose (to 29.6%). Deposits placed by non-financial institutions declined at the end of 2001 by 23.2% year-on-year and this fall was reflected in the share of these deposits going down (to 16.7%), even though they remained the second most important source in total liabilities of the savings banks. Deposits from the banking sector strongly increased in 2001 (up by 131.7%) due a maturing deposit from the non-bank sector placed with a savings bank. In spite of high rate growth the share of deposits from the banking sector on average total liabilities decreased to 8.3%. The proportion of capital to average total liabilities declined to 9.2% in 2001.

The maturity of deposits from the non-bank sector placed with the savings banks was slightly longer in 2001. At the year-end the maturity composition of deposits showed the following: demand deposits 5%, short-term 70.3% and long-term 24.7%.

...and are generally passed on as loans to households

Funds collected by the savings banks are generally passed on as lending to households, and grew by 19.6% totalling at year-end 2001 81.3% of savings banks' **average assets**. The share of investments in the banking sector increased by the end of 2001 to 5.7%, in non-financial institutions it decreased to 3.1% of assets. The share of investments in securities of savings banks in 2001 totalled only 1.9% of average assets.

The proportion of short-term and long-term loans and advances to the non-bank sector which stood at 36.4:63.6 at the end of 2000 improved to 42.7:57.3 in 2001 following a shift in long-term lending to current maturity in one of Slovenia's savings banks.

As at 31 December 2001, exposure of the savings banks to credit risk amounted to 14.4 billion tolars. With the share of A-graded clients lower by 0.1 percentage point (down to 96.9%), the quality of the savings banks' loan portfolio slightly deteriorated in comparison with the end of 2000. The share of bad and doubtful assets in gross assets was 4.5% (at year-end 2000: 4.5%). There were no cases where savings banks exceeded the limits on allowed for the largest exposures.

All savings banks generated profit

In 2001, all savings banks operated at a profit. Their aggregate profit totalled 220.7 million tolars - by 63.8 million tolars or 40.7% more than in 2000. In comparison with 2000, gross income went up by 226.7 million tolars, that is by 33% in 2001, largely due to higher net interest (up 126.8 million tolars) and fees and commissions (up 79.7 million tolars). Operating expenses increased by 131.9 million tolars (up 28.3%) in 2001. As operating expenses grew faster than total assets, their share in average assets in 2001 grew from 3.8% to 4.3%. Savings banks in 2001 set aside provisions in the amount of 94.3 million tolars or 48.8% more than in 2000.

Interest margin of savings banks ahead of interest margin of banks

In 2001, the savings banks achieved a high return of 1.6% on average assets and on equity of 17.2%. Unlike the banks, the interest margin of the savings banks in 2001 increased by 0.5-percentage point and to 4.1% and was better than the banks. During the last quarter of 2001, the nominal interest spread of the savings banks was 4.5 percentage points (2000: 4.7 percentage points) and real interest spread was 3.3 percentage points (2000: 3.1 percentage points).

The reduction in the **capital adequacy** ratio of the savings banks continued – with 11.1% as at 31 December 2001, it was by a 0.2 percentage point below the figure at the end of 2000 when it stood at 11.3%.

3.4 Supervision of banks and savings banks

The Strategic Plan for the Supervision of Banks' Operations for the period 2000–2003 sets the number of full-scope examinations at 7 to 9 a year, and targeted examinations of a segment of operations conducted institutions (banks, savings banks and savings and loan undertakings) in the band at 30 a year. It can happen that a bank or a savings bank as is currently practise be examined several times a year. The areas to be examined are selected on the basis of information obtained beforehand and analysis of operations of individual credit institutions, or it is done in response to an initiative coming from another department of the Bank of Slovenia or other competent institutions. A special area for examination is risk assessment associated with information technology. By means of targeted or full-scope examinations, there is a possibility of in-depth examination of the areas associated with higher degrees of risk or the areas where the Bank of Slovenia lacks adequate or verified data.

To ensure continuing supervisisory oversight of banks and savings banks, statutory returns are sent to the Bank of Slovenia on a regular basis to the analysts who check them. In addition, the examiners verify the on the ground practice. By subscribing to the so-called four-eye principle, analysts and examiners join forces and are jointly responsible for supervision of individual banks and savings banks.

The analysts are responsible for on-going vigilance of performance delivered by credit institutions on the basis of data and information received at least on a monthly basis, they take part in assessing results of operations of banks and savings banks, issuing and amending authorisations to take up and pursue business of a bank, they weigh proposals of new systemic solutions, advise in the course of implementation of standards for safe and sound operations, keep an eye on observance of restrictions in place for the purpose of maintaining safe and sound operations, they participate in the preparations for supervisory visits to banks and savings banks, in periodic discussion at senior executive level of banks and savings banks, and other institutions, they draft materials for the work of the bodies of the Bank of Slovenia, etc. In case of findings that do not fit into routine operating results for the respective bank or the savings bank, the analysts notify examiners and management of the Banking Supervision Department, so as to provide the grounds to decide whether or not an on-site examination of the bank or the savings bank in question will be necessary. Having identified irregularities in the business of the bank or savings bank, the analysts and examiners take the necessary steps and monitor the actions taken to remedy the situation.

Since banks and savings banks are associated with a markedly high level of credit risk, the stress of the supervisory visits is on verifying that credit institutions have in place the appropriate classification of on- and off-balance sheet items. Particular attention is being paid to consolidated supervision – the examination of the bank in question and its connected entities. The examiners of the Bank of Slovenia verify the financial statements of connected persons, the bank's policy (present and future) in relation to the connected persons (clients), quality of their assets – investments, governance and relations with the bank and operational risk. These data serve to the

Box 6: **Improvement of the harmonisation of Core Principles for Effective Banking Supervision**

The Governing Board of the Bank of Slovenia adopted at its 239th session held on 17 January 2002 the Action Plan to improve compliance with the Core Principles for Effective Banking Supervision based on the findings of the Peer Review Mission that visited Slovenia at the end of September 2001. The Action Plan ties down the measures to be taken with the aim of improving the compliance with the Core Principles in the areas where the Republic of Slovenia still is not completely in line or the members of the mission commented at the present position. In accordance with the Action Plan, the Governing Board of the Bank of Slovenia has endorsed the following:

1. Additional resources will be secured for uninterrupted research activities of the Banking Supervision Department (education, reward, etc.) being essential to increase recruitment and retention of high calibre-staff not only in the ambit of the banking profession but also in comparison with the audit profession and other regulators of financial markets.
2. An initiative to amend the provisions of the Banking Act concerning licensing and shareholders' structure of banks will be made to enable banking supervisors to get strong instruments for control in the issues related to a bank's owners and exercising oversight over banks' capital investments in other entities. When acquiring a qualifying holding (above 10%) of voting rights or of the bank's capital, in accordance with the EU Banking Directive it will be obligatory to obtain a prior authorisation from the Bank of Slovenia. Such an authorisation will also be required for major capital investments that banks may decide to make in other entities.
3. As regards banks' lending and investment policy, large exposure limits and extending loans and advances to connected persons, surveillance and supervision of the implementation of Article 39 of the Act on Modifications and Amendments to the Banking Act will be at the focus of supervisory efforts. More specifically, the provisions of the Article stipulate that banks may not conclude new business during the transitional period which could lead to an increase in unauthorised exposure to persons in a special relationship with the bank in question, i.e. would mean exceeding new limits put in place in 2001.
4. The requirements for management and control of market risks on a consolidated basis will be implemented alongside with the implementation of the provisions related to capital requirements for market risks on a stand alone basis. As regards the regulatory area the stress wil be on developments around the world and adding to regulations and to legal basis if needed to become fully compliant with the standards advocated by the Bank for International Settlements (BIS), or EU directives referring to the banking sector.

By enacting an appropriate modification to the Banking Act and secondary legislation, detailed quantity and quality standards to be met by internal models with regard to management and control of market risks, i.e. determination of capital requirements for market risk will be defined. In addition to the education and training of supervisors, efforts will also focus on the education of banks in this field.

examiners to establish *inter alia* whether provisions and value adjustments made to accommodate the bank's exposure (loans and advances, capital investments) to connected persons are adequate.

In 2001, the examiners of the Banking Supervision Department in the course of on-site supervisory visits to banks and savings banks – alongside conventional areas of examination – paid special attention to supervision on a consolidated basis, market risk, implementation of the laws governing consumer loans, prevention of money laundering, payment transactions carried out on behalf of legal entities, card operations, etc.

The planned volume of examinations within the framework of on-site supervisory oversight of banking operations for 2001 was (subject to minor changes due to take-overs) entirely met. Full-scope examinations were carried out in seven banks and one savings bank.

8 full-scope and 30 target examinations plus 20 examinations related to information technology

In addition to 8 full-scope examinations, 30 targeted examinations of banks, savings banks, savings and loan undertakings and other undertakings were carried out by business area, without taking into account examinations concerning information technology. In 2001, IT systems were the subject of 20 examinations within the framework of full-scope examinations of banks or savings banks or targeted examinations.

The Banking Supervision Department filed in 2001 a motion to initiate a bankruptcy procedure, that is it issued a decision to instigate compulsory liquidation in three savings and loan undertakings.

As regards the prevention of money laundering, the examiners of the Banking Supervision Department in 2001 carried out 25 one-day examinations in practically all banks and savings banks and together with colleagues from other departments of the Bank of Slovenia they took part in the verification of the criteria for the migration of payment operations to banks.

Supervsion extended to operations of legal entities connected with the bank in question

In accordance with the Banking Act, the Bank of Slovenia is authorised for supervisory oversight of legal persons connected with a bank, should that appear necessary within the framework of oversight of operations of the bank in question. In 2001, the examiners of the Bank of Slovenia carried out in seven banks independent targeted examinations of operations of companies, which are wholly-owned subsidiaries of the banks in question (leasing companies).

The mandate given to the Bank of Slovenia to exercise its supervisory power in cases where there is a justified doubt that the corporate entity provides banking services without being authorised by the Bank of Slovenia, has been extended to include other persons. In 2001, the examiners of the Bank of Slovenia acted on the basis of announcements made by competent state institutions (most frequently the Ministry of the Economy and/or the Market Inspectorate of the Republic of Slovenia) and initiatives given by the members of the Governing Board of the Bank of Slovenia conducted six direct examinations of »non-bank« companies suspected of pursuing an activity for which they have not been duly authorised by the Bank of Slovenia.

In accordance with the Core Principles for Effective Banking Supervision, the supervisors of banking operations of the Bank of Slovenia keep in touch on a regular basis with management of banks and savings banks also by holding routine annual meetings at the end of a full-scope examination or otherwise. These meetings serve in the first place to assess operating results and the state of affairs of the bank or the savings bank in question, and to learn about its strategy for the future.

The exchange of opinions and information between supervisors and management of the respective bank or the savings bank is also a precondition for taking timely and appropriate action in the face of possible difficulties that these institutions may encounter in the ordinary course of their business.

Co-operation with other supervisory authorities

The Banking Supervision Department of the Bank of Slovenia fosters relations with other supervisory authorities at home and abroad. Through memoranda of understanding signed with the Market Securities Agency and the Insurance Supervision Agency, cooperation with these supervisory authorities has been developing with exchanges of opinions and suggestions and information sharing. Regarding supervision of persons who allegedly engage in banking operations without being duly authorised by the Bank of Slovenia, the Bank's examiners worked together with the Market Inspectorate of the Republic of Slovenia. Co-operation with the Office for the Prevention of Money Laundering is well developed.

International collaboration

Liaison with foreign supervisory authorities has been progressing, memoranda of understanding (MoUs) were in signed 2001 with the Austrian Federal Ministry of Finance (Bundesministerium für Finanzen), the German Federal Supervisory Office for the Credit System (Bundesaufsichtsamt für das Kreditwesen), Bank of Italy (Banca d´Italia), the National Bank of Macedonia (Narodna banka Makedonije), the Agency for Banking of the Federation of Bosnia and Herzegovina (Agencija za bankarstvo Federacije Bosne i Hercegovine) together with the Agency for Banking of Republika Srbska (Agencija za bankarstvo Republike Srpske) and the Central Bank of Bosnia and Herzegovina (Centralna Banka Bosne i Hercegovine). The MoU with the French Banking Commission (Commision Bancaire de France) is in preparation.

Examinations conducted abroad

The memoranda of understanding were the basis for carrying out four examinations of operation in 2001 of the subsidiaries (banks and non-banks) and branches of the largest Slovenian bank (in Germany, the U.S.A., Switzerland, and Italy) together with foreign supervisors or autonomously.

4. FINANCIAL MARKETS

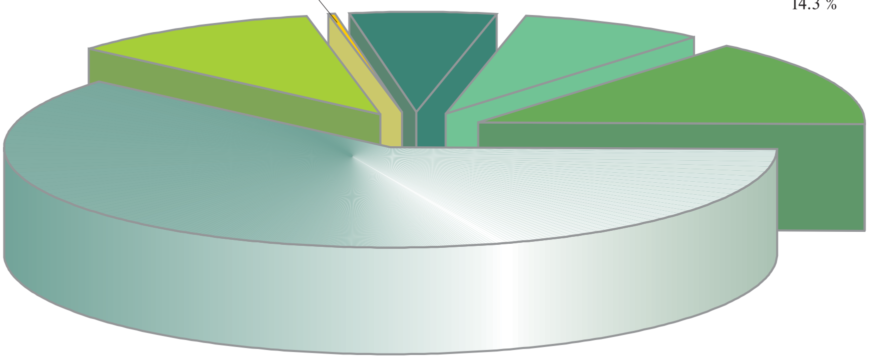
Monetary financial institutions prevailed in the financial market

One of the features of the Slovenian financial market is the prevalence of monetary financial institutions. The share of **non-monetary financial institutions** added up to 25% of aggregated assets of the Slovenian financial system. At year-end 2001, the breakdown of non-monetary financial institutions showed 35 authorised investment companies, 18 mutual funds and 15 insurance undertakings (10 conventional insurance undertakings, 2 reinsurance undertakings and 3 specialised public institutions). Slovenia adopted the legal framework in early 2000 for the provision of voluntary supplementary pension insurance. At year-end 2001 the list of operators of pension schemes featured 7 mutual pension funds and 6 pension companies. Among the financial institutions that provided brokerage services were 11 banks and 20 stockbroking companies.

Stable share of unused ownership certificates

The aggregate assets of **authorised investment companies** amounted at year-end 2001 to 571.2 billion tolars; a fall of 0.4% in comparison with the end of 2000. The share of unused ownership certificates at end of 2001 remained largely the same as at the end of 2000. This share was still composed of just below one third of all assets of authorised investment companies. The total value of investments of **mutual funds** stood at 14.7 billion tolars at year-end 2001 and showed a year-on-year rise of 37%.

Chart 14: **Financial intermediaries by total assets** (at year-end 2000)



Source: Bank of Slovenia.

Table 19: **The composition of Slovenian financial system** (in millions of tolars)

Total assets	1998		1999		2000	
	in SIT millions	%	in SIT millions	%	in SIT millions	%
Central bank	**618,699**	**15.2**	**677,177**	**14.4**	**769,100**	**14.3**
Commercial banks	**2,412,723**	**59.3**	**2,763,260**	**58.9**	**3,286,058**	**61.1**
Non-monetary financial intermediaries	**1,039,059**	**25.5**	**1,250,461**	**26.7**	**1,324,247**	**24.6**
Authorised investment companies	576,908	14.2	599,165	12.8	566,937	10.5
Mutual funds	4,368	0.1	8,821	0.2	10,737	0.2
Insurance companies	217,286	5.3	264,558	5.6	321,823	6.0
Other	240,498	5.9	377,917	8.1	424,749	7.9
Total	**4,070,481**	**100.0**	**4,690,898**	**100.0**	**5,379,405**	**100.0**

Source: Bank of Slovenia.

Insurance and reinsurance undertakings come after authorised investment companies as the second-largest non-bank financial intermediaries. The gross calculated premium of 13 insurance undertakings at year-end 2001 amounted to 222.5 billion tolars, while the gross claims carried by all insurance undertakings was 142.2 billion tolars, a claim ratio of 0.64. At year-end, the insurance sector had 280.9 billion tolars in investments in the financial market. As regards the composition of the investments made, investments in banks and in government securities were predominant.

The importance of **agency financial institutions** for the Slovenian financial market is best illustrated by the value of investments made through that group of financial institutions. The total value of these investments at the end of September 2001 amounted to 912.5 billion tolars; hence this item showed a 10.8 % rise with respect to the end of 2000.

