BANKA SLOVENIJE

ANNUAL REPORT

YEAR 2000

BANKA SLOVENIJE
BANK OF SLOVENIA

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Mr. President, Honourable Members of Parliament,

The Governing Board of the Bank of Slovenia adopted at its 223rd session held on 27 March 2001 the report for the year 2000 and financial statements audited by PriceWaterhouseCoopers, Chartered Accountants and Registered Auditors from Zurich.

Allow me to point at keynote developments and trends, which have come to the fore over the past year setting the background of the monetary and exchange rate policies defined and implemented by the Bank of Slovenia.

The rise in inflation from the record-low 4.3 per cent in the middle of 1999 may be attributed to two reasons. The first one was the introduction of the value-added tax that pushed prices up but had a short-lasting effect, and the second one was the oil price hike. Between February and October last year, oil prices growth rate persisted in the 40 per cent bracket at annual level. Thus the effects of the introduction of the value added tax – only the direct ones – stoked up inflation in 1999 to between 2.5 and 3 percentage points, and the same percentage in direct effects only was added by the run-up in world oil prices in 2000.

Looking ahead, we may expect the delayed impact of last year's rising economic costs on the rate of inflation over the next few months. On the other hand, the risk of tipping the scales of inflation upward may be offset by the beneficial effect of competitive business climate and other/market mechanisms, which have already sent the Slovenian inflation rate down to just above 4 per cent. All bets would be off, if the past inflation were to feed through to wage gains and other income and expenditure. The current economic trends and conditions arising from the proposal of the budget for the year 2001 should make us all beware of inflationary pressures, which under the circumstances have fair chances to gain momentum during the year.

Encouraged as we may be by the performance of the Slovenian economy, there is a dampening effect of new real imbalances. In the dry language of figures, public deficit is still under control, but the evolving trends are becoming increasingly unfavourable. The reasons for difficulties associated with public finance could not be described as one-off or ad-hoc plights. After all, the analyses of the structure of the underlying reasons stoke for this trend have already been made and the course has been chartered. As long as the structural changes are not made, the exercise repeated every year of "closing" the Government budget and other expenditures of the Treasury will be increasingly tedious and futile process. At the same time, by postponing reforms, we leave in place the factor that contributes significantly to instability in the long run, which in turn will affect the process of confidence- building at home and abroad.

In an environment where the general government deficit exerts a direct pressure on the subjects of the economic policy, Slovenia's external deficit may seem a more distant threat. The truth is that a balanced budget is just one aspect of the aggregate balance of a country's economy posted as the balance on the current account. External deficit is the aggregate indicator of economic stability or instability.

Among the principal reasons for Slovenia's external deficit, there are many acting as triggers for growth in general government deficit. Among them is growth in government expenditure for wages, pensions and other transfers that exceeds the amount of collected taxes, i.e. the decline in disposable taxpayers income; or the volume in growth of government and other investments carried for statistical purposes outside general government since they are not funded by taxes but by borrowing. In some instances, the problems are substituted. Thus at the end of the day, high growth in wages paid by the private sector and high final consumption have the beneficial *impact on public finance, since it means rising substantially the tax base. On the other hand, it also bolsters rise in external deficit. In 1999, the wage and consumption hike proved highly beneficial for public finance and damaging for the balance of payments, as opposed to 2000 when the effect was the other way round.*

The processes where growth in consumption outpaces growth in domestic product feed on the rising accessibility of cross-border sources of financing based on further liberalisation of capital movements and competitiveness of financial intermediaries. In 2000, new net foreign loans and advances to the corporate sector accounted once more for around 80 per cent compared to financing extended by domestic banks. Even the domestic bank looked for refinancing across the border and borrowed from foreign credit institutions over 40 per cent of funds passed on as new loans and advances to corporate customers.

No doubt that cross-border sources of financing constitute a reliable and valuable supplement to domestic savings, though on the other hand they also poise as a factor contributing to instability, since they offer the possibility for consumption independently from product created, income and savings. And since we have entered a period in which the course forward means further opening of the financial market and entries of new foreign banks in the banking industry, these movements are to gain momentum and step up pace of autonomous behaviour of consumption and imports eventually resulting in soaring external deficit.

Since 1993, Slovenia's annual GDP growth has averaged 4.5 per cent, rising by around 2 percentage points annually above the economic growth in the European Union whose business cycles have a strong impact on developments in Slovenia. Over the past two years, the rates of GDP and income growth have already been coupled with rising instability. In conclusion, consumption has been rising even faster. How broad national economic imbalances can we afford without jeopardising further growth and development is hard to tell. After all, the criteria in this area are changing due to the globalisation process. Adverse movements and a loss of confidence on similar markets may be significant motives to persuade foreign investors to withdraw from the Slovenian market. There would be some serious problems also in the case of speculative interventions on the money market, primarily by deploying short-term capital that basically follows fluctuations in inflation and interest rates.

Economists generally agree that expansion policies designed to create and increase government deficit with the aim to shore up or even boost economic growth is outdated. Over the past decade featuring high growth rates in many parts of the world, the four-per-cent deficit the USA sported in 1990 has been transformed to over one-per-cent surplus in 2000. During the same period, the deficit posted in the eurozone countries has decreased from four per cent to one per cent of GDP. We have in both cases a huge closed market boasting high purchasing power and low foreign-trade ratio, with a credible currency and a tradition in price and financial stability. In short, we are referring to two economic environments Slovenia cannot match.

The causes for such turnarounds have been of cyclical nature but only up to a point. In other words, they have been linked to automatic fiscal improvements in the economic trends, since during that period the deficit of the industrialised countries adjusted for cyclical changes has decreased on average by around 3 percentage points of GDP. Discretionary decisions of the economic policy standard-setters have been in the background of such developments. They have been taken due to strategic reasons, even though to lower a fiscal deficit is not more straightforward in those countries than it is in Slovenia. Past experiences, as well as longer transitional periods clearly indicate that in a long run, there is a tangible positive correlation between low budget deficit and high-flying economic performance. Any beneficial effects of an expansion economic policy would be short-lived.

What has already been said in respect of the general government deficit, largely applies to the aggregate national economic, i.e. external deficit. As a rule, in the "developing economies" where the national economic policy is generally structured around the aim to catch up with the leading countries, economic growth containing external deficit, that is growth as a result of deficit, is not regarded as a functioning model of economic development. A positive development policy is founded as it was the case in the past, and even more so at present, on economic and technological restructuring of the private sector towards international integration and exports efficiency. Economic growth fuelled by a rise in domestic consumption and consequently accompanied by external deficit is not sustainable over a long term.

The Bank of Slovenia has pursued a monetary policy designed to keep at bay impacts of both foreign and domestic developments and thus safeguard domestic prices from excessive volatility. At the same time, the Bank has sought to do so at costs that would be the least possible burden on the national economy. A myriad of data contained in this Annual Report demonstrate that growth in base money stock, as well as in transaction money, has been very modest in comparison with real GDP growth and inflation, as well as in relation to the previous year. In other words, within the limits of the resources it had at its disposal, the Bank has made efforts to limit the use of instruments of financial repression on the domestic market to the minimum. At the same time the Governing Board of the Bank of Slovenia has made a judgement to adjust the monetary policy instruments to reflect the recent market changes and to fine-tune them to the monetary policy instruments deployed by the European Central Bank (ECB), which means that in practice, the interventions of the central bank on the markets will be more straightforward and transparent.

The opening in the field of financial services to the world and further deregulation on the domestic market will undoubtedly act as a positive stimulus to step up activities not only in the financial, but also in the real sector. We are also aware that these processes will have a direct bearing on exposure to risk. Therefore, the task to ensure national economic balance is going to be more demanding than it has been so far, even though the level of instability reached at present is all but insignificant. Efforts should focus on the systemic stability, and should be the bottom line of all economic policies, the entire community, and individuals.

Not merely the act of joining the European Union, but the convertible domestic currency for the capital account and freedom of shareholders and in the first place of the owners of monetary assets are the corner stones – another commitment to prudent behaviour in the real economy in line with the behaviour prevailing on the EU market where most Slovenian companies earn their bread and butter. Should we fail to embrace such thinking and such behaviour in particular over the forthcoming decade, the circumstances may deteriorate rather quickly widening the gap between the goals we have jointly set and our day-to-day situation.

I have the privilege to submit to you Mr. President and to the honourable Members of Parliament the Annual Report of the Bank of Slovenia for the year 2000, and I use this occasion to thank you for your contribution during the last year and throughout the past ten years. Your confidence, support and understanding for the work of the Bank of Slovenia have provided a valuable input to cementing the stability and to the rising credibility our state enjoys at home and abroad. We are convinced that it has been also thanks to mutual trust we have been able to do our respective roles in meeting our responsibilities, and trust is priceless when it comes to money matter. Likewise, fear and distrust may cost dearly. Both arise from our experience; hence the responsibility for the future rests with all of us and in the new conditions, it is even larger.

I am very grateful to all members of the Governing Board of the Bank of Slovenia for their dedication and commitment indispensable in our joint efforts to define the monetary policy and monitor its implementation.

My thanks also go to all the staff of the Bank of Slovenia in different working areas for their contribution to providing the Bank with the economic indispensable for defining and implementing the monetary policy measures and for high quality supervision and surveillance of those economic sectors whose oversight falls within the scope of responsibility of the Bank of Slovenia. We have sought – and I am positive it will also the case in the future – to meet best practice in matters of curbing inflation and creating confidence in the domestic currency and its stability. A relentless focus on the tolar needs to remain unshaken and it is up to all of us to safeguard its value, not only at home but also abroad.

Ljubljana, 27 March 2001

Dr. France Arhar
Governor

1. ECONOMIC ENVIRONMENT

1.1. International economic developments

The main feature of 2000 was a buoyant global economy activity accompanied by rising inflation in a number of countries. A hike in inflation rates was generally fuelled by changes in the world price of oil, which also affected overall conditions of trade, and sent import prices soaring as opposed to shrinking prices exported commodities fetched in cross-border markets.

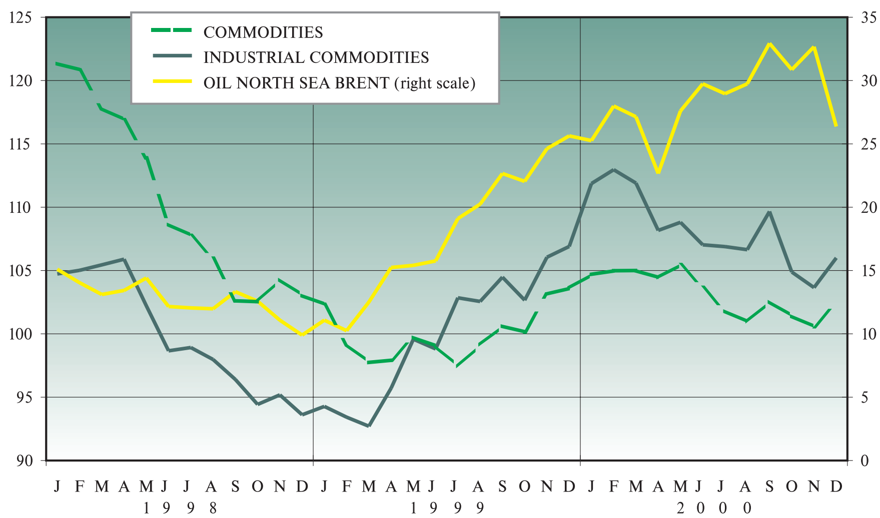
Record high economic growth in the last decade

The estimates made by the International Monetary Fund (IMF) in respect of global economic growth posted in 2000 put the figure at 4.7 per cent – a record high in the last decade. More vigorous growth in economic activity was achieved in the first half of year, followed by a slowdown in the second half of the year in most countries. The European Union notched 3.3 per cent growth, while the United States with 5.0 per cent growth, remained in the driver's seat for the fourth consequtive year with more than 4.0 per cent economic growth, staying ahead of the European Union since 1992. The lowest economic growth last year was posted by Japan - around 2 per cent – where the burnt of the crisis is still widely felt.

Revived growth enjoyed by main trading partners

During the past year, Germany and Italy being Slovenia's largest treading partners from the EU Member States posted economic growth below average. Nevertheless,. with growth of 3.1 per cent Germany almost doubled the 1999 figure of 1.6 per cent, and Italy did the same with 2.9 per cent growth in 2000 agaist 1.4 per cent in 1999. After a plunge to -0.4 per cent in 1999, Croatia's gross domestic product was on the road to recovery last year when its growth was estimated at 3.4 per cent. The economies CEFTA countries grew in 2000 at a rate of approximately one percentage point year-on-year. The most impressive rebound was achieved by the Czech Republic although the result was a meagre 2.7 per cent growth rate, with Slovakia trailing behind with 2.1 per cent. Last year's economic growth managed by Russia was estimated to be 7.0 per cent, and was mainly driven by a rise in the price of oil.

Figure 1: **Commodity** (1999=100) **and oil prices** (North Sea Brent in US$ per barrel) **in international markets** (1998- 2000)



Source: The Economist, London; OPEC Bulletin, Vienna.

High growth in international trade

Such vigorous economic activity was also accompanied by growth in international trade. According to the OECD figures, growth in global trade in 2000 was 13.3 per cent, or twice more than in the preceding year. Imports of goods of eight largest Slovenia's trading partners excluding Croatia increased by 11.4 per cent in real terms during 2000 (the rise in the case of Germany was 12.6 per cent). Foreign demand kept impetus during the first half of 2000, but then started to lose breath in the second half of the year.

60 per cent growth in oil prices ...

... has been pushing prices up around the globe.

The price of crude oil that took an unward turn in the beginning of 1999 continued to grow throughout 2000. Only in April and December the price of oil declined substantially. Thus in 2000, the price of North Sea Brent averaged 28.5 US dollars per barrel or a stunning 60 per cent more than a year earlier. Growth in oil prices fuelled growth in import prices of countries, which rely on the import of oil and ignited a rise in consumer prices, as well as producer prices. In turn, inflation rose year-on-year. In eleven EU Member States participating in the monetary union, consumer prices increased by 2.6 per cent in 2000 (compared to a 1.7 per cent rise a year earlier). In addition to the rising prices of oil, marked depreciation of the euro was another component of inflation pressures. During 2000, consumer prices in the United States grew by 3.4 per cent compared to 2.7 per cent in 1999. Consumer prices rose soared in CEFTA countries by about 10 per cent or by a slightly lower percentage with the expception of the Czech Republic where the rise was 3.9 per cent.

The value of euro against US$ in 2000 down by 13 per cent

During 2000, the euro continued to lose value against the US dollar and averaged 0.924 US dollars compared to 1999 when the euro was worth 1.067 US dollars. Thus the euro depreciation against the US dollar spanning the year 2000 was a hefty 13 per cent.

During the year under review, prices of other commodities were not so volatile as the price of crude oil. Compared to 1999, prices quoted in US dollars increased by 3.2 per cent on average during 2000, with prices of industrial goods going up by 8.2 per cent, and prices of foodstuffs decreasing by just below one per cent.

5.1 per cent deterioration in Slovenia's foreign trade

Slovenia's trade performance deteriorated in 2000 by 5.1 per cent in relation to 0.4 per cent in 1999. Consequently, the current account balance of payments dipped by around 2.5 per cent of GDP mostly driven by a rise in the price of oil and rather massive changes in exchange rates. Depreciation of the euro against the US dollar is to blame for adverse developments in 2000. Compared to the average figure for year 1999, Slovenian export prices quoted in US dollars decreased by 8.1 per cent, while import prices in US dollars dropped by 3.2 per cent.

ECB and Federal Reserve aim to curb inflation by interest-rate policy measures

The main feature of interest rates in international money markets during 2000 was the upward trend, which came to a halt during the run-up to the year's end. Thus the LIBOR interest rate on deposits denominated in US dollars with a three-month maturity period averaged 6.53 per cent in 2000 compared to 6.55 per cent in December. The interest rate on euro-denominated deposits with the same maturity period averaged 4.39 per cent compared to 4.94 per cent in December. In line with its primary objective to maintain price stability over a medium term, the European Central Bank (ECB) increased key interest rates six times last year adding up to a rise of 1.75 percentage points. At the end of 2000, the refinancing interest rate arrived at 4.75 per cent. The rise in key interest rates determined by the Federal Reserves (Fed Funds) was more modest and amounted to a hike of one percentage point. By subscribing to such interest-rate policy, the central bank of the United States was trying to relieve inflationary pressures threatening to overheat the domestic economy by exploding growth in domestic demand.

1.2. Gross domestic product, employment and labour costs

Relatively high economic growth in Slovenia ...

Slovenia's economic growth in 2000 was rather high for the second year in a row. In the wake of a 5.2 per cent rise in the national economic activity in 1999, GDP grew by 4.8 per cent in real terms last year. With a 9.8 per cent rise in value added, the catering sector posted the strongest growth followed by the manufacturing sector (9.2 per cent) and the financial intermediation (5.9 per cent). These developments may be regarded as more favourable as a measure of stability and sustainability of growth than in 1999 when the construction sector surged by 15.8 per cent, trade by 6.3 per cent, while real estate, leases and business services went up by 4.7 per cent. Slovenia's economic growth cooled down after the exploding domestic demand that peaked in summer 1999 and in 2000 was again driven by foreign demand. Even the figures illustrating the rise in components of GDP expenditure indicate a marked slowdown in growth of domestic consumption as opposed to exports whose share of contribution to the vigorous national economic activity was the most significant. A breakdown of domestic spending shows that government spending growth rate outpaced other items, leaving investments and household expenditures behind. By cutting back on the current account deficit, the difference between domestic savings and gross investments has narrowed as well.

... influenced by external demand.

Table 1: **Selected economic indicators**

	1994	1995	1996	1997	1998	1999	2000
Real growth of gross domestic product [1] in %	5.3	4.1	3.5	4.6	3.8	5.2	4.8
Gross domestic product in millions of US$	14,386	18,744	18,878	18,208	19,585	20,071	18,167
Gross domestic product per capita in US$	7,233	9,431	9,481	9,163	9,878	10,078	9,128
Structure of Gross domestic product in % of GDP							
Agriculture, forestry and fishing	4.0	3.9	3.8	3.7	3.6	3.2	2.9
Industry and construction	34.4	32.7	32.6	32.9	33.1	31.6	33.1
- Manufacturing industry	26.2	24.6	24.1	24.3	24.1	23.4	24.3
Services	47.1	48.2	48.6	49.5	49.1	51.4	49.5
Total value added	85.5	84.8	85.0	86.1	85.8	86.2	85.5
Compensation of employees	58.0	57.2	54.8	53.6	52.3	51.8	52.2
Taxes on production and imports, minus subsidies	14.2	14.9	15.3	14.9	15.4	16.1	16.1
Gross operating surplus and mixed income	27.8	27.9	29.9	31.5	32.4	32.0	31.7
- Exports of goods and services	60.0	55.2	55.8	57.4	56.6	52.8	59.0
- Imports of goods and services	57.8	57.2	56.8	58.3	58.2	56.9	62.5
Net exports	2.2	-2.0	-1.0	-0.8	-1.5	-4.4	-3.5
Private final consumption	56.7	58.5	57.5	56.4	55.7	55.7	54.8
Government consumption	20.2	20.1	20.1	20.4	20.3	20.2	20.8
Gross investment	20.9	23.3	23.4	24.1	25.6	28.4	28.0
Active population [2] in thousands	936	952	942	978	978	959	963
Employed and self-employed	851	882	875	906	901	885	894
Unemployed	85	70	69	72	77	73	69
Unemployment rate (% of unemployed in active population)	9.1	7.4	7.3	7.4	7.9	7.6	7.2
Real growth of gross wage per employee in %	3.6	5.1	5.1	2.4	1.6	3.2	1.6
Labour productivity growth in %	5.0	3.3	4.4	5.1	3.8	4.2	3.5

1 Since 1995 in constant prices of 1995; previously in constant prices of 1992.
2 Internationally comparable figures under the ILO methodology.
Source: Statistical Office of the Republic of Slovenia and the Institute for Macroeconomic Analysis and Development of the Republic of Slovenia

Encouraged by a high rise in added value generated by manufacturing industries, the vigorous growth enjoyed by industrial production triggered in the middle of 1999 by strong foreign demand also continued throughout 2000. The physical volume of industrial production in manufacturing industries increased by 7.0 per cent in 2000 compared to a year earlier, whereas the aggregate industrial output jumped by 6.2 per cent. During the year under review, the strongest rise in the production volume was posted by consumer goods (6.8 per cent) and the lowest growth was achieved by the manufacturers of capital investment goods (3.5 per cent) with inventories accounting for a 6.5 per cent rise.

Strong growth in industrial output

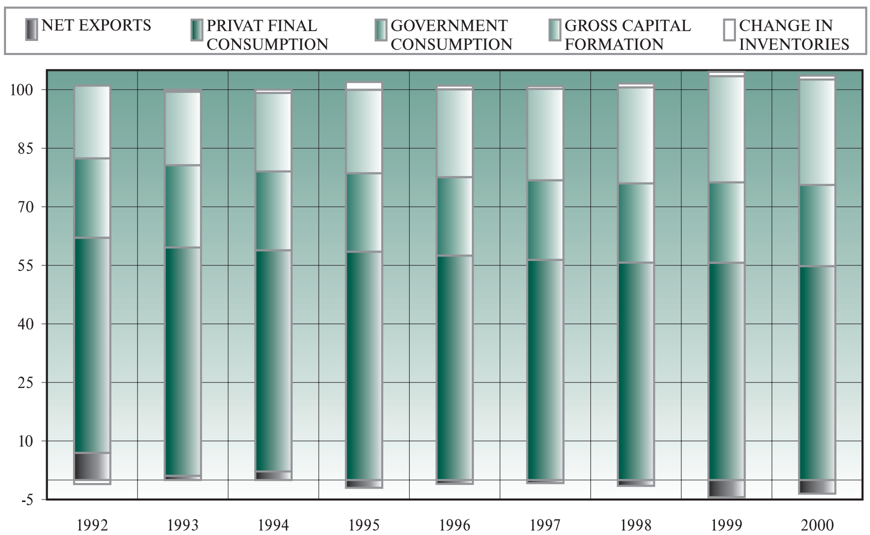
Wages and salaries grew in real terms

Wages and salaries rose below the planned figure for 2000 posted at 2.5 per cent growth in real terms. The annual rate of growth in gross wages and salaries averaged 10.6 per cent for 2000 translating into a 1.6 per cent rise in real terms. The growth in wages and salaries in the trade sector lagged behind productivity growth by 5.5 percentage points in real terms based on the twelve-month average data. After a decline posted for a couple of years, the share of compensation of employees in GDP stopped slipping due to a relatively high nominal growth in wages and owing to the differences between the implicit GDP deflator and the consumer price index. Hence the share of wages and salaries accounted for 52.2 per cent of GDP in 2000 as opposed to 51.8 per cent in 1999. Due to sluggish domestic demand, the cost structure GDP was affected by declining shares of taxes levied on goods and services and import levies, resulting in a decreased share of taxes on production and imports (from 18.3 per cent of GDP in 1999 to 18.0 per cent of GDP in 2000). The share of gross surplus generated by operating activities fell in respect of the preceding year (32.0 per cent of GDP), also due to the falling share of subsidies landing at 31.7 per cent of GDP (estimate).

Encouraging signs in employment trends

A rise in the number of employed people witnessed in 1999 (partly due to methodological changes in counting the persons employed in public works) also persisted in 2000. The number of employed people increased by 1.2 per cent in 2000 on average with the growth rate in the number of jobs in the retail private sector (3.0 per cent) clearly heading the scoreboard followed by jobs created in enterprises and institutions (1.3 per cent). The number of unemployed persons fell in 2000 by 10.4 per cent below the 1999 level, and the rate of unemployment was 12.0 per cent in

Figure 2: **GDP structure** (1992-2000)



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

December (in December 1999: 13.0 per cent). Despite the upturn in the manufacturing industries, the number of employees dropped by 0.3 per cent during the year under review, whereas the number of jobs jumped by a 3.7 per cent in the trade sector and by 3.4 per cent in the construction and financial intermediation sector.