The primary securities market is still underdeveloped

The primary securities market in Slovenia is still underdeveloped. In 2001, only one bank bond was publicly floated (2.2 billion tolars), and the Republic of Slovenia issued seven bonds in the total value of 83.4 billion tolars.

Most securities floated in the market were issued by non-financial institutions…

The Clearing and Depository Corporation or the KDD (Klirinško depotna družba) carried 1,033 registered securities of 885 issuers - 915 shares and 118 bonds at the end of December 2001. The value of shares registered with the KDD at the end of December 2001, carried at market or book value amounted to 2.961 billion tolars (64.8% of GDP). With 78% of cumulative stock value, the non-financial institutions headed the list of the issuers of shares (excluding insurance undertakings) followed

Box 7: **The role of the Bank of Slovenia in the development of the money market**

The Bank of Slovenia played a pro-active role in 2001 by taking part in the activities aimed at the development of the money market. The milestones in these activities are listed below:

- **Signing of the Agreement with the Ministry of Finance**
  In April 2001, the Bank of Slovenia and the Ministry of Finance signed the Agreement on Joint Actions in the Domestic Money Market serving as a basis for the Ministry of Finance to start issuing Treasury bills with one-month maturity.
- **Co-operation with The Clearing and Depository Corporation - KDD (Klirinško depotna družba d. d.**)
  The KDD in co-operation with the Bank of Slovenia devised a new service that enables simultaneous transfer of securities and payment in the over-the-counter market (DVP – Delivery versus Payment).
- **Amendment to the draft bill of the Bank of Slovenia Act**
  Acting on an initiative by the Bank of Slovenia, the draft bill of the Bank of Slovenia Act was amended through the submitter, conferring upon the Bank of Slovenia the right to lay down the rules for trading in the money market.
- **Selection of official market makers and floating of Treasury bills**
  The Bank of Slovenia and the Ministry of Finance signed in November 2001 a framework agreement with five banks on maintaining the secondary market of Treasury bills. The Agreements stipulates that the Bank of Slovenia put in place the infrastructure for the announcement of buying and selling quotations, which the official market makers make public from mid-December onward on the website of the Bank of Slovenia.
- **Notifications to non-bank investors**
  The Bank of Slovenia and the Ministry of Finance have notified major potential investors of the possibilities for trading in Treasury bills.
- **Repurchase agreements related to deals in short-term securities**
  The market will develop in two phases: the first phase will address repo operations involving short-term and the second one will deal with repo operations involving long-term securities. To this end the Bank of Slovenia has prepared a draft of the framework agreement for repo operations involving short-term securities to be finalised with banks in the course of 2002. Furthermore, with effect from 1 January 2002, repo operations involving short-term government-issued securities have been excluded from the mandatory reserve base.

by banks (15%) and other financial intermediaries (6%). The government was ahead of other shareholders with the largest portfolio (26%), households came second (20%) followed by non-financial institutions (20%), other financial intermediaries (19%), non-residents (10%), and banks (4%). The bonds entered into the securities register kept by the KDD in terms of market, or nominal value amounted to 583 billion tolars (12.7% of GDP) at the end of December 2001. The most important issuer of bonds was the general government (77% of cumulative value of bonds), banks followed (13%) and then non-financial institutions (9%). As for the holders of bonds, banks ranked first (47%), followed by insurance undertakings (20%), households (14%), general government (7%), non-financial institutions (6%), other financial intermediaries (4%) and non-residents (2%).

… most bonds were issued by government

At the end of 2001, 270 securities (194 shares and 76 bonds) of 220 issuers were traded on the **Ljubljana Stock Exchange (LSE)**. Total market capitalisation at the end of December 2001 was 1.380 billion tolars, this figure being 30% of gross domestic product. In 2001, the value of the concluded deals was 348.6 billion tolars meaning a rise of 29.3% on a year earlier. Over one half of turnover came from the deals related to blocks of securities. Most of the turnover was performed through shares (84%). The most traded shares were those of Pivovarna Union, Krka, Lek, Pivovarna Laško and Blagovnotrgovinski center. The share of the turnover arising from trade in shares of authorised investment companies accounted for 19.4 per cent of overall trade in 2001. The value of the Slovenian stock exchange index (SBI20) increased in 2001 by 19%, while the increase in the value of the index of authorised investment companies (PIX) was more modest (4.4%). A break down of indices by industry shows that the value increased most in the following groups: oil (41.5%), followed by food and beverages (32.6%), transport (22.5%), chemical industry (12.1%), pharmaceutical products (3.9%) and trade (0.3%). In 2001 the concentration of corporate ownership continued as more take-overs and mergers took place. The most publicised events were take-over bids in the banking sector (SKB banka) and in the beer brewing and beverage sector (Pivovarna Union).

More deals concluded on the Ljubljana Stock Exchange…

… and increased value of the Slovenian stock exchange index

Investments made by non-residents in Slovenian securities reached 68 billion tolars in 2001 - almost eight times the amount in 2000. Most investments (93%) were concluded as over-the-counter deals, and the largest deals were for the shares of Simobil, SKB banka, Banka Koper and Pivovarna Union.

Investments made by residents in securities issued abroad. At the end of December 2001, residents had 69.6 billion tolars in investments in securities issued abroad by non-residents (83% in bonds) and investments in securities issued by residents in the amount of 53.7 billion tolars (all in Eurobonds of the Republic of Slovenia).

BANKA
SLOVENIJE
BANK OF SLOVENIA

5. OTHER FUNCTIONS

5.1. Management of foreign-exchange reserves

By definition, the foreign exchange reserves of the Bank of Slovenia consist of the following:

- foreign cash and balances on accounts abroad,
- firstclass securities of foreign issuers,
- monetary gold,
- special drawing rights (SDRs) and the reserve tranche with the International Monetary Fund (IMF).

International reserves of the Bank of Slovenia up from US$3,196 m to US$4,397 m

In 2001, the international reserves of the Bank of Slovenia increased from US$3,196 million to US$4,397 million. This increase mainly stems from one-week swaps between the commercial banks and the Bank of Slovenia, the operation that during the year under review increased from US$67.1 million to US$ 1,039.7 million. The liabilities of the Bank of Slovenia to domestic sectors arising from issued bills denominated in foreign currency and foreign exchange accounts of banks and government with the Bank of Slovenia which are an integral part of foreign exchange reserves (foreign cash, balances on accounts held abroad, foreign securities) rose from US$1,733 million to US$1,952 million in 2001. The other part of the reserves - own funds without foreign exchange liabilities, was up from US$1,463 million to US$2,445 million in 2001. A significant increase in the value of monetary gold took place in 2001 (from US$0.1 million to US$67.2 million) after the Bank of Slovenia received in June its allotment of the property of the National Bank of Yugoslavia. The aggregate claims of the Bank of Slovenia on foreign counterparties comprise in addition to official foreign exchange reserves and holdings with the International Monetary Fund, other holdings such as the balances on the fiduciary accounts in Luxembourg held with Dresdner Bank and Societe Generale in the total amount of US$60.6 million as at 31 December 2001.

Table 20: **International monetary reserves and foreign exchange reserves of the banking system** (year-end in millions of US dollars)

	BANK OF SLOVENIA							BANKS
	Foreign exchange reserves							
	Gold	SDRs balances	Reserve position with the IMF	Foreign exchange reserves	Total	Thereof: the equivalent of foreign currency liabilities * to residents	Other claims from abroad	Foreign exchange reserves of commercial banks
1992	0,1	-	-	715.5	715.5	465.1	1.4	448.1
1993	0,1	0.0	17.6	770.1	787.7	425.2	1.1	796.5
1994	0,1	0.1	18.8	1,480.1	1,499.0	868.5	103.3	1,283.1
1995	0,1	0.1	19.1	1,801.6	1,820.8	1,259.2	170.1	1,624.1
1996	0,1	0.1	18.5	2,278.7	2,297.4	1,280.0	33.7	1,845.4
1997	0,1	0.1	17.4	3,297.2	3,314.7	1,779.3	41.3	1,079.7
1998	0,1	0.2	65.4	3,572.9	3,638.5	1,852.1	46.8	1,208.6
1999	0,1	1.6	107.6	3,058.8	3,168.1	1,699.1	52.0	1,056.4
2000	0.1	3.7	82.3	3,110.0	3,196.1	1,732.8	58.1	1,266.2
2001	67.2	5.0	80.6	4,244.3	4,397.1	1,952.4	76.1	1,494.1

* Subscribed bills denominated in foreign currency and foreign exchange balances on accounts of banks and government with the Bank of Slovenia.

Source: Bank of Slovenia.

In 2001, the Bank of Slovenia made arrangements for two credit lines in the aggregate amount of 150 million euros for the purpose of short-term financing, but no unwinding took place in 2001 under either credit line.

Credit balances and the reserve tranche with the International Monetary Fund add up to US$80.6 million, and stem from the quota assigned to Slovenia within the framework of the International Monetary Fund and funding financing arranged by the International Monetary Fund under the *Financial Transactions Plan* (FTP).

The Governing Board of the Bank of Slovenia prescribes on a quarterly basis the framework guiding principles for the management of the portfolio that consists of foreign exchange reserves of the Bank of Slovenia, namely its currency composition, average maturity, that is interest sensitivity of foreign exchange deposits and investments in securities, and the selection of the banks. In the light of the criteria for administration of foreign exchange reserves being currently in force, they may only be invested in financial instruments with supranational, national and banking quality risk, and there is a list of approved partner banks and limits for each single bank with regard to its credit rating. The existing criteria take into account foreign exchange risk and stipulate that the amounts of assets in certain currencies, which have their counter item on the liabilities side denominated in foreign currency shall correspond to the amounts in the relative currency in foreign exchange liabilities with the determined span of the possible deviation. The currency composition of own funds of the Bank of Slovenia (whose liability items are not denominated in foreign currency) is thoroughly specified with permitted deviations. The criteria also balance the average modified duration of capital market instruments and specify the average maturity of money market instruments.

In 2001, the Bank of Slovenia in line with the strategy set by the Governing Board of the Bank of Slovenia increased the share of investments in securities, primarily government-issued, and thus alongside improved liquidity contained credit risk.

5.2. Banking services to central government

Cross-border payment operations

Pursuant to the Foreign Exchange Act, the Bank of Slovenia carries out cross-border payment operations and other operations denominated in foreign currency on behalf of the Republic of Slovenia. The amount of outgoing payments that the Bank cleared in 2001 was 810.5 million euros and paid out 6.1 million euros in cash. Inward flows totalled 645.2 million euros, the payments made to domestic commercial banks amounted to 82.2 million euros and foreign cash refunds added up to 1.3 million euros. The Bank sold to the budgetary recipients 136.0 million euros and bought from them 89.6 million euros (of which monetisation accounted for 47.1 million euros); the difference to the value of outgoing payments consisted of disbursements made under lending facilities and donations from abroad.

Maintaining tolar accounts

The turnover on the government account in 2001 amounted to 207,191 million tolars and it was largely generated by transactions involving Treasury bills. Therefore, the account in question is due to be transformed by 30 June 2002 into the government transaction (Treasury) account.

In accordance with the provisions laid down in the Public Finance Act (Official Gazette of the Republic of Slovenia, Nos. 79/99, 124/00 and 79/01) and the Act on the implementation of the Budget of the Republic of Slovenia for the Year 2001

(Official Gazette of the Republic of Slovenia, No. 32/01), the municipalities had to comply with the requirement to transfer their accounts from the Agency of the Republic of Slovenia for Payments to the Bank of Slovenia. The complexity of the task called for the setting up of a cross-institutional project where the Agency of the Republic of Slovenia for Payments, the Bank of Slovenia and the Ministry of Finance took part. The Bank of Slovenia opened one transaction account for each municipality in one or more currencies. The migration was carried out step-by-step between 3 October 2001 and 28 December 2001 in line with the plan that classified the municipalities in several groups in relation to the closing down of the Agency of the Republic of Slovenia for Payments.

Accounts of municipalities moved to the Bank of Slovenia

The municipalities are obliged even after the account migration to submit payment orders to the Agency of the Republic of Slovenia for Payments and receive from it all return information. The municipalities dispose of funds on transaction accounts at their discretion and invest excess balances with commercial banks with different maturities. The accounts for government revenues whose balances are daily transferred to transaction accounts with the Bank of Slovenia remained with the Agency of the Republic of Slovenia for Payments. It is expected that by 30 June 2002, Administration for Public Finance Payments, responsible for keeping sub-accounts for transaction (Treasury) accounts of municipalities will be established.

The turnover through transaction accounts of municipalities in 2001 included 66,410 million tolars in inflows and 61,410 million tolars in outflows.

Operations involving stamps, securities and cash

During the year under review, the Bank of Slovenia conducted on behalf of the Republic of Slovenia operations related to the issuance, distribution and safekeeping of coins, duty stamps and tobacco stamps.

The Bank of Slovenia released in circulation a new commemorative coin of 100 tolars in 500,000 pieces and 49 million pieces of coins having nominal value of 10, 2 and 1 tolars. Overall, between the year 1993 and the end of the year 2001, 372 million coins were put in circulation (until 2000 this figure was 336 million), being 988 million tolars worth (until 2000 this figure was 791 million tolars). The quantity of coins in circulation rose in 2001 by 10.7 %.

The quantity of coins in circulation rose by 10.7 % year-on-year

Commemorative coins were also minted on the occasion of the 10th anniversary of independent Republic of Slovenia and the tolar as its legal tender, and namely: a gold piece, a silver piece and a circulating coin. Last year, the cashiers of the Bank of Slovenia and authorised agents sold 6,097 pieces of commemorative coins, of which 1,721 pieces in gold and 4,376 pieces in silver.

Commemorative coins for the 10th anniversary of independent Republic of Slovenia and the tolar

In 2001, administrative and court duty stamps were issued in the value of 4.9 billion tolars (2000: 5.6 billion tolars). Expert and technical work in connection with tobacco stamps comprised the provision of the required quantity and adequate composition of tobacco stamps and supplying manufacturers, that is importers of tobacco products. Overall, 225 million tobacco stamps were issued (in 2000: 208 million pieces).

Furthermore, the Bank of Slovenia discharged tasks concerning the acceptance and processing of redeemed bonds and coupons at maturity. In 2001, the Bank took over 27,850 coupons and 11,280 blocks of RS 02 government bonds.

In addition, the Bank handled 3,139 incoming and outgoing cash payments in tolars and effected 14,675 incoming and outgoing payments in foreign currencies for travelling expenses and other activities of government bodies.

5.3. Cash operations

Under statutory authorisation, the Bank of Slovenia is entrusted with the task of ensuring a smooth supply of tolar banknotes for the government.

At year-end there were banknotes in circulation worth 166 billion tolars

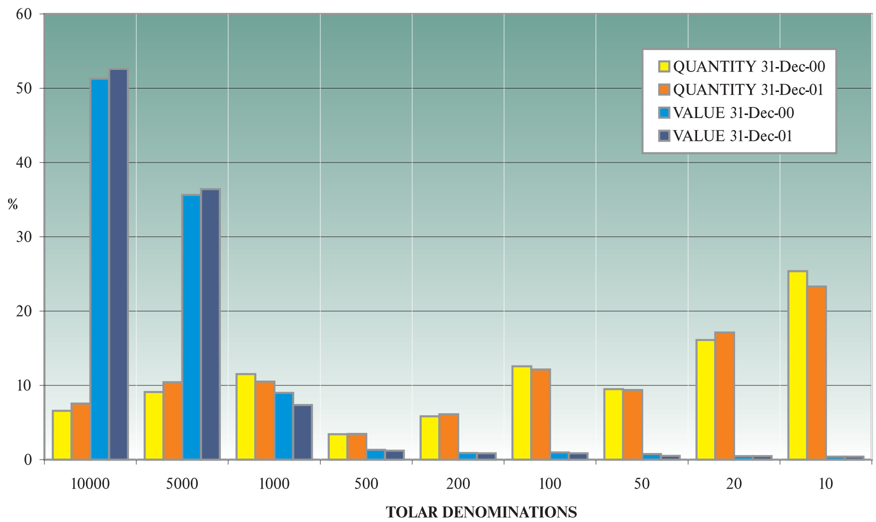
The total number of banknotes in circulation as at 31 December 2001 was 115.5 million to a value of 166 billion tolars (including cash balances in banks). The value of the banknotes in circulation increased by 19 % compared to 2000 and the quantity of the banknotes in circulation rose by 6 %. A breakdown of cash in circulation over the last six years is shown in Table 20. At the end of 2001, banknotes accounted for 99.4 % of value and 23.7 % of the quantity of cash in circulation. As regards value, the banknote of 10,000 tolars was the most important denomination (52.6 % of the value of all banknotes in circulation), which together with the 5,000-tolar banknote (36.4 % of the value of all banknotes in circulation) represented the backbone of cash operations. The role of the 1,000-tolar banknote has been gradually declining both in terms of quantity and in terms of value (this denomination accounts for 7.3 % of the value of all banknotes in circulation as opposed to 2000 when it accounted for 9.0 %). A comparison between the value and quantity composition of banknotes in circulation between 2000 and 2001 is illustrated in Figure 15.

Table 21: **Cash in circulation** (1996–2001) in billions of tolars

At year-end	Banknotes in circulation	Coins in circulation	Total cash in circulation
1996	71.4	0.4	71.9
1997	85.7	0.5	86.1
1998	104.7	0.6	105.2
1999	142.5	0.6	143.1
2000	139.6	0.8	140.4
2001	165.8	1.0	166.8

Source: Bank of Slovenia.

Chart 15: **Breakdown of banknotes in circulation by volume and denomination** (at the end of 2000 and 2001 in %)



Source: Bank of Slovenia.

The money-counting unit of the Bank of Slovenia counted 60.4 million banknotes, of which 41.9 million banknotes were sorted. In line with the requirement to procure adequate quality of the banknotes in circulation, 13.9 million banknotes unfit for the circulation were extracted and destroyed (2000: 30.6 million), 4.8 million banknotes withdrawn 1,000- tolar banknotes were the biggest type.

During the year under review, the supply of the country with tolar cash was carried out through contractual depots of banknotes of the Bank of Slovenia and the organisational units of the Agency of the Republic of Slovenia for Payments (hereinafter: the Payments Agency). In both cases the Bank of Slovenia sets the ceiling on treasury holdings on a quarterly basis and monitors their operations on a daily basis. During 2001, all depots complied with the authorised limits and no irregularities were detected in operations involving cash.

During the first half of 2001, the following banknotes were printed: a 500-tolar banknote, 6 million pieces, and a 200-tolar banknote, 7 million pieces, due to the rising need for these two denominations, and to replace worn-out and damaged banknotes.

Together with the Bank Association of Slovenia, commercial banks and other competent institutions, the Bank of Slovenia co-ordinated and directed activities under the euro cash project.

As regards counterfeits, the Bank of Slovenia examined a year earlier 3,288 pieces (2000: 4,981 pieces) of counterfeited banknotes, discovered and confiscated in the territory of the Republic of Slovenia. The Bank of Slovenia co-operated with the Ministry of Home Affairs and Interpol. Most counterfeits were banknotes in foreign currencies (2,499 counterfeits), although over the last few years, this number has been in decline (3,593 counterfeits in 2000 and 6,079 in 1999). As the changeover date for banknotes and coins in euro was drawing closer, it was observed mainly during the last quarter of 2001 that the number of counterfeited national currencies of the EMU countries was raising, mainly D-marks and Italian lire.

Box 8: **Supply of cash**

In 2001, eight depots for banknotes were in operation the Bank of Slovenia within the framework of five commercial banks - depositories.

In order to make the operations of such depots cost-effective, they have continued to get cash from the network of the Agency for Payments in the area where the depot is located for as long as the relative unit of the Agency for Payments is in business. The depots of banknotes operated by the Bank of Slovenia partly obtain cash from ordinary cash operations conducted by banks and savings banks, which are the users of its services.

The direct depot users have entered into legal agreements with the depositories for the services of the relevant depot, other banks satisfy their needs for banknotes by purchasing from and selling to the depositories (retail banknote market). This way of satisfying the needs for banknotes enjoyed a sharp rise in 2001 in comparison with 2000.

As the accounts of legal persons gradually migrate to commercial banks and the movement of cash payment operations from the Agency for Payments has entered the final phase scheduled for completion in 2002 alongside the arrangements for closing down the Agency for Payments, the banks may carry out the acceptance and payment of legal entities' cash. The banks obtain cash from business partners; to supply cash in the central bank's distribution points (depots of banknotes of the Bank of Slovenia and from the Agency for Payments for the time being) has also a role to service surpluses or deficits of cash from the ordinary course of operations. Consequently, already it circulates in cash payment operations 70 % of processed orders, in the banking system that is 40% by value.

As regards detected counterfeited banknotes, Slovenia ranks in the middle of European countries

The value of the counterfeits of Slovenian tolars has been increasing since 1994 but the value of these counterfeits is very small in comparison with the value of cash in circulation (from 0.0010 ‰ in 1994 to 0.0352 ‰ in 2001). The aggregate value of confiscated counterfeits of Slovenian banknotes stood at 5,878,050,00 tolars last year. The Ministry of Home Affairs asked the Bank of Slovenia for an expert opinion concerning the following counterfeited banknotes: 536 samples of 10,000 tolars, 69 samples of 5,000 tolars, 170 samples of 1,000 tolars, and 14 samples of other denominations. As opposed to a year earlier, the number of counterfeits of 10,000-tolar denomination declined by 32.2 %, counterfeits of 5,000-tolar denominations dropped by 84.9 %, while the number of counterfeits in 1,000-tolar denominations rose by 37.1 %. For every one million banknotes in circulation, 6.8 counterfeits were discovered and this indicator ranks Slovenia in the middle among European countries.

The operations in relation to the issuance of Bank of Slovenia bills included custody, distribution and acceptance of redeemed bills. In 2001, 51 separate Bank of Slovenia bills were processed at redemption.

5.4. Payment systems reform

The final phase of the payment systems reform

The momentum of the efforts to reform the Slovenian payment systems was maintained throughout 2001. The final phase of the reform launched on 11 September 2000 and went on all last year. The task was to transfer the accounts of legal entities from the Agency for Payments into the banking environment. The deadline for this task expires on 30 June 2002 when the Agency for Payments ceased to perform payment services. In addition to the migration of accounts of legal entities, other activities concerning payment systems were proceeding with the aim to improve the structure and the operating mode of the payment systems and consequently boost their effectiveness as far as risks and costs are concerned.

Migration of accounts of legal entities

The migration of accounts took more time than originally planned

By subscribing to the step-by-step approach for the migration of accounts of legal entities from the Agency for Payments to commercial banks, the process has been unrolling with a higher degree of predictability and easier control; hence the phasing out of the Agency for Payments has been facilitated. The legal entities have been classified in seven groups (i.e. operational plans) and those groups were scheduled for migration on a quarterly basis. In 2001, the second, third, fourth and fifth operational plans were on the timetable. However, the groundwork was somewhat more difficult than expected. By the end of 2001, the number of accounts of legal entities transferred to banks was just below 17,700. According to the estimate made by the Bank of Slovenia, this figure represented around 40 % of accounts of all entities obliged to transfer their accounts to banks.

The lag in migration at the end of 2001 was thus more than 11,000 accounts, that is 39 % of those legal entities who according to the operational plans were supposed to have already transferred their accounts to the banks. The delay in meeting the milestones did not mean that the completion date for the migration process was moved and hence the payment systems reform would be extended, since 30 June 2002 as the winding-up date for the Agency for Payments was incorporated in the new Payment Transactions Act. Overall, the migration process has been going on steadily and smoothly along the set guidelines.

Reviews of the Expert Committee

On the basis of the decree of the Governing Board of the Bank of Slovenia, the Expert Committee of the Bank of Slovenia responsible for the verification of the harmonisation between the documentation (when providing payment services for legal entities in the country) with the actual state of affairs in the banks, continued its work also in 2001.

The Expert Committee was appointed in April 2000 on the basis of the decree passed by the Governing Board of the Bank of Slovenia and its original task was defined as reviewing the documentation sent by banks to substantiate compliance with the Criteria to Provide Payment Services for legal entities in the country and to prepare opinions for granting licences for provision of payment services to legal entities. The mandate conferred upon the Expert Committee was extended in May 2000 to encompass reviews of the banks in the field of carrying out of payment operations and related functions.

Therefore, the Expert Committee's agenda included the oversight of the carrying out of payment operations, cash-related operations, information technology and internal audit. The Expert Committee completed the programme, making examinations in all banks authorised by the Bank of Slovenia to provide payment services for legal entities in the country, by the end of June 2001.

Settlement of the cash part of securities transactions

The activities continued in 2001 within the framework of a multi-institutional project of introducing the settlement of the cash part of the settlement of deals involving securities in central bank's money through the accounts held with the Bank of Slovenia launched with the aim to substitute the current transactions settlement settled within the framework of the Agency for Payments. The project has been run by the Bank of Slovenia and the Clearing and Depository Corporation (Klirinška depotna družba - KDD).

The activities planned under the project were running on two main segments. In more specific terms, as regards putting in place the cash part of settlement of securities transactions concluded on the Ljubljana Stock Exchange through the RTGS system and in connection to the cash settlement of over-the-counter deals (OTC) in central bank money in line with the principles of the DVP (Delivery versus Payment), also by using the RTGS system.

The first part of the project was directly linked to the migration since it envisaged the transfer of certain cash accounts of the participants in the securities market to the Bank of Slovenia (part of accounts, i.e. house accounts, were opened with commercial banks). The clearing procedures related to these operations and the cash settlement logic were not changed. This part of the project was realised by the end of June 2002.

The second part of the project that was successfully completed in July 2001 when the clearing settlement account of the KDD was opened within the framework of the RTGS system meant a considerable quality improvement with regard to the settlement of over-the-counter deals. So far, the participants in trading in the OTC market were exposed to the counterparty/settlement risk (the principal risk). By the completion of the second part of the project, the DVP mechanism came into life, which ensures that the final transfer of securities occurs only upon the final transfer of cash. By deploying the RTGS system, the KDD (acting as an agent for the deal) is responsible to ensure that both sides of the deal (in securities and in cash) are settled simultanously in a very short period of time (no later than on the same business day) against settlement in cash through the RTGS system. The application of the DVP mechanism for over-the-counter (OTC) trading is not mandatory and has been designed in the first place to back the development of the short-term money market.

Integrated small value payment system

The concept of putting in place the integrated small value payment system (ISVPS) subject to a prior approval of the Governing Board of the Bank of Slovenia, was presented in January 2001 to all banks – the initiative to foster interbank co-operation in that field got a unanimous backing.

Conceived as a backing for the realisation of the described concept, the blueprint envisaged a two-tier organisational structure of the banking environment, i.e. called for redefining of strategic decisions in the Committee for Payment Services and operating execution of tasks at the level of the project team.

Agreement on co-operation in effecting retail payments

In the light of the aforementioned, a proposed agreement was drafted in the Bank of Slovenia for co-operate in the field of small value payments that addresses the areas and the way in which the signatories (banks, savings banks and the Bank Association of Slovenia) would collaborate with the aim to put in place the systems for effecting small value payments, including the establishment of the aforementioned Committee.

Box 9: **The Bill for a Payment Transactions Act**

The first section of the bill of the Payment Transactions Act addressed the institutional, material and operational issues connected with the carrying out of the payment services. More specifically, it defined the relationship between the providers of payment services, specified the minimum requirements for the regulation of relations between the providers/operators and the users of payment services, and set the minimum criteria for the provision of payment services (deadlines for the execution of a payment order, finality of a payment, responsibility of the provider for damage, etc.).

In addition, the bill also addressed the settlement of liabilities between providers of payment services. It is essential to distinguish between high-value and small-value (retail) payments. On the basis of the new Act, management of the payment system for high-value payments effected between the providers of payment services will be entrusted to the Bank of Slovenia and these payments will be effected in real time. The bill prescribes the issuance of appropriate licences by the Bank of Slovenia for the provision of settlements and management of the payment systems for retail payments and thus introduces two services related to payment operations. In addition to the issuing of licences to carry out the payment services, the settlements and management of the payment systems, the bill also set out further supervisory oversight of the Bank of Slovenia of regularity and legality of the way in which these services and activities are carried out.

One of the key areas addressed under the bill for a Payment Transactions Act is also the issuance of electronic money. By addressing this issue under the new Payment Transactions Act, the foundations for a comprehensive regulation of payment operations have been built. The bill focuses also on the aspects related to the institutions involved in the issuance of electronic money and the services such an institution will be authorised to provide. The provisions of the bill have been harmonised with Directive 2000/46/ES that addresses the carrying out of services and oversight of the carrying out of services related to the issuance of electronic money.

The second section of the bill deals with the dissolution of the Agency for Payments and the establishment of the Public Payments Administration (UJP) within the framework of the Ministry of Finance and the Agency of the Republic of Slovenia for Public Finance Records and Services (AJPES), to be established by the Government of the Republic of Slovenia. The Agency for Payments will cease to provide payment operations with effect from 30 June 2002, while the other tasks the Agency has been discharging on the basis of the law will be taken over by the AJPES and UJP when these two bodies become operational. The Agency for Payments will be wound up as of 1 January 2003.

Agreement was reached to cooperate in the development of new and standardisation of the existing payment instruments, the preparation of common standards for automated processing of payments, for the designing of the settlement guarantee scheme for payment systems, the integration of the existing clearing and settlement systems and the defining and orienting of activities of the clearing house. Overall, these are the areas where synergy —in interbanking co-operation can be anticipated, while the relation between a bank and a customer belongs to competitive environment. The banks have endorsed the contents contained in the agreement, and the time frame envisages the signing of the agreement early in 2002 and subject to the adoption of a code of practice, activities focused on achieving the set objectives may commence.

Efforts focused on standardisation and electronic operations

Accelerated preparations of the common standard for the electronic exchange of data between economic entities

Electronic exchange of data is moving to the centre-stage and the number of economic entities who participate in it is rising dramatically. As regards the inter-bank environment, the exchange of payment messages has been arranged by means of applying S.W.I.F.T. international standards. Nevertheless, there is a problem of the electronic exchange of data between banks and other economic entities - above all their clients. In 2001, the Chamber of Commerce and Industry of Slovenia (CCI) acting upon an initiative of the Bank of Slovenia and Ministry for the Information Society of the Republic of Slovenia stepped up efforts focused on the preparation of a common standard for the electronic exchange of data between economic entities. Commitment to address the issues in the area of electronic commerce was clearly expressed at the conference of competent institutions that took place in May 2001. The outcome of the exchange of opinion was also the decision to set up a task force for the introduction of common standards for electronic data exchange across all industries of Slovenia's economy including the banking sector.

The bill of the Payment Transactions Act

The second reading of the bill on payment operations completed…

The National Assembly at its 10th regular session held on 21 November 2001 finished the second reading of the draft of the Payment Transactions Act. Modifications and amendments were made to the bill and it is noteworthy that the National Assembly endorsed all amendments summing up the proposals made by the Bank of Slovenia.

The National Assembly has given a mandate to the Government of the Republic of Slovenia to prepare a bill for the third reading by incorporating the endorsed amendments. The bill that was presented to the National Assembly for the third (and the final) reading was subject to taking into account the endorsed modifications and amendments addressing comprehensively payment operations within the country and was at the same time harmonised with the EU legislation and the relative recommendations of the European Union.

… to add provisions to the substance of the Banking Act

The bill, by defining the payment services and the criteria for the provision of these services, amends the provisions laid down in the Banking Act in the segment that specifies other financial services the banks and the savings banks may provide subject to obtaining the appropriate licence from the Bank of Slovenia.

The Bank of Slovenia as a participant in the Giro Clearing system

As from 1 August 2001, the Bank of Slovenia became a participant in the Giro Clearing system. Until that date, the Bank of Slovenia was only a direct participant of the RTGS system. With effect from 1 August 2001, all non-urgent retail payment orders (small value orders up to 2 million tolars) debiting and crediting the Bank of Slovenia and its customers are submitted to the Giro Clearing system. The goal to be achieved by the Bank of Slovenia becoming a member of the Giro Clearing system has been to allow large-scale small value payments debiting and crediting the Bank of Slovenia and its customers (the central government or more specifically the Ministry of Finance) to be processed via the Giro Clearing system, mainly because it is considerably cheaper comparison with the RTGS system.