The number of vacancies was rather different from one sector of the processing industries to the other. While there were considerable job cuts in vehicle and boat production, textile and leather-processing industries, new jobs were opened in the metallurgy, as well as in the electrical and optical equipment industries. The number of jobs in services rose by 2.7 per cent and stayed ahead of employment growth in industry where it was negative (-0.9 per cent). As regards regional patterns of unemployment, there were no major changes in 2000 with the highest number of registered jobless people in Podravska, Pomurska, Savinjska and Posavska regions. On the other hand, unemployment dropped considerably in the northern Primorska region.

Unemployment sliding the second year in a row

According to official estimates, the count of internationally comparable active population increased last year by four thousand persons, while the number of the unemployed decreased by exactly the same number of persons. Thus the unemployment rate fell for the second consecutive year after a hike in 1998 (7.9 per cent) and averaged 7.2 per cent for the year 2000. In the critical groups of unemployed people are still in the first place those who have been out of work for longer periods of time, the young (first-time seekers of employment), people over 40 years of age, workers with low a level of education or few skills. In 2000, the issues in relation to employment conditions including the black labour market moonlighting and employment and work of foreigners were addressed under the Aliens' Employment and Work Act and the Labour Act, as well as through amendments to the Labour Inspection Act. Moreover, Slovenia started in 2000 with the implementation of the National Employment Action Plan drawn up along the

Novelties in labour law and employment policy

Box 1: **Wage adjustment in 2000 and 2001**

In accordance with the agreement concluded by social partners relating to the wage policy for the period 1999-2001, base wages were adjusted in January 2000 (a rise of 2.4 per cent) and in August (a rise of 3.7 per cent) as a result of the growth in consumer prices, which in July exceeded the 4 per cent threshold and reached 4.3 per cent.

Wages were due for another round of adjustment of 4.5 per cent in January 2001, i.e. for the entire rate of growth in consumer prices above 5 per cent (3.9 per cent) in 2000, as well as for the 85 per cent difference between 4.3 and 5 per cent rise in prices, i.e. by 0.6 per cent. If public sector wages had grown in 2001 in line with the endorsed obligations (ratios going up in public administrations, research, health sector and health care) it would have meant a whopping 4 per cent rise in real terms (whereby the private sector have grown by 3 and the public sector by 7 per cent), so the trade unions for the public sector and the Government adopted at the end of year annexes to the effective agreement of the policy of wages in 2001. Under the new provisions, base wages were to increase as of 1 January 2001 by 3,6 per cent in the public sector, and in the private sector by the unamended 4.5 per cent of base wages following a faillure of the negotiators to reach a mutually satisfactory agreement.

Under the terms of the amended agreement between the social partners, the second adjustment would take place in August 2001 when base wages in the state/public sector increased by the difference to the pre-set 6.3 per cent growth in wages in 2001. That part should be increased in accordance with the amended collective agreements for branches aimed at narrowing the gap between wages. The agreement also envisages a safeguard stipulating that wages are due for yet another round of adjustment in the case that prices grew in 2001 above the 7 per cent benchmark. The benchmark price growth excluded a rise in prices of tobacco products and alcoholic drinks. Nevertheless, the real growth in wages pencilled in 2001 should not exceed 2.5 per cent; hence it would lag behind the projected rise in labour productivity pencilled at 3.0 per cent. In the light of the fact that the current agreement on the wage policy for the period 1999-2001 expires on 30 June 2001, social partners should reach an agreement on the wage-setting principles to be applied over a longer period as soon as posssible.

EU guidelines on employment from 1998. The Action Plan is based on: increasing the employability of population, encouraging private business initiative, enhancing company and worker flexibility, and creating equal employment opportunities. The pending Collective Agreements Act and Employment Relationships Act both in the parliamentary procedure should provide a new framework for individual labour relations and remove some rigidities.

1.3. Public finance

During 2000, there were no major institutional changes in the filed of public finance as we could witness a year earlier when the list included the implementation of the Value-Added Tax Act, Excise Duty Act, Public Finance Act, Pension and Disability Insurance Act and the Accountancy Act.

Budget deficit tops 1.4 per cent of GDP

A rise in prices due to external factors coupled with a decline in domestic and a rise in foreign demand among the reasons for rising budget deficit

According to the preliminary data released by the Ministry of Finance, the general government balance in 2000 amounted to a deficit of 56 billion tolars or 1.4 per cent of GDP. The deficit exceeded the projected figure and rose above the 1999 level when it amounted to 0.6 per cent of GDP. Among the principal reasons for the rising deficit in fiscal 2000 was the inflation that driven by externalities overshot the projected figure, as well as s slump in domestic consumption offset by more vigorous exports. The higher inflation led to the adjustment of wages early in the year and eventually pushed pension benefits up by the pre-set percentage of wage growth. The revenue numbers were also lower than expected – in particular the influx of funds from the value-added tax and excise duties was weaker than projected. This was due to flagging domestic consumption (lower receipts from value-added tax) and higher growth in exports (higher value-added tax refunds). The influx of funds from excise duties also fell short of the projected figures and excise duty rates remained stagnant in the beginning of the year despite optimistic expectations. To remedy the situation, the Slovenian Government moved towards the end of 2000 to curb spending of budgetary recipients and transferred part of outstanding financial liabilities incurred in 2000 to the following budgetary year. Hence budgetary revenues for the year 2000 include value-added tax payments made in January 2001 for obligations incurred in 2000. January tax revenues arising from the tax payable on merchandise (currently value-added tax; sales tax before that) arising from obligations for the preceding year have been allocated to the budget since 1996.

According to the preliminary data, general government revenues in 2000 topped 1,726 billion tolars or 42.7 per cent of GDP declining by 0.3 per cent in real terms on a year-on-year basis after a rise by 7.2 per cent in real terms posted in 1999. A breakdown of general government revenues in 2000 in comparison with the preceding year shows that personal income tax in real terms rose by 3.0 per cent and contributions for social safety increased by 2.3 per cent, while taxes on goods and services (value-added tax and excise duties accounting for 90 per cent) declined in real terms by 7.9 per cent.

General government expenditure amounted to 1,781 billion tolars or 44 per cent of GDP and rose in 2000 by 1.4 per cent in real terms as opposed to 1999 when this rise was 6.8 per cent. Among some of the major items on the expenditure side there were expenses for wages and salaries, which grew in ream terms by 1.5 per cent, expenses for goods and services, which increased by 4.0 per cent, and transfers to households, which went up by 3.6 per cent (pension benefits accounting for 67 per cent of transfers to households rose by 2.2 per cent).

As regards the account for financial assets, inflows amounted to approximately 6 billion tolars in 2000, whereas in 1999 there was approximately one billion in outflows. The revenues of the Republic of Slovenia from privatisation amounting to approximately 4 billion tolars in 2000 are also included in this budgetary item. More substantial inflows from pending privatisation of some state-owned property have been announced for the year 2001 when the Slovenian Government is to sell off the two state-owned banks, national Telekom, power distribution companies and some other enterprises.

Net repayments in domestic and net borrowing in foreign markets

General government net indebtedness as carried on the financing account amounted to 57.7 billion tolars in 2000 according to the preliminary data. This item includes net 12.1 billion tolars repaid in the country and net 69.8 billion tolars received abroad. The bulk of cross-border indebtedness arises from the issue of bonds euro-denominated in the amount of 400 million euros.

Approximately half of government debt to domestic creditors

As at 30 September 2000, central government debt amounted to 1,043 billion tolars, with domestic debt accounting for approximately one half of the aggregate debt and cross-border borrowing accounting for the other half. As opposed to the end of 1999, when central government debt amounted to 893 billion tolars, it increased in real terms by 7.2 per cent; securities issued accounted for 82 per cent of the debt, while the rest arises from borrowings. In addition to the euro bonds issued by the Republic of Slovenia in foreign markets, there were also securities issued in the domestic market As regards short-term bills with maturity periods of three and six months, twelve-months bills were issued in May last year in the amount of 2 billion tolars. As regards long-term bonds, there was approximately 38 billion tolars in new issues, and bonds in the value of approximately 64 billion tolars fell due.

1.4. Financial market

Total assets of non-monetary financial intermediaries less than a half of total assets of monetary financial intermediaries

Monetary financial intermediaries have preserved their leading position in the Slovenian financial market. In terms of total assets, **non-monetary financial intermediaries** do not reach a half of total assets held by monetary financial intermediaries. At the end of 2000, the composition of non-monetary financial intermediaries was as follows: 43 authorised investment companies, 19 mutual funds, 16 insurance companies (among them 10 classical insurance companies, 3 re-insurance companies and 3 specialised public institutions), as well as around 80 leasing companies. Agency financial institutions (excluding banks' agency operations) account for a modest percentage of total assets of the Slovenian financial sector. At the end of 2000, 11 banks and 23 brokerage companies engaged in this business segment.

Unused privatisation vouchers account for one third of assets of authorised investment companies

Total assets of **authorised investment companies** at the end of 2000 amounted to 573.5 billion tolars, or by 4 per cent less than at the end of 1999. Unused privatisation voucher accounted for just under one third of all assets, compared to the end of 1999 when privatisation vouchers accounted for more than a half of all assets of authorised investment companies.

The scope of financial intermediation provided by the **agency financial institutions** (or financial agents) in the Slovenian financial market is demonstrated by the value of assets invested through this group of financial institutions. The cumulative value of invested assets topped 823.9 billion tolars at the end of 2000 posting a 26 per cent rise compared to the end of 1999.

Insurance and reinsurance companies come right after authorised investment companies as the second largest group of non-bank financial intermediaries. Leasing companies also hold a prominent place among non-monetary financial intermediaries.

In 2000, five bonds and one share were floated on the primary market,

The **primary securities market** (initial public offerings) remains relatively undeveloped in Slovenia. In 2000, there were six initial public offerings (IPOs) - five bonds and one share – and their aggregate value was 11.8 billion tolars.

… 198 shares and 68 bonds were traded on the Ljubljana Stock Exchange,…

On the **Ljubljana Stock Exchange (LSE)** 266 securities (198 shares and 68 bonds) floated by 224 issuers were traded as at the end of 2000. Cumulative market capitalisation posted at the end of December amounted to 1,138 billion tolars, and accounted for 27 per cent of GDP. In 2000, the value of trading deals totalled 269.6 billion tolars – a rise of 1.5 per cent compared to 1999. Trading with shares accounted for the bulk of closed deals (78 per cent). The most traded shares in 2000 included the shares floated by Mercator, Krka, Petrol, Lek and SKB banka. The shares of authorised investment companies have gained weight (31 per cent of total trading with shares). The value of the Slovenian Stock Exchange Index (SBI20) increased in 2000 by 0.1 per cent, the value of the Authorised Investment Companies Index (PIX) rose by 2.5 per cent. The value of trading deals concluded in 2000 outside the organised market totalled 171.5 billion tolars, exceeding the 1999 level by 27 per cent.

Portfolio investments - investments made by non-residents in Slovenian securities topped 8.7 billion tolars in 2000 and as much as 98 per cent was traded outside the organised market.

.. 915 shares and 100 bonds on the books of Central Securities Clearing Corporation.

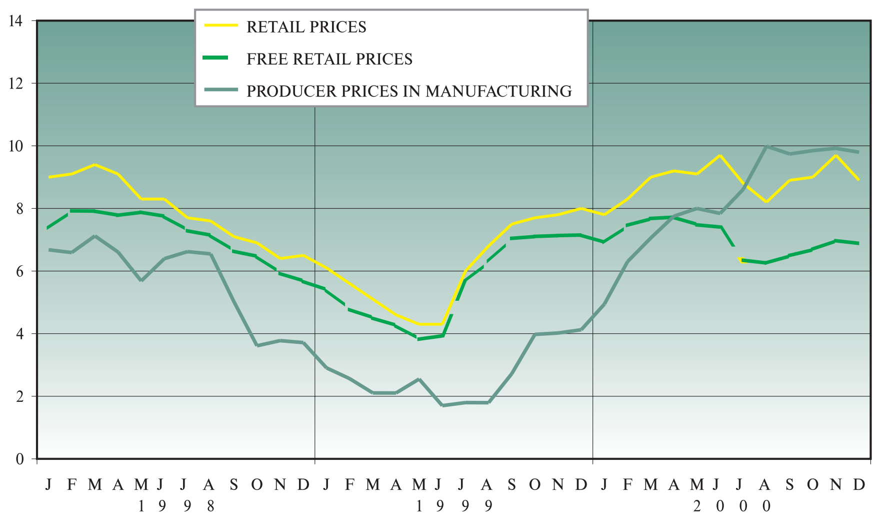
The **Central Securities Clearing Corporation** (abbreviated in the Slovenian language to KDD) had on its books at the end of December 2000 1,015 securities issued by 878 issuers, including 915 shares and 100 bonds. The value of shares registered with the Central Securities Clearing Corporation at the end of December 2000 carried at market i.e. book value amounted to 2,699 billion tolars (65 per cent of GDP), while the value of bonds marked-to-market, i.e. nominal value was 472 billion tolars (11 per cent of GDP).

1.5. Prices

8.9 per cent growth in prices fuelled by external factors

Exposure to adverse external factors affected movements in prices witnessed in 2000 and fed through to the domestic inflation rate. Thus the growth in consumer prices topped 8.9 per cent last year (annual average).

Figure 3: **Prices** (annual growth rates from 1997 to 2000 in per cent)



Source: Statistical Office of the Republic of Slovenia, Bank of Slovenia.

After a protracted period of dynamic developments in activities designed to lower inflation, the inflation trend changed direction in the middle of 1999. Even though that turnaround coincided with putting into effect the tax reform, it was predominately triggered by the developments in the external environment. Marked growth in prices of oil in the world markets that practically tripled prices compared to the level recorded some a year and a half ago accounted for a lion's share of around 20 per cent interim rise in import prices in 2000. Slovenia shared the destiny of many a country around the globe where oil price hikes have fed through to the consumer prices index (CPI) and manufacturers price index (9.2 per cent).

19.9 per cent growth in administered prices

In 2000, administered prices jumped by 19.9 per cent pushed by oil derivatives prices soaring by 32.7 per cent and some other administered prices. Despite such unfavourable price factors, other prices increased last year by a modest 6.9 per cent compared to a 7.2 per cent rise in 1999.

1.6. Balance of payments

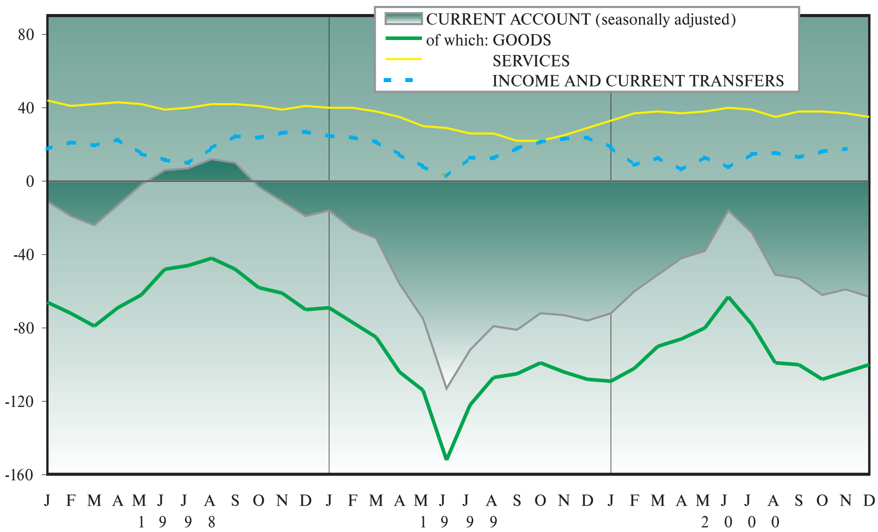
Current-account cross-border transactions recorded a deficit in the amount of 594 million US dollars in 2000, i.e. 3.3 per cent of GDP. Net inflow from cross-border financial transactions topped 1,055 million US dollars, i.e. 5.8 per cent of GDP and was allocated to level the current-account deficit and boost foreign exchange reserves by 461 million US dollars. The bulk of inflows over the last year was composed of flows, which directly increase external debt.

Lower year-on-year current account deficit in dollars despite unfavourable price factors …

… due to hefty surplus in services and lower deficit in goods trade.

The deficit of the current account of the balance of payments amounted to 594 million US dollars in 2000 (3.3 per cent of gross domestic product), i.e. 188 million dollars less than in 1999. Despite unfavourable price factors, the bulk of improvement in the current-account balance arises from a lower deficit in the exchange of goods (164 million dollars), while one third was contributed by a higher surplus in the exchange of services. The balance of capital and labour incomes deteriorated by 36 million dollars, while the balance of current transfers was preactically unchanged in relation to 1999.

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



Source: Statistical Office of the Republic of Slovenia, estimates of Analysis&Research Department of Bank of Slovenia

The deficit in the exchange of goods (according to the balance-of-payments statistics) amounted to 1,081 million dollars, i.e. 5.9 per cent of gross domestic products (as opposed to 1,245 million dollars, i.e. 6.2 per cent of gross domestic product in 1999). According to the preliminary data for 2000, the Slovenian companies exported goods in the value of 8,731 million dollars posting a rise of 2.2 per cent in US dollars compared to exports of goods realised in 1999.

Measured in US dollars, the Slovenian companies imported more goods in 2000. During the year 2000, the companies imported goods in the value of 10,115 million dollars (in C.I.F. terms), i.e. 0.3 per cent more than a year earlier. Moreover, the ratio showing the coverage of imports with exports was 86.3 per cent - better than in 1999 when this percentage was 84.8.

Exports of goods grew by 11.2 per cent and imports of goods rose by 3.6 per cent in real terms

The real rates of growth in the exchange of goods were higher that revealed by the relevant figures in US dollars. As in 1999, this was the result of the US dollar strengthening against the euro, i.e. the currencies used in the countries of the European Union, which are the main trading partners for the Slovenian exchange of goods. In 2000, the share of deals in US dollars on the exports side amounted to 10.4 per cent, while on the imports side it was 17.9 per cent. The rest of the trade is mostly contracted in the currencies of the EU Member States with approximately one fifth of all trade deals being concluded in the euro. When the change in export prices quoted in US dollars (by applying index of 91.9) and in import prices quoted in US dollars (by applying index 96.8) are excluded from the calculations, the result for 2000 is 11.2 per cent real growth in exports of goods and 3.6 per cent growth in imports of goods in real terms.

Terms of trade affect current account deficit

The deficit in the trade of goods measured by trade statistics topped 1,384 million dollars last year and was lower year-on-year by 153 million dollars. In real terms, the deficit in the trade of goods last year compared to 1999 was lower by 28.1 per cent (and by around one-tenth above the respective figures posted in 1998). Vigorous real growth in exports of goods encouraged by strong foreign demand was a significant element to drive the deficit down. Exports achieved in 2000 were a crucial factor of the last year's economic growth, and the rate of growth in exports in 2000 outpaced the 1999 performance. The deficit in the trade of goods was inflated by unfavourable terms of trade (deterioration by 5.1 per cent). If the terms of trade had remained unchanged last year, the deficit would have been lower by around 2.5 per cent of gross domestic product.

According to the preliminary data for 2000, the competitive edge of the Slovenian economy measured by the market share held by Slovenian exporters in the European Union being the major Slovenia's trading partner as somewhat blunt last year. The sharpest drop in the market share held by Slovenian companies was witnessed last year in the German and Italian market. On the other hand, Slovenian exporters managed to cut a fatter slice of the French and Austrian markets.

Record-low share of consumer goods in exports and imports

Real growth in imports of goods lagged behind growth in exports, partly as a result of exceptionally high figures posted in 1999 when imports soared on the eve of the introduction of the value added tax. Imports of goods went up stimulated by favourable domestic economic activity. The trend of the fast growth in imports of capital investment goods present for some years already, continued in 2000. The structure of the last year's trade reveals that alongside vibrant domestic and cross-border economic activities, the share of intermediate goods posted the strongest rise. On the exports side of the balance of payments in 2000, the exports of intermediate goods accounted for more than a half of total exports (52.8 per cent). A similar trend could be observed on the imports side (59.0 per cent) due to the last year's rise in the share of intermediate goods increased by 2.8 percentage points. On the other hand, the share of consumer goods decreased in 2000 both on the exports (36.9 per cent) and on the imports side of the balance of payments (24.8 per cent) hitting the record-low level since 1991.

Shares of trade with EU Member States unchanged in the wake of Russia and Kosovo crisis

The regional composition of exports and imports of goods in 2000 was slightly changed in respect of 1999. The share of the European Union Member States decreased last year on the exports side to 63.9 per cent (in 1999 it was 66.1 per cent), and on the imports side it fell to 67.8 per cent (1999: 68.9 per cent) thus sliding back to the 1997 level, i.e. to the period prior to the Russian and Kosovo crisis. Germany still headed the list of Slovenia's major EU trading partners with 27.2 per cent of exports and 19.0 per cent of imports, followed by Italy (exports: 13.6 per cent, imports: 17.4 per cent), Austria (exports: 7.5 per cent, imports: 8.2 per cent) and France (exports: 7.1 per cent, imports: 10.3 per cent). The 2000 deficit in the trade with Member States of the European Union amounted to 1,276 million dollars (in 1999: 1,295 million dollars), and was the worse in the trade with Italy (573 million dollars) and France (423 million dollars). The surplus arose last year from the trade with other countries of the European Union, which are not among Slovenia's leading partners (Denmark, Greece, Portugal). A more substantial surplus was incurred only through the trade with Germany. Last year as the rise in both imports and even more markedly exports of goods was below-average figures, the surplus amounted to 457 million dollars and was by 98 million dollars below the 1999 level.

Growing trade with countries of former SFR Yugoslavia.

A surge in trade with the countries of former SFR Yugoslavia occurred in 2000 when the rise measured in US dollars was just below 5 per cent. Exports to FR

Table 2: **Regional composition of foreign trade** (1998-2000, in millions of US$)

	EXPORTS			IMPORTS			TRADE BALANCE		
	1998	1999	2000	1998	1999	2000	1998	1999	2000
European Union (15)	**5,928**	**5,650**	**5,580**	**7,017**	**6,945**	**6,856**	**-1,089**	**-1,295**	**-1,276**
Austria	621	622	656	802	805	832	-180	-183	-177
France	748	491	619	1,258	1,100	1,043	-511	-609	-423
Italy	1,255	1,176	1,188	1,697	1,686	1,761	-442	-511	-573
Germany	2,572	2,627	2,376	2,089	2,072	1,919	482	555	457
CEFTA	**608**	**622**	**692**	**778**	**851**	**920**	**-170**	**-229**	**-228**
Czech Republic	150	159	151	264	281	252	-114	-122	-102
Hungary	141	145	168	244	267	294	-103	-123	-125
Poland	181	190	226	78	111	137	103	79	89
EFTA	**98**	**112**	**125**	**208**	**239**	**213**	**-110**	**-127**	**-88**
Non-European OECD members	**382**	**387**	**404**	**737**	**717**	**680**	**-356**	**-330**	**-276**
USA	252	258	270	296	293	299	-44	-34	-30
Countries of former SFR Yugoslavia	**1,397**	**1,296**	**1,364**	**593**	**572**	**594**	**805**	**724**	**769**
Croatia	815	671	688	432	444	448	384	227	241
FR Yugoslavia	103	85	143	68	36	41	35	49	102
Countries of former USSR	**330**	**213**	**281**	**216**	**201**	**263**	**114**	**12**	**18**
Russian Federation	235	129	191	178	159	231	58	-30	-40
Other countries	**307**	**267**	**286**	**561**	**557**	**590**	**-254**	**-290**	**-303**
TOTAL	**9,051**	**8,546**	**8,731**	**10,111**	**10,083**	**10,115**	**-1,060**	**-1,537**	**-1,384**

Source: Statistical Office of the Republic of Slovenia; figures for 2000 are preliminary.

Yugoslavia were particularly strong. Thus during the past year, Slovenian companies exported goods in the value of 143 million US dollars compared to 85 million US dollars in 1999. Croatia still remains the most important trading parter in this group of countries accounting for over a half of total trade with the countries of former SFR Yugoslavia and holding the third place among target markets for Slovenian exporters, and being on the fifth place on the list of the countries, which export to Slovenia. On the eve of the Russian crises, Slovenia posted over 100 million US dollars of surplus earned through trading with the countries of former Soviet Union. Last year, Russia/CIS countries were in the group of the countries that accounted for a surge in the volume of trade by one third. Despite some encouraging signs, Slovenia's exports and hence trade surplus still lag behind the figures recorded some years ago. As regards the trade figures with CEFTA countries, the upward trend persisted last year as the share of exchange of goods with this group of countries rose by approximately one tenth. Exports to the CEFTA market increased by 11.3

Growing trade also with former Soviet Union…

… and CEFTA countries.