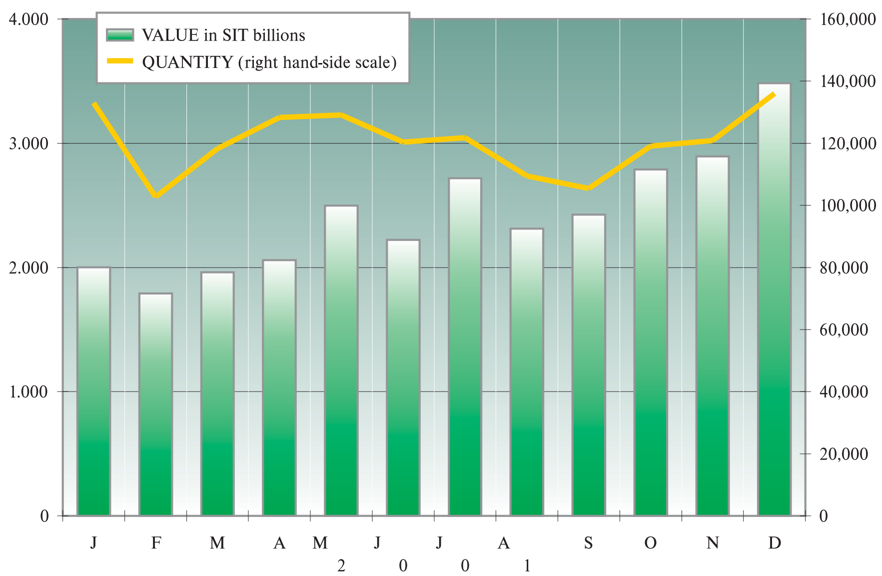
Statistics related to payment systems operations

In 2001, 1,444,594 payments were effected through the RTGS system (38.9 % more than in 2000) in the cumulative value of 29,153 billion tolars (31.2 % more than in 2000). On average, 5,825 payments were settled daily and the average value of these payments stood at 20.2 million tolars per payment.

The system of Giro Clearing being the second fundamental part of the reformed payments systems handled during that period of time 48,180,832 non-urgent small payments of under 2 million tolars (38.3 % more than in 2000), whose cumulative value amounted to 3,794 billion tolars (35.4 % more than in 2000). The value of settlements of the payments in question in central bank money through the RTGS system was 1,431 billion tolars, i.e. 38 % of gross value of payments. On average, 194,278 payments whose average value was 78,745 tolars were processed daily.

The aforementioned data for both systems clearly show that the number and the value of payments has increased, mostly as a consequence of the accounts migration, since a portion of transactions previously carried out within the Agency for Payments became interbank transactions.

Chart 16: **The volume of payments in the RTGS system in 2001**



Source: Bank of Slovenia.

5.5. Statistical system

The statistical system of the Bank of Slovenia serves to support monetary policy of the Bank of Slovenia, notifies the domestic and foreign public of the financial and macroeconomic developments in Slovenia, and collaborates with the statistical sections of the international institutions of which Slovenia is member or strives to become one.

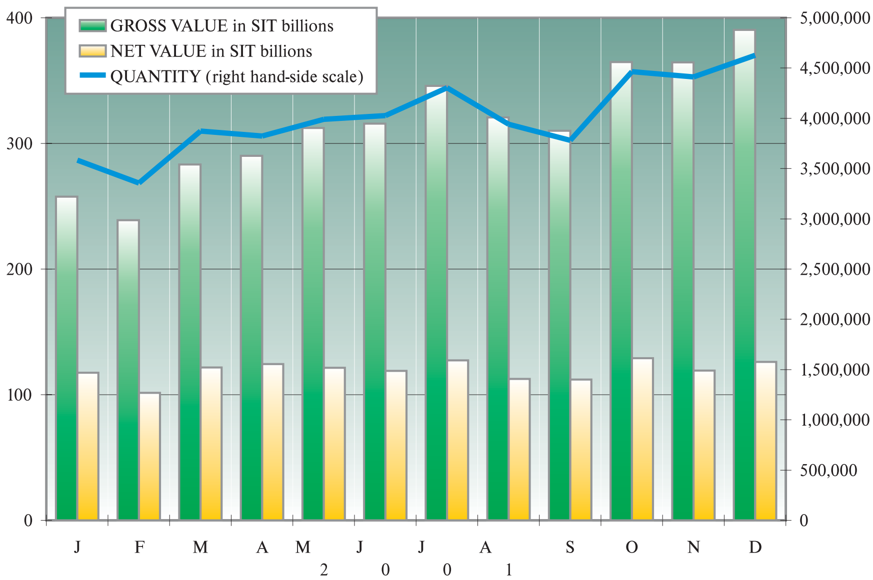
In 2001, the National Statistics Act was amended to mirror the harmonisation of the Slovenian statistics with the statistical responsibilities in the European Union and in particular to enhance professional independence of national statistics, protection of statistical confidentiality and more flexible monitoring and implementation of the statistical research programme.

The responsibilities of the Bank of Slovenia will be extended to include financial accounts in addition to monetary and balance of payments statistics

In line with the new medium-term statistical programme, the Bank of Slovenia has also assumed the role of a developer of financial accounts in accordance with international standards. Thus financial accounts being the third key statistical segment have joined monetary and balance of payments statistics as the segments already entrusted to the Bank of Slovenia. These statistics are mainly based on the data derived from direct and indirect returns submitted by banks and companies, as well as on the data on exchange of goods prepared by the Statistical Office of the Republic of Slovenia on the basis of customs declarations. In addition to these sources of date the Bank of Slovenia collects, compiles and publishes data statistics related to modern payment instruments, financial markets, etc.

In 2001, the Bank of Slovenia modernised direct reporting concerning the balance of payments and the international investment position from the technological and material aspects partly owing to then funds procured under the Phare programme. These changes have reduced the burden of reporting requirements observed in the study prepared in 2000 by the FIAS, a joint service of International Finance Corporation and The World Bank as one of administrative barriers to foreign direct investment.

Chart 17: **The volume of payments in the Giro Clearing system in 2001**



Source: Bank of Slovenia.

The pace of convergence with monetary statistics methodology of the euro area has accelerated

The methodological basis for the quoted statistics is the standards of the International Monetary Fund (the IMF), and because of convergence with the acquis communautaire of the European Union more and more also the standards of the Eurostat and the European Central Bank. Above all, the process is gaining momentum due to the harmonisation with monetary statistics of the euro area. The Bank of Slovenia releases on its web pages data in accordance with the Statistical Data Dissemination Standards drawn up by the International Monetary Fund, prepared jointly with the Statistical Office and the Ministry of Finance. These standards prescribe regular and timely release of methodologically appropriate key macroeconomic data according to a pre-announced calendar. Compliance with the standards enhances macroeconomic transparency that is essential to early recognition of financial difficulties, and therefore is important for access to international financial markets.

Monthly press conferences on the balance of payments

The key financial and macroeconomic data for Slovenia are published in the monthly The Bulletin (Bilten). Besides the Bulletin, there is the quarterly issue of information called Financial Markets (Finančni trgi) and the annual Direct Investments. All publications are, together with the information on the balance of payments and longer time series of data from The Bulletin, also available on the web site of the Bank of Slovenia. Under the programme of updates on the web site, key statistical data have priority. As well as to the list of domestic and foreign users, the Bank of Slovenia forwards statistical data to the International Monetary Fund, Eurostat and the OECD. Data on the balance of payments were for the first time released at monthly press conferences in 2001.

In addition to regular meetings in working groups and at seminars of Eurostat and the ECB, the representatives of the Bank of Slovenia also take part in plenary meetings of the Committee on Monetary, Financial and Balance of Payments Statistics (CMFB), the most prominent body for the co-ordination of strategic issues related to European financial statistics.

5.6. International relations and co-operation

The succession agreement concluded

In 2001, the countries who are successors to the SFRY signed the succession agreement. So far, this agreement has been ratified by Bosnia and Herzegovina and Macedonia with pending ratification in parliaments of other successor countries. The distribution of property of the former SFRY was agreed under the auspices of the Bank for International Settlements (BIS) allocating to the Bank of Slovenia 16.39 % of assets of the National Bank of Yugoslavia (shares and gold).

In 2001, the final procedures under the negotiations with the governments of creditor countries in framework of the Paris Club were successfully concluded.

Box 10: **The division of property held with the BIS**

The agreement reached as to the formula for the division of property concluded by the succession countries of the SFRY with the Bank for International Settlement (BIS) was realised in June 2001. The assets were divided in accordance with the accepted formula of the International Monetary Fund. The Bank of Slovenia obtained 16.39% of the assets of the former National Bank of Yugoslavia, consisting of 1,310 shares in capital and bank balances in the BIS in the countervalue of US$4.4 million and gold worth US$65.2 million at the then market value. Having completed the procedure of splitting up the assets among the successor states, the BIS purchased »symbolic shares«, which the central banks of the successor countries paid in on the basis of temporary extraordinary issue of new shares within the third tranche of paid in capital.

Slovenia's quota in the International Monetary Fund (IMF) remained unchanged and amounts to 231.7 million SDR, which means 0.109 % of votes of all members.

The Republic of Slovenia participated in granting loans within the framework of the FTP

Slovenia, which as the first transition country in 1998 joined the group of countries whose currencies are used by the IMF to extend lending facilities to members within the framework of the Financial Transaction Plan (FTP), participated in 2001 in wrapping up lending facilities in the amount of 4.9 million SDR. Since the beginning of its participation in the FTP, Slovenia's contribution has totalled 54.9 million SDR and during the same period it received 22.89 million SDR.

Two visits of the Mission of the International Monetary Fund

In 2001, the Mission of the IMF visited Slovenia twice: in January 2001 according to the requirement to draw up a report under Article IV for consultation for the year 2001 and in December 2001 for the purpose of preparing the report in the context of Article IV for consultation mission for the year 2002. In May 2001, the Board of Executive Directors of the IMF examined two reports on Slovenia and namely the regular report in the context of Article IV for consultation mission and the Report on the Financial System Stability Assessment (FSSA), which was made public. The monitoring of the implementation of the Action Plan drawn up on the basis of the findings made by the Mission of the IMF and the World Bank within the framework of the Financial Sector Assessment Program (FSAP) designed to test functioning and robustness of Slovenia's financial system has continued. The Board of Executive Directors of the IMF will assess the regular report on Slovenia under Article IV for consultation under the IMF's Statutes for the year 2002 in the first half of March 2002.

Strengthened relations between the Bank of Slovenia and the European Central Bank

The European Central Bank (ECB) in 2001 strengthened further bilateral and multilateral relations with the central banks of the countries, which are candidates to join the EU. The Bank of Slovenia's working relations intensified in key areas referring to central banking as regards legislation related to the EMU, in the field of statistics and payment systems.

The report drawn up by the ECB on the Status of legal preparation of accession countries in the areas of Community law of concern to the Eurosystem (ECB and NCBs, which have introduced the euro), which was prepared for the first time by the ECB in 2000, was updated. The report analyses the acceptance and implementation of the EU's acquis communautaire and it is mostly concerned with independence of central banks, other legislation concerning the monetary area, as well as legislation governing the banking sector and financial markets. The purpose of the report for the year 2001 was to extend the areas that call for alignment of national legislation of the candidate countries, including collateral, legal aspects and regulation of the settlement systems and insolvency law.

The Bank of Slovenia took part in the Partnership Programme upon the euro cash launch

In 2001, the Bank of Slovenia participated with the ECB in the so-called Partnership Programme tailored to disseminate information and the participation in the preparation for the introduction of euro banknotes and coins in the euro area. The Euro 2002 Information Campaign in Slovenia went on in co-operation with the Bank Association of Slovenia and the Delegation of the European Commission in the Republic of Slovenia.

The chapter on the free movement of capital closed

The Bank of Slovenia continued to actively participate in the review of alignment between Slovenia's legislation and the acquis of the EU, and the realisation of additional negotiating positions for free movement of capital. The number of provisionally closed chapters of the acquis at the end of 2001 increased to twenty-six. Alongside the chapter dealing with the freedom to provide services as well as the economic and monetary union, the chapter on the free movement of capital was closed too. The Bank of Slovenia took part in the compilation of the regular report on the Republic of Slovenia's progress towards accession to the European Union, as well as in defining modifications and amendments to the National Programme of the Republic of Slovenia for the adoption of the acquis by the end of 2002.

The Bank of Slovenia was an active participant in the sub-committee for internal market, which is in its new composition also responsible for financial services and right to establishment, and in the Sub-committee for economic and monetary issues, which in its changed composition deals with the free movement of capital and statistics. In September 2001, an expert group visited Slovenia and assessed whether the existing supervisory structures and systems are sufficient, it examined their activities in Slovenia; hence the peer review also assessed the Bank of Slovenia as far as supervision of banking operations is concerned.

The Bank of Slovenia was a co-host and a co-organiser of the annual meeting of the members of the EABH and the regular annual theme conference with the title "The Role of the 20th Century Banking in Crisis Situations and Restructuring" that took place on 18 and 19 May at the National Museum in Ljubljana. The first part of the Conference addressed Slovenian experiences in relation to the theme followed by speeches given by high-profile academics specialised in the history of economy and banking from Europe and beyond. The Conference attracted approximately 130 participants altogether including speakers from Slovenia.

Paid tribute to the tenth anniversary of monetary independence

On the occasion of another landmark event in 2001, the Bank of Slovenia paid tribute to the tenth anniversary of monetary independence of Slovenia and marked the first decade of its activity. The Governor of the Bank of Slovenia hosted a conference attended by several incumbent and former governors of European central banks and representatives of foreign commercial banks that at the time when Slovenia became a sovereign state assisted the Bank of Slovenia through high-level consultations and expert visits, and arranged the first foreign loan facility for the young state.

Technical cooperation with central banks

In 2001, the Bank of Slovenia was highly involved in central bank technical assistance. A valuable exchange on vital issues with six central banks from the EU Member States highlighted the experiences they had gained in four fields of operations. A priority task for the Bank of Slovenia has been to become familiar with EU directives and to facilitate the transposition of European norms and standards. In turn, the Bank of Slovenia gave above all technical assistance to the central banks of the countries of former SFRY and received nine delegations of those banks within the framework of expert visits. In the absence of training courses in the area of central banking at home, the Bank of Slovenia in 2001 used the training courses provided by the International Monetary Fund, World Bank, Bank for International Settlements, and other institutions and central banks.

6. FINANCIAL STATEMENTS

Statement of responsibilities of the Governing Board

The Law on the Bank of Slovenia (the Bank) and the Statutes of the Bank require the Governing Board to prepare financial statements for each financial year which give a true and fair view of the state of affairs of the Bank and the surplus or deficit of the Bank for that period. In preparing those financial statements the Governing Board is required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state whether applicable accounting standards have been followed; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Bank will continue in business.

The Governing Board has a general responsibility for taking such steps as are reasonably open to it to safeguard the assets of the Bank.

Report of the Auditors

To the Governing Board of the Bank of Slovenia

We have audited the balance sheet of the Bank of Slovenia ("the Bank") as of 31 December 2001 and 2000 and the related statements of income and expenditure, of changes in equity and of cash flows for the years then ended as set out on pages 79 to 97 ("the financial statements"). These financial statements are the responsibility of the Bank's Governing Board. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with International Standards on Auditing as promulgated by the International Federation of Accountants. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements present fairly, in all material respects, the financial position of the Bank as of 31 December 2001 and 2000, and the results of its operations and its cash flows for the years then ended in accordance with International Accounting Standards and Slovenian Law.

PricewaterhouseCoopers AG

A. Schönenberger
Authorised Auditors

K. Morscher

Zürich, 9 April 2002

Statement of income and expenditure

for the year ended 31 December (in millions of tolars)

	Notes	**2001**	2000
Operating income:			
Interest income	4	**44,583**	35,010
Interest expenses	5	**25,529**	18,580
Net interest income		**19,053**	16,430
Net foreign exchange gain/loss		**22,397**	28,642
Gain (loss) from unrealized price revaluation of securities		**3,972**	3,557
Loss from unrealized gold revaluation		**-63**	-
Net investment income		**45,360**	48,630
Fee and commission income		**1,123**	914
Fee and commission expense		**356**	332
Net fee and commission income		**768**	582
Other operating income		**289**	225
Total operating income		**46,417**	49,436
Operating expenses	6	**3,930**	3,685
Provisions and write-offs	7	**7,690**	308
Operating surplus available for appropriation		**34,798**	45,443
Appropriations:			
Transfer to foreign exchange reserves		**22,397**	28,642
Transfer to general reserves - price risks		**3,972**	3,557
Financial results after the appropriation of net foreign exchange gain/loss and gain (loss) from unrealized price revaluation		**8,428**	13,244
Transfer to general reserves - other risks		**6,321**	9,933
Total transfer to reserves	14	**32,691**	42,132
Provision for transfer of surplus to the budget of RS		**2,107**	3,311
Total appropriations		**34,798**	45,443

The notes on pages 83 to 97 form an integral part of the financial statements.

Balance sheet

at 31 December (in millions of tolars)

	Notes	**2001**	2000
Assets			
Financial assets			
Foreign currency assets			
Gold and gold receivables	8	**16,869**	20
Cash and deposits		**492,109**	237,070
Derivative financial instruments	9	**21**	-
Investment securities available for sale	17	**580,193**	475,274
Receivables from the Republic of Slovenia		**8,509**	8,180
International Monetary Fund		**21,479**	19,557
Accrued interest and other assets		**11,978**	8,052
Total		**1,131,158**	748,153
Domestic currency assets			
Receivables from Succession Fund	10	**-**	8,650
Due from banks		**438**	566
Reverse - repo agreements		**-**	6,299
Accrued interest and other assets		**2,290**	926
Total		**2,728**	16,441
Fixed assets	11	**2,608**	2,777
Total assets		**1,136,494**	767,371
Liabilities and reserves			
Serviced liabilities			
Foreign currency liabilities			
Current accounts and deposits to banks		**31,842**	35,997
Derivative financial instruments		**-**	9
Bank of Slovenia bills		**460,837**	361,168
IMF and other international financial organisations		**5**	5
SDR allocation	12	**8,013**	7,534
Accrued interest and other liabilities		**191**	23
Total		**500,889**	404,736
Domestic currency liabilities			
Current accounts and deposits		**85,557**	71,835
Overnight deposits		**35,372**	-
Bank of Slovenia bills		**125,912**	6,946
Republic of Slovenia deposits		**28,837**	3,411
Accrued interest and other liabilities		**6,629**	5,797
Total		**282,308**	87,990
Banknotes in circulation	13	**165,778**	139,644
Provision for transfer of surplus to the budget of RS		**2,107**	3,311
Total liabilities		**951,082**	635,681
Reserves	14	**185,411**	131,691
Total liabilities and reserves		**1,136,494**	767,371

The notes on pages 83 to 97 form an integral part of the financial statements.

Statement of changes in equity

for the year ended 31 December (in millions of tolars)

	General reserve	Foreign exchange reserve	Revaluation reserve	Welfare reserve	Operating surplus/ deficit	Total equity
Balance at 31 December 1999	**6,644**	**81,126**	**1,115**	**616**	**-**	**89,501**
Operating surplus	-	-	-	-	45,443	45,443
FX gains/losses	-	28,642	-	-	-28,642	-
Operating surplus retained in general reserve	13,490	-	-	-	-13,490	-
Contributions to welfare fund	-	-	-	58	-	58
Provisions for transfer to RS	-	-	-	-	-3,311	-3,311
Total movement	13,490	28,642	-	58	-	42,190
Balance at 31 December 2000	**20,134**	**109,768**	**1,115**	**673**	**-**	**131,691**
Balance at 1 January 2001						
- as previously reported	**20,134**	**109,768**	**1,115**	**673**	**-**	**131,691**
Effect of adopting IAS 39	-9	-	-	-	-	-9
Welfare reserve transfer	673	-	-	-673	-	0
- as restated	**20,799**	**109,768**	**1,115**	**-**	**-**	**131,682**
Arising in the period						
Increase by transfer (BIS)	21,039	-	-	-	-	21,039
Operating surplus	-	-	-	-	34,798	34,798
FX gains/losses	-	22,397	-	-	-22,397	-
Operating surplus retained in general reserve	10,293	-	-	-	-10,293	-
Provisions for transfer to RS	-	-	-	-	-2,107	-2,107
Total movement	31,332	22,397	-	0	0	53,729
Balance at 31 December 2001	**52,131**	**132,165**	**1,115**	**0**	**0**	**185,411**

An analysis of the movements in each category within ‘Reserves’ is presented in Note 14.

The notes on pages 83 to 97 form an integral part of the financial statements.

Statement of cash flows

for the year ended 31 December (in millions of tolars)

	Notes	2001	2000
Cash flows from operating activities			
Interest received		**41,534**	34,233
Interest paid		**-25,569**	-17,380
Other		**-169**	-2,008
Net cash flow from operating activities		**15,797**	14,845
Cash flows from investing activities			
Purchase of securities		**-624,042**	-1,160,943
Proceeds from sale of securities		**553,917**	1,148,419
Purchase of time deposits		**-10,114,544**	-7,459,519
Proceeds from redemption of time deposits		**9,854,193**	7,432,675
Loans and reverse repo to domestic banks		**-57,553**	-299,050
Repayment from domestic banks		**63,848**	314,233
Purchase of fixed assets		**-189**	-310
Proceeds from sale of fixed assets		**3**	15
Net cash flow from investing activities		**-324,366**	-24,479
Cash flows from financing activities			
Issue of banknotes in circulation		**26,331**	-2,695
Issue of Bank of Slovenia bills	18	**4,023,304**	2,703,367
Repayment of Bank of Slovenia bills	18	**-3,824,130**	-2,702,549
Republic of Slovenia deposit		**19,896**	-
General reserves increase by transfer		**21,039**	-
Other, net		**-2,744**	-2,016
Net cash flow from financing activities		**263,696**	-3,892
Exchange rate effect		**1,223**	-2,526
Net cash flow from all activities		**-43,650**	-16,052
Cash and cash equivalents at beginning of year		**-91,949**	-75,898
Cash and cash equivalents at end of year	19	**-135,599**	-91,949
Increase (decrease) in cash and cash equivalents		**-43,650**	-16,052

The notes on pages 83 to 97 form an integral part of the financial statements.

These financial statements were approved by the Governing Board on 9 April 2002 and were signed on its behalf by:

Mitja Gaspari
President of the Governing Board and
Governor of the Bank of Slovenia

In accordance with Article 82 of the Law on the Bank of Slovenia these financial statements have still to be approved by the Parliament of the Republic of Slovenia.

Notes to the financial statements

1 Constitution

The Bank of Slovenia (the Bank) is the central bank of the Republic of Slovenia. It was constituted by the Law on the Bank of Slovenia dated June 25, 1991. The Bank is self governing and is an independent institution with its own distinct legal personality. The Republic of Slovenia guarantees the obligations of the Bank which is supervised by Parliament. The Bank shall take care of the stability of domestic currency and of general liquidity of payments within the country and with foreign countries.

2 Accounting standards and conventions

These financial statements have been prepared in accordance with International Accounting Standards (IAS) as promulgated by the International Accounting Standards Committee under the historical cost convention as modified by the revaluation of available for sale securities, financial assets and liabilities held for trading, and all derivative contracts. These were adopted by the Governing Board at the 90th meeting on 9 May 1995.

3 Specific accounting policies

Foreign currencies

Foreign currency financial assets and liabilities have been translated into Tolars (SIT) using the middle exchange rates of the Bank of Slovenia applying at the balance sheet date. Transactions in foreign currencies have been translated into SIT using exchange rates applying on the settlement dates of those transactions.

Income recognition

Interest income is recognised in the statement of income and expenditure as it accrues, other than interest of doubtful collectibility which is credited to a suspense account and excluded from interest income. The closing balance of the suspense account is netted in the balance sheet against accrued interest receivable. Suspended interest is written off when there is no longer any realistic prospect of it being recovered.

Fees and commissions receivable mainly arise from payment and settlement services, supervisory and regulatory functions and the distribution of fiscal stamps on behalf of the state. Fee and commission income is recognised in the statement of income and expenditure as it accrues.

Financial assets and liabilities

All financial assets are initially recognised at cost in the balance sheet on a settlement date basis. The settlement date is the date that an asset is delivered to or by an enterprise. Financial liabilities are recognised in the balance sheet when the Bank becomes a party to the contractual provisions of the instrument.

Financial assets and liabilities are offset and the net amount reported in the balance sheet when there is a legally enforceable right to set off the recognised amounts and there is an intention to settle on a net basis, or realise the asset and settle the liability simultaneously.

Gold and gold receivables

The Bank's gold holdings are valued on the basis of the dollar market price per fine ounce of gold. The revaluation gain or loss due to the price of fine ounce and dollar exchange rate movements is reported in the statement of P&L as gain (loss) from gold valuation. The net amount of unrealised gain is transferred to special sub account of general reserve or releases general reserves according to the governing Board decision.

Investment securities

The Bank invests in marketable securities as a part of its management of international reserves. The Bank doesn't hold trading securities portfolio nor held to maturity securities. All investment securities are classified as available for sale and is carried at market value. When the securities are disposed of, the related accumulate fair value adjustment is included in the income statement gain less losses from investment securities. The effect of securities price changes appears in Statement of income and expenditure under the item Gain (loss) from unrealised price revaluation of investment securities. The net amount of unrealised gain (loss) is transferred to general reserves or releases general reserves according to the Governing Board decision.

Derivative financial instruments

The bank does not use derivative financial instruments except foreign exchange swap arrangements with domestic banks and forwards for purposes of implementing monetary policy and managing loans to banks. Both are recognised on the balance sheet at their fair value. Gains are accrued over the life of the swap and reported in the P&L as swap gains. The market value is derived from the difference between forward price and market price of the underlying item.

Hedging

The Bank has not designated any transactions as hedges during the year.

Reverse – Repurchase Transactions

Securities purchased under agreements are recorded to resell (reverse repos) in the Balance sheet and reported within »Domestic currency assets«. The difference between purchase price and sale price represents interest income. It is accrued over the life of the repo agreement.

Originated loans and provisions for loan impairment

Loans are carried at amortised cost and are recognised when drawn down. When there is evidence that the loans may not be repaid in all amounts due to original contractual terms, a loan provision is established. When a loan is deemed uncollectable, it is written off against the related provision for impairments. The amount of the provision is the difference between the carrying amount and the recoverable amount.

Current accounts and deposits

Borrowings are recognised initially at cost. Subsequently, borrowings are stated at amortised cost.

Bank of Slovenia bills

Bank of Slovenia bills comprises bills in domestic currency and bills in either EUR or USD. Tolars bills are issued with maturities of sixty and two hundred and seventy days. Foreign currency bills are issued with maturities from two to six months. Both kinds of Bank of Slovenia bills are carried at amortized cost.

Fixed assets

Investment properties located in Austria are carried at fair value and are not depreciated. The Bank's policy is to obtain an outside appraisal and revaluation of these properties once every 5 years. The last revaluation was performed in 1999. All other fixed assets are stated at cost and net of depreciation except for land, which is not depreciated. Property revaluations are taken to reserves.

Depreciation is provided on a straight line basis so as to write off the cost of the assets over their estimated useful lives at the following annual percentage rates:

Buildings	1.3 – 1.8 %
Computers	20 – 33 %
Other equipment	10 – 25 %

Gains and losses on disposal of fixed assets are determined as the difference between net disposal proceeds and the carrying amount of the asset and are recognised as income or expense in the statement of income and expenditure.

Banknotes in circulation

Banknotes issued by the Bank represent a charge on the Bank in favour of the holder and are recognised as a liability at face value.

Cash flows

Cash and cash equivalents is defined as net freely transferable cash in convertible currency and demand deposits.

Cash flows from investing activities comprise cash movements in Bank portfolios, arising from the performance of the functions of the central bank. Also included are cash flows arising from movements in IMF Special Drawing Rights and fixed assets. Cash flows from financing activities are those arising from the issue of currency, the issue of Bank of Slovenia bills and movements in Republic of Slovenia deposits. Operating activities include income and expenditure cash flows not included as investing or financing activities.

Cash movements in portfolios have been presented on a gross basis.

Taxation

The Bank is not subject to Slovenian profit taxes.

Appropriations

In accordance with the Law on the Bank of Slovenia, net foreign exchange gains are transferred to foreign exchange reserves. Foreign exchange reserves can only be used for covering the realized foreign exchange loss. According to Governing Board decision net gain (loss) from unrealized price revaluation of marketable securities and gold are transferred to general reserves, as well as the part of surplus that can be used for covering other risks. Any remaining surplus after transfer to the foreign exchange reserves and to the general reserves is appropriated by the Republic of Slovenia. A loss is covered from the Bank's general reserves; if these prove insufficient, the loss shall be covered from the budget of the Republic of Slovenia.

Changes in accounting policies; Implementation of IAS 39

There has been a change in accounting policies since the previous year. In the year 2001 the Bank adopted the IAS 39 Financial Instruments: Recognition and Measurement which is effective for periods on or after 1 January 2001. The financial effects of adopting IAS 39 are reported in the Statement of changes in equity. Due to the adoption of the new revaluation method for securities already in 2000, the effect of implementation IAS 39 is not material.

4 Interest Income

	2001 SIT millions	2000 SIT millions
Interest income from foreign currency		
Income on gold assets	**64**	-
Interest on deposits	**13,036**	9,090
Income on investment securities	**27,337**	23,397
Interest on International Monetary Fund deposits	**597**	827
Total	**41,033**	33,314
Interest income from domestic currency		
Interest on loans to banks	**1,249**	105
Interests from Reverse - repo agreements	**413**	1,473
Swap gains	**1,888**	118
Total	**3,550**	1,696
Total interest income	**44,583**	35,010

Income on investment securities consists of the following:

	2001 SIT millions	2000 SIT millions
Interest income	**26,528**	23,105
Gains less losses from investment securities on sale	**809**	292
Total investment income on marketable securities, net	**27,337**	23,397

5 Interest expenses

	2001 SIT millions	2000 SIT millions
Interest expenses on foreign currency		
Interest on current accounts and deposits	**1,693**	1,389
Interest on Bank of Slovenia bills	**17,818**	14,786
Total	**19,511**	16,175
Interest expenses on domestic currency		
Interest on current accounts and deposits	**701**	659
Interest on overnight deposits	**120**	-
Interest on Republic of Slovenia deposits	**455**	56
Interest on Bank of Slovenia bills	**4,743**	1,690
Total	**6,019**	2,404
Total interest expenses	**25,529**	18,580

6 Operating expenses

	2001 SIT millions	2000 SIT millions
Staff costs	**2,221**	1,958
Administration costs	**1,456**	1,327
Printing and minting costs	**106**	273
Other	**146**	128
Total operating expenses	**3,930**	3,685

The Bank employed 387 employees on 31. December 2001 (2000: 382 employees).

7 Provisions and write-offs

	2001 SIT millions	2000 SIT millions
Receivables from Succession Fund	**8,650**	-
Due to banks	**-1,010**	132
Off balance sheet items	**50**	176
Total provisions	**7,690**	308

8 Gold and gold receivables

	2001 SIT millions	2000 SIT millions
Gold	**174**	20
Gold deposits	**16,694**	-
Total gold and gold receivables	**16,869**	20

9 Derivative financial instruments

Foreign exchange swaps and currency forwards

The Bank entered into certain foreign exchange swap agreements in 2001 and in 2000 which require the Bank to buy EUR for SIT and /or to sell EUR for SIT. The value of derivative instruments and currency forwards are at follows at 31 December:

	2001		2000	
	Fair value	**Notional amount**	Fair value	Notional amount
	SIT millions			
Foreign exchange swaps				
- to be received forward against EUR	**21**	**260,909**	-9	15,461
- to be given forward against EUR	**-**	**-**	0	212
Currency forward				
- to be given forward against EUR	**0**	**3,919**	-	-
Total derivative financial instruments	**21**	**264,828**	-9	15,673

The notional amounts of certain types of financial instruments provide a basis for comparison with instruments recognised on the balance sheet but do not necessarily indicate the amounts of future cash flows involved or the current fair value of the instruments and therefore do not indicate the Bank's exposure to credit or price risks. The derivative instruments become favourable (assets) or unfavourable (liabilities) as a result of fluctuations in market interest rates or foreign exchange rates relative to their terms.

10 Receivables from Succession Fund of the RS

The Succession Fund of the Republic of Slovenia was established in February 1993 (Official Gazette of the Republic of Slovenia 10/93) as an intermediary in the process of the division of assets and liabilities of former Yugoslavia. It assumed, on behalf of the Republic of Slovenia, all the claims on and the obligations to the former National Bank of Yugoslavia which included SIT 8,650 million due to the Bank.