Table 3: **Balance of payments**
(1996-2000 in million of US$, preliminary figures for 2000)

	1996	1997	1998	1999	2000
A. CURRENT ACCOUNT	**31**	**11**	**-147**	**-783**	**-594**
- in % of GDP	***0.2 %***	***0.1 %***	***-0.8 %***	***-3.9 %***	***-3.3 %***
1. Goods	-825	-776	-789	-1,245	-1,081
2. Services	633	630	492	364	426
2.1. Transport	73	97	131	142	139
2.2. Travels	638	669	530	415	440
- exports	1,240	1,187	1,088	954	957
2.3. Other	-78	-136	-169	-193	-153
3. Income	132	39	28	-24	-60
3.1. Labour income	210	179	179	174	152
3.2. Investment income	-78	-140	-151	-199	-212
4. Current transfers	91	118	122	123	121
B. NET FINANCIAL INFLOWS	**871**	**666**	**347**	**650**	**1,055**
- in % of GDP	***4.6 %***	***3.7 %***	***1.8 %***	***3.2 %***	***5.8 %***
1. Government bonds [1]	163	184	113	365	224
Other (including loans)	-69	-27	-20	16	126
2. Bank of Slovenia	129	-9	-51	-51	12
3. Private sector:					
3.1. Foreign direct investment (inflow) [2]	129	335	248	181	181
3.2. Foreign portfolio investment (inflow) [2]	68	92	6	-3	25
3.3. Trade credits (net)	-294	-339	-428	-335	-232
3.4. Loans (inflow)	529	357	294	754	810
- Banks [1]	291	-15	41	257	279
- Enterprises	238	372	253	497	531
3.5. Other (including all outflows)					
- Households	37	151	89	-223	16
- Banks, enterprises	186	-156	33	-80	-159
4. Net errors and omissions	-5	77	62	27	53
C. FOREIGN EXCHANGE RESERVES (increase (-))	**-902**	**-678**	**-200**	**132**	**-461**
1. Bank of Slovenia	-587	-1,287	-112	126	-196
2. Banks	-315	610	-88	6	-265

1 Excluding the book-entry transfer of external debt of banks to government liabilities (NFA bonds) in June 1996 and after the deduction of transactions of domestic banks with government bonds.

2 Figures for the period from September 1996 to February 1997 estimated within the framework of constant stock of cumulative direct and portfolio investments.

Source: Bank of Slovenia.

per cent (share of total exports: 7.9 per cent) and imports rose by 8.1 per cent (the share of total imports of goods: 9.1 per cent).

Rising surplus on exchange of services

Another feature of 2000 was a buoyant rise in the exchange of services, both on the exports and even more markedly on the imports side. In comparison with 1999, exports of services increased by 12 per cent in real terms, while imports rose by 7 per cent. The surplus posted by the exchange of services topped 426 million dollars, i.e. it was by 62 million dollars higher than in 1999, while in real terms even the highest surplus recorded so far in the exchange of services in 1998 was below the 2000 figure.

Thanks to the lower deficit in the exchange of goods, the deficit for goods and services fell from 881 million dollars in 1999 to 655 million dollars in 2000, i.e. from 4.4 per cent to 3.6 per cent of gross domestic product. The two-thirds of the falling deficit figure was contributed by the lower deficit incurred through the exchange of goods, whilst the rest came from the services account.

All more prominent groups of services posted improved trade balances in 2000 either by means of a faster rise in exports than in imports, or by squeezing the volume of imports. Revenues generated by the tourist industry totalled 957 million dollars, and rose by 17 per cent in real terms year-on-year, overshooting by 9 per cent the 1998 figure (it is more appropriate to benchmark the 2000 figure against the 1998 figure since the year 1999 was an exceptionally bad year hit by the Kosovo crisis). Expenditure for the tourist industry increased on a more modest scale, i.e. by 12 per cent, and at the year-end totalled 517 million dollars. The surplus generated by the tourist industry rose from 415 million dollars to 440 million dollars, or by 25 per cent in real terms.

Surplus on tourist services up 25 in real terms

As for transport services, exports were going up and the rise in imports trailed behind. The surplus amounted to 139 million dollars and was 3 million dollars below the 1999 figure, while in real terms the surplus jumped by over 10 per cent. Following a longer period of net inflows and the red figure in 1999, building and construction services were back on track last year when exports recovered and imports stalled resulting in a modest surplus amounting to 13 million dollars. Intermediation services kept a high profile among export-oriented services and posted a hike in real terms both in the value of exports (120 million dollars) and imports (79 million dollars). Miscellaneous business and technical services experienced a plunge in imports in 2000 shedding 26 million dollars and landing at 206 million dollars resulting in a decrease in deficit being at 84 million dollars. On the other hand imports of licences, patents and copyrights continued its upward trend (up by 49 million dollars) and communications services (up by 50 million dollars).

Interest expense up due to rising external debts and higher interest rates

Net inflow from labour income totalled 152 million dollars last year, or 22 million dollars less than in 1999, thus staying at the same level in real terms. Deterioration disclosed on the capital account in 2000 is a result of a growing external indebtedness and higher interest rates. Income from capital (mostly on foreign exchange reserves) totalled 216 million dollars (6 million dollars more than in 1999). Capital expenditures totalled 429 million dollars comprising payments of interest on external debt in the amount of 275 million dollars - 20 million dollars more than in 1999. The last year’s gains of foreign investors appear on the basis of preliminary estimates to have stayed in real terms at the same level as in 1999 (when they jumped by 50 per cent). Appropriations of profits and dividends fell short of the 1999 levels (41 million dollars as opposed to 57 million dollars), while the estimate in respect of retained, i.e. reinvested profits in the amount of posted in 1999 actually went up in real terms when taking into account a 15 per cent hike of the US dollar against other currencies.

During the year under review, net inflows from current transfers totalled 121 million dollars, or 2 million dollars more than in 1999. On the inflows side official inward transfers rose, while on the outflows side outward transfers from other sectors increased.

Inflow from cross-border financial transactions surges

Net inflows from cross-border financial transactions in 2000 amounted to 1.55 million dollars, i.e. 5.8 per cent of GDP (in 1999: 3.2 per cent). The most significant source of inflows to Slovenia in 2000 was borrowing abroad through the issuance of debt instruments. In case of inflows from investments in equity, there were no substantial changes compared to 1999.

In March 2000, the Republic of Slovenia issued Eurobonds in the amount of 400 million euros. By means of the additional net drawings of foreign loans in the amount of 126 million dollars, the Government obtained cross-border financing in the net amount of 484 million dollars compared to 444 milion dollars in 1999.

In 2000, the Slovenian banks and insurance companies more than doubled their asset holdings in eurobonds issued by the Republic of Slovenia. Namely, these holdings surged from 63 million dollars in 1999 to 134 million dollars in 2000. Net financial inflows channelled to the private sector posted an impressive increase. These developments were not caused so much by new borrowing abroad as by more modest volumes of cross-border crediting through trade credits and compared to 1999, practically negligible net transactions of individuals in foreign cash.

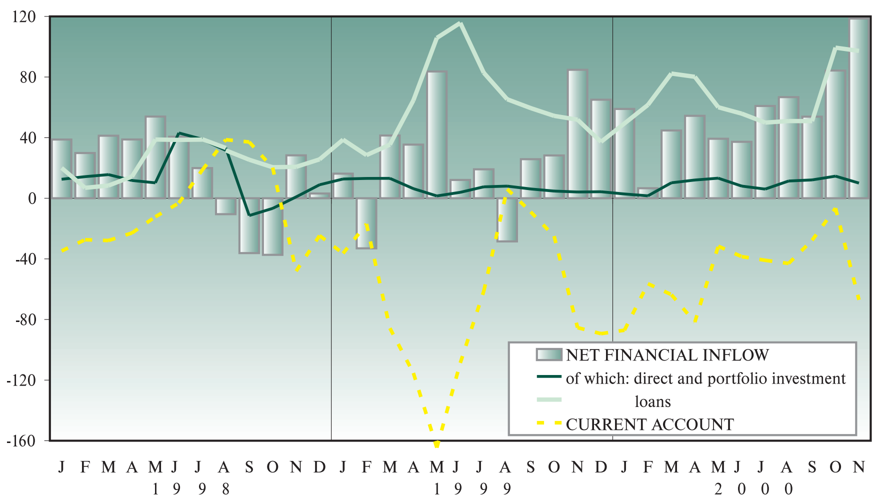
Upbeat note in outward investments

Foreign direct investment inflows totalled 181 million dollars and remained at the 1999 level . Reinvested profits of foreign shareholders accounted for more than a half of that amount. On the other hand, growth in outward direct investment of Slovenian companies stayed on track with 48 million dollars (10 million dollars more than in 1999). As much as 80 per cent of all outward direct investments was chanelled into the countries of former SFR Yugoslavia.

Revived foreign portfolio investments

Having witnessed for a year and a half a decline in foreign portfolio investments as non-residents continued to pull out of the Slovenian corporate sector, portfolio investments made a U-turn last year exceeding disposal of shares. Thus the aggregate net portfolio assets throughout the year totalled 25 million dollars and stayed much below the levels achieved prior to 1998. There was a rise in the amount of investments of Slovenian residents in foreign equity shares - from 0.5 million dollars in 1999 (after restrictions were lifted in September) to 17 million dollars in 2000.

Figure 5: **Balance of payments current account financing**
(in millions of US$, moving average 3)



Source: Bank of Slovenia.

Slovenian companies continued in 2000 to raise financing across the border. Net foreign financing inflows channelled to corporate borrowers in Slovenia amounted to 531 million dollars (497 million dollars in 1999) pushing the share of foreign financing in the entire lending to the corporate sector up by 7 percentage points, i.e. from 37 per cent in 1999 to 44 per cent in 2000.

Share of foreign loans in corporate sector financing topped 44 per cent

The amount of lending extended to the banks in Slovenia by foreign creditors rose from 257 million dollars in 1999 to 279 million dollars at the end of 2000. The banks mostly tapped into foreign sources for the purpose of balancing their maturity structure of liabilities and assets, but they also borrowed abroad to obtain additional, mainly long-term sources to be passed on as loans to domestic customers and partly as funds required strengthening their capital base. After two years of trimming assets available for lending operations outside Slovenia, the banks practically suspended last year cross-border lending since the repayments under the granted loans exceeded new drawings by 4 million dollars. Instead of banks, the companies took over last year increasing net granted loans and advances from 35 million dollars in 1999 to 70 million dollars in 2000. The corporate sector also financed foreign borrowers through net commercial credits in the amount of 232 million dollars (335 million dollars in 1999).

Net credits granted by corporate sector to foreign borrowers increase

As regards the transactions of individuals in foreign cash, the overall situation was clearly cooling off compared to the past years. Namely, the holdings of individuals in foreign cash decreased last year by 16 million dollars, as opposed to 1999, when they increased by 223 million dollars.

Given the current account deficit in the amount of 594 million dollars and net financial inflows in the amount of 1,055 million dollars, the aggregate foreign exchange reserves of the Bank of Slovenia and the banking sector in 2000 increased by 461 million dollars. The balance of foreign exchange reserves rose from 4,115 million dollars at the end of 1999 to 4,370 million dollars at the end of 2000. The fact that the growth was lower in comparison to the value of cross-border transactions may be explained by the changes in the rates of exchange in favour of the US dollar (206 million dollars).

Foreign exchange reserves go up despite current account deficit

1.7. External debt

Slovenia's external debt rose at the end of 2000 to 6,217 million dollars, or 817 million dollars more than at the end of 1999. The external debt swelled by 1,140 million dollars in actual cross-border borrowing partly offset by as much as 322 million dollars in exchange differences, which lowered the debt. As for maturity, long-term debt accounted for 98.4 per cent of aggregate debt. As regards currency composition of Slovenia's external debt, debt denominated in euro and the foreign currencies under the euro umbrella accounted for 83.6 per cent, debt denominated in US dollar accounted for 12.3 per cent and other foreign currencies accounted for 4.1 per cent of all claims. Compared to the past few years, the share of the debt denominated in euro increased, while the share of claims in US dollars decreased.

External debt rises to US$ 817 million

In 2000, the Slovenian banks registered new borrowing in the amount of 2,148 million dollars concluded with foreign creditors – a drop of 10.5 per cent compared to the preceding year. The government sector registered new cross-border financing agreements in the amount of 507 million dollars, or 15.8 per cent more than in 1999. The value of financing agreements backed by the guarantee issued by the Republic of Slovenia totalled 93 million compared to 700 million dollars registered in 1999. The funds provided under the financing agreements have been earmarked to the motorway construction (49.1 per cent), exports crediting (32.3 per cent) and directly to non-financial institutions (18.6 per cent). The banks registered 520 million dollars in new financing agreements; the rest of the private sector registered 1,028 million dollars in new financing agreements including natural persons who registered new financing in the amount of 9.5 million dollars. Natural persons entered into financing agreements primarily with Austrian banks.

Among newly registered credit operations in 2000 there was 243 million dollars in long-term commercial credits, 1,518 million dollars in financial credits and 387 million dollars in issued bonds. The Republic of Slovenia issued in March 2000 bonds in the nominal value of 400 million euros with the maturity period of ten years and at 6 per cent fixed interest rate. In addition, for the purpose of providing funds for the budget, the Government resorted to a short-term bridge-over loan in the amount of 100 million D-marks from the revolving credit facility with a foreign bank. A breakdown of financial credits shows: a facility for providing financing within the country (47.1 per cent), for by liquidity of banks (29.3 per cent), for specific project financing (10.6 per cent), for repayment of cross-border lending arrangements (4.7 per cent) and for other purposes (8.3 per cent).

Shorter maturity of new loans

The average contractual maturity of new long-term borrowing was 7 years and 6 months compared to 1999 when the average maturity was 10 years and 7 months. The average weighted interest rate under long-term loan agreements was 5.5 per cent as opposed to 4.2 per cent in 1999.

Regular servicing of liabilities to creditors of London and Paris Club

The Republic of Slovenia continued to service regularly its liabilities arising from the principal and accrued interest under the respective loan agreement and repaid 254.2 million US dollars in 2000. In accordance with the regulation of relations in respect of unallocated debts of former SFR Yugoslavia, the Republic of Slovenia has observed its obligations by making regular payments to the countries grouped in the London Club as well as the Paris Club. Outstanding liabilities include 32 million US dollars in claims of Germany on the Republic of Slovenia and obligations under the agreements pending signing, i.e. ratification with Great Britain, Norway and Italy (6 million US dollars).

The balance on the fiduciary account with Dresdner Bank in Luxembourg paid in towards the settlement of liabilities incurred by former SFR Yugoslavia under the Treaty of Osimo and the Treaty of Rome, amounted to 45.8 million US dollars as at 31 December 2000.

Table 4: **Slovenia's external debt** (balance at year-end in US$ million)

	1993	1994	1995	1996	1997	1998	1999	2000
1. Long-term debt - total	1,744	2,172	2,916	3,931	3,988	4,805	5,283	6,118
1.1. Public and publicly guaranted	1,206	1,331	1,437	1,996	2,014	2,326	2,451	2,665
1.1.1. Institutional creditors	723	749	702	770	711	740	650	743
1.1.2. Private creditors	483	582	735	1,226	1,303	1,586	1,801	1,922
1.2. Private non-guaranteed	538	841	1,479	1,935	1,974	2,479	2,832	3,453
2. Use of IMF credits	12	7	4	1	-	-	-	-
3. Short-term debt	117	79	50	49	135	110	117	99
External debt stock	**1,873**	**2,258**	**2,970**	**3,981**	**4,123**	**4,915**	**5,400**	**6,217**
Undisbursed debt	382	579	431	562	440	494	982	901

* In 1996, the Republic of Slovenia agreed to take over part of unallocated debt of former SFR Yugoslavia under the New Financing Agreement from 1988 and bilateral agree ments with the government of FR Germany. The issues of Eurobonds floated by the Republic of Slovenia included: DM 400 million in 1997, EUR 500 million in 1998, EUR 400 million in 1999, and EUR 400 million in 2000.

Source: Bank of Slovenia.

2. MONETARY POLICY

2.1. Monetary policy objectives and money supply

Monetary policy objectives and indicators

Under the Law on the Bank of Slovenia, the Bank's core purpose relates to price stability, i.e. the integrity and value of the domestic currency and the support of general liquidity of domestic and cross-border payments. The ultimate objective of the monetary policy set for the year 2000 was to continue efforts focused on reducing inflation down to the level generally maintained in EU Member States. Since 1997, the intermediate objective of the monetary policy has been growth in broad monetary aggregate M3 as the medium-term monetary policy orientation. The link between the monetary policy and M3 and M3 and consumer price growth as the ultimate objective of the monetary policy, is a long-term goal. In order to steer market rates efficiently, the Bank of Slovenia also uses other indicators and operational targets. Among significant monetary policy indicators, the Bank uses surplus/deficit of supply over demand for transaction money, the rate at which mandatory reserves maintained by banks are exceeded, demand at auctions for instruments made available by the Bank of Slovenia, as well as the money market interest rate.

Box 2: **Intermediate monetary policy target for 2000**

The Bank of Slovenia pursues the intermediate monetary policy objective for the year 2000 endorsed by the Governing Board at its session held on 25 January 2000. Namely, annual growth in monetary aggregate M3 was pencilled between the average figure for the last quarter of 1999 and the last quarter of 2000, i.e. in the band between 12.0 and 18.0 per cent. The assumptions used by the Governing Board of the Bank of Slovenia to define the monetary policy objective within the said band was real annual growth in GDP of 4.0 per cent, general government budget deficit up to 1.0 per cent of GDP, and real wage growth up to 2.5 per cent. Within this context the Bank of Slovenia has announced that it will strive to create conditions for stability of currency and thus support forecasts of the Government of the Republic of Slovenia on inflation in 2000. At the same time it has expressed awareness that inflationary pressures and inflation will be susceptible to impulses coming from abroad, while on the domestic market, it will mostly depend on general growth in wages, as well as on the implementation of policy regarding administered prices. Therefore, the Governing Board of the Bank of Slovenia has appealed to social partners to contain appetites when negotiating wage policy. The Bank of Slovenia has expressed readiness to contribute to the stability of the domestic currency by consistent foreign exchange rate policy formulated with the aim of decreasing external imbalance.

Actual annual growth in M3, measured as described above amounted to 16.3 per cent – the figure falling in the upper half of the band set as the intermediate target. The Governing Board of the Bank of Slovenia at its session held on 30 January 2001 estimated that the monetary policy in 2000 was in line with guidelines. The Bank of Slovenia prepared for 2001 a new projection of growth in M3.

Monetary aggregate M3 comprises practically all liabilities of the monetary system in domestic currency, including deposits of the General Government deposits denominated in foreign currency and placed with banks. Other liabilities of the monetary system include broadly speaking only capital and reserves, while the number of liquid non-banking instruments despite growth is still very small.

The bulk of M3 annual growth of 16.3 per cent derived from growth in foreign exchange deposits placed with banks. This particular aggregate increased between the last quarter of 1999 and the last quarter of 2000 by 32.1 per cent. Deposits in foreign currency placed by individuals rose by 24.1 per cent, while deposits of non-financial enterprises in foreign currency nearly tripled. Rather impressive growth in foreign exchange deposits witnessed during the year under review was fuelled by new foreign exchange accounts of non-financial enterprises with commercial banks and relatively fast growth in exchange rates. The rise in time deposits denominated in tolars placed with commercial banks and the Bank of Slovenia was 12.4 per cent outpacing the rise of 7.4 per cent in deposits in tolars repayable on demand.

Assumptions and projections taken into consideration

When setting the monetary policy objectives for the year 2000, the Bank of Slovenia took into account the key macroeconomic projections drawn in the Budget Memorandum presented to the National Assembly by the Government of the Republic of Slovenia. The key macroeconomic figures for 2000 were: 4.0 per cent annual growth in gross domestic product, 2.5 per cent annual growth in real net wages, and general government deficit of 1.0 per cent of gross domestic product. The developments in the international environment were seen as a catalyst for relatively high growth in economic activity due to take the lead again after 1999 when domestic demand gave a boost to growth. Already at the beginning of the last year, the Bank of Slovenia became aware of the potentially threatening rise in inflationary pressures from abroad, mainly as a result of high prices of oil and other commodities in international markets. The Bank of Slovenia made a commitment to support the inflation target defined by the Government of the Republic of Slovenia within the framework of its competence.

Furthermore, the projections were made on the assumption that the conditions for the cross-border exchange would deteriorate, leading to a deficit in the current account of the balance of payments that is almost entirely financed by hefty inflows of capital from abroad. Following a slump in domestic consumption after the introduction of value-added tax (VAT) and owing to institutional factors such as pension and housing savings, to get the structure of broad money (M3) back on track would call for increasing the share of long-term savings in the M3 structure.

Monetary policy assumptions in line with projections made at the beginning of the year

The basic assumptions have actually moved in accordance with the projections made at the beginning of the year. According to the latest estimates, economic growth was somewhat higher, while the current account of the balance of payments was below the 1999 level due to extremely strong foreign demand despite of somewhat impaired terms of trade. During the year under review, capital inflows were vigorous and in addition to financing the current account deficit, also increased international foreign exchange reserves.

Inflation on the consumer price measure notched 8.9 per cent exceeding the estimated figure for 2000. It fed on rising prices of oil and other commodities in

Table 5: **Supply of base money**
(in billions of tolars)

	As at 31 December			Quarterly changes in 2000				
	1998	**1999**	**2000**	**I**	**II**	**III**	**IV**	**Total**
1. Net foreign assets	593.9	629.6	736.0	68.7	-11.2	27.7	21.2	106.4
2. Domestic liabilities in foreign currency	-298.6	-334.3	-394.0	-97.1	38.5	7.1	-8.1	-59.7
- foreign currency bills	-282.4	-310.4	-358.3	-25.8	2.7	-13.4	-11.5	-47.9
- foreign currency deposits of the budget	-16.2	-23.9	-35.7	-71.3	35.8	20.4	3.4	-11.7
3. Net foreign currency assets (1+2)	**295.4**	**295.3**	**342.1**	**-28.4**	**27.2**	**34.8**	**13.1**	**46.7**
4. Time deposits of the budget	**0.0**	**0.0**	**0.0**	**-6.0**	**6.0**	**0.0**	**0.0**	**0.0**
5. Loans to banks	**3.9**	**25.8**	**10.5**	**19.5**	**-17.2**	**-10.5**	**-7.1**	**-15.3**
6. Tolar bills	**-80.1**	**-27.4**	**-6.9**	**8.7**	**10.9**	**-4.3**	**5.1**	**20.4**
7. Other items net	**-45.2**	**-83.2**	**-130.1**	**-16.1**	**-6.6**	**-20.0**	**-4.2**	**-46.8**
8. Net tolar assets (4 to 7)	**-121.4**	**-84.8**	**-126.5**	**6.1**	**-6.9**	**-34.8**	**-6.1**	**-41.7**
9. Base money (3+8)	**174.0**	**210.5**	**215.6**	**-22.3**	**20.3**	**0.0**	**7.0**	**5.1**
- bank reserves	74.4	79.4	87.4	-3.4	12.3	-2.4	1.5	8.1
- other sight deposits	5.9	6.2	8.4	0.3	1.7	1.2	-1.1	2.2
- currency	93.7	125.0	119.8	-19.2	6.3	1.1	6.6	-5.2

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

international markets. This has also reflected on the structure of growth in individual price groups owing to a rise in administered prices by 19.9 per cent (prices of crude oil derivatives jumped by 32.7 per cent) while other prices increased by 6.9 per cent.

The General Government sector deficit was 1.4 per cent of GDP exceeding the target figure pencilled in the Budget Memorandum. The principal reason for the deficit above the target figure has been the changed structure of demand in GDP (higher exports and lower domestic spending), which compared to 1999 have led to a decrease in taxes levied on goods and services by 7.9 per cent in real terms.