The Agreement on Succession Issues was signed on 25 May 2001 in Vienna. The Article 10 of the Annex C to the Agreement stipulates that none of the successor States will enforce financial claims or start legal proceedings, connected to the introduction of its new currency or re-establishing its monetary independence, against any other successor State. The Governing Board of the Bank of Slovenia has established that the Agreement abolishes the possibilities and expectations that the claim against the Succession Fund would be repaid totally or partially in the future. Because of the expected inability to pay the Bank of Slovenia's claims against the Succession Fund of the Republic of Slovenia in the amount of 8,649,807,115 SIT was written off.

11 Fixed assets

	Land and buildings	Computers & equipment	Total
		SIT millions	
Cost or valuation			
At 1 January 2000	2,641	2,118	4,759
Additions	41	191	232
Disposals	-	-80	-80
At 1 January 2001	2,682	2,229	4,912
Additions	50	140	190
Disposals	-	-73	-73
At 31 December 2001	**2,732**	**2,297**	**5,029**
Depreciation			
At 1 January 2000	556	1,289	1,846
Disposals	-	-70	-70
Charge for the year	20	339	359
At 1 January 2001	576	1,559	2,134
Disposals	-	-68	-68
Charge for the year	20	335	355
At 31 December 2001	**596**	**1,825**	**2,421**
Net book value			
At 31 December 2001	**2,136**	**471**	**2,608**
At 31 December 2000	2,107	671	2,777

Included in land and buildings at 31 December 2001 and 2000 is an amount of SIT 1,115 million relating to investment properties in Austria.

Amounts included in income statement:

	2001 SIT millions	2000 SIT millions
Rental income from investment properties	**177**	164
Direct operating expenses	**135**	130
Total income from investment properties	**42**	33

12 SDR allocation

	2001 SIT millions	2000 SIT millions
SDR allocation	**8,013**	7,534
Total SDR allocation	**8,013**	7,534

The SDR allocation liability carried an interest rate of 2.23% at 31 December 2001 (2000: 4.34%). Interest paid by the Bank is recharged directly to the Republic of Slovenia, thereby giving a nil effective interest rate.
Receivables from the Republic of Slovenia have a carrying value equal to principal and are mostly funded by Special Drawing Rights allocations. Interest borne on the funding is recharged directly to the Republic.

13 Banknotes in circulation

Value of banknotes in circulation by denomination:

		2001 SIT millions	2000 SIT millions
SIT	10	**269**	276
SIT	20	**395**	350
SIT	50	**542**	516
SIT	100	**1,401**	1,369
SIT	200	**1,411**	1,267
SIT	500	**2,001**	1,862
SIT	1,000	**12,137**	12,542
SIT	5,000	**60,197**	49,629
SIT	10,000	**87,019**	71,426
Total		**165,372**	139,238
Tolar coupons		**406**	406
Total		**165,778**	139,644

14 Reserves

	2001 SIT millions	2000 SIT millions
Balance at 1 January	**131,691**	89,501
Adoption of IAS 39 at 1 January 2001	**-9**	-
Abolition of welfare fund	**-673**	-
Increase of general reserve	**673**	-
New balance at 1 January	**131,682**	89,501
Increase of general reserve - BIS	**21,039**	-
Transfer to foreign exchange reserve	**22,397**	28,642
Transfer to general reserve - price risk	**3,972**	3,557
Transfer to general reserve - other risk	**6,321**	9,933
Contributions to the welfare fund	**-**	58
Balance at 31 December	**185,411**	131,691
Represented by		
Foreign exchange reserve	**132,165**	109,768
General reserve - price risk	**7,537**	3,574
General reserve - other risk	**44,594**	16,561
Investment properties revaluation	**1,115**	1,115
Welfare fund	**-**	673
Total reserves	**185,411**	131,691

The general reserve has been established in recognition of the price, economic and other risks inherent in the discharge of the Bank's responsibilities, and its portfolio of financial assets. Reserves for price risks are only available to offset the deficit arising from the unrealized loss from securities revaluation.

The foreign exchange reserve relates to cumulative net foreign exchange gains which by law are only available to offset any future net foreign exchange losses and are not distributable.

The welfare fund had been established to provide recreational and other facilities for the staff of the Bank. The assets representing the fund were included in the Bank's balance sheet and any movement in asset values was taken directly to reserves. The Governing Board decided that, as at 1. January 2001, the fund is transferred to general reserves and proceeds and expenses are incorporated in the profit and loss account due to the essence and unsignificance of the business.

In the year 1996, the Act on the Bank of Slovenia Membership in the Bank for International Settlements came into force. By that Act, the Republic of Slovenia permitted membership of Bank of Slovenia in BIS. Five years later, in the year 2001, an agreement between successor states regarding proportional shares was reached and the Republic transferred the proportional share of capital and of the other bank balances of the former National Bank of Yugoslavia in the BIS to Bank of Slovenia. The Republic of Slovenia's participation of 16.39% of the former NBY assets in BIS amounts to 82 million USD. Transferred assets that were booked on Bank of Slovenia account, per BIS assembly date 13. June 2001, consisted of gold (SIT 16.9 billion), deposits (SIT 1.1 billion) and BIS shares (SIT 2.9 billion).

15 Commitments and off balance sheet instruments

Letters of Credit

The aggregate amounts of outstanding letters of credit at the year end were:

	2001 SIT millions	2000 SIT millions
Foreign currency letters of credit	**13**	12

Foreign exchange swaps and currency forwards

The Bank entered into certain foreign exchange swap agreements and currency forwards in 2001 and in 2000 which require the Bank to buy EUR for SIT and to sell EUR for SIT. The notional amounts of these instruments are shown in Note 9.

Litigation and other provisions

There are certain legal claims pending or threatened involving the Bank, which have not yet been settled. The claims relate mainly to disputes about wages in the early 1990's. The Governing Board believes that sufficient provision has been made in the accounts for any expected loss from future settlement. Detailed information in accordance with IAS 37 "Provisions, Contingent Liabilities and Contingent Assets" has not been given as this is considered by Governing Board to be prejudicial to the Bank of Slovenia's position in these cases.

16 Fair value of financial assets and liabilities

The following table summarises carrying amounts and fair values of those financial assets and liabilities not presented on Bank of Slovenia balance sheet at their fair value. The estimated fair values of fixed interest bearing deposits and of Bank of Slovenia bills are based on discounted cash flows using prevailing money market interest rates for debts with similar credit risk and remaining maturity.

	Carrying value		**Fair value**	
	2001	2000	**2001**	2000
	SIT millions	SIT millions	**SIT millions**	SIT millions
Assets				
Cash and deposits	**492,109**	237,070	**492,673**	232,234
Due to the banks	**438**	567	**453**	568
Reverse repo agreements	**-**	6,299	**-**	6,309
Liabilities				
Bank of Slovenia bills in foreign currency	**460,837**	361,168	**460,817**	361,168
Bank of Slovenia bills in domestic currency	**125,912**	6,946	**126,355**	6,941

The fair values of deposits approximate their carrying amounts as they are payable on demand or of very short maturity.

Due to the specific role of IMF holdings and the SDR allocation, fair values of both do not differ from their carrying amounts.

The fair value of currency in circulation is considered to be its face value.

17 Risk Management

Credit Risk

All marketable securities are interest bearing bonds. All marketable securities and deposits are held with foreign banks.

All foreign banks in which the Bank places funds have a credit rating of at least AA- as graded by Fitch. The maximum credit risk exposure at 31 December 2001 in the event other parties fail to perform their obligations is the amount recorded in the financial statements as financial assets. Sovereign issuers' exposure consists of OECD countries, the Republic of Slovenia and the Succession Fund of the Republic of Slovenia (year 2000). The Governing Board believes that there is no significant concentration of credit risk.

Concentrations of securities by currency and type of counterparty are as follows at 31 December 2001:

	EUR	USD	Other	Total
		%		
Sovereign bonds	**49.70**	**15.27**	**0.44**	**65.40**
Supranational securities	**1.27**	**6.01**	**0.65**	**7.93**
Foreign banks securities	**20.50**	**4.02**	**2.14**	**26.66**
December 31, 2001	**71.47**	**25.30**	**3.23**	**100.00**
Sovereign bonds	12.72	17.72	1.53	31.98
Supranational securities	1.65	4.72	0.48	6.85
Foreign banks securities	53.77	5.24	2.16	61.17
December 31, 2000	68.14	27.68	4.17	100.00

Interest rate risk

Average effective interest rates:

	2001				2000
	Repricing Period				
	3 month or less	**3 month to 1 year**	**Over 1 year**	**Total**	Total
			%		
Assets					
Foreign currency assets					
Gold and gold receivables	**0.53**	**0.66**	**-**	**0.62**	-
Cash and deposits	**3.29**	**-**	**-**	**3.29**	5.09
Derivative financial instruments	**0.50**	**-**	**-**	**0.50**	-
Investment securities available for sale	**3.86**	**3.85**	**4.27**	**4.16**	5.23
International Monetary Fund	**1.96**	**-**	**-**	**1.96**	3.88
Domestic currency assets					
Due from banks	**11.35**	**11.33**	**11.00**	**11.28**	9.80
Reverse - repo agreements	**-**	**-**	**-**	**-**	10.63
Liabilities					
Foreign currency liabilities					
Current accounts and deposits	**1.99**	**-**	**-**	**1.99**	5.15
Derivative financial instruments	**-**	**-**	**-**	**-**	5.00
Bank of Slovenia bills	**3.27**	**2.95**	**-**	**3.24**	5.00
Domestic currency liabilities					
Current accounts and deposits	**0.92**	**-**	**-**	**0.92**	0.96
Overnight deposits	**3.92**	**-**	**-**	**3.92**	-
Bank of Slovenia bills	**8.07**	**11.36**	**-**	**9.04**	9.10
Republic of Slovenia deposits	**5.20**	**-**	**-**	**5.20**	1.00

The effective interest rates shown represent average interest at the end of the reporting period.

Interest sensitivity of assets and liabilities

	2001			
	Repricing period			
	3 months or less	3 months to 1 year	Over 1 year	Total
	SIT millions			
Assets				
Foreign currency assets				
Gold and gold receivables	16,869	-	-	**16,869**
Cash and deposits	492,109	-	-	**492,109**
Derivative financial instruments	21	-	-	**21**
Investment securities available for sale	30,574	119,343	430,277	**580,193**
Receivables from the RS	496		8,013	**8,509**
International Monetary Fund	21,479			**21,479**
Domestic currency assets				
Due from banks	212	152	75	**438**
Total assets	**561,759**	**119,494**	**438,365**	**1,119,618**
Liabilities				
Foreign currency liabilities				
Current accounts and deposits	31,842	-	-	**31,842**
Bank of Slovenia bills	412,845	47,992	-	**460,837**
IMF and other IFO	-	-	5	**5**
SDR allocation	-	-	8,013	**8,013**
Domestic currency liabilities				
Current accounts and deposits	85,557	-	-	**85,557**
Overnight deposits	35,372	-	-	**35,372**
Bank of Slovenia bills	88,652	37,260	-	**125,912**
Republic of Slovenia deposits	28,837	-	-	**28,837**
Total liabilities	**683,106**	**85,252**	**8,018**	**776,377**
Net interest sensitivity gap	**-121,347**	**34,242**	**430,347**	**343,241**
December 31, 2000				
Total assets	503,882	40,591	211,123	755,596
Total liabilities	434,758	52,134	5	486,897
Net interest sensitivity gap	69,124	-11,543	211,118	268,699

Currency risk

The nature and manner in which the Bank conducts its operations, principally in relation to monetary policy management and foreign currency reserve management, give rise to currency concentrations in the financial assets. This primarily arises from country and counterparty concentration of exposures.

Basic guidelines for the management of the Bank's international reserves are set by the Governing Board of the Bank and revised on a quarterly basis; the guidelines prescribe the currency structure, average term of deposits and of investments in foreign securities, as well as selection of foreign banks.

These concentrations of risk by currency and type of counterparty are as follows at 31 December 2001:

	SIT	EUR	USD	Other	Total
			SIT millions		
Assets					
Foreign currency assets					
Gold and gold receivables	-	-	-	16,869	**16,869**
Cash and deposits	-	451,417	40,029	663	**492,109**
Derivative financial instruments	-	21	-	-	**21**
Investment securities available for sale	-	414,660	146,780	18,753	**580,193**
Receivables from the RS	-	-	-	8,509	**8,509**
International Monetary Fund	-	-	-	21,479	**21,479**
Accrued interest and other assets	-	6,214	2,139	3,625	**11,978**
Domestic currency assets	2,728	-	-	-	**2,728**
Total assets	**2,728**	**872,312**	**188,948**	**69,898**	**1,133,886**
Liabilities					
Foreign currency liabilities					
Current accounts and deposits	-	7,708	23,941	193	**31,842**
Bank of Slovenia bills	-	413,208	47,629	-	**460,837**
IMF and other IFO	-	-	-	5	**5**
SDR allocation	-	-	-	8,013	**8,013**
Accrued interest and other liabilities		172	-	18	**191**
Domestic currency liabilities	282,308	-	-	-	**282,308**
Total liabilities	**282,308**	**421,089**	**71,571**	**8,229**	**783,197**
Net balance sheet position	**-279,580**	**451,223**	**117,378**	**61,669**	**350,689**
Off balance sheet net position	**3,912**	**-260,909**	**-**	**-**	**-256,997**
December 31, 2000					
Total assets	16,441	540,511	157,791	49,852	764,594
Total liabilities	87,990	346,008	51,017	7,710	492,725
Net balance sheet position	-71,549	194,502	106,774	42,142	271,869
Off balance sheet net position	212	-15,461	-	-	-15,249

Maturities of assets and liabilities

	Remaining period to the contractual maturity date			
	3 months or less	**3 months to 1 year**	**Over 1 year**	**2001 Total**
	SIT millions			
Assets				
Foreign currency assets				
Gold and gold receivables	-	-	16,869	**16,869**
Cash and deposits	492,109	-	-	**492,109**
Derivative financial instruments	21	-	-	**21**
Investment securities available for sale	30,574	119,343	430,277	**580,193**
Receivables from the RS	338	158	8,013	**8,509**
International Monetary Fund	1,261	-	20,217	**21,479**
Accrued interest and other assets	6,176	2,644	3,158	**11,978**
Domestic currency assets				
Due from banks	212	152	75	**438**
Accrued interest and other assets	2,009	24	257	**2,290**
Total assets	**532,700**	**122,320**	**478,866**	**1,133,886**
Liabilities				
Foreign currency liabilities				
Current accounts and deposits	31,842	-	-	**31,842**
Bank of Slovenia bills	412,845	47,992	-	**460,837**
IMF and other IFO	-	-	5	**5**
SDR allocation	-	-	8,013	**8,013**
Accrued interest and other liabilities	191	-	-	**191**
Domestic currency liabilities				
Current accounts and deposits	85,557	-	-	**85,557**
Overnight deposits	35,372	-	-	**35,372**
Bank of Slovenia bills	88,652	37,260	-	**125,912**
Republic of Slovenia deposits	28,837	-	-	**28,837**
Accrued interest and other liabilities	1,699	702	4,229	**6,629**
Total liabilities	**684,995**	**85,955**	**12,247**	**783,197**
December 31, 2000				
Total assets	292,889	95,725	375,980	764,594
Total liabilities	428,439	52,525	11,761	492,725

Liquidity risk is the risk that a company will face inability in raising funds at short notice to meet its immediate liabilities associated with financial instruments. Liquidity risk is also the risk of selling a financial asset quickly at significantly lower value than its fair value.

The matching and controlled mismatching of the maturities is a key criterion in determining and managing the Bank's foreign currency assets and liabilities. This is reflected in appropriate maturities of foreign assets additionally taking into account potential needs for intervention. The Bank has set controls that encounter different liquidity ratios for different instruments. These limits as well as currency and credit risk exposures are monitored daily. Additionally, the Bank has standby credit facility arrangements.

One of the Bank's primary task is to takes care of the stability of domestic currency and to ensure liquidity of payments within the country. The nature of these activities are such that the Bank is not subject to the liquidity constraints that impact on other entities.

18 Supplemental cash flow information: cash flows from Bank of Slovenia bills

	2001 SIT millions	2000 SIT millions
Source		
Foreign currency bills	**80,343**	22,004
Tolar bills	**118,832**	-
Total	**199,174**	22,004
Disbursements		
Tolar bills	**-**	-21,186
Total	**-**	-21,186
Total net source	**199,174**	818

19 Supplemental cash flow information: cash and cash equivalents

	2001 SIT millions	2000 SIT millions
Foreign currency assets		
Cash	**3,136**	1,238
Total assets	**3,136**	1,238
Foreign currency liabilities		
Demand deposits	**-8,864**	-17,941
Domestic currency liabilities		
Commercial banks demand deposits	**-78,594**	-66,801
Overnight deposits	**-35,372**	-
Non-bank deposits	**-15,905**	-8,445
Total liabilities	**-138,735**	-93,187
Cash and cash equivalents	**-135,599**	-91,949

Foreign currency cash assets include IMF balances of SIT 1,261 million (2000: SIT 838 million) and do not include time deposits of SIT 474,537 million (2000: SIT 223,835 million) or other assets of SIT 15,697 million (2000: SIT 12,955 million).

Foreign currency demand deposits do not include restricted deposits of SIT 22,978 million (2000: SIT 18,056 million).

Domestic currency liabilities include Republic of Slovenia deposits of SIT 8,942 million (2000: SIT 3,412 million).

7. APPENDICES

7.1. Statutory basis and tasks of the Bank of Slovenia

The Constitution of the Republic of Slovenia gives the Bank of Slovenia independence and makes it directly accountable to the National Assembly…

The Bank of Slovenia was established on 25 June 1991 as Slovenia's central bank. under the Bank of Slovenia Act derived from the Basic Constitutional Charter on Independence of the Republic of Slovenia. With effect from 8 October 1991 when Slovenia's legal tender - the tolar - was introduced the Bank of Slovenia discharges all functions as the monetary authority.

Article 152 of the Constitution of the Republic of Slovenia gives the Bank of Slovenia independence and makes it directly accountable to the National Assembly.

The Bank of Slovenia Act 1991 establishes two bodies of the Bank of Slovenia: the Governing Board of the Bank of Slovenia and the Governor of the Bank. The Governing Board of the Bank of Slovenia is composed of eleven members: Governor as President of the Governing Board, Deputy Governor, three Vice Governors and six non-executive members appointed from the ranks of experts of recognised professional experience. Governor and the six non-executive members are appointed by the National Assembly on a proposal made by President of the Republic of Slovenia. The Deputy Governor and the three Vice Governors are appointed by the National Assembly on a proposal made by Governor. All members of the Governing Board are appointed for a six-year term. The Governing Board acts by a two-third majority.

… and responsible for securing stability of the national currency and general liquidity in domestic and cross-border payments.

Among the operational responsibilities conferred upon the Bank of Slovenia by law, are activities conducted primarily with a view to securing stability of the national currency and general liquidity in domestic and cross-border payments. The Bank's tasks in relation to its functions and responsibilities comprise the following:

- Regulates the quantity of money in circulation,
- Ensures general liquidity of banks and savings banks and of cross-border payments,
- Supervises banks and savings banks,
- Issues banknotes and procures banknotes and coins for circulation,
- Prescribes reporting requirements necessary for discharging its functions,
- Prescribes rules for implementation of the deposit guarantee scheme for retail deposits, and
- Provides banking services to the Government of the Republic of Slovenia.

In addition, the Bank of Slovenia also performs other tasks and carries out activities in accordance with the provisions of the Banking Act, Foreign Exchange Act and the Securities Market Act.

The Bank of Slovenia has operational independence to define and implement monetary policy and to discharge other tasks and powers conferred upon it by law. The Governing Board and the Governor of the Bank of Slovenia report to the National Assembly. The Bank of Slovenia submits reports on its activities to the National Assembly, including its financial plan and annual statement of accounts.

Access of government to loans from the Bank of Slovenia is restricted by law to short-term loans up to the ceiling of 5.0 per cent of the budget and one fifth of the budget deficit projection.

7.2. Profit and loss account and balance sheet

Profit and loss account data for five years

From 1 January to 31 December (in millions of tolars)

	1997	1998	1999	2000	2001
			SIT millions		
Operating income:					
Interest income	19,475	29,188	29,724	35,010	44,583
Interest expenses	17,727	24,701	16,885	18,580	25,529
Net interest income	**1,749**	**4,487**	**12,839**	**16,430**	**19,053**
Net foreign exchange gain/loss	16,797	-4,753	38,399	28,642	22,397
Gain (loss) from unrealized price revaluation of securities	-	-	-8,292	3,557	3,972
Loss from unrealized gold revaluation	-	-	-	-	-63
Net investment income	**18,546**	**-266**	**42,946**	**48,630**	**45,360**
Fee and commission income	192	1,054	699	914	1,123
Fee and commission expense	676	286	408	332	356
Net fee and commission income	**-485**	**768**	**291**	**582**	**768**
Other operating income	190	245	253	225	289
Total operating income	**18,251**	**747**	**43,490**	**49,436**	**46,417**
Operating expenses	2,670	2,923	3,298	3,685	3,930
Provisions and write-offs	718	312	-	308	7,690
Operating surplus available for appropriation	**14,862**	**-2,489**	**40,192**	**45,443**	**34,798**
Appropriations:					
Transfer to foreign exchange reserves	16,797	-4,753	38,399	28,642	22,397
Transfer to general reserves - price risks	-	-	-	3,557	3,972
Financial results after the appropriation of net foreign exchange gain/loss and gain (loss) from unrealized price revaluation	-1,935	2,264	1,793	13,244	8,428
Transfer to general reserves - other risks	-1,935	1,457	1,554	9,933	6,321
Total transfer to reserves	14,862	-3,297	39,952	42,132	32,691
Provision for transfer of surplus to the budget of RS	-	807	240	3,311	2,107
Total appropriations	**14,862**	**-2,489**	**40,192**	**45,443**	**34,798**

Balance sheet data for five years

As at 31 December (in millions of tolars)

	1997	1998	1999	2000	2001
	SIT millions				
Assets					
Financial assets					
Foreign currency assets	**574,280**	**600,916**	**640,950**	**748,154**	**1,131,158**
Gold and gold receivables	16	15	18	20	16,869
Cash and deposits	374,860	260,545	181,102	237,070	492,109
Derivative financial instruments	-	-	-	-	21
Investment securities available for sale	182,213	314,660	423,983	475,274	580,193
Receivables from the Republic of Slovenia	6,483	6,781	7,260	8,180	8,509
International Monetary Fund	2,951	10,582	21,490	19,557	21,479
Accrued interest and other assets	7,757	8,333	7,097	8,052	11,978
Domestic currency assets	**19,161**	**13,124**	**31,456**	**16,441**	**2,728**
Receivables from Succession Fund	8,650	8,650	8,650	8,650	-
Due from banks	4,962	697	3,630	566	438
Reverse - repo agreements	5,178	3,454	18,550	6,299	-
Accrued interest and other assets	370	323	626	926	2,290
Fixed assets	2,072	2,372	2,914	2,777	2,608
Total assets	**595,512**	**616,412**	**675,320**	**767,372**	**1,136,494**
Liabilities and reserves					
Serviced liabilities					
Foreign currency liabilities	**310,442**	**307,081**	**343,047**	**404,736**	**500,889**
Current accounts and deposits to banks	12,694	16,356	23,990	35,997	31,842
Derivative financial instruments	-	-	-	9	-
Bank of Slovenia bills	291,863	284,865	312,009	361,168	460,837
IMF and other international financial organisations	40	59	58	5	5
SDR allocation	5,805	5,772	6,868	7,534	8,013
Accrued interest and other liabilities	40	29	122	23	191
Domestic currency liabilities	**147,292**	**154,982**	**100,058**	**87,990**	**282,308**
Current accounts and deposits	57,259	66,515	65,167	71,835	85,557
Overnight deposits	-	-	-	-	35,372
Bank of Slovenia bills	75,674	79,904	27,101	6,946	125,912
Republic of Slovenia deposits	11,279	2,317	2,303	3,411	28,837
Accrued interest and other liabilities	3,081	6,246	5,487	5,797	6,629
Banknotes in circulation	85,653	104,667	142,489	139,644	165,778
Provision for transfer of surplus to the budget of RS	-	807	240	3,311	2,107
Total liabilities	**543,386**	**567,538**	**585,833**	**635,681**	**951,082**
Reserves	52,126	48,874	89,484	131,691	185,411
Total liabilities and reserves	**595,512**	**616,412**	**675,318**	**767,372**	**1,136,494**

7.3. Important measures taken in 2001

7.3.1. Monetary and exchange rate policy measures

January	**Outright sale of foreign exchange to contracting banks** Between 30 January and 5 February, the Bank of Slovenia was selling foreign exchange to banks as an outright transaction. The foreign exchange derived from the repurchase arrangement under which the banks had sold them to the Bank of Slovenia during that period under the bid for temporary sale of foreign exchange for 7 days.
February	**Tolar bills** The Bank of Slovenia suspended on 16 February the Decree on the Issue of 270-day Tolar Bills at Nominal Interest Rate. **Foreign currency bills** The Bank of Slovenia revoked the option of the subscription for bills in euros and US dollars with maturity of 180, 270 and 360 days.
March	**Liquidity loan of last resort** With effect from 5 March, in addition to banks, savings banks authorised to carry out banking operations under the Banking Act are also eligible to make drawings under the liquidity loan of last resort. **Bank of Slovenia interest rates** As of 12 March, the Bank of Slovenia increased interest rates on certain monetary policy instruments: 2-day tolar bills from 5 % to 6.5 %, 12-day from 7 % to 8.5, 60-day from 10 % to 11 %, minimum bid rate on 7-day and 2-month repo of bills denominated in foreign currency went up from 10.5 % to 11 % and the interest rate on a lending facility granted against pledging 12-day tolar bills rose from 10% to 11 %.
April	**Discount and Lombard rates of the Bank of Slovenia** As of 1 April, the discount rate was increased from 10 % to 11 % prompting the rise of the Lombard rate from 11 % to 12 %. **Temporary purchase/sale of foreign exchange** With effect from 26 April, banks sell foreign exchange to the Bank of Slovenia or buy foreign exchange from it temporarily for 7 days up to the amount of matched foreign exchange position.
May	**Lombard loan** The Bank of Slovenia shortened the maturity of the Lombard loan to one day (previously 5 business days) and extended the time for unwinding the facility until 03:00 p.m. (previously until 01:00 p.m.), and changed the method for setting interest rates, so as to make them less directly dependent on the discount rate of the Bank of Slovenia. **Time deposits of the Ministry of Finance on the basis of the sale of one-month Treasury bills** On 9 May, the Ministry of Finance sold at auction the first issue of one-month Treasury bills and on the following day made a deposit with the Bank of Slovenia in the entire amount of sale proceeds (2.0 billion tolars). In accordance with the agreement concluded with the Bank of Slovenia, the Ministry of Finance may, after the expiration of a two-month transitional period, use the proceeds obtained by selling one-month Treasury bills to finance budgetary expenditures or place them as deposits with the Bank of Slovenia.
June	**Tolar bills** On 14 June, the Bank of Slovenia re-launched the offer to banks and savings banks to subscribe 270-day tolar bills on the basis of an open tender. The interest rate was set at 11.5 %.

Overnight deposits With effect from 2 July, the Bank of Slovenia makes available overnight deposit to banks and savings banks. The interest rate was set at 5.5 %. Overnight deposit replaced the 2-day tolar bills, which were withdrawn with effect from 30 June 2001. **One-month Treasury deposits** As of 10 July, a two-month transition period ended during which the Ministry of Finance in accordance with the agreement on joint intervention in the money market could not use the sale proceeds from the issue of the one-month Treasury bills to balance budget liquidity.	**July**
Temporary purchase/sale of foreign exchange As of 5 September, the provision saying that the banks with short/long open foreign exchange position are not eligible to sell to the Bank of Slovenia/ purchase from it foreign exchange under this instrument, was cancelled. **Intervention in the foreign exchange market** Due to stagnating market exchange rates in the second half of August, the Bank of Slovenia intervened on 13 September in the foreign exchange market by setting the base rate and the highest spread between buying and selling rate. The period of intervention continued into the following year.	**September**
Temporary purchase/sale of foreign exchange With effect from 25 October, the Annex to the Agreement on Co-operation between Banks and the Bank of Slovenia in interventions in the foreign exchange market signed with 20 banks came into force. In accordance with the Agreement, the price for temporary purchase, that is sale of foreign exchange for a 7-day period changed to 4.5 %, and 2.5 %. The interest rate on refinancing operations with the Bank of Slovenia was specified (8.25 %) and the interest rate on investments with the Bank of Slovenia (6.25 %). At the same time, the bids for temporary purchase and sale of foreign exchange with maturity of two weeks were suspended. **Overnight deposit** As of 29 October, the interest rate on overnight deposit was reduced from 5.5 % to 4.5 %.	**October**
Tolar bills As of 2 November, the interest rate on 60-day tolar bills was reduced from 11 % to 9 %. **Tolar bills** As of 22 November, the first auction of 270-day tolar bills took place. At the same time, the open tender for tolar bills with the same maturity was wound up. **Two-month forward purchase of foreign exchange** With effect from 22 November, two-month forward purchase of foreign exchange from participating banks was launched with the aim to generate signals as to the desired growth of the exchange rate (set in accordance with the growth of base exchange rate).	**November**
Overnight deposits As of 3 December, the interest rate on overnight deposit was reduced to 4 %. **Tolar bills** As of 3 December, interest rate on 60-day tolar bills was reduced to 8.5 %, on 21 December to 8.0 %. As of 20 December, 12-day tolar bills were discontinued, and consequently as of 31 December a 3-day liquidity facility available to banks against pledging these bills was suspended. **Repo of foreign currency bills** For both 7-day and 60-day repo of foreign currency bills the minimum bid interest rate was reduced from 11% to 9.5% with effect from 21 December.	**December**

7.3.2 Supervisory measures

Februar	Decree on Modifications to the Decree on the Conditions to Be Met by Credit Intermediaries
March	Decree on Capital Adequacy of Banks and Savings Banks Decree on Annual Fee and Lump-Sum Charges for Prudential Supervision and Duties for Deciding on Applications for Issuing Authorisations
May	Decree on Modification to the Decree on Granting Special Liquidity Loans in Co-operation with Banks
June	Decree on Tolar Maturity Ladder
July	Act on Modifications and Amendments to the Banking Act Decree on Guarantee Scheme for Investors' Claims with Stock-broking Companies Instructions for Reporting on Largest Depositors Instructions for Completing the Report on Tolar Liquidity Flows in Banks Instructions for Drawing Up the Report on Liquidity Ratios of Tolar Maturity Ladder Decree on Tolar Maturity Ladder of Savings Banks
September	Decree on Modification to the Decree on Compliance of Savings and Loan Undertakings with the Provisions of the Banking Act Decree on Modifications and Amendments to the Decree on Compliance of Savings and Loan Undertakings with the Provisions of the Banking Act Decree on Modifications and Amendments to the Decree on Annual Fee and Lump-Sum Charges for Prudential Supervision and Duties for Deciding on Applications for Issuing Authorisations Decree on Modifications and Amendments to the Decree on Large Exposure of Banks and Savings Banks Decree on Modifications and Amendments to the Decree on Detailed Contents of Reports under Article 127 of the Banking Act Decree on Modification of the Decree on the Detailed Method for the Calculation of Liabilities, Assets and Holdings for the Purpose of Determining Net Indebtedness Decree on Modifications and Amendments to the Decree on Tariffs for Charging Payments for Services Provided by the Bank of Slovenia
October	Decree on Detailed Contents of Documentation to be Enclosed to the Application for Issuing Authorisation for Discharging the Function of Member of the Management Board, and Bankruptcy Administrator of a Bank and a Savings Bank Decree on Amendment to the Decree on the documentation serving as a basis of assessment of a foreign bank's branch capacity to perform the services which are the subject of the foreign bank's application for authorisation to establish a branch Decree on Amendment to the Decree on the laying down of the terms and conditions to be complied with by a bank and/or a savings bank in order to perform banking and/or other financial services and on the laying down of documentation on the basis of which it may be determined whether the company will be able to carry out the activities which are the subject of the application for authorisation

Decree on Daily Planning of Tolar Liquidity and Monitoring of Depositor Concentration Decree on Modification to the Decree on Capital Adequacy of Banks and Savings Banks Decree on the Narrowest Liquidity Range which the Bank Shall Have to Ensure	**October**
Instructions for the Implementation of the Decree on the Narrowest Liquidity Range which the Bank Shall Have to Give Assurance of Decree on Modifications and Amendments to the Decree on Compliance of Savings and Loan Undertakings with the Provisions of the Banking Act Decree on Modifications to the Decree on Tolar Maturity Ladder of Savings Banks Instructions for Drawing Up the Report on Liquidity Ratios of Tolar Maturity Ladder of Savings Banks	**November**
Instructions for Completing the Report on Tolar Liquidity Flows in Banks Decree on Modification to the Decree on the Classification of On-Balance Sheet Assets and Off-Balance Sheet Items of Banks and Savings Banks Decree on Modifications and Amendments to the Decree on Modifications to the Decree on Capital Adequacy of Banks and Savings Banks Decree on Modification to the Decree on the Narrowest Liquidity Range which the Bank Shall Have to Give Assurance of	**December**

7.4. Governance and organisation chart

7.4.1. Changes to the composition of the Governing Board of the Bank of Slovenia in 2001

As of 1 April 2001, Mitja Gaspari was appointed Governor of the Bank of Slovenia by the National Assembly of the Republic of Slovenia for a six-year term. Mr. Gaspari replaced Dr. France Arhar who had served as Governor from 1 April 1991.