Support to stable and manageable growth in foreign exchange rate

Within the framework of the objectives determined in relation to inflation, growth in broad monetary aggregate, and money in circulation, the Bank of Slovenia sought to support in the course of 2000 a stable and manageable exchange rate movement. The Bank's performance in this field was guided by the recognition of how deeply the movements in the exchange rate may affect the current account of balance of payments, inflation and the currency structure of savings. At the end of March, the Bank of Slovenia signed a new agreement with the banks on their participation in interventions in the foreign exchange market. The agreement enables the Bank to implement a more efficient and more transparent foreign exchange policy, while the participating banks gain a tool to steer more easily their tolar and foreign exchange liquidity.

Gradual rise in interest rates

Due to the rising domestic and foreign inflationary pressures, the Bank of Slovenia was gradually rising interest rates on its key instruments. Thus from the beginning of the last year, interest rates on tolar bills increased from 1.7 to 5.0 per cent on 2-day, from 3.2 to 7 per cent on 12-day, from 7.0 to 10 per cent on 60-day and from 9 to 11.0 per cent on 270-day instruments. The discount and Lombard rates increased in June and in December by 1 percentage point each time. At the end of the year, he discount rate was at 10 per cent and the Lombard rate was 11.0 per cent. The interest rate on liquidity loan granted against 12-day tolar bills pledged as collateral increased from 5.7 to 10.0 per cent, while the base interest rate for temporary purchase of bills denominated in foreign currency went up from 7.8 to 10.5 per cent.

Streamlining Bank of Slovenia monetary policy instruments

During the year under review, the Bank of Slovenia continued to streamline its monetary policy instruments and improved their transparency. Within the framework of these efforts, the Bank abolished in 2000 bills with warrants, twin bills and tolar bills with maturity of 7, 14 and 30 days. Furthermore, the Bank abolished liquidity loans granted against the pledge of 30-day tolar bills. By introducing 7-day temporary purchase of foreign currency bills, the Bank has laid the grounds for reducing mismatch in short-term tolar liquidity, whereas 60-day instruments provide a source of tolar liquidity with longer maturity.

6.5 per cent rise in volume of base money

The quantity of the base money measured by average daily balances increased by 6.5 per cent between the last quarter of 1999 and the last quarter of 2000, i.e. decreased by 2.5 per cent in real terms. Cash in circulation rose by 6 per cent, reserves of banks by 5.4 per cent and other deposits repayable on demand with the Bank of Slovenia by 24.8 per cent. Growth in the base money in the first six months of 2000 was 1.5 per cent, and in the second six months was 4.9 per cent.

Base money issue through foreign exchange transactions

During the first quarter of 2000, the Bank of Slovenia issued base money through tolar transactions, as opposed to the second quarter onward when the Bank issued base money through foreign exchange transactions. Likewise, during the first quarter the Bank of Slovenia was a net vendor of foreign exchange (43 billion tolars), while from April to December it was a net buyer of foreign exchange (41.1 billion tolars). Throughout the year, the Bank sold net 37.9 billion tolars in foreign exchange, and bought net from the government budget 36 billion tolars in foreign exchange. Net foreign assets of the Bank of Slovenia rose mainly on the account of net subsriptions of bills denominated in foreign currency. This item increased by 47.9 billion tolars, the rise in foreign exchange deposits of the government budget amounted to 11.7 billion tolars and there was also a relatively fast-paced growth in foreign exchange rate.

During the first quarter of 2000, the Bank of Slovenia issued net through tolar transactions 22.2 billion tolars in base money. Part of the issuance was through lending in the amount of 19.5 billion tolars and through net tolar bills on maturity in the amount of 8.7 billion tolars. The balance of outstanding tolar bills decreased in the second quarter by additional 10.9 billion tolars and at the end of June topped 7.8 billion tolars. The volume of base money was falling during the same period through net repayments of credits. In the second half of 2000, net repayments under credits amounted to 17.6 billion tolars, while the balance of outstanding tolar bills remained practically unchanged.

16.3 per cent growth in M3

Monetary aggregate M3, measured by average daily balances increased from the last quarter of 1999 until the last quarter of 2000 by 16.3 per cent, or by 6.5 per cent in real terms. After achieving modest growth of approximately 12.0 per cent in the first four months, there was a prolonged upbeat trend in current movements until August, followed by a stagnation that lasted until the end of the year when the figure lingered around 18 per cent. During the same period, monetary aggregate M1 increased by 7.0 per cent. Exceptionally modest growth was achieved by the so-called transactional money and was predominately a result of restoring demand for transaction money to the level of long-term balance (prior to the introduction of VAT), the replacement of short-term deposits in tolars by foreign exchange deposits as a consequence of relatively fast growth in foreign exchange rate and the

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

	As at 31 December			Quarterly changes in 2000				
	1998	**1999**	**2000**	**I**	**II**	**III**	**IV**	**Skupaj**
1. Net foreign assets	**701.8**	**711.6**	**825.0**	**84.2**	**-15.4**	**43.1**	**1.4**	**113.3**
2. Domestic assets	**1,422.0**	**1,700.7**	**2,002.6**	**67.5**	**90.5**	**60.5**	**83.4**	**301.9**
General Government: bonds	255.4	253.5	286.0	16.2	12.4	5.7	-1.8	32.6
loans	106.6	133.2	161.1	-7.8	-1.9	15.3	22.3	27.9
Enterprises : securities	66.9	76.2	89.5	0.5	4.8	-1.2	9.3	13.4
loans	690.2	798.4	970.7	42.3	58.5	26.0	45.5	172.3
Households: loans*	302.8	439.4	495.2	16.4	16.6	14.7	8.1	55.9
3. Issued securities	**-73.2**	**-64.0**	**-79.2**	**2.9**	**-6.8**	**-5.8**	-5.5	-15.2
4. Foreign currency deposits of the	**-16.2**	**-23.9**	**-35.7**	**-71.3**	**35.8**	**20.4**	3.4	-11.7
5. Other items net	**-344.2**	**-411.3**	**-507.3**	**-33.9**	**-25.4**	**-33.8**	-3.0	-96.0
6. M3 (1 to 5)	**1,690.3**	**1,913.1**	**2,205.4**	**49.6**	**78.6**	**84.4**	**79.7**	**292.3**
- foreign currency deposits with	428.1	497.2	662.9	48.6	39.6	48.3	29.2	165.7
7. M2	**1,262.2**	**1,415.9**	**1,542.5**	**0.9**	**39.0**	**36.1**	**50.5**	**126.5**
- time deposits with banks	829.8	891.2	971.5	16.1	5.5	31.0	27.7	80.3
- time deposits with Bank of	0.0	0.0	0.0	6.0	-6.0	0.0	0.0	0.0
- saving deposits	99.7	124.9	147.1	16.1	8.0	0.2	-2.0	22.2
8. M1	**332.7**	**399.8**	**423.9**	**-37.2**	**31.5**	**4.9**	**24.9**	**24.1**
- sight deposits with banks	233.2	268.7	295.7	-18.3	23.5	2.5	19.3	27.1
- sight deposits with Bank of	5.9	6.2	8.4	0.3	1.7	1.2	-1.1	2.2
- currency in circulation	93.7	125.0	119.8	-19.2	6.3	1.1	6.6	-5.2

* A change in the methodology of compiling information relating to corporate and retail lending in 1999.

Source: Bank of Slovenia.

possibility given to companies to open foreign exchange accounts (under the Foreign Exchange Act 1999). Time deposits denominated in tolars increased by 12.4 per cent; the highest increase was achieved by deposits due between 90 and 365 days (20.0 per cent) and time deposits due after one year (15.9 per cent). The dynamics of growth in foreign exchange deposits markedly outpaced the dynamics in growth in tolar deposits. Aggregate increase in foreign exchange deposits was a hefty 32.1 per cent, while their share in M3 went up during one year from 25.0 to 28.7 per cent.

Monetary multiplier between monetary aggregate M1 and base money in 2000 remained remarkably stable just like in previous years and amounted on average 1.97. Over a year's period, the M2 multiplier increased by 4.2 per cent, while the M3 multiplier rose by 9.2 per cent.

As opposed to the first half of 2000 when domestic deposits were the sole source of broad money issue, in the second half of the year the money was issued both through net foreign assets and through domestic claims. The share in increase of net foreign assets in M3 amounted to 26.0 per cent in the first half of 2000 compared to 42.0 per cent in the second half of the year. Throughout the year foreign exchange deposits were increasing rather evenly and represented the main source of generating net foreign assets.

19.7 per cent growth in corporate lending and 12.8 per cent growth in retail lending

During the year under review, growth in entire lending totalled 17.2 per cent; growth in lending to companies and financial institutions topped 19.7 per cent, to General Government 16.6 per cent, while loans to individuals notched 12.8 per cent. Non-financial enterprises lending was gaining momentum until the middle of 2000, and then slowed down. Somewhat sluggish borrowing by the non-financial enterprises sector despite high-note economic activity could be accounted for to the rising borrowing from foreign banks. The share of cross-border borrowing in the entire borrowing amounted to a hefty 44 per cent. Short-term tolar lending in domestic lending to the non-finacial enterprises sector accounted for just below two-thirds of the increase achieved in domestic lending operations, and foreign exchange in tolar long-term lending accounted for one third of new lending from domestic banks. Lending to households was back to normal after the surge in 1999 with long-term loans on the top of the leaderboard.

2.2. Interest rates

Movements in lending and deposit bank interest rates …

Lending and deposit interest rates charged by banks were rising in the first half year 2000 in line with the movements in the inflation rate during the year. In the third quarter of 2000, the rise in interest rates slowed down, and then went up steeply over the last months of 2000. Only nominal interest rates paid on deposits denominated in tolars and repayable on demand remained at the same level - one percentage point - until December 2000.

… follow changes in base interest rate.

During the year under review, the base interest rate (abbreviated TOM in the Slovenian language) was rather stable compared to 1999 and ranged between 0.7 and 0.8 per cent on a monthly basis, i.e. between 8.6 and 9.9 per cent on annual level. The average base interest rate in 2000 amounted to 8.9 per cent and equalled the annual inflation rate for 2000, exceeding by 2.6 percentage points the base interest rate in 1999.

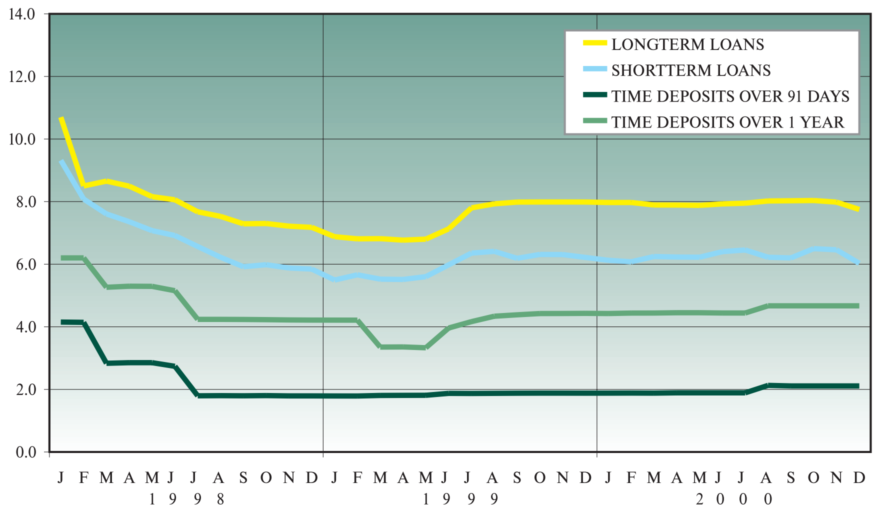
Interest rates on deposits varied and changed differently. A change in interest rate movements was partly induced by the recommendation regarding cap interest rates on deposits made by the Bank Association of Slovenia in August. The Association suggested to increase interest rates on deposits due within 91 and 180 days by 0.25 percentage points to 2.25 per cent, on deposits due within 181 days and one year and on deposits due within one to two years by 0.5 percentage point to 3.25 per cent, i.e. 4.0 per cent. Thus the slope of the curve showing the maturity composition of interest rates on deposits paid by banks rose steeply particularly in its first part. The interest rate on deposits due within one to three months did not change during the year under review remaining at 0.9 per cent above the base interest rate, while the interest rate on time deposits due within three months rose from 1.9 per cent above the base interest rate in January to 2.1 per cent above the base interest rate in December. Stronger growth was posted by the interest rates paid on deposits from other banks with maturity date after one year, which increased by 0.25 percentage points above the base interest ratre to 4.7 per cent above the base interest rate.

In 2000, there were no major changes in movements in lending interest rates above the base interest rate for the last months of the year. The average declared interest rate on short-term loans and advances ranged between 6.1 and 6.45 per cent above the base interest rate during the first eleven months. The trend reversed in December when it dropped to 5.9 per cent above the base interest rate. During the same period, the average monthly interest rate on long-term loans was 8.0 per cent above the base interest rate and in the last month of 2000 it decreased to 7.7 per cent above the base interest rate. Both kinds of interest rates have in common a higher degree of stability compared to 1999, particularly in the case of long-term lending interest rate.

Dynamic fluctuations in inter-bank interest rates

Despite the fact that a key feature of lending and deposit interest rates during the year under review was a relatively high degree of stability, and most changes in nominal interest rates can be accounted for by fluctuations in the base interest rate, the interest rates prevailing on the money market were oscillating considerably. During the first quarter of 2000, there was an upward movement in inter-bank interest rates and this upward trend persisted until May 2000. At the time, the movement of this interest rates was following the movement in the interest rate for temporary purchase of 28-day bills denominated in foreign currency with obligation to repurchase. As from July 2000, the interest rate quoted at auctions of temporary repurchase of 60-day bills denominated in foreign currency steadily increased, followed by less pronounced growth in interest rates at the end of the first six months of 2000 on seven-day temporary repurchase of bills denominated in foreign currency, while the inter-bank interest rate started to go down after July 2000, The Bank of Slovenia namely rose the basis of interest rate on temporary purchase of bills denominated in

Figure 6: **Average interest rates by banks**
(above base interest rate, in % p.a.)



Source: Bank of Slovenia

foreign currency five times in 2000. The interest rate increased from 7.8 per cent in January to 10.5 per cent in December and thus strengthened restrictive monetary policy. The movement in inter-bank interest rates has changed since the agreement between the Bank of Slovenia and twenty-two banks on participation of banks in interventions on the foreign exchange market; hence, the interest rate changed at least up to a point as a result of developments in the foreign exchange market. During the period when the Bank of Slovenia intervened in the foreign exchange market by means of the intervention exchange rate (this happened from 19 July until 18 September 2000 and from 27 October until 14 November), the interest rate decreased sharply. Before and after the intervention period, the interest rate was increasing or at least it was stagnating depending on the current liquidity of the banking system. Thus in 2000, the inter-bank interest rate under the described fluctuations between 8.1 and 6.1 per cent averaged 6.3 per cent.

Movement in interest rate instruments of BoS in accordance with restrictive monetary policy management

In line with the austerity in defining and implementing monetary policy, the Bank of Slovenia has also changed most of other monetary policy instruments derived from interest rates. Discount and Lombard interest rates have gone up twice, viz. in June from 8 to 9 per cent, i.e. Lombard interest rate from 9 to 10 per cent and in December from 9.0 to 10.0 per cent, i.e. from 10.0 to 11.0 per cent. Otherwise, interest rates in 2000 went up for the first time already at the end of February when interest rate on overnight liquidity facility rose by 0.2 percentage point. At the end of March, interest rates on liquidity facility granted on the basis of pledging twelve-day tolar bills as collateral, and interest rates on two- and twelve-day bills went up. In the second half of 2000, namely in September, November and December interest rates were rising steadily predominately on tolar bills. The strongest rise in interest rates was in the group of 60- and 270-day tolar bills outpacing the group of bills with shorter maturity periods. Thus the interest rate on a three-day liquidity loan in 2000 increased from 5.7 per cent to 7.0 per cent, the interest rate on two-day tolar bills went up from 1.7 per cent to 5.0 per cent, twelve-day bills from 3.2 per cent to 7.0 per cent, and 60- and 270-day tolar bills from 7.5 to 10 per cent and from 9.0 to 11.0 per cent, respectively.

Movements in interest rates on foreign currency bills kept abreast of interest rates on the euro-money market

When determining interest rates for bills denominated in foreign currency, the Bank of Slovenia took into account changes in interest rates on instruments with the same maturity offered on the euro-money market. Thus interest rates in January 2000 on

Table 7: **Interest rates of the Bank of Slovenia and the money market**
(monthly average balances in 2000, interest rate in %, annualised)

	Temporary repurchase		Lomard loan	Bank of Slovenia tolar bills		Money market	Treasury bills			Base interest
	7 days	2 months	5 days	12 days	60 days	up to 30 days	3 months	6 months	12 months	
January	-	8.07	9.00	3.20	7.00	6.87	10.41	9.50	-	8.58
February	-	8.24	9.00	3.20	7.00	7.12	10.61	10.50	-	9.20
March	-	8.74	9.00	3.27	7.77	6.99	10.27	10.50	-	8.58
April	-	8.90	9.00	4.00	8.00	7.54	10.51	11.38	-	8.88
May	9.39	8.79	9.00	4.00	8.00	8.11	12.05	11.38	12.83	9.86
June	9.36	9.39	10.00	4.00	8.00	7.57	12.14	12.38	12.83	8.88
July	9.04	9.36	10.00	4.00	8.00	7.23	11.54	12.38	12.76	9.86
August	9.00	9.04	10.00	4.00	8.00	5.33	10.60	11.67	12.76	8.58
September	9.53	9.00	10.00	6.00	8.50	6.26	10.52	11.67	11.76	8.88
October	9.60	9.53	10.00	6.00	8.50	7.02	10.57	11.36	11.76	8.58
November	9.64	9.60	10.00	6.28	8.92	6.15	10.58	11.36	11.75	8.88
December	10.93	9.64	11.00	7.00	10.00	7.22	11.51	11.49	11.75	9.86

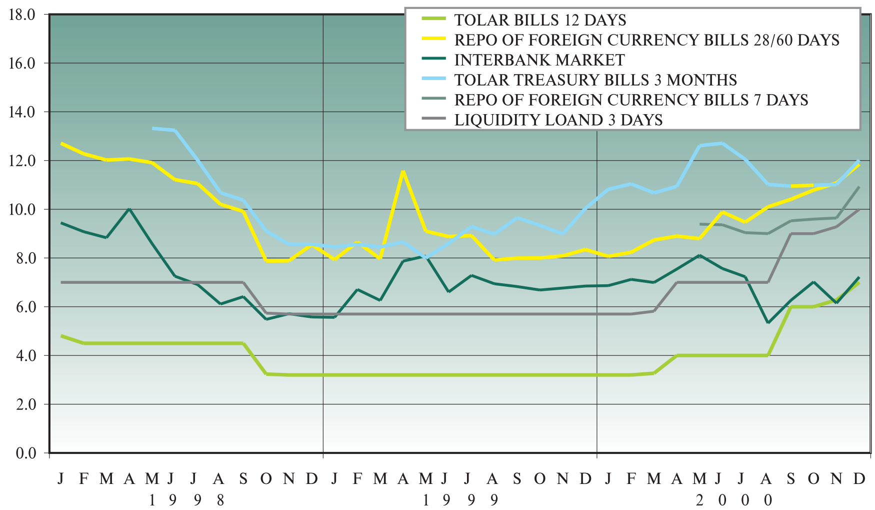
Source: Bank of Slovenia

euro-denominated bills ranged from 3.31 per cent on 60-day bills to 3.43 per cent on 360-day bills, while for bills denominated in US dollars the span was from 6.02 per cent on 60-day bills to 6.16 per cent on 360-day bills. At the end of 2000, interest rates on bills denominated in euro reached the value of 4.76 per cent on 60-day bills and 4.68 per cent on 360-day bills, while for bills denominated in US dollars the span was from 6.42 per cent on 60-day bills to 6.00 per cent on 360-day bills.

A wider range of treasury bills offered by Ministry of Finance

Among key instruments structured to facilitate the functioning of the money market with regard to fluctuations in interest rates in 2000 there were also three- and six-month treasury bills issued by the Ministry of Finance of the Republic of Slovenia. As from May 2000, the Ministry of Finance added to the spate of its instruments twelve-month treasury bills. The prices of these securities reached at monthly auctions moved in a similar way. Nevertheless, the movements in these prices were in different brackets and were alternated by offering six- and twelve-month bills. The yield achieved upon maturity of three-month treasury bills on the primary market increased from January to the end of the year under review by 1.2 percentage points, i.e. from 10.8 per cent to 12.0 per cent. The record high interest rate values were achieved at half year (12.7 per cent). In the case of six-month treasury bills, the yield upon maturity ranged beween 10.8 per cent at the February auction and 11.8 per cent at December auction. However, average annual yield on six-month treasury bills exceeded by 0.2 percentage points the average yield on three-month treasury bills. As regards the interest rate on treasury bills with one year agreed maturity period, it could hardly be representative since only four auctions took place in 2000. The yield until maturity was gradually decreasing from the initial 12.9 per cent to 11.7 per cent at the end of 2000.

Figure 7: **Interest rates of the Bank of Slovenia and the money market**
(monthly average above base interest rate in % p.a.)



Source: Bank of Slovenia

2.3. Foreign exchange market and exchange rates

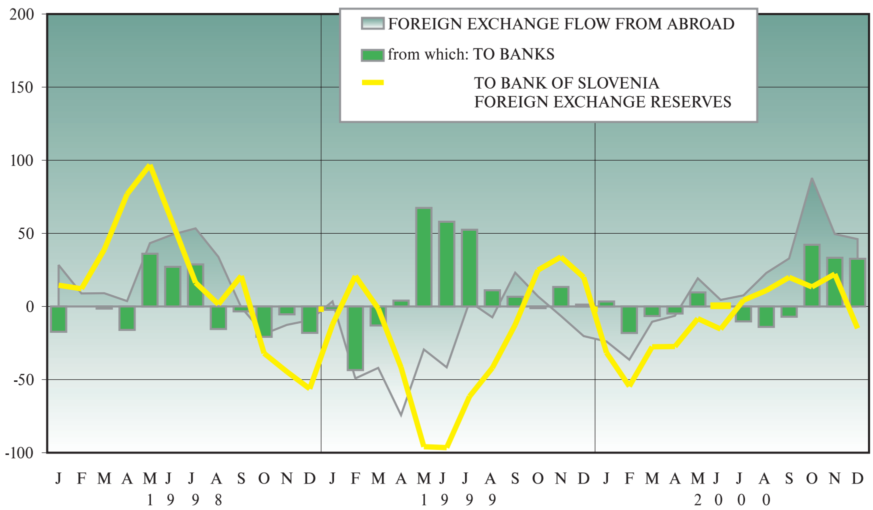
Impact of movements in balance of payments and investment policy

The developments in the foreign exchange market in 2000 were strongly affected by movements in the balance of payments and decisions made by economic subjects with regard to placements of their assets. Intense cross-border borrowing has fed through vigorous financial inflows and topped 1055 million US dollars at year-end (record high after Slovenia's independence) and went entirely towards financing deficit in curent transactions in the amount of 594 million dollars and boosted foreign exchange reserves of the banks and the Bank of Slovenia by 461 million dollars. On the other hand, balance of foreign exchange deposits of individuals since the end of 1999 until the end of 2000 increased by 212 million dollars to 2,523 million dollars, the balance on accounts of the non-financial enterprises sector in foreign currency rose by 149 million dollars to 303 million dollars. The sum of the two items increased foreign exchange liabilities of banks by 361 million dollars, which in addition to the requirements to adjust their foreign exchange positions spurred their demand for foreign currency.

Three distinct periods on foreign exchange market

The developments on the foreign exchange markets in 2000 could be divided in three periods. The main feature of the first quarter was strong demand for foreign exchange that exceeded supply, the second quarter saw balanced supply of and demand for foreign exchange, while the strong supply of foreign exchange that exceeded demand was the characteristic of the second half of the year. The aggregate net sales realised by the banks on the foreign exchange market and by the exchange offices in the first quarter of 2000 totalled 139.7 million US dollars in foreign exchange, in the second quarter the banks realised net purchase in the amount of 9.8 million dollars, and in the second half of the year they purchased foreign exchange in the value of 272 million dollars (including net offer of non-residents in the ammount of 236 million dollars). Throughout 2000, the banks purchased foreign exchanges on the foreign exchange market net 182 million dollars, and through the exchange offices sold net foreign cash in the value of 40 million dollars.

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



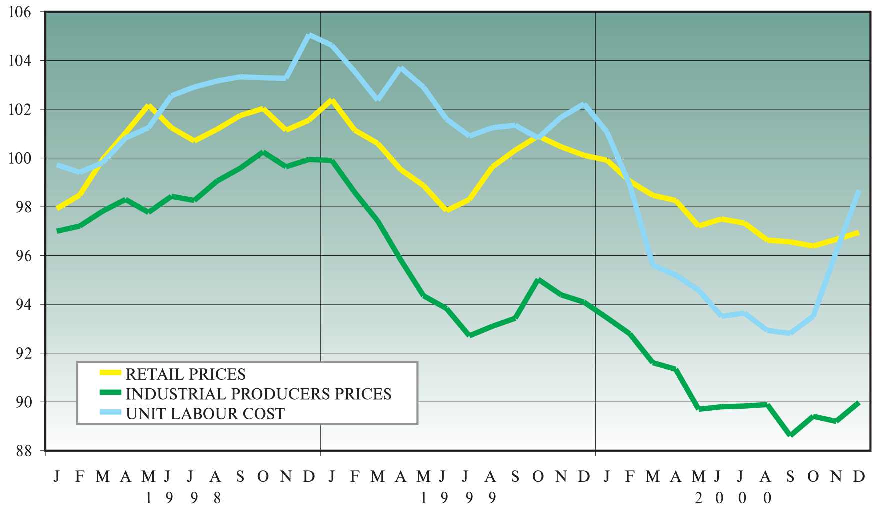
* Inflow from the rest of the world withouth direct flows from abroad to the Bank of Slovenia (interests, etc. and reduced for net payments from foreign exchange account of the government).

Source: Bank of Slovenia.

Fuelled by demand for foreign currency in the foreign exchange market that exceeded supply, the exchange rate for D-mark in December 1999 and during the first two months in 2000 increased by 0.8 per cent. To smooth out the imbalance in the foreign exchange market and stabilise the exchange rate, the Bank of Slovenia offered the banks to »purchase foreign exchange to underwrite 120-day bills denominated in foreign currency«. During the first three months, the banks purchased from the Bank of Slovenia foreign exchange in the counter value of 245 million dollars. The temporary repurchase instruments, i.e. purchase of foreign exchange under the covenant to repurchase, i.e. sell foreign exchange within 60 days, have enabled the banks to manage foreign exchange liquidity more easily. By means of increased supply of foreign exchange and short response time to the movements in exchange rates applied on its instruments, the Bank of

Slovenia was in a position to slow down growth in exchange rates. Growth in the exchange rate for D-mark fell in March to 0.7 per cent. As of 24 March 2000, the Bank of Slovenia entered into a new agreement on participation with twently-two banks. Under the new agreement the said instruments were discontinued and replaced by a seven-day temporary purchase and selling of foreign exchange with contractual repurchase. The change has enabled the Bank of Slovenia to steer the exchange rate policy in a more transparent and effective manner, while the banks have obtained easier and cheaper (surcharge of 1 per cent) management of tolar and foreign exchange liquidity. The average dynamics of changes in the exchange rate was stable in the second quarter at around 0.6 per cent. Due to accelerated growth in exchange rates in June and at the beginning of July, the Bank of Slovenia intervened in the foreign exchange market during the period from 18 July until 19 September by determining the base exchange rate with the aim to curb growth in exchange rates. In July, growth of D-mark slowed down to 0.5 per cent, in August to 0.3 per cent, while in September and October it was 0.4 per cent. Between 27 October and 14 November, the Bank of Slovenia intervened again in the foreign currency market by determining the base exchange rate with the purpose to revive its growth. During the last two months, growth in the exchange rate in the foreign exchange market averaged 0.6 per cent.

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



Source: Bank of Slovenia

Fluctuations in exchange rate for D-mark in exchange offices in 2000 were more or less in line with the exchange rate in foreign exchange market with the exception of two short periods when the exchange rate for D-mark rose in exchange offices faster - 0.9 per cent in February and June.

Exchange rate of exchange offices generally in line with rates on foreign exchange market

Throughout the year 2000, the exchange rate for D-mark in the foreign exchange market increased by 7.1 per cent to 108.8 tolars for one D-mark, while on the menjalniškem market D-mark grew by 7.2 per cent to 108.7 tolars. Nevertheless, growth in the exchange rate for D-mark lagged behind the increase in consumer prices (8.9 per cent), retail prices (10.6 per cent) and prices of industrial products (9.2 per cent).

Nominal effective exchange rate (measured by weights of foreign trade basket of currencies) in 2000 increased by 9.8 per cent, a rise of over 3 percentage points vover the rise of D-mark and one percentage point above the inflation rate, mainly due to growth in the value of US dollar.

Real effective exchange rate. During the year under review, the tolar depreciated in real terms 4.6 per cent, as measured by the ratio between the change in exchange rate and the ratio between foreign and domestic producer prices by 3.6 per cent as opposed to relative labour costs per unit of production. The lowest depreciation of the tolar was 3.3 per cent, compared to consumer price index. Real depreciation varied from one currency to another, but the sharpest drop in the value of the tolar was against US - 12.7 per cent – and the slightest was against the euro - 0.6 per cent.

Real depreciation of tolar between 3.3 and 4.6 per cent

2.4. Instruments used

The objective of monetary policy has been set out by taking into consideration activities of foreign exchange rate policy, changes in cash in circulation, deposits of the Republic of Slovenia, as well as other activities of the Bank of Slovenia, on the side of instruments it was reflected in considerable reduction in tolar bills, aggregate balance of temporary foreign exchange repurchase bills and lending.

Monetary policy instruments

Lending facilities

Lending facilities made available by the Bank of Slovenia were not so crucial in the year 2000 as in 1999, and average annual balances of outstanding lending facilities dropped from 1.6 billion tolars in 1999 to 0.7 billion tolars in 2000. During the year under review, the volume of lending peaked in February and was again high between April and July.

Declining importance of Bank of Slovenia loans

Lombard loans are availabe to banks on the basis of the open tender as five-day facilities at the interest rate one percentage point above the discount rate. Due to a rise in the discount rate, the interest rate on Lombard loans increased from 9.0 to 10.0 per cent as at 1 June 2000 and to 11.0 per cent as at 1 December. The percentage available to the borrowing bank to be drawn against securities pledged as collateral was raised from 2.5 to 5.0 per cent in December 1999, was again reduced to 2.5 per cent at the beginning of 2000, and as from 17 April 2000 onward, this percentage is again 5.0 per cent.

The banks resorted to Lombard loans in December 2000, while the average outstanding balance was 367 million tolars.

Liquidity loans are mainly made available to banks for the purpose of steering short-term tolar liquidity of the banking system. In 2000, the average balance of liquidity lending amounted to 190 million tolars (as opposed to 1.2 billion tolars in 1999). The banks drew these loans on the basis of bills pledged as collateral (66.0 per cent of average balance of entire liquidity lending) overnight liquidity loans (24.0 per cent), and liquidity loans of last resort (11.0 per cent).

On the basis of tolar bills the banks may tap into lending facility for three, i.e. five working days on the basis of subscribed 12-, i.e. 30-day tolar bills. The instrument of a five-day loan on the basis of 30-day bills was discontinued at the end of March 2000.

Overnight liquidity loan is made available by the Bank of Slovenia with the aim to influence inter-bank interest rate or in the case of imbalance between demand and supply on the inter-bank money market. The Bank of Slovenia offered this kind of facility due to impaired liquidity of the banking system between January and July 2000, though the interventions were limited to the days when higher volume of transactions in the payment operations called for higher balance on settlement accounts (the days when VAT and excise duties fall due, and on the pay-day for pension benefits).

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

	Balance 12/31/99	Average daily balance per quarter in 2000				Balance 12/31/00
		I.	II.	III.	IV.	
Loans to banks	**3,077**	**828**	**888**	**367**	**687**	**112**
Lombard loans	859	75	667	201	523	0
Liquidity loans	2,065	601	89	34	52	0
Other*	152	152	132	132	112	112
Temporary purchase of bills	**18,550**	**24,813**	**25,349**	**11,651**	**6,279**	**6,299**
Bank of Slovenia tolar bills	**28,046**	**30,616**	**14,279**	**11,679**	**10,506**	**6,946**
Tolar bills	17,629	19,652	11,475	11,679	10,506	6,946
– 60 and 270 days	11,529	14,080	10,497	8,300	7,409	5,675
– Other	6,101	5,571	978	3,379	3,096	1,270
Twin bills	1,386	2,903	0			
Bills with warrants	9,031	8,062	2,805			
Cumulative effect of government time deposits and supplementary shortterm lending	**0**	**5**	**-31**	**0**	**0**	**0**
Accepted government deposits	0	369	1,315	0	0	0
Supplementary short-term lending facility	0	374	1,284	0	0	0
Reserves of banks and saving banks**	**84,222**	**81,453**	**83,220**	**85,285**	**87,295**	**89,380**
Required	79,322	77,789	80,537	82,727	84,187	85,113
Excessive reserves	4,900	3,664	2,683	2,558	3,108	4,267
Foreign exchange minimum of banks	**446,609**	**463,090**	**494,738**	**523,851**	**560,007**	**569,696**
Bills denominated in foreign currency	**306,604**	**320,958**	**326,017**	**337,759**	**349,630**	**357,633**
Temporary purchase of foreign exchange	**3,858**	**3,481**	**10,603**	**7,539**	**9,640**	**15,535**
Temporary sale of foreign exchange		**0**	**1,600**	**5,014**	**1,763**	**213**

* Long-term selective lending facility granted prior to monetary independence.
** Reserve requirement, surplus and cumulative reserves as at 31 December represent average for December.
Source: Bank of Slovenia; excluding accrued interest and discount.

Liquidity loan of last resort is available against securities pledged as collateral and the banks may tap into this facility on the basis of open supply charged at legal late interest rate. In 2000, the banks used this facility only in January.

As regards special liquidity loan with participation of banks, the Bank of Slovenia signed the fifth consecutive agreement in 2000 under which the banks agree to participate in the provision of liquidity loans with 21 banks. The banks signatories of the agreement are entitled to remuneration in the amount of 1.5 per cent of the amount of the stand-by facility. Also in 2000, there was no need to reach for the facility.

Temporary purchase of foreign currency bills

Within the framework of its operations in the open market aimed at providing sources of liquidity to the banks, the Bank of Slovenia changed its offer in 2000 in the segment of temporary purchase of foreign currency bills with obligatory repurchase In the middle of the year, the instrument available since April 1994 under which the Bank of Slovenia offered to the banks at daily auctions to purchase foreign currency bills, obliging them to repurchase the bills after 28 days, was replaced by two new instruments.

Two new instruments under temporary purchase of foreign currency bills

The first new instrument was a 7-day bill denominated in foreign currency with obligatory repurchase, which enables the banks to manage their intra-month liquidity. This instrument enabled Bank of Slovenia to react more actively to the developments in the money market by changing daily the quota of these repo bills. The second new instrument was a 2-month foreign currency bill with obligatory repurchase (repo) that the Bank of Slovenia uses to steer part of base money growth in a longer run.

In the case of 28-day repo bills, the amount provided to the banks on a daily basis (daily quota) ranged between 2.5 and 12 million euros, while in the case of 7-day repo bills, the amount offered daily varied between 2.5 and 9 million euros. As regards the quotas for 2-month repo bills, the Bank of Slovenia allotted to the bidders between 5 and 12 million euros at auctions held on a regular basis twice a month as from 11 July onward. The average balances of aggregate temporary purchases were rising until April, and then started to fall until the end of the year.

Bills denominated in tolars

Less tolar bills offered to banks only…

During the period under review, the Bank of Slovenia mainstreamed the array of bills denominated in tolars offered to different groups of investors. All securities made available to the general public were discontinued, also for the non-financial enterprises sector and individuals. The roster of maturities of tolar bills was also reduced. The total value of outstanding tolar bills, *viz*. simple tolar bills, bills with warrants and twin bills, decreased from 28 billion tolars at the end of 1999 to 7 billion tolars at the end of 2000.

…significantly reduce value of subscribed tolar bills.

Tolar bills are dematerialised nontransferable securities, offered by the Bank of Slovenia to the banks and savings banks through open tenders. Only the banks may subscribe non-serial 2-, 12- and 30-day bills, 7- and 14-day bills are reserved for the savings banks, while 60- and 270-day bills, which are issued only in series, are available to both banks and savings banks. The banks could subscribe 28-day bills (the only discounted bill) at regular weekly auctions. At the end of March, the Bank of Slovenia discontinued 7-, 14-, 28 and 30-day tolar bills. The balance of outstanding bills with maturity of 60 and 270 days was decreasing, while the balance of outstanding bills with shorter maturity periods (up to but not over 30 days) was changing along with the excess liquidity of the banks and savings banks.

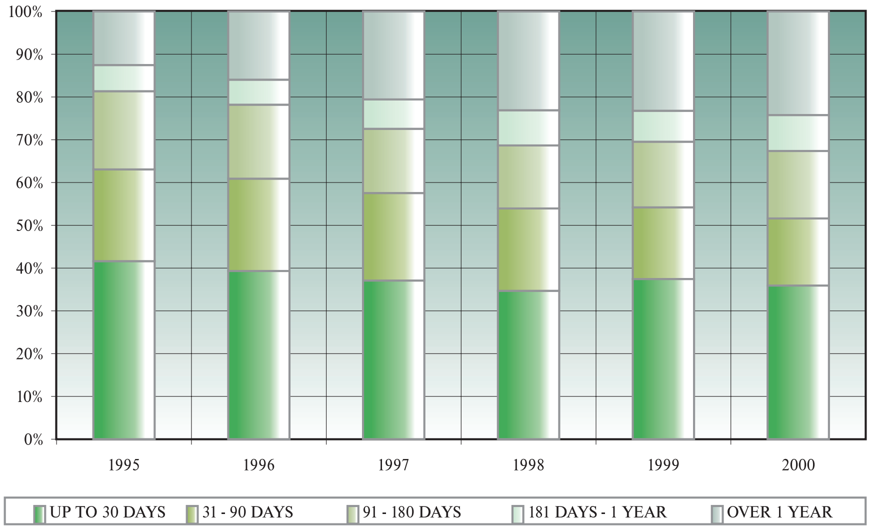
Twin bills are serial and materialised securities issued to a bearer subscribed at discount and denominated in tolars. These bills are redeemed and interest accrues in two parts: the tolar part is revalued at base interest rate, and the foreign currency part redeemable in D-marks. In March 2000, the Bank of Slovenia redeemed from the holders the final 12th issue of twin bills (issued in April 1999).

Bills with warrants are transferable, serial, dematerialised registered securities with nominal interest rate and maturity of six months, subscribed at a discount. A warrant composed of several detachable parts is attached. The holders of warrants may use the bill (without the warrant) to purchase a new bill in tolars or a bill denominated in foreign currency with maturity over 120 days at a discount. The amount of such discount depends on the rise in prices, i.e. the rise in middle exchange rate of the Bank of Slovenia benchmarked against official inflation estimates and the number of warrants, which the holder may submit for redemption upon the purchase of a new bill. The Bank of Slovenia was issuing these bills from 1 June 1994 until 1 December 1999, when the last issue was placed on the market – the 14th issue without warrant. Investors could claim in 2000 the discount in the amount of 25.7 million tolars upon the subscription of the 14th issue of these bills. The Bank of Slovenia redeemed on 1 March the 13th, and on 25 May the last, 14th issue of bills with warrants.

Mandatory reserves

The required minimum reserves of banks, savings banks and savings and loan undertakings authorised to engage in banking business in Slovenia are calculated on all deposits in tolars, loans taken and securities issued held by the non-bank sector. The ratio between the mandatory reserves (also referred to as obligatory reserves) and their basis depends on the maturity structure of deposits: 12.0 per cent for deposits repayable on demand (sights deposits) and deposits repayable within thirty days, 6 per cent on time deposits between thirty-one days up to three months, 2 per cent on time deposits above three and less than six months, 1.0 per cent above six months up to one year, and zero per cent on time deposits above one year.

Figure 10: **Average structure of tolar deposits**
(1995 – 2000)



Vir: Banka Slovenije.

Mandatory reserve requirement basically unchanged

For the purpose of compliance, eligible assets include cash balances and balances on settlement accounts (for the banks, which are direct participants in the real-time gross settlement system – the RTGS), i.e. on special accounts earmarked for mandatory reserves (indirect participants in the RTGS). The assets in the settlement, i.e. the special account earn interest at one-per cent annual interest rate, albeit only up to the amount of the caclulated mandatory reserves for the preceding month. Since December 2000, the banks participating in the National Housing Savings Scheme, have been allowed to comply with the entire liability arising from the assets gathered under the Scheme by pledging as collateral subscribed 60-day tolar bills issued by the Bank of Slovenia.

The **basis for mandatory reserves** increased in 2000 by 11.7 per cent (as opposed to 13.5 per cent in 1999) and amounted to 1,525 billion tolars in December 2000. Time deposits due within one year grew by 10.6 per cent, deposits due over one year rose by 15.2 per cent, and their structural share increased to 24.2 per cent.

Average reserve rate falls to 5.6 per cent

The **calculated reserve requirement** (according to stipulated rates with regard to maturity of deposits) grew by 7.3 per cent over a year's period to 85.1 billion tolars in December 2000. The average mandatory reserve rate on aggregate tolar deposits was decreased due on a change in the structure in favour of deposits placed on a longer term by 0.3 percentage points compared to the year 1999 when the reserve requirement was 5.6 per cent. Furthermore, the average rate of calculated reserves based on deposits due within one year fell during the year under review and averaged 7.5 per cent (1999: 7.7). per cent).

Box 3: **National housing savings scheme**

The Act on the National Housing Savings Scheme was adopted on 11 October 2000 (Official Gazette of the Republic of Slovenia, No. 86/00). The Act set out terms and conditions of annual tenders for savings for residential property, selection criteria for banks authorised to collect deposits and grant housing loans, terms and conditions of savings, reporting and oversight of the implementation of the scheme, as well as other details in connection with the implementation of the scheme. The savings contract under the savings scheme may be concluded for the period of five or ten years, depositors may pay monthly or annual deposits. A premium is credited to the balance on the savings account at the end of each year from the budget by the Housing Fund of the Republic of Slovenia. Upon maturity, the depositor is eligible for a long-term housing loan with the repayment period twice the savings one. The amount of the loan is at least a double amount of the saved amount (including accrued interests and premiums).

Article 4 of the Act on the National Housing Savings Scheme defines assets obtained on the basis of the National Housing Savings Scheme as long-term ones; hence these assets are not subject to the mandatory reserve requirement. Under Article 43, this provisions also applies if a bank meets the provisions laid down in the Act even relating to assets under the first National Housing Savings Scheme from the year 1999, prior to the effectiveness of the Act on the National Housing Savings Scheme (the legal basis for the first scheme was a decision adopted by the Government of the Republic of Slovenia). On the other hand, the provisions of the scheme leave the door open to depositors to abandon the scheme and the bank has to pay back the (at notice in the first scheme and within 100 days in subsequent ones). From the angle of exposure to liquidity risk, the assets gathered under the scheme have features of deposits repayable on demand (at notice within one day, i.e. within 100 days). In accordance with the effective mandatory reserve requirement set out in the Law on the Bank of Slovenia, for the purpose of mandatory reserves these assets bear a 12 per cent, i.e. 2 per cent rate.

On the basis of the findings on the collision between legal acts and the invasion of the Act on the National Housing Savings Scheme into the area of the central bank's responsibility guaranteed by the Constitution, as well as in the light of effectiveness of the provisions of the Act into the first savings scheme in arrears, the Bank of Slovenia petitioned the Constitutional Court of the Republic of Slovenia to rule on the conformity of the said provisions with the Constitution. Until the Constitutional Court does not make its ruling, the banks are entitled to meet the entire reserve requirement arising from the assets gathered under the National Housing Savings Scheme by subscribing 60-day bills of the Bank of Slovenia, which makes the instrument income-neutral.

The **actual reserves** on average exceeded the reserve requirement by 3.7 per cent (1999: 3.2 per cent). The banks averaged the lowest percentage of overshooting the reserve requirement, as opposed to the savings banks, which were well above the regulatory minimum. The daily holdings on the settlement, i.e. special account shall reach at least 50 per cent of liabilities for the preceding month. The banks and savings banks may use such holdings for overnight liquidity settlement only against payment of interest equal to the legal penal rate.

Deposits from the Central Government and supplementary short-term lending facility

The Bank of Slovenia accepts deposits of the Ministry of Finance on the basis of the Decision on Conducting Operations for the Republic of Slovenia and the contract agreement. The impact of transfer of time deposits from commercial banks to the Bank of Slovenia has been offset by a supplementary short-term facility offered by the Bank of Slovenia to the commercial banks in adequate amount and with similar maturity. In 2000, the Bank of Slovenia accepted six deposits due within eleven days (all in the first half of the year). The daily balance of these deposits averaged 421 million tolars exceeding the average balance of supplementary short-term facility by 7 million tolars.

Foreign exchange rate policy instruments

In line with its core purposes, the Bank of Slovenia steers the foreign exchange rate by means of various instruments. Through final and temporary buying and selling of foreign exchange, the Bank encourages supply, i.e. demand in the foreign exchange market. Furthermore, within the framework of the agreement between the Bank and

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

	1999		2000	
	EUR million	SIT billion	EUR million	SIT billion
Final purchase of foreign exchange	**169.3**	**32.7**	**217.4**	**44.2**
Interventions involving buying or base exchange rate	39.0	7.5		
Payment and other operations for Central Government	130.3	25.2	217.4	44.2
Final selling of foreign exchange	**391.3**	**76.3**	**285.3**	**57.5**
For purchase of foreign currency bills	333.3	65.1	245.0	49.3
Interventions with selling or base exchange rate	6.5	1.3		
Payment and other operations for Central Government	51.5	9.9	40.3	8.2
Temporary purchase and repurchase of foreign exchange	**139.0**	**27.0**	**2,271.2**	**471.9**
Temporary purchase of foreign exchange (open bid)	10.0	1.9		
Temporary purchase under contract – two months	129.0	25.2	18.5	3.7
Temporary purchase under contract– one week			1,727.6	359.0
Repurchase of foreign exchange (open bid)				
Repurchase under contract – two months				
Repurchase under contract – one week			525.1	109.2
Repurchase of foreign exchange	**119.5**	**23.5**	**2,218.6**	**460.5**
Temporary sale under contract – two months				
Temporary sale under contract – one week			526.1	109.4
Resale of foreign exchange (open bid)	10.0	1.9		
Resale under contract– two months	109.5	21.6	38.0	7.6
Resale under contract – one week			1,654.5	343.5

* Calculated at the current exchange rate for SIT/DEM and DEM/EUR.
Source: Bank of Slovenia.

commercial banks on their participation in interventiona in the foreign exchange market (for details see Box 4), it conveys exchange rate policy signals and constrains the span in exchange rates, applied when the banks enter into deals with counterparties. The exchange rate may also be managed by means of issuing bills denominated in foreign currency,

By regulations, which cap the banks' assets held in certain currencies, i.e. limit certain kinds of instrumenta (foreign exchange minimum and open position in foreign currency), as well as thorugh changes in capital inflow and outflows.

Purchase and sale of foreign exchange

In 2000, the Bank of Slovenia was selling foreign exchange to banks and was buying foreign exchange from them on the basis of bid made to all banks, and on the basis of instruments derived from the agreements to participate in the interventions of the Bank of Slovenia in the foreign exchange market. The Bank also purchased and sold foreign exchange for cross-border payment transactions within the framework of the execution of the budget, and in relation to any other business carried out for the account of the Central Government.

Shrinking net tolar issue through foreign exchange transactions

In 2000, the Bank of Slovenia bought foreign exchange from banks and the Central Government in the amount of 516.1 billion tolars and sold them foreign exchange for in the amount of 518.0 billion tolars. These operations together with redeemed parts of twin bills in foreign currency reduced the **net cumulative issue of tolars from foreign exchange transactions** for 15.5 billion tolars to 164.3 billion tolars.