7.4.2 Members of the Governing Board of the Bank of Slovenia as at 31 December 2001

President of the Governing Board of the Bank of Slovenia

Mitja Gaspari
(Governor)

Members of the Governing Board of the Bank of Slovenia

Samo Nučič
(Deputy Governor)

Darko Bohnec
(Vice Governor)

Janez Košak, M.Sc.
(Vice Governor)

Andrej Rant
(Vice Governor)

Tatjana Fink
(Trimo, Trebnje)

Bine Kordež, M.Sc.
(Merkur, Kranj)

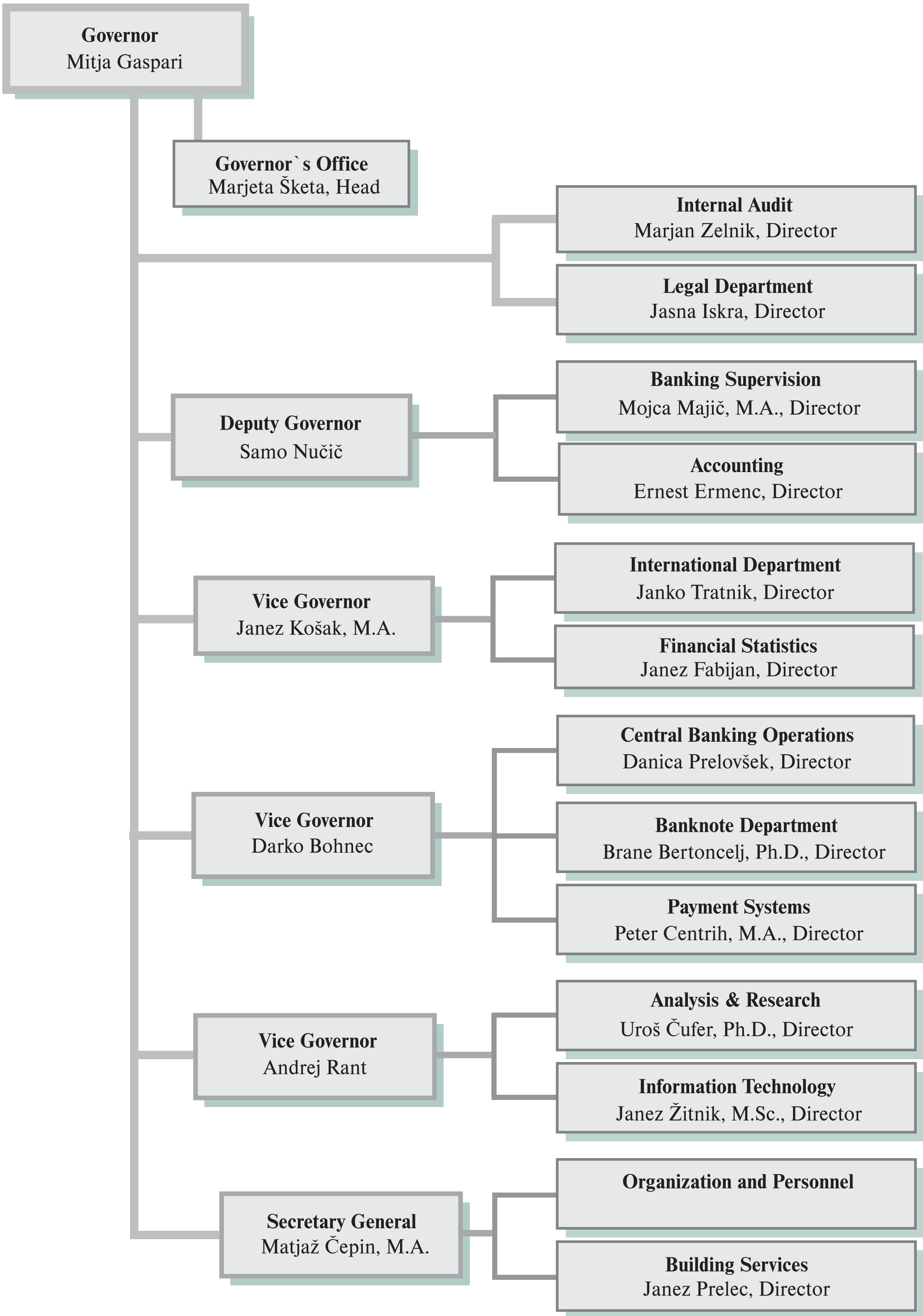
Vladimir Lavrač, M.Sc.
(Institute of Economic Research, Ljubljana)

Leon Repovž, Ph.D.
(Faculty of Business Administration and Economics, Maribor)

Ivan Ribnikar, Ph.D.
(Faculty of Economics, Ljubljana)

Dušan Zbašnik, Ph.D.
(Faculty of Business Administration and Economics, Maribor)

7.4.3. Organisation chart of the Bank of Slovenia as at 31 December 2001



7.5. Publikacije in spletna stran

Title and description	Contents
Monthly Bulletin · monthly · Slovene · English translation	Macroeconomic statistical data focused on monetary statistics, exchange rates and cross-border economic relations. A review of current trends in figures; notes on methodology; an overview of banks operating in Slovenia, a data release calendar.
Annual Report · annual (spring) · Slovene · English translation	The report presented the Bank of Slovenia to the National Assembly of the Republic of Slovenia An outline of economic developments, monetary policy, operations of banks and the Bank of Slovenia, as well as other tasks and activities carried on by the Bank of Slovenia.
Report on Supervision of Banking Operations · annual (autumn) · English translation	The report presented to the Banking Supervision Department to the National Assembly of the Republic of Slovenia on banks' operating results, developments related to the legal framework for supervision and surveillance of banking operations, and supervision of banks and savings banks.
Direct Investment · annual · bilingual issue in Slovene and English	A statistical survey of inward and outward direct and portfolio investments (year-end stock).
Presentations and Analyses · quarterly · Slovene	Speeches given by the Governor of the Bank of Slovenia before the National Assembly of the Republic of Slovenia, analytical and methodological surveys concerning monetary, balance of payments and related areas.
Financial Markets · quarterly · Slovene	Statistical survey of non-monetary financial intermediaries, securities market and interest rates.
Monetary Survey · monthly · Slovene	Current analytical macroeconomic survey of monetary and balance of payments movements.
Outlook	The publication is dedicated to predictions of macroeconomic developments and projections of fundamental macroeconomic indicators for Slovenia for the forthcoming two-year period.
Working papers of Analysis & Research Department	The papers published in this collection address all areas of professional and working interest of the central bank. The content of papers varies from general to in-depth analytical studies.
Website · table of contents for pages in Slovene http://www.bsi.si/html/... ...kazalo.html · table of contents for pages in English http://www.bsi.si/html/... ...eng/index.html	Homepage of the Bank of Slovenia presenting the institutions, Slovenia's banknotes and coins, laws and regulations related to the central bank's area of work, and other useful information. Up-to-the-minute data on exchange and interest rates, and securities issued by the Bank of Slovenia, as well as the landmark publications in electronic form.

7.6. Glossary of selected terms

Base interest rate (TOM) – Officially determined indexation rate for assets and liabilities calculated as the average monthly inflation rate (with effect from January 1998, the retail price index was replaced by the consumer price index) for the last month or for the last few months (currently for 12 months).

Base money – Cash in circulation, banks' reserves and book money (deposits repayable on demand) with the Bank of Slovenia.

Bills denominated in foreign currency (foreign currency bills) – Short-term securities of the Bank of Slovenia subscribed for and redeemed in foreign currency.

Capital – the sum of core capital and supplementary capital I referred to in point 4.1 of the Decision on Capital Adequacy of Banks and Savings Banks (Official Gazette of the Republic of Slovenia, Nos. 16/01, 82/01 and 103/01) less deductible items referred to in point 5 of the Decision on Capital Adequacy of Banks and Savings Banks (Official Gazette of the Republic of Slovenia, Nos.16/01, 82/01 and 103/01). The banks obliged to comply with capital requirements for foreign exchange and market risks may add to the sum also the amount of used eligible supplementary capital II referred to in point 4.2 of the Decision on Capital Adequacy of Banks and Savings Banks (Official Gazette of the Republic of Slovenia, Nos. 16/01, 82/01and 103/01).

Capital adequacy ratio – The ratio between the bank's capital and risk-weighted assets plus other risk-adjusted items

Classification of assets – Banks and savings banks classify assets (claims) in five groups on a scale from A (best) to E (worst) based on assessment and evaluation of the ability of the borrower (counterparty) to meet obligations (repay the debt) at maturity.

Group A comprises: claims on the Bank of Slovenia and the Republic of Slovenia; claims on borrowers where the possibility of loss if a borrower failed to honour their commitment to repay contractual obligations is unlikely, and who meet their commitment to repay contractual obligations on due dates, i.e. exceptionally within 15 days after due date; claims collateralised with first-class security within the meaning of Clause 8 of the relative Decision.

Group B comprises: claims on borrowers who are expected to maintain cash flow still sufficient to enable timely settlement of obligations on due dates, but whose financial standing is currently weak and does not show signs indicating substantial deterioration in future; borrowers who repeatedly meet their obligations with up to a 30-day delay, occasionally also with a delay between 31 and 90 days.

Group C comprises: claims on borrowers who are expected to have cash flow insufficient to meet their obligations at maturity; borrowers who are significantly undercapitalised; borrowers who do not have sufficient long-term sources of financing long-term investments; borrowers who fail to provide to the bank current and satisfactory information or appropriate documentation in relation to claims (receivables), collateral and sources of repayment; borrowers who repeatedly meet their obligations with a delay between 31 and 90 days, occasionally also with a delay between 91 and 180 days.

Group D comprises: claims on borrowers where the possibility of loss is high; borrowers are faced with problems of liquidity and insolvency; a motion to commence proceedings against borrowers has been lodged with a competent court, *viz.* compulsory settlement or bankruptcy; borrowers who are in the process of rehabilitation, i.e. compulsory settlement; borrowers in bankruptcy; borrowers who repeatedly meet their obligations with a delay between 91 and 180 days, occasionally also with a delay between 181 and 365 days, but it is justified to expect that the claim will be partly met.

Group E comprises: claims on borrowers who are not expected to meet their obligation to repay the debt; claims founded on a disputable legal basis.

Connected client (special relationship with a bank) – An entity that in the relationship with the bank is a directly or indirectly the parent undertaking, i.e. an entity that the bank controls directly or indirectly or a relationship with an entity, which is directly or indirectly controlled by the same entity that controls the bank.

- **Financial institutions –** In terms of the official division in sectors based on the ESA95, the financial institutions sector is divided in five sub-sectors: the central bank, other monetary financial institutions, other financial intermediaries except insurance undertakings and pension funds, auxiliary financial institutions and
- insurance undertakings and pension funds. **Monetary financial institutions** include: the central bank and other monetary financial institutions, which carry out financial intermediation. **Non-monetary financial institutions** comprise other financial intermediaries except insurance undertakings and pension funds, auxiliary financial institutions, and insurance undertakings and pension funds.

Foreign exchange minimum – The minimum amount of assets denominated in foreign currency held by banks.

Interest (nominal) spread – The difference between the average nominal interest rate the bank earns on its assets and average nominal interest rate the bank pays on its liabilities of the same maturity.

Large exposure – The bank's exposure to a counterparty, which amounts to or exceeds 10 % of the bank's capital (own funds).

Mandatory reserve – The prescribed amount of assets commonly computed as a percentage of banks' deposits and other liabilities that banks are obliged to keep on their settlement accounts or a special mandatory reserve accounts with the Bank of Slovenia as well as cash balances.

Money market – The interbank financial market where prime (gilt-edged) short-term securities are traded.

Monetary aggregates (M1, M2 and M3) – Monetary aggregates with differentiated liquidity grade. **M1** is the highest liquidity grade and comprises banknotes and coins in circulation and deposits with domestic banks and the Bank of Slovenia repayable on demand and denominated in tolars. **M2** is composed of M1 and savings and time deposits with domestic banks and the Bank of Slovenia. **M3** comprises M2 and retail deposits denominated in foreign currency with banks; as from September 1999, M3 also includes deposits with domestic banks from all non-monetary sectors denominated in foreign currency.

Monetary sector – The sector composed of the Bank of Slovenia and commercial banks. The savings banks and savings and loan undertakings whose combined share is less than 2% of aggregate total assets of monetary financial institutions (as defined by the ECB) shall not be deemed to form part of the monetary sector. Such treatment is in conformity with the regulations of the ECB, which provide for non-inclusion of small-scale institutions of up to 5% of aggregate total assets of national monetary financial institutions.

Monetisation – The transformation of assets purchased by the central bank and commercial banks into money. Banks purchase (financial) assets, i.e. claims or grant loans from newly generated or issued money.

(Net) interest margin – The ratio between net interest income (the difference between real and revaluation interest income and expense) and average gross interest-earning assets.

Net provisions – The difference between assets (claims) written-off and value adjustment of bad and doubtful assets (claims), expense for provisions and income from recovered debts, as well as income from released provisions and value adjustments in profit and loss statement.

Nominal interest rate – Overall interest rate composed of the indexation part being a compensation to the creditor or s depositor for inflation and the real part.

Other assets – Investments in capital of related (dependent) and unrelated (independent) undertakings, tangible fixed assets, intangible long-term assets, subscribed but not fully paid capital and redeemed own shares, prepayments and accrued income, and other assets, such as cheques, interest receivable, fees and commissions, etc.

Other liabilities – Accrued expenses and deferred income, long-term and general provisions and other liabilities.

Open foreign exchange position (open position in foreign currency) – The balance between on-balance sheet asset items over liability items of a bank denominated in foreign currency.

Operating expenses – The sum of general administrative expenses (staff costs and other administrative costs), depreciation and taxes.

Provisions – General provisions against potential future losses and specific provisions against potential losses arising from on- and off-balance sheet items and country risk.

Repo (repurchase operation)– the arrangement to sell (or purchase) of an asset (securities) whereby the seller has a right and an obligation to repurchase (or sell)it at a specific price on a future date or on demand. Under the repo transactions concluded between the Bank of Slovenia and banks, the ownership of the securities is retained by the seller and the buyer puts a lien on them.

Revaluation interest – A part of agreed interest on tolar-denominated loans granted by banks and tolar deposits placed with banks, meant to compensate the creditor or the depositor for inflation.

Secondary liquidity – The amount of the bills of the Bank of Slovenia in domestic and foreign currency, and bills and bonds of the Republic of Slovenia (investments in securities of the Bank of Slovenia and the Republic of Slovenia in domestic and in foreign currency, bills the Bank of Slovenia and RS, short-term bonds RS).

Sterilisation – By definition, it is the sale of short-term government securities by the central bank for the purpose of offsetting the impact of the purchase of foreign exchange on the quantity of base money. In Slovenia, sterilisation means selling the Bank of Slovenia bills denominated in foreign currency by the Bank and selling the bills denominated in tolars by the Bank of Slovenia to neutralise the impact that such purchases of foreign exchange have on the quantity of base money.

Swap – the arrangement to purchase (or sell) a currency whereby the buyer has a right and an obligation to sell (or purchase) it on a future date. Under this type of transaction foreign exchange shall be transferred from the sellers to the buyer's account.

Total assets – The amount of all asset or liability balance sheet items (of a bank).

Tolar bills (TBZ) – Short-term debt securities issued by the Bank of Slovenia denominated in tolars.