Box 4: **Contractual participation of banks in foreign exchange market interventions**

The Bank of Slovenia signed the agreement on the participation of commercial banks in interventions on the foreign exchange market with the first banks at the end of 1997. The terms and conditionsof the agreement, which was amended by an annex to the agreement signed at the end of 1999, laid down mutual rights and obligations in the following cases: (1) intervention buying rate, (2) intervention selling rate, (3) determining maximum margin between buying and selling rates applied by the banks, and (4) temporary purchase of foreign exchange and (5) temporary sale of foreign exchange for the period of two months. The Bank of Slovenia remunerated the banks signatories of the agreement for opportunity costs associated with contractual obligations (for an in-depth description see the Annual Report of the Bank of Slovenia for 1999, box 8, page 40).

As a result of institutional changes, primarily due to the introduction of foreign exchange accounts for legal persons and the possibility for cross-border investment in securities, volatity in foreign currency flows has substantially increased. Therefore, the Bank of Slovenia moved at the beginning of the year 2000 to amend the nature of the contractual relationship under the agreement. The new agreement effective as from the beginning of April 2000 onward, and has been signed by twenty-two banks. The landmark changes compared to the old agreement are summarised below:

- During the period of intervention, i.e. when it estimates that the conditions in the foreign exchange market are not in line with exchange rate policy target, the Bank of Slovenia will **determine the base exchange rate**, which the banks signatories of the agreement shall comply with and apply on all operations in the foreign exchange market along with the ceiling margin rate. During the periods when the Bank of Slovenia does not intervene by setting the base exchange rate, the banks may determine buying and selling exchange rates at their discretion.
- The Bank of Slovenia provides to the signatories of the agreement **the standing facility to purchase or sell foreign exchange on a temporary basis for the period of one week**, at the implicit interest rate of one per cent p.a. These buying or selling deals are concluded on a temporary basis at the base exchange rate, and in its absence, at average market exchange rate.
- Irrespective of the intervention to determine the base exchange, the Bank of Slovenia may **buy from the banks signatories of the agreement or sell to them foreign exchange through final transactions,** whereby it directly reduces the accumulated balance of temporary purchase, i.e. sale of foreign currency.

Through **final transactions,** the Bank of Slovenia only sold foreign exchange to the banks against subscription of bills denominated in foreign currency. Thus the banks purchased from the Bank of Slovenia 245 million euros in the countervalue of 49.3 billion tolars.

Temporary forex-related transactions gain importance

As regards **temporary transactions** involving foreign currency, the amount of purchases and sales increased significantly compared to previous years; on the one hand, this was due to shorter maturity of instruments of temporary sale and purchase (from two months down to one week), and on the other hand it was a result of a more frequent application of these instruments. The Bank of Slovenia made a temporary purchase of foreign exchange in the aggregate amount of 362.7 billion tolars, and sold on a temporary basis foreign exchange totalling 109.4 billion. By taking into account reverse part of operations, the base money increased by 11.4 billion tolars in 2000.

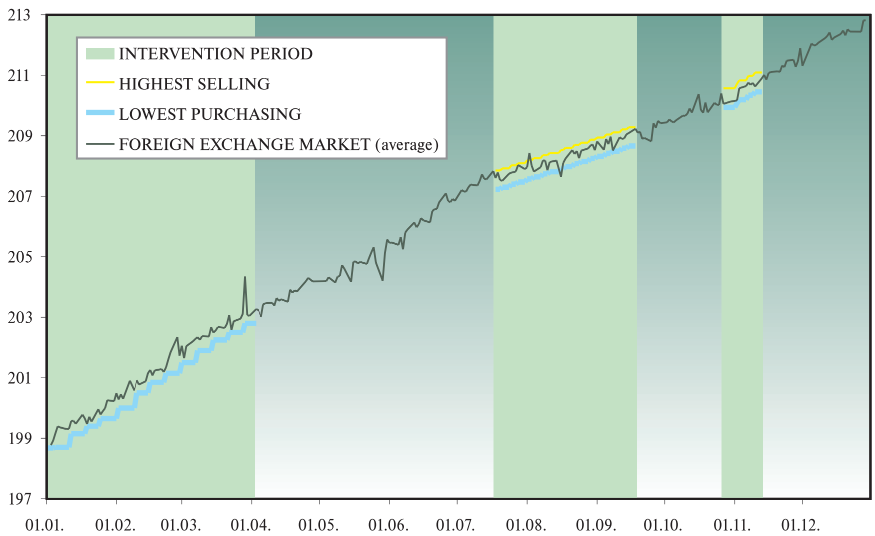
Conveying exchange rate policy signals

Participation of banks in interventions in foreign exchange market

In 2000, or more precisely during the effectives of the first agreement with the »Club of Banks« until the first days of April, the Bank of Slovenia did not directly intervene in the foreign exchange market by intervention buying or selling exchange rate. Throughout the said period, under the exchange rate regime, the Bank of Slovenia determined to the banks, signatories of the agreement, which were selling to the the Bank of Slovenia foreign exchange on a temporary basis, floor buying rates. Nevertheless, such interventions did not have any serious impact on fluctuations of market exchange rates during the periods of self-regulating growth in exchange rates.

After the new agreement was concluded with the "Club of Banks", the Bank of Slovenia intervened twice in the market by setting the base exchange rate and by modelling through it the ceiling and the floor buying exchange rate. The first intervention was in force from the middle of July until the middle of September, the second one lasted from the end of October until the middle of November. By means of the first intervention the Bank of Slovenia was curbing too fast and by the second one it was giving impetus to growth in the market exchange rate.

Figure 11: **Exchange rates in foreign exchange market** (in SIT/EUR) **during intervention periods**



Source: Bank of Slovenia.

Foreign currency bills

The Bank of Slovenia issues bills denominated in foreign currency as short-term, transferable, registered, non-serial and non-materialised securities sold through open supply. Subscribed at a discount and denominated in the euro (as from February 1999 onward; prior to that date in D-marks) or US dollars. Due to the change in foreign exchange legislation, and particularly due to the introduction of the possibility for legal persons to open foreign exchange accounts with domestic banks, the Bank of Slovenia limited at the beginning of May 2000 subscription of bills to the domestic banks, as opposed to the previous period when other domestic legal persons were also eligible. The Bank of Slovenia adjusts interest rates on its bills to interest rates prevailing in foreign money markets.

Subscription of foreign currency bills limited to banks

Until February 2000, investors could claim a discount when subscribing a bill with maturity of 180, 270 or 360 days on the basis of parts of the warrant. The amount of the discount depended on the difference between movements in middle exchange rate of the Bank of Slovenia and estimated inflation and on the number of presented warrants, within the framework of the correspondent issue of bills with warrants.

Bills in foreign currency are eligible as collateral for banks to participate in most lending facilities made available by the Bank of Slovenia. These bills may be pledged as collateral for Lombard loans or may be sold to the Bank of Slovenia on a temporary basis. Likewise, these bills may be sold to the Bank of Slovenia as collateral for liquidity and short-term borrowing, while underlying assets under the bills are also eligible as collateral for securing deals made.

The bulk of demand for bills denominated in foreign currency derives from the foreign exchange minimum requirement. The banks regulated by the Bank of Slovenia have to meet at least 60.0 per cent of their statutory commitment by investments in bills denominated in foreign currency due within 120 days. This kind of bills accounted for 96 per cent of aggregate balances.

In December 1999, the banks held in their portfolios on average 310.9 billion tolars in foreign currency bills. In April and May, the average outstanding respective balance slightly dropped, but the general trend during the year under review was upward, climbing to 360.5 billion tolars in December 2000 – a 16.0 per cent rise January to December.

Foreign exchange minimum (liquid assets of banks in foreign currency)

For the purpose of ensuring general liquidity in cross-border payments, and with the aim to meet liabilities arising from foreign exchange deposits placed by residents and non-residents, the Slovenian banks shall comply with the requirement to have holdings in foreign currency and liquid foreign exchange assets abroad that meet the foreign exchange minimum requirement on a daily basis (minimum daily working balances in foreign currency).

No change in methodology for calculation of foreign exchange minimum

During the year under review, the Bank of Slovenia did not make any amendments and/or modifications to the methodology introduced in 1999 for the calculation of the foreign exchange minimum. Nevertheless, the Bank adopted in September 2000 the Decree (Decision) on Foreign Currency Maturity Ladder drawn up with the aim to lay grounds for effective monitoring and measuring of foreign exchange liquidity of the Slovenian banks in 2002 when reporting commitments are due to switch from monthly to daily reporting.

Under the effective methodology, the amount of foreign exchange minimum shall be computed by taking into account deposits placed by individuals in foreign currency, balances on foreign exchange accounts of domestic legal persons, balances on accounts of non-residents in foreign currency and savings in tolars with the option

Box 5: **Cross-border capital movements**

The Europe Agreement signed by the Republic of Slovenia of the one part and the European Community and its Member States, of the other part, came into force on 1 February 1999. As regards capital movements liberalisation, a four-year transitional period relating to controls on short-term capital movements has been agreed. As regards foreign direct investment, no restrictions are in place. The Government of the Republic of Slovenia made a commitment already in 1999 within the framework of its negotiating position to bring the scope and concept of capital movements in line with the *acquis*.

As for the lifting of individual, sector-specific restrictions on the right to establishment, further liberalisation is linked to amending legislation governing the respective area. There are several bills pending promulgation in the National Assembly aimed at removing restrictions on the freedom of establishment in sectors: media, telecommunications and transport. In 2001, the focus is on the legislative work in relation to companies for management of investment funds, private investigators and exploitation of natural resources under terms of concessions, whereas in 2002, it will have to be extended also to the field of lottery games.

A significant step towards alignment with the *acquis* in the field of capital movements liberalisation in the Republic of Slovenia has been made by implementing the new foreign exchange legislation in April, i.e. September 1999, which lifted a number of restrictions in the field of inward and outward capital flows. Some restrictions remain for the time being. Although the Government of the Republic of Slovenia believes that such controls are still appropriate, they have not been directly addressed under the Foreign Exchange Act, but have been devolved to the Bank of Slovenia or the Ministry of Finance.

As from the effectiveness of the Foreign Exchange Act in April 1999, cross-border credit transfers are completely liberalised, though the restrictions in relation to short-term capital movements are still in place. In response to the appeal made by the European Union to Slovenia to liberalise capital movements prior to or upon accession of the EU, and to prepare a liberalisation timetable with milestones in the process of removing the remaining restrictions on capital flows complete with target dates and an outline of interim liberalisation steps, the Governing Board of the Bank of Slovenia adopted on 8 June 2000 a timetable for the liberalisation of cross-border capital movements. The Bank of Slovenia made a commitment to abolish the existing restrictions on some capital movements no later than by the milestones set out under the liberalisation timetable, viz.:

- The Bank of Slovenia will phase out the requirement under which non-residents shall pay a premium on the option to purchase foreign exchange in three steps. The first step was at the end of 2000, the second at the end of 2001, and the final one at the end of 2002.
  In accordance with the above commitment, as from 1 January 2001, the Governing Board of the Bank of Slovenia shortened the period after which non-residents are not required to pay a premium on the option to purchase foreign exchange from one year to six months,
- The Bank of Slovenia will finally lift the requirement relating to the compulsory payment of a premium for the option to purchase foreign exchange from the Bank of Slovenia in the amount of the balance on the respective custody account at the end of 2002.
  There is a marked downward trend in the scope of custody account obligations and the originally set at 2.5 per cent on a quarterly basis. As early as at the beginning of 2000, the premium was decreased to 0.7 per cent and continued to go down throughout the year even though the Bank of Slovenia made commitment to remove the premium requirement at the end of 2002. The trend started in 2000 continued in 2001, when the Bank of Slovenia cut the premium for the first quarter of 2001 to 0.2 per cent.
- By the end of 2000, the Bank of Slovenia was to lift any remaining restrictions on withdrawals of tolar cash from non-resident accounts.
  In accordance with its commitment, the bank of Slovenia abolished all restrictions on withdrawals of cash in tolars from accounts of non-residents as at 1 January 2000.
- By the end of 2001, the Bank of Slovenia is to fully liberalise restrictions on physical transfers of financial assets of residents to and from Slovenia. Nevertheless, the notification and reporting requirement under the Money Laundering Act will remain in force after the liberalisation of physical transfers of financial assets (cash) by residents and non-residents of Slovenia.
- By the middle of 2001, the Bank of Slovenia will lift restrictions on opening of cross-border current and deposit accounts by the non-financial enterprises sector, and on other sectors (households) by the date Slovenia joins the EU.

to covert such balances into foreign currency in the amount of 100 per cent of deposits, i.e. balances on deposits repayable on demand and time deposits due within 30 days, 95.0 per cent of deposits due after 31 days but within 90 days, 75 per cent of deposits due after 91 days but within one year, and 35.0 per cent of deposits due after one year.

In 2000, the funds held in accordance with the foreign exchange minimum requirement rose from 456 billion tolars in January to 570 billion tolars in December 2000. Namely, savings deposits of individuals in foreign currency increased by 70 billion tolars, balances on foreign exchange accounts of non-residents grew by 8 billion tolars, and balances on foreign exchange accounts of domestic legal persons and sole traders (entrepreneurs) rose by 36 billion tolars. Hence the foreign exchange minimum requirement was exceeded by a record high 26.4 per cent at the end of November. The lowest percentage above the minimum requirement as recorded at the end of April notching 15.0 per cent.

The banks operating in Slovenia complied with the foreign exchange minimum requirement throughout the year 2000 by steering their respective liquidity positions with liquid and first-class assets. Namely, the banks held net credit items denominated in foreign currency on accounts with foreign banks, net balances of short-term assets in foreign currency due from domestic and foreign bank, foreign cash and cheques, short-term claims denominated in foreign currency on the Bank of Slovenia, the bills issued by the Bank of Slovenia denominated in foreign currency (due within 120 days), as well as by investments in eligible foreign debt securities. The banks had to hold at least 60 per cent of the foreign exchange minimum in the bills issued by the Bank of Slovenia denominated in foreign currency.

Open foreign exchange position of banks

An important tool in monitoring exposures to currency risk is the requirement that the banks, which engage in operations involving foreign means of payment shall calculate their open position in foreign currency on a daily basis (also referred to as open foreign exchage position). The open foreign exchange position may not exceed 20 per cent of the bank's capital (own funds), while the average monthly open foreign exchange position may not exceed 10 per cent of the bank's capital (own funds). Claims denominated in tolars and off-balance sheet items are not included in the calculation.

As regards the aggregate open foreign exchange position of banks as at 29 December 2000, it was short since liabilities in foreign currency exceeded assets in foreign currency by 16,837 million tolars. Thus the banks' aggregate open foreign exchange position accounted for 6.8 per cent of capital. At the end of year, 21 banks disclosed a long open foreign exchange position as opposed to only four Slovenian banks with a long foreign exchange position.

At year end 21 »short« and 4 »long« foreign exchange positions of banks

Foreign portfolio investment

As regards investments made by non-residents in securities (foreign portfolio investment), the Bank of Slovenia has left controls on short-term capital flows in place for the time being in terms of the Europe Agreement concluded between the Republic of Slovenia and the European Community and its Member States that allows a transitional period on the way to the full-scope liberalisation of foreign portfolio investment. Foreign portfolio investitors may purchase securities through a stock-broking company or a local bank by debiting their custody accounts opened with the respective bank. Upon each purchase transaction, the bank shall pay a premium for the purchase of foreign currency option from the Bank of Slovenia, except in the case where the non-resident makes a legally binding commitment not to dispose of the securities in question for the period of one year. Under the legally binding commitment, the foreign portfolio investor pledges to abstain from selling such portfolio investment to a domestic person or from disposing of the securities portfolio in any other way.

Premiums for the purchase of foreign currency options from the Bank decrease

The premium levied on the purchase of foreign currency options from the Bank of Slovenia was 0.7 per cent of the balance of purchases made under the respective securities portfolio in the first quarter of 2000. It was decreased in the second and third quarter to 0.5 per cent, and was further reduced to 0.4 per cent in the fourth quarter. By paying for the premium, the respective bank, i.e. the foreign portfolio investor is entitled to the purchase of foreign exchange from the Bank of Slovenia (foreign currency option).

Oversight of implementation of monetary policy measures

The Bank of Slovenia monitors implementation of measures and compliance with the rules laid down in options made available when the Bank intervenes in the open market. Oversight is carried out through controls of banks, savings banks and savings and loan undertakings referred to as direct (on-site examination) and indirect (off-site supervision). The Bank implements this task on the basis of Article 50 of the Law on the Bank of Slovenia and pursuant to the Decree on Oversight of Implementation of Measures and on Measures Against Banks and Savings Banks. Off-site supervision is an ongoing process of screening prudential reports and statutory returns that banks and savings banks submit to the Bank of Slovenia. The examiners of the Bank of Slovenia conduct additional controls at certain intervals by examining business books and other documents in the respective bank or savings bank (on-site supervision).

Oversight of monetary policy measures reveals 25 cases of non-compliance

Supervision and surveillance activities carried out in the Slovenian banks and savings banks in the course of 2000 revealed cases of non-compliance with the remedial measures aimed at compliance with prudential requirements. Namely, the Bank of Slovenia commenced proceedings in 28 cases where non-compliance had been detected (in 1999: 16). There were 17 banks and 11 savings and loan undertakings examined by the Bank's examiners and in 25 cases a violation was established and a ruling issued. The bulk of non-compliance was detected in meeting the reserve requirement, particularly in connection with funds collected under the so-called na tional housing savings scheme Prohibition of purchase of securities from the Bank of Slovenia and capping growth of placements for a certain period were the most frequent corrective actions taken during the period under review.

In addition to the afore-mentioned measures, the Bank of Slovenia sent written notifications to banks and savings banks in relation to detected irregularities, minor shortcomings and defaults in prudential reports asking for remedial steps to be taken.

As regards operations of foreign exchange offices, the Bank of Slovenia conducted 22 on-site inspections in 2000 – one control was carried out in a bank authorised by the Bank of Slovenia and 21 controls were carried out in contractual exchange offices. The Bank's examiners prepared the records of those inspections and in five cases notified the competent district attorneys responsible for corporate offences, to the Foreign Exchange Inspectorate of the Republic of Slovenia, 12 motions to institute penal proceedings, and five motions were lodged with magistrates. Furthermore, eleven authorisation were revoked on a temporary basis and two authorisations for foreign exchange operations were annulled.

In 2000, three cases of non-compliance were detected through indirect control of foreign exchange operations conducted by the banks. Namely, two banks failed to reach the foreign exchange minimum and one did not comply with the mandatory subscription of bills denominated in foreign currency. The Bank of Slovenia issued two rulings requesting corrective measures to be taken with the aim to be in compliance with the statutory requirements.

3. BANKING SECTOR

During the year, the banks operating in Slovenia's banking environment have aligned with the requirements laid down in the Banking Act 1999. The structure of the banking sector has practically remained the same and even the overall number of banks at the end of 2000 was at the 1999 level.

Banks and savings banks meet requirements under Banking Act 1999

3.1. Banking sector structure

As at 31 December 2000, there were twenty-five operating banks in Slovenia including four subsidiaries of foreign banks and one branch of a foreign bank. In addition, three savings banks and sixty-six savings and loan undertakings also provided banking services.

The number has been going down since 1994 when there were thirty-three operating banks in Slovenia. Readiness to consolidate the ranks was best witnessed in 1998 when three banks were taken-over and operations of one bank were wound-up. There was another take-over in 1999 but the score at the end of the year was twenty-five following the incorporation of a subsidiary (Hypo Alpe-Adria-Bank d.d.) and the opening of the first branch of a foreign bank in Slovenia (Kaerntner Sparkasse AG, Celovec, Podružnica v Sloveniji). In April 2000, proceedings to wind-up Hipotekarna banka d.d. Brežice instituted in December 1998 entered the final phase. Nevertheless, it did not affect the overall number of operating banks in 2000, since Hipotekarna banka had already been struck off the register.

Bank count unchanged but…

The number of savings banks at the end of 2000 as opposed to the end of 1999 was cut in half as a result of restructuring that includes two mergers and self-initiated proceedings for a winding-up of a savings bank. As for operating savings and loan undertakings, their total number decreased by two undertakings during the year under review.

… the number of savings banks halved.

Out of twenty-five banks, which conducted activities in Slovenia at the end of 2000, there were ten banks in the hands of domestic shareholders, while foreign shareholders had at least a participating interest in six banks. There are also nine banks controlled by domestic shareholders, but in six of them equity holdings of foreign shareholders did not exceed 1 per cent. As for the savings banks in Slovenia, all are in the hands of domestic shareholders and are mostly private.

As regards ownership of banks in Slovenia, private shareholders prevail. The exceptions are the two largest banks, Nova Ljubljanska banka (hereinafter: NLB) and Nova Kreditna banka Maribor (hereinafter NKBM), which came under state governance within the framework of the rehabilitation programme. In addition, approximately one-fifth of Slovenska investicijska banka, d.d. and indirectly Poštna banka Slovenije d.d.. are state-controlled banks.

Table 10: **Ownership structure of the banking sector**
(equity holding in %)

	31/Dec/1999	31/Dec/2000
Non-residents	11.3%	12.0%
Central government	41.4%	36.8%
Other domestic persons	47.3%	51.2%

Source: Bank of Slovenia.

Box 6: **Deposit guarantee scheme**

Under the new deposit-guarantee scheme drafted in line with the EC Directive on Deposit-Guarantee Schemes (94/19/EC) and determined by provisions of the Banking Act 1999 (Official Gazette of the Republic of Slovenia, No. 7/99), which became effective on 1 January 2001, the responsibility for repaying eligible funds to the public rests with banks and savings banks whose registered office is within the territory of the Republic of Slovenia. Detailed standards have been elaborated in the Decision on Deposit-Guarantee Scheme (Official Gazette of the Republic of Slovenia, No. 61/00) and the Decision on Adjustment of Minimum Initial Capital of Banks, Guaranteed Deposits and Minimum Initial Capital of Savings Banks (Official Gazette of the Republic of Slovenia, No. 102/00)

The mechanism of the scheme is activated by the bankruptcy proceedings in a bank or a savings bank providing repayment of guaranteed deposits placed by individual depositors in the amount of up to 4.2 million tolars (approximately 20,000 euros). For the purpose of calculating the amount of guaranteed deposits, the sum of all balances on accounts of a single depositor is reduced by the sum of the bank's claims on that depositor. Guaranteed deposits shall be repaid from liquid funds provided by the Bank of Slovenia by the receiver- a bank appointed by the Bank of Slovenia - no later than three months after bankruptcy proceedings were initiated in the failed bank or a savings bank.

In terms of the Banking Act 1999, a deposit shall mean the aggregate balance of all contractual claims of the respective client/depositor on the bank to keep a current or giro account, savings deposits, cash balances and certificates of deposit, i.e. treasury bills provided they have been issued as registered securities. A deposit is not guaranteed in the cases listed below:

1. When a deposit is placed by another bank or a financial institution in their own name and for their own account,
2. When a deposit is related to activities for which the owner of the deposit has been charged with money laundering and the sentence passed against the defendant is final
3. When a deposit is placed by other governments, central banks and local communities,
4. When a deposit is placed by a member of the bank's management, i.e. supervisory board or by a member of his/her immediate family
5. When a deposit is placed by a shareholder who has at least a 5 per cent equity holding in the bank's capital, i.e. in voting rights,
6. When a deposit is placed by a legal person controlled by the bank,
7. When a deposit is placed by a member of management, i.e. supervisory board of a legal person under items 5 and 6 or a member of his/her immediate family,
8. When a deposit is eligible to be included in the calculation of the bank's capital (subordinated deposit),
9. When a deposit is placed by a legal person classified under the Company Law as a large or a medium-sized company.

Furthermore, the following deposits are not covered by the deposit-guarantee scheme: bearer's deposits and all anonymous deposits where a positive identification of the depositor is not possible prior to the opening of bankruptcy proceedings against a bank or a savings bank.

Participation in the deposit-guarantee scheme is obligatory for all banks, savings banks and savings and loan undertakings authorised by the Bank of Slovenia to provide banking services including accepting deposits, as well as for branches of banks with the registered office outside the territory of the Republic of Slovenia, which are partly or fully included in the host country deposit-guarantee scheme. The branches of foreign banks are obliged to invest at least 2.5 per cent of the balance of guaranteed deposits placed with the respective branch as at the last day of the preceding half-year in short-term securities issued by the Bank of Slovenia or by the Republic of Slovenia.

As from the day of full-fledged membership of the European Union, deposits placed with the branch of a bank from a Member State will be guaranteed under the deposit-guarantee system effective in the Member State where the bank has its registered seat of office (home country), provided the Bank of Slovenia recognises the deposit-guarantee scheme in place in the Member State as equal to the scheme provided in the Republic of Slovenia. Branches of foreign banks may be included in the deposit-guarantee scheme in place in the Republic of Slovenia for supplementary cover. Before Slovenia's accession, the Bank of Slovenia may at its discretion rule require for the authorisation to establish a branch of a foreign bank that the branch joins the deposit-guaranteed scheme in the Republic of Slovenia, in the case where the deposit-guarantee scheme of the home country falls short of the level of protection provided in the Republic of Slovenia.

In terms of the market share held by Slovenian savings banks and savings and loan undertakings (measured by their total assets), it remained conspicuously low at the end of 2000 – a mere 2.2 per cent market share (savings banks: 0.4 per cent, savings and loan undertakings: 1.8 per cent). Thus the yawning gap between banks and other credit institutions has not been bridged.

How developed the banking sector is may be illustrated by the ratio between aggregated total assets of banks and gross domestic product. At the end of December 2000, aggregated total assets of banks accounted for approximately 79 per cent of GDP, whereas aggregated total assets of banks, savings banks and savings and loan undertakings pushed this figure up to approximately 81 per cent of GDP.

The deadline set under the Banking Act 1999 for the banks and savings banks to be fully compliant with the requirements introducedunder the new law during an 18-month transitional period expired on 20 August 2000. The requirements include:

- To posses the minimum amount of initial capital,
- To subscribe initial capital as non-materialised registered common shares (up to one-third of shares may be issued as preferential shares),
- An authorisation of the Bank of Slovenia to obtain a qualifying holding,
- To appoint a management board to direct the bank composed of at least two persons whose suitability is checked by the Bank of Slovenia,
- To staff the internal audit department of the respective bank/savings bank with persons of professional competence, knowledge and experience, and
- To demonstrate the compliance of the articles of association of the respective bank with effective legislation.

Banks authorised by the Bank of Slovenia under the Banking Act 1999 to provide banking and other financial services are those credit institutions, which have fulfilled the requirements set out in the new law and which have already qualified as providers of designated financial services. As regards all other financial services, the banks have to prove to the central bank that they have human resources, technology and organisational structure to deliver those services.

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

	Authorisation requested*	1999		2000	
		granted	rejected	granted	rejected
1.	Licence for banks and savings banks to provide banking services	-	-	-	-
	Authorisation to provide banking services	2	-	25	-
2.	Authorisation to provide ancillary banking services	1	2	-	-
	Authorisation for trading in securities	1	-	-	-
	Authorisation to provide other financial services	24	-	194	1
3.	Authorisation to a foreign bank to set up a branch in Slovenia	1	-	-	-
4.	Authorisation for merger/acquisition of a bank or a savings bank	1	-	2	-
5.	Authorisation to a foreign bank to set up a representative office	2	-	-	-
6.	Authorisation to a domestic shareholder to acquire a stake in excess of 15% of capital	2	-	-	-
	Approval to a shareholder to acquire a qualifying holding	8	5	9	-
7.	Authorisation to members of management board	18	1	25	2
	Total	60	8	255	3

* Authorisations issued to banks and savings banks by 20 February 1999 under the Law on Banks and Savings Banks may substantially differ from authorisations issued under the Banking Act 1999.

Source: Bank of Slovenia

3.2. Review of banks' performance

18.3 per cent growth in business volumes

Total assets of all banks operating in Slovenia amounted to 3,178.7 billion tolars as at 31 December 2000 (unaudited figures). Thus aggregate total assets posted 18.3 per cent nominal, i.e. 8.6 per cent real growth (these figures do not include the branch of NLB in Italy in comparison with the end of 1999. It was the second highest real growth in the volume of business within the domestic banking system over the last five years (in 1998, this figure was 9.1 per cent).

In 2000, only one of twenty-five banks failed to beef up its total assets. The rates at which total assets grew in real terms were between 2.6 and 32.1 per cent, whereas nominal growth ranged from 11.7 to 43.9 per cent. Only the latest entrants into the banking environment posted above-average growth rates of total assets: the bank established in 1999 and the branch of a foreign bank established in Slovenia. The only ailing bank in the local banking environment that faced considerable difficulties in 2000 saw its total assets decrease by 3.5 per cent in real terms (in nominal terms its total assets increased by 5.1 per cent).

Solid market shares of the largest banks and high bank concentration

The two main features of the banking sector in Slovenia over the past seven years have been: stable market shares held by the largest banks measured in terms of unconsolidated total assets, and a high concentration of banks for a small economy as Slovenia's is. At the end of 2000, the market share of the largest Slovenian bank including its five subsidiaries (also referred to as daughter banks) was 36.0 per cent. The market share of the three largest banks at the end of 2000 was 50.2 per cent, while starting with 1994 onward this share ranged between 50.6 and 53.0 per cent. By slicing a 62.3 per cent of the market at the end of 2000, the five largest banks practically remained in the bracket between 61.9 and 63.2 per cent achieved between 1994 and 1999. The top seven banks managed to keep between 71.0 and 73.9 per cent of aggregate total assets of Slovenia's banking sector during the period same period (at the end of 2000: 73.2 per cent), while ten largest banks had between 79.7 and 82.5 per cent (at the end of 2000: 81.7 per cent).

Compared to 1999, the average **structure of liabilities** shows that the share of deposits placed by the banking sector in 2000 has gone up from 10.7 per cent to 11.1 per cent, while the share of deposits by the non-bank sector (non-financial enterprises, households, central government, other financial institutions, non-profit institutions serving households and non-residents) has decreased during the past year. The drop from 69.3 to 68.6 per cent is a result of reduced structural shares of

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

Name	Total assets in SIT millions		Nominal growth in %		Market share in %	
	31-Dec-99	31-Dec-00	1999/1998	2000/1999	31-Dec-99	31-Dec-00
NLB *	752,343	904,757	13.9	20.3	28.0	28.5
NKBM	321,813	368,109	12.9	14.4	12.0	11.6
SKB banka	307,637	323,353	9.4	5.1	11.5	10.2
Banka Koper	167,905	198,310	22.4	18.1	6.3	6.2
Banka Celje	155,712	188,133	15.3	20.8	5.8	5.9
Abanka	149,301	185,182	21.3	24.0	5.6	5.8
Gorenjska banka	130,310	159,137	20.6	22.1	4.9	5.0
Aggregate total assets – top 7 banks	1,985,022	2,326,982	14.7	17.2	73.9	73.2
Aggregate total assets – all 25 banks	2,687,600	3,178,721	13.8	18.3	100.0	100.0

* Figures for 31 December 2000 excluding the Italian branch of NLB.
Source: Bank of Slovenia

deposits placed by non-financial enterprises and general government by one percentage point (to 13.9 per cent, i.e. 6.9 per cent); hence the record low figures over the past four years have been posted. This has happened mainly due to relatively strong growth enjoyed by total liabilities and accentuated above-average rise in liabilities arising from securities, as well as other liabilities. Additionally, the upward trend seen in the average structure of liabilities has also been fuelled by new categories of subordinated liabilities (subordinated loans) and funds for general banking risks as laid down within the framework of modifications to the chart of accounts for banks and savings banks implemented in 1999. Both items recorded a high growth rate over the past year.

Banks' liabilities to customers grew by 16 per cent

Movements on the liabilities side of balance sheets of the banks operating in Slovenia based on net figures, shows that trends have been rather favourable during the year under review. **Liabilities of banks to the non-bank sector** (also referred to as customer accounts) were gradually rising during 2000 and at the end of the year notched 16.0 per cent growth in nominal terms (in 1999, this figure was 11.5 per cent). This is partly a result of rising interest rates on deposits over the past year by 1.2 percentage points, i.e. 0.5 percentage point in real terms.

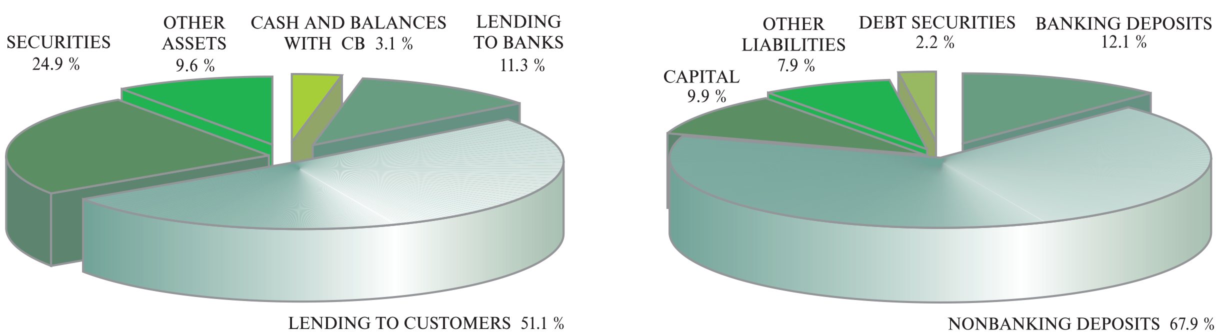
Sharp growth in corporate foreign exchange accounts…

Having plunged by 5.3 per cent in real terms in 1999, deposits placed by non-financial enterprises stagnated in the first half of 2000, but then picked up and pencilled 11.6 per cent growth (2.5 per cent in real terms). Above-average growth rates have been recorded by foreign-exchange accounts of non-financial enterprises since they were introduced in 1999. At the end of 2000, balances on these accounts were by 105.3 per cent above the respective figure year-on-year - a rise of 88.5 per cent in real terms. The share of foreign-exchange accounts in the structure of all deposits from non-financial enterprises has gone up grew from 9.9 to 18.3 per cent during the year under review.

… citizens' deposits in foreign currency have grown over the past year.

There was strong growth in deposits from households (citizens and sole entrepreneurs) in 2000 when these funds accounted for the largest portion of liabilities to customers other than banks (60 per cent of deposits from customers i.e. 40.7 per cent of total liabilities at the end of 2000). Deposits from citizens increased in nominal terms by 25.5 per cent (15.2 per cent in real terms) and deposits in tolars and deposits in foreign currency remained balanced. Therefore, the share of foreign-exchange deposits in overall deposits of citizens was relatively stable rising from 44.8 per cent at the end of 1999 to 45.0 per cent at the end of 2000, despite the last year's pick up in the growth in foreign exchange deposits by individuals (15.8 per cent real growth after flat figures were posted for a couple of years).

Figure 12: **Average structure of banks' assets and liabilities** at 31 December 2000



Source: Bank of Slovenia

Deposits of citizens accounted for as much as 98.4 per cent share in deposits at the end of 2000 by households, and deposits of sole entrepreneurs accounted for a 1.6 per cent share. The portion of households' deposits repayable on demand dropped from 43.3 per cent at the end of 1999 to 38.0 per cent at the end of 2000. On the other hand, the respective portions of short- and long-term savings at the end of 2000 increased year-on-year from 53.2 to 57.8 per cent and from 3.5 to 4.2 per cent, respectively.

Long-term savings of households rising

Short-term savings have grown steadily throughout the past year topping a 36.0 per cent increase, but long-term savings have posted even more vigorous growth during the first and the fourth quarter of 2000 reaching 47.0 per cent. Such a good result has put long-term savings of households back on track following sliding figures in 1997 and 1998 when long-term deposits accounted for 2.4 per cent and 2.0 per cent of overall deposits, respectively. The key factor behind the new rally in long-term savings has been national housing savings scheme, as well as some other similar savings packages. In 2000, growth in short-term deposits with maturity between 91 and 180 days of 43.2 per cent, i.e. 31.5 per cent in real terms, and in deposits due between 181 days and one year of 42.8 per cent, i.e. in real terms 31.1 per cent, was above trend. On the other hand, time deposits placed by households due within one month decreased during the past year by 787 million tolars. Deposits by sole entrepreneurs grew by 8.5 per cent in 2000. Savings in foreign currency soared by a hefty 74 per cent, i.e. by 59.8 per cent in real terms, while tolar funds decreased by 0.4 per cent in real terms.

As for deposits gathered from other customers within the non-bank sector (central government, other financial institutions, non-profit institutions serving households and non-residents), the sharpest drop was recorded in central government funds (down 3.3 percentage points i.e. to 7.9 per cent at the end of 2000). These deposits shrank last year by 37.6 billion tolars or by 18.0 per cent compared to the respective figure for 1999. The portion of deposits gathered from other financial institutions was also affected during 2000 and decreased by a half of a percentage point landing at 7.4 per cent. Deposits from non-profit institutions serving households increased by 10.0 per cent in real terms during the year under review. As for deposits from non-residents, they rose by 14.0 per cent but their aggregate share in deposits from the non-bank sector at the end of 2000 was still 4.2 per cent.

In 2000, **banks' sources of funds** (liabilities) increased by 24.8 per cent compared to 38.1 per cent in 1999, pushing the share of sources of funds of the banking sector in average total liabilities up from 10.7 per cent in 1999 to 11.1 per cent in 2000. Both Slovenian and foreign banks provided the impetus to operations. During the first and partly during the second quarter of 2000, the central bank was the most important provider of funds. The trend was reversed in the second half of the year

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

	31-Dec-99	31-Mar-00	30-Jun-00	30-Sep-00	31-Dec-00
Demand deposits of nonbanks	34.9	34.0	34.8	34.1	33.5
Shortterm deposits of nonbanks	56.8	57.0	56.2	56.5	57.7
Longterm deposits of nonbanks	8.4	9.0	9.0	9.4	8.8
Total deposits of nonbanks	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**
Shortterm loans to nonbanks	57.2	56.6	57.3	56.6	57.5
Longterm loans to nonbanks	42.8	43.4	42.7	43.4	42.3
Claims from guarantees issued	0.2	0.2	0.2	0.2	0.1
Total loans to nonbanks	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**

Source: Bank of Slovenia

when the local and foreign commercial banks took the lead. The share of funds provided by the central bank in sources of funds eventually fell from 7.0 per cent at the end of 1999 to 1.7 per cent at the end of 2000. Although the share of domestic banks in sources of funds picked up in 2000 (from 27.5 per cent to 32.1 per cent year-on-year), the domestic banking sector continued in 2000 to search for financing across the border. As a result, foreign funding rose from 65.5 per cent in 1999 to 66.3 per cent in 2000.

The share of liabilities arising from **securities issued** in the average structure of liabilities was steady and notched 1.9 per cent at the end of 2000. Nevertheless, liabilities arising from securities soared by 42.4 per cent in real terms during the past year as opposed to 1999. Long-term liabilities stayed ahead of short-term liabilities, 44.8 and 38.4 per cent, respectively. The share of capital in the average structure of liabilities dropped from 10.2 per cent in 1999 to 9.2 per cent in 2000, whereas the share of other liabilities grew from 8.0 per cent to 9.1 per cent year-on-year.

Lending to non-bank sector picks up

A breakdown of the **structure of total assets** in 2000 reveals an increase in the share of lending to the non-bank sector (customers) from 49.0 to 51.1 per cent. By growing 17.0 per cent in nominal terms during the year under review, customer lending fell short of the respective figure for 1999 - 25.2 per cent. The composition of loans and advances to the nonblank sector in 2000 was not substantially different from loans and advances extended in 1999, except for a rise in lending to non-financial enterprises (from 56.0 to 57.1 per cent), central government (from 9.0 to 9.3 per cent) and other financial institutions (from 2.4 to 2.6 per cent). The opposite trend was posted by structural shares related to citizens (from 26.7 to 25.8 per cent), sole entrepreneurs (from 4.3 per cent to 4.0 per cent), and non-residents (from 1.5 to 1.0 per cent) lost momentum.

During the year under review, lending to non-financial enterprises was rising steadily and posted year-end growth in 19.3 per cent, considerably more than the 1999 growth rate of 15.6 per cent. Lending to households rose by 12.5 per cent during the past year compared to 45.3 per cent in 1999, mostly due to sluggish demand of citizens for loans during the past year (an increase of 13.2 per cent) as opposed to high-note lending operations in 1999 (an increase of 25.1 per cent). Lending to sole entrepreneurs even went down in real terms by half a percentage point. Lending to non-profit institutions serving households followed suit and shed 6.5 per cent in real terms, while lending to non-residents plunged by 27.1 per cent. There was growth in lending to general government at approximately the same level as in 1999 (21.0 per cent in nominal, i.e. 11.1 per cent in real terms), and the most vigorous rise was posted by loans and advances to other financial institutions (29.8 per cent in nominal, i.e. 19.2 per cent in real terms).

The maturity structure of loans and advances extended to the non-bank sector carried on the assets side of banks' balance sheets has changed little over the past four years, tipping the scale mainly in favour of long-term lending. Thus the ratio between short-term and long-term lending in 1997 was 58.1 per cent to 41.9 per cent, whereas in 2000 it was 57.6 per cent to 42.4 per cent. Short-term lending rose by 18.1 per cent in 2000 (8.4 per cent in real terms), including a rise in loans in foreign currency of 13.7 per cent (4.4 per cent in real terms). Long-term loans in foreign currency soared and posted a rise of 43.1 per cent (31.4 per cent in real terms), outpacing the growth of the aggregate long-term lending of 15.6 per cent, i.e. 6.1 per cent in real terms.

Another downturn in investments in securities.

During 1997 and 1998, investments in securities accounted for approximately one-third of average aggregate total assets of banks but the trend reversed in 1999. Hence the share of investments banks made in securities fell to 28.5 per cent and continued to go down during 2000. At the year-end, investments in securities accounted for 25.8 per cent of banks' average aggregate total assets. The composition of securities portfolio has been changing over the past few years. Namely, the share of the item "other securities" increased from 6.2 per cent at the end of 1997 to 12.9 per cent at the end of 2000 at the expense of a decrease in the respective shares of securities issued by central government (from 43.7 to 41 per cent) and the Bank of Slovenia (from 50 cent to 46.1 per cent).

Investments in securities grew in 2000 by 11.9 per cent (2.8 per cent in real terms), headed by a rise in short-term securities issued by central government (treasury bills) and other securities (equity shares issued by banks and other issuers, other securities floated by banks, non-residents, other governments, etc.). Investments in these securities surge most in the fourth quarter of financial year as a result of efforts focused on the placement of funds in securities non-financial enterprises towards the end of the year for the purpose of reducing banks' tax base. There was a pick up in the growth of short-term securities issued by the Bank of Slovenia after two lean years; hence a nominal rise of 11.4 per cent (2.3 per cent in real terms).

The composition of securities portfolios comprising securities issued by the central bank held by the commercial banks has changed during the past year in favour of bills denominated in foreign currency. Hence the share of tolar-denominated bills dropped from 18.4 per cent in 1997 to 1.9 per cent in 2000. During the same period, the share of bills denominated in foreign currency grew from 81.6 to 98.1 per cent.

Investments in the banking sector increased in 2000 by 42.1 per cent (in real terms by 30.5 per cent) with time deposits enjoying the strongest growth. Therefore, the share of investments in other banks grew in the average structure of total assets from 9.4 per cent in 1999 to 10.2 per cent in 2000. The structure of investments in other banks has been modified over the past four years due to a gradual rise in the share of time deposits denominated in tolars at the expense of the share of time deposits in foreign currency, while the minor share of sight deposits in foreign currency fluctuated during the period under review. Since that segment is relatively small, the changes did not affect overall figures. At the end of 2000, time deposits in foreign currency accounted for 79.2 per cent (1999: 77.0 per cent), time deposits in tolars accounted for 16.7 per cent (1999: 13.8 per cent, and deposits repayable on demand in foreign currency (sight deposits) accounted for 4.0 per cent (1999: 9.2 per cent) of investments in the banking sector

The share of the balance sheet item **cash and balances with the central bank** in aggregate total assets has slightly decreased over the past four years landing at 3.1 per cent at the end of 2000 (1997: 3.7 per cent) compared to the share of **other total assets** that has slightly grown topping 8.1 per cent (1997: 7.4 per cent).

The share of **average liabilities denominated in foreign currency** in **aggregate average liabilities of banks** was going down from year 1997 (35.8 per cent) until 1999 (30.5 per cent) only to start rising again over the past year when it reached 32.7 per cent at year-end. A similar trend can be observed in the **average share of total assets denominated in foreign currency in aggregate average total assets of banks** that first decreased from 32.8 per cent in 1997 to 29.6 per cent in 1999 and then rose again last year to 31.6 per cent. In 2000, both total assets and total liabilities denominated in foreign currency grew steadily with sources of funds – liabilities - in foreign currency taking the lead by growing 28.2 per cent in nominal, i.e. 17.7 per cent in real terms than foreign-currency assets that rose by 27.1 per cent in nominal, i.e. 16.7 per cent. in real terms. During 2000, the banks averaged 3.5 per cent more sources of funds – liabilities - than assets, though far below the 9.1 per cent mark recorded in 1997.

Secondary liquidity in the banks decreased from 17.5 per cent at the end of 1997 to 13.7 per cent of total assets at the end of 2000. Thus the funds held by the banks within the framework of secondary liquidity management totalled 438.5 billion tolars at year-end 2000 – in real terms 7.4 per cent below the 1999 level, mainly due to the flattening of the volume of tolar-denominated treasury bills. During the year under review, the banks maintained the level of compliance with the statutory liquid-asset requirements set out in the Decree on the Required Adjustments of the Maturity Structure between Assets and Liabilities. The liquid-asset requirement (the ratio referred to as the liquidity ladder) produced at the end of 2000 the following ratios that show assets versus liabilities: 2.04 in the first class, 1.51 in the second class, and 1.29 in the third class. The ratios achieved in 1999 were slightly below last year's figures: 1.98; 1.42; 1.21.

Improved liquidity ladder ratios between assets and liabilities

Efforts focused on reducing volatility of funding by diluting the **concentration of deposits** continued throughout 2000. Expressed as a percentage of the aggregate total funding liabilities to the public, large depositors (the first thirty depositors excluding banks and individuals) accounted for 53.3 per cent at the end of 1997 dropped to 48.5 per cent at the end of 2000. Concentration of deposits in the top three banks was below the banking sector average (between 28.0 and 43.7 per cent). Nevertheless, a relatively high share of retail deposits from citizens in aggregate deposits from the non-bank sector is a mitigating factor as far as liquidity risk is concerned. Namely, retail deposits have grown over the last four years from 52.6 per cent at the end of 1997 to 59.0 per cent at the end of 2000.

Increased dispersion of deposits

The banks' earnings in 2000 totalled 32.5 billion tolars in **profit before taxes** including **net revaluation income** in the amount of 38.6 billion tolars. As opposed to 1999, the banks' earnings grew by 61.6 per cent (48.4 per cent in real terms), but compared to the 1999 result when one of Slovenia's largest banks was in the red, profit before taxes were 28.2 per cent below pre-tax profit in 1998 in real terms. **After-tax profit** amounted to 19.9 billion tolars at the end of 2000 – 82.3 per cent growth in real terms year-on-year.

32.5 billion tolars before taxation…

… and 19.9 billion tolars in after-tax profit.

Earnings brought by **net interest income**, which in 2000 amounted to 123 billion tolars**,** were again more subdued after modest growth in 1998 dropping by 2.7 per cent in 1999 in real terms due to the impact the loss incurred by one of the largest Slovenian banks. Net interest income posted growth of 29.8 per cent i.e. 19.1 per

Table 14: **Principal balance sheet items of the banking sector**

	Amount in millions of tolars		Nominal growth, in %		Real growth, in %
	31-Dec-99	31-Dec-00	1999/1998	2000/1999	2000/1999
Deposits with Central bank	88,761	98,625	4.8	11.1	2.0
Loans to banks	252,615	358,859	11.1	42.1	30.4
Loans to nonfinancial enterprises	777,134	928,065	15.6	19.4	9.7
Loans to households	429,999	483,789	45.3	12.5	3.3
Loans to government	124,719	150,921	20.2	21.0	11.1
Securities	708,622	792,870	-0.8	11.9	2.7
Other assets	305,750	365,593	21.5	19.6	9.8
Total assets	**2,687,600**	**3,178,721**	**14.4**	**18.3**	**8.6**
Liabilities to banks	309,002	385,614	38.1	24.8	14.6
Liabilities to nonfinancial enterprises	395,257	441,147	2.3	11.6	2.5
Liabilities to households	1,033,559	1,293,711	14.2	25.2	14.9
Libilities to government	208,773	171,202	1.3	-18.0	-24.7
Libilities from securities	44,755	69,405	-22.4	55.1	42.4
Other liabilities	416,972	502,031	32.3	20.4	10.6
Capital	279,281	315,611	9.0	13.0	3.8
Total liabilities	**2,687,600**	**3,178,721**	**14.4**	**18.3**	**8.6**

Source: Bank of Slovenia

cent in real terms compared to 1999. Income arising from **net fees and commissions** totalled 37.7 billion tolars and in nominal terms remained at the 1999 level (11.9 per cent), whereas in real terms, this income source has actually lost 2.7 per cent year-on-year due to a rise in consumer prices in 2000. **Net income from financial transactions** (calculated as trading gain after the deduction of any trading loss and gains from investment securities) in the amount of 13.4 billion tolars rose last year by 40.0 per cent above the 1999 level (28.5 per cent in real terms). Higher gains on banks' capital investments and foreign exchange trading income have contributed to the vigorous growth in this item. The item referred to as **net other** increased in 2000 by 12.3 per cent (i.e. 3.1 per cent in real terms) and topped 4.7 billion tolars at year-end.

With 26.5 per cent, growth in gross income …

Nominal growth in the banks' **gross income** to 169.4 billion tolars in 2000 has outstripped growth rates recorded over the past few years and reached 26.5 per cent (16.2 per cent in real terms). Such a vigorous rise is the result of a high increase both in the net trading-related income segment (28.5 per cent) and the increase in net interest income (19.1 per cent). Other elements of gross income also increased year-on-year: the share of net interest income and the share of net trading-related income rose (from 70.8 to 72.6 per cent and from 7.1 to 7.9 per cent, respectively), while the share of net fees and commissions dropped (from 25.2 to 22.3 per cent).

… and growth in operating expenses of 14.2 per cent…

Operating expenses amounted to 99.7 billion tolars in 2000 and year-on-year went up in real terms by 4.8 per cent (14.2 per cent in nominal terms). If the composition of operating expenses incurred by the banks is analysed, then upward pressure on **labour costs** is revealed (a rise of 2.7 per cent in real terms, i.e. 11.9 per cent in nominal terms), as well as on **other general administrative expenses** (10.7 per cent in real terms, i.e. 20.5 per cent in nominal terms), the latter group comprising mainly outsourced services, as well as services provided by consultants, chartered accountants and certified auditors and other related services plus maintenance costs for fixed assets. The share of operating expenses in gross income compared to 1999 dropped last year from 65.2 to 58.9 per cent, while the share of labour costs has decreased from 32.6 to 28.9 per cent of gross income.

… net income rose by 49.7 per cent.

That the Slovenian banks have been effectively controlling costs during the past year is also reflected in 69.7 billion tolars in **net income** that after declining for two years in real terms picked up last year and increased by 49.7 per cent (37.5 per cent in real terms).

Table 15: **Principal items in adjusted profit and loss account of banks**

	Amount in millions of tolars		Share in %		Nominal growth in %	
	1999	2000*	1999	2000	1999/ 1998	2000/ 1999
Net interest income		122,966	70.8	72.6	5.1	29.8
Net fees and comissions		37,728	25.2	22.3	11.7	11.9
Net financial operations		13,355	7.1	7.9	42.6	40.0
Net other		-4,696	-3.1	-2.8	-19.0	12.3
Gross income		**169,353**	**100.0**	**100.0**	**9.8**	**26.5**
Operating expenses		99,680	65.2	58.9	13.2	14.2
- labour expenses		48,891	32.6	36.5	14.0	11.9
Net income		**69,673**	**34.8**	**52.1**	**3.9**	**49.7**
Net provisions and net write-offs		-37,141	-19.7	-27.7	40.4	40.7
Profit before tax		**32,532**	**15.0**	**24.3**	**-22.5**	**61.6**
Profit after tax		**19,945**	**7.5**	**14.9**	**-37.4**	**98.5**

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

In 2000, the banks allocated 37.1 billion tolars to **net provisions**, or 10.7 billion tolars more year-on-year. Thus net provisions posted a 40.7 per cent nominal growth (i.e. 29.2 per cent in real terms) compared to 1999. On average, net provisions tie up 1.3 per cent of total assets of banking system.

Net revaluation income in the amount of 38.6 billion tolars in 2000 jumped by 54 per cent (41.5 per cent in real terms), demonstrating the extent to which the so-called inflationary gains have fed through to increases in overall earnings of the Slovenian banks over the past few years.

Profits earned by banks up again after flat figures in 1999

The pick up in the banks' earnings in 2000 to the levels enjoyed in 1997 and 1998 is a relieving sign after lacklustre results in 1999 and falling profitability ratios. In particular, **return on average assets** dropped in 1999 to 0.8 per cent, whilst **return on average equity** plunged to 7.8 per cent (as a result of the loss incurred by one of the largest banks), but there was a turnaround resulting in return on average assets of 1.1 per cent and return on average equity of 11.3 per cent at year-end.

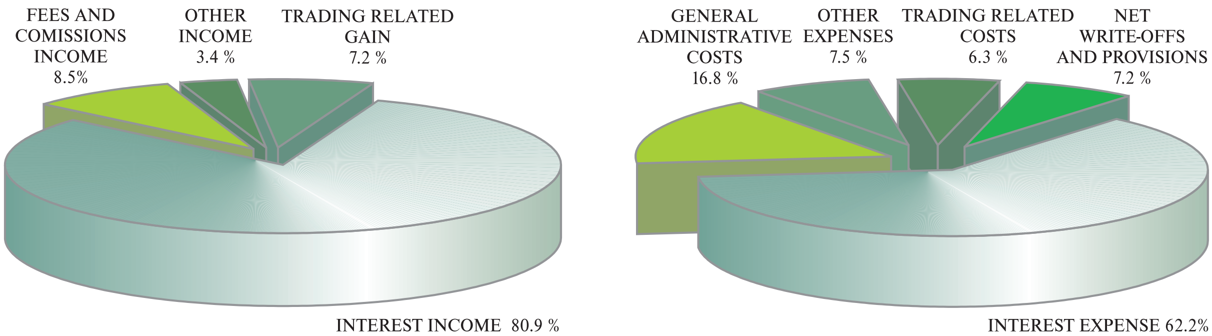
The banking sector's ratio between **operating expenses and average total assets** remained with 3.4 per cent unchanged in 2000. General administrative expenses, depreciation/amortisation and other operating expenses (taxes, social security contributions, membership fees, and other), form the numerator of this ratio.

Table 16: **Composition of net revaluation income of banks** (in millions of tolars)

	1998	1999	2000
Net revaluation gain or loss	23,596	25,073	38,623
Net revaluation interest	32,769	35,081	51,536
- reval. income [1]	162,430	182,013	286,270
- reval. expense [2]	129,662	146,932	234,734
Net other	-9,172	-10,008	-12,912
- reval. income (fixed assets., capital investments., other)	9,092	10,050	13,450
- reval. expense (capital, other)	18,264	20,058	26,362
Capital revaluation adjustment	17,228	19,041	25,112
Foreign exchange trading gain or loss	-1,095	-57	-2,059
Gain or loss on contracts with foreign currency clause	239	202	274

1 Arising from foreign exchange gains, from granted loans and placed deposits with/without foreign currency clause, from securities
2 Incurred by foreign exchange losses, by taking loans/deposits, by issuing securities, by assuming liabilities in tolars with foreign currency clause
Source: Bank of Slovenia.

Figure 13: **Composition of banks' income and expenses** in 2000



Source: Bank of Slovenia.

Net interest rate margin recovers after three lean years

The ratio between net interest income and average gross interest-earning assets referred to as the **net interest margin** has recovered during the past year after a fall that lasted for three years (from 4.9 per cent in 1997 to 4.0 per cent in 1999) was on the road to recovery in 2000 by rising to 4.5 per cent. Such a twist has been possible owing to banks' earnings arising from net interest income that for the first time after three years grew faster than average gross interest-earning assets. Namely, net interest income rose by 29.7 per cent, i.e. 19.1 per cent in real terms compared to average gross interest-earning assets that grew by 16.2 per cent, i.e. 6.7 per cent in real terms. Different banks made different deals during the past year; hence their net interest margins varied from a modest 2.2 per cent to a solid 7.9 per cent.

Interest spread shrinks from 4.9 percentage points in 1997 to 2.7 percentage points in 2000

Interest spread, the difference between average annual real interest rate charged on loans and paid on deposits denominated in tolars, i.e. on assets from the non-bank sector (customer accounts), was sliding from 4.9 percentage points at the end of 1997 to 3.7 percentage points at the end of 1998 to land at 3.3 percentage points at the end of 1999. In 2000, the downward trend continued; hence at year-end, interest spread earned by the banks that operate in Slovenia pencilled meagre 2.7 percentage points.

During the period between 1995 and 1999, capital held by the banks was rising at the average annual growth rate of 7.2 per cent, whereas risk-weighted assets were growing at the rate of 16.8 per cent. Consequently, **capital adequacy ratio** (calculated as the ratio between capital and risk-weighted assets) has been decreasing over the past few years. Nevertheless, banks managed to maintain this important ratio at a comparatively high level (1995: 21.5 per cent; 1997: 19.0 per cent; 1999: 14.0 per cent). Such safety margin may partly be attributed to stringent capital requirements all banks applying for a full licence to provide banking services had to meet with the aim to enhance stability of the financial system and encourage banks to join forces and follow strategies of reducing costs through rationalisation of branch and staff numbers. The minimum ratio provided for in Council Directive on a solvency ratio for credit institutions remains at 8 per cent for banks and savings banks. Thus the capital base of banks and savings banks erects a firewall between assets and potentially threatening non-performing assets and allows further growth in risk-weighted assets of banks only within the framework of their capital.

Banks maintain capital adequacy ratio between 9.6 and 29.9 per cent

A slight decrease in capital adequacy ratio during the second quarter of 2000 (from 13.7 to 13.6 per cent) was largely caused by enforcing the capital requirements, which regulate risk-adjusted assets where weighting is applied to contain exposure to currency risk. As at 31 December, the banking sector's capital adequacy ratio averaged 13.5 per cent. The figure varied enormously from one bank to another - from 9.3 to 25.9 per cent. In ten banks the capital adequacy ratio was below the industry average (less than 13.5 per cent) and in three banks in this group the capital adequacy ratio was below 10.0 per cent.

The banks' **capital**, calculated in accordance with the decision on the methods for the calculation of capital, capital requirements and capital adequacy ratio to be

Table 17: **Banks' key performance ratios**

	12/31/98	12/31/99	12/31/00
Return on average assets	1.2	0.8	1.1
Return on average equity	11.3	7.8	11.3
Net interest margin	4.5	4.0	4.5
Labour cost/average assets	1.8	1.7	1.7
Other operating expenses/Average assets	1.8	1.7	1.7

Source: Bank of Slovenia.

followed by the banks and savings banks, was 259.7 billion tolars as at 31 December 2000 including aggregate initial capital in the amount of 241.9 billion tolars.

As regards management and containment of **credit risk**, the banks should focus efforts on avoiding excessive concentration of exposures to a single client or group of connected clients. An important criterion of large exposure of a bank to a client or group of connected clients is its value. In the case where the value of a bank's exposure is equal to or exceed 10 per cent of the bank's capital, such exposure shall be considered a large exposure under the Decree on Large Exposure of Banks and Savings Banks. The sum of all large exposures may not exceed 800 per cent of the respective bank's capital, and the limit on a bank's exposure to a single client may not exceed 25 per cent of its capital.

Banks' aggregate large exposure comfortably below regulatory limits

As at 31 December 2000, aggregate large exposure incurred by the Slovenian banks was well below regulatory requirements – this figure averaged 185.1 per cent of capital. Three banks reported of exposure to group connected clients of 25 per cent, and two of them exceeded this criterion by less than 1 per cent and one by 12.1 per cent, respectively. During the same reporting period, three banks reported positions where the 20 per cent limit on exposure to clients those banks controlled directly or indirectly i.e. to parent undertakings. The deviations reported by the banks ranged from 0.1 per cent to 24.3 per cent. Under the Banking Act 1999, the banks have time until 31 December 2001 to comply with the large exposure requirements and where a bank exceeds limits on large exposures, it shall remedy the situation.

For the purpose of assessing credit risk, banks and savings banks grade on-balance sheet assets and off-balance sheet items in five groups on the basis of the criteria set for the purpose of classifying assets. As at 31 December 2000, the banks had in their loan portfolios less A-graded assets compared to 1999 (a drop of 1.1 percentage points) and less E-graded assets (a drop of 0.1 percentage point) in favour of a slight increase in B-graded assets (a rise of 1.1 percentage point) and C- and D-graded assets (a rise of 0.1 percentage point). If claims on the Bank of Slovenia and the Republic of Slovenia were deducted from aggregate exposure of the banking sector, the structure of the loan portfolio as at 31 December 2000 would be as follows: A: 83.9 per cent, B: 9.5 per cent, C: 2.0 per cent, D: 2.0 per cent in E: 2.0 per cent.

The volume of bad and doubtful assets was rising in 2000 at the same rate as the overall operations conducted by the banks - 18.4 per cent, i.e. 8.8 per cent in real terms and 18.3 per cent, i.e. 8.6 per cent in real terms, respectively. The portion of bad and doubtful assets in gross total assets compared to the end of 1999 grew from 11.6 per cent to 13.0 per cent, while the portion of value adjustments in gross assets of banks rose from 6.3 to 6.5 per cent. The coverage of bad and doubtful assets with value adjustments have gradually decreased over the past four years landing at the end of 2000 at 44.7 per cent (1997: 55.6 per cent).

Table 18: **Classification of on- and off-balance-sheet items of banks, value adjust ments and provisions** (in millions of tolars)

	31/Dec/1999					31/Dec/2000				
	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	2,751,937	88.5	*(85,0)*	178	0.1	3,264,439	87.4	*(83,9)*	171	0.1
B	196,315	6.3	*(8,2)*	22,479	18.7	277,864	7.4	*(9,5)*	30,728	21.4
C	63,123	2.0	*(2,7)*	18,553	15.4	77,144	2.1	*(2,6)*	20,726	14.4
D	46,511	1.5	*(2,0)*	27,225	22.6	58,745	1.6	*(2,0)*	33,743	23.5
E	51,794	1.7	*(2,2)*	51,789	43.1	58,289	1.6	*(2,0)*	58,351	40.6
Total	3,109,680	100.0		120,223	100.0	3,736,481	100.0		143,719	100.0

Note: Percentages in brackets exclude claims on the Bank of Slovenia and the Republic of Slovenia.
Source: Bank of Slovenia.

As at 31 December 2000, aggregate exposure of banks to credit risk was 3,736.5 billion tolars (including 3,034.8 billion tolars in on-balance sheet assets and 701.7 billion tolars in off-balance-sheet risk-weighted items). Exposure to a single client increased to 120.1 million tolars in comparison with 1999 – a 7.3 per cent rise. Over the last four years, the banks have substantially improved the ratio between recovered and written-off assets - 48.7 per cent at the end of 2000 (1997: 12.1 per cent).

3.3. Review of operations of savings banks

Share of savings banks in banking sector remains 0.4 per cent

At the beginning of 2000, there were six savings banks operating in Slovenia and by the end of the year their number plunged to three. During the year under review, one savings bank joined a large savings bank, one savings bank was taken over by a commercial bank from the middle market section, and in the middle of 2000, proceedings to wind-up one savings bank were initiated. Total assets of the remaining three savings banks at the end of 2000 stood at 12.3 billion tolars posting a year-on-year rise of 11.5 per cent. Thus the share of savings banks in Slovenia's banking environment remains fairly modest (0.4 per cent).

Deposits by households rise to 26.5 per cent share in savings banks' liabilities

The savings banks vary considerably in terms of business volumes and the composition of their balance sheet items. Following record high deposits placed by non-financial enterprises in 1999, this group of deposits experienced a drop by 1.3 percentage points last year. Nevertheless, with a 21 per cent share, these deposits provide the second largest source of funds in the savings banks' liabilities structure. In the group containing deposits of the non-bank sector, the share of deposits of households remains strong rising in the average structure of liabilities from 22.0 per cent to 26.5 per cent year-on-year. On the other hand, deposits from the banking sector decreased in real terms by 44.2 per cent last year and at year-end amounted to 681 million tolars or 9.1 per cent of liabilities carried on the books of the Slovenian savings banks.

76.1 per cent of savings banks' total assets allocated to lending to households

Funds gathered by the savings banks are mainly passed on as lending to households. Namely, loans and advances have increased by 22.3 per cent in real terms during the past year and at the end of 2000 stood at 76.1 per cent of average aggregate total assets of the savings banks. The share of loans and advances to the banking sector decreased to 5.4 per cent at the end of 2000, and lending to non-financial enterprises also lost edge and was 8.9 per cent of average total assets. After exceptional growth in 1994, the savings banks gradually pulled out of securities investment; hence their share in average aggregate total assets at the end of 2000 was 1.7 per cent.

As much as 60.7 per cent of savings banks' lending to the non-bank sector is long-term

The proportion between short-term and long-term lending of the savings banks to the non-bank sector at the end of 1997 was 64.1 per cent against 35.9 per cent, but it gradually improved and at the end of 1999 this percentage was practically levelled. While short-term lending decreased in real terms by 12.2 per cent, long-term lending bounced by 37.4 per cent, and long-term lending outstripped short-term loans and advances last year: 60.7 per cent against 39.3 per cent. The maturity structure of deposits from the non-bank sector placed was somewhat improved in favour of longer repayment periods. Namely, the share of long-term deposits grew from 21.2 per cent at the end of 1999 to 23.8 per cent at the end of 2000, the share of short-term deposits dropped from 74.5 per cent to 72.0 per cent, while the share of deposits repayable on demand remained flat at 4.2 per cent.

In 2000, all savings banks operated with profit generating 156.9 million tolars in pre-tax profit, i.e. 24.5 million tolars less than in 1999. Gross income earned in 2000 compared to 1999 decreased in real terms by 16.5 per cent mainly due to thinner earnings arising from net interest income and net financial transactions. Net fees and commissions grew in real terms by 8.9 per cent. Expenses dropped in real terms by 18.0 per cent with labour costs falling by 23.1 per cent. The share of labour costs in average total assets dropped from 2.4 per cent in 1999 to 1.7 per cent year-on-year, and the share of aggregate operating expenses shrank from 5.0 per cent to 3.8 per cent at the end of 2000. The savings banks earmarked net provisions in the amount of 61.6 million tolars, or 13.9 per cent more in real terms compared to 1999.

Average return on assets earned by the savings banks decreased to 1.3 per cent, and return on equity plunged from 17.7 per cent in 1999 to 12.6 per cent in 2000. In 2000, the savings banks' interest rate margin continued to grow thinner and after losing 1.5 percentage points was at 3.6 per cent and for the first time lagging behind the banks' interest rate margin.

As at 31 December 2000, exposure of the savings banks to credit risk amounted to 11.7 billion tolars. As opposed to1999, the quality of loan portfolios managed by the savings banks has improved, and the share of A-graded clients rose by 5.5 percentage points to 97 per cent. By restructuring the loan portfolio, the savings banks have reduced the share of bad and doubtful assets in gross total assets (from 8.7 per cent at the end of 1999 to 4.5 per cent at the end of 2000). The sum of large exposure reported by the savings banks as at 31 December 2000 - 23.2 per cent of capital was

Box 7: **Savings and loan undertakings**

Just as in the case of banks and savings banks authorised under the Banking Act 1999, savings and loan undertakings will have to be in line with the provisions of EU directives, which govern credit institutions. Since the alignment with capital and other requirements call for a major overhaul, savings and loan undertakings need a longer transitional period; hence a five-year period has been envisaged for savings and loan undertakings to complete the transformation process, i.e. become compliant. The Bank of Slovenia has elaborated on the steps of this process in the Decree on Bringing of the Operations of Savings and Loan Undertakings into Line with the Provisions of the Banking Act (Official Gazette of the Republic of Slovenia, No. 109/99). Savings and loan undertakings have been given time until 31 December 2004 within the framework of negotiations with the European Union to transpose capital and other requirements necessary for safe and sound operations in line with the EU banking directives.

Save in the case of savings and loan undertakings, which had passed a decision by 29 January 2001 to begin activities leading to winding-up of business, all savings and loan undertakings shall comply with the provisions of the Banking Act 1999 in line with the conditions and milestones laid down in the Decision on Compliance of Savings and Loan Undertakings with provisions of the Banking Act. The requirements also apply to those savings and loan undertakings, which would opt for a merger with another institution later on. As for the future of savings and loan undertakings in the Republic of Slovenia, eighteen savings and loan undertakings have declared interest in aligning with the requirements set out in the Banking Act 1999, thirty will amalgamate with the Association of Savings and Loan Undertakings, thirteen will join banks and savings banks, while the remaining undertakings have been wound-up.

Terms and conditions for setting up and running savings and loan undertakings in the Republic of Slovenia were laid down in a special law on savings and loan undertakings promulgated back in 1969 and superseded by the effective law in 1990. The law does not prescribe minimum capital base (initial capital) and leaves to the founders to set out terms and conditions governing operating activities of savings and loan undertakings. Under the effective law, founders are jointly and severally liable for savings deposits and all liabilities incurred by the respective savings and loan undertaking.

The Bank of Slovenia has been responsible for monitoring savings and loan undertakings for statistical purposes and within the framework of implementing its monetary policy objectives. Under the Law on Banks and Savings Banks, savings and loan undertakings are required to keep books of account and comply with the requirement to maintain mandatory reserves. Hence savings and loan undertaking have been sending monthly reports to the Bank of Slovenia on balances on accounts, financial statements and reports on compliance with the mandatory reserve requirement since 1992. As from 1995, savings and loan undertakings also abide by the regulatory requirement to submit reports relating to their average interest rates.

substantially below the regulatory requirements. Other ratios that serve as a safeguard against excessive concentration of credit exposure (to single clients and group of connected clients, as well as in the case where a client is the parent undertaking or the subsidiary of the savings bank) in relation to the respective savings bank's capital, were all within the regulatory limits last year.

Downward trend in lending and deposit rates and…

… thinner real interest spread in savings banks.

Over the past years, lending interest rates and interest rates paid on deposits by the savings banks have been above levels offered by the banks, but this is gradually changing. During the last quarter of 2000, real lending interest rate charged by the savings banks was 7.5 per cent as opposed to 5.7 per cent charged by the banks, whereas real deposit interest rate paid by the savings banks was 4.4 per cent as opposed to 3 per cent paid by the banks. As a result, real interest spread earned by the savings banks was with 3.1 percentage points still above the interest spread made by the banks (2.7 percentage points), but the savings banks are slowly losing advantage.

Average capital adequacy in the savings banks was 11.3 per cent as at 31 December 2000 – a considerable drop with respect to 14.4 per cent at the end of 1999. One savings bank reported capital adequacy ratio just at the regulatory minimum - 8 per cent.

3.4. Review of supervision of banks and savings banks

Ongoing screening of prudential reports and statutory returns coupled with on-site examinations (by following the so-called four-eye principle) helps foster market discipline and provides information as to a bank's activities and the risks it is exposed to. Supervision and surveillance of banks and savings banks is regarded as an ongoing process and the analysts and examiners of the Bank Supervision Department strive to safeguard solidity and integrity of banking business without undue disturbance of a market economy mechanisms.

Off-site supervision analysts have responsibility to participate in assessing operating results of banks and savings banks, in granting new authorisations and amending the extent of services under the authorisations already granted. They also evaluate drafts of new systemic solutions, advise banks and savings banks as to the implementation of standards for safe and sound banking operations, monitor compliance with the regulatory requirements and prudential limits designed to ensure orderly and prudent conduct of business, and oversee capacity and efficiency of the banks and savings banks by verifying information contained in statutory returns at least once a month. Analysts also provide valuable input in the course of preparations for on-site examinations of the banks in savings banks and take part in meetings with senior management of a bank or a savings bank, or other institution, they draft materials on professional issues, etc. If while carrying out their tasks, analysts become aware of certain facts, which are liable to affect the financial situation or the accounting and administrative organisation of the respective bank or savings banks, they notify the examiners and management of the Bank Supervision Department. In the case where irregularities are detected in a bank or a savings bank, appropriate corrective actions are taken and both examiners and analysts monitor the implementation of such remedial measures.

In 2000, 6 full-scope examinations and 23 targeted examinations were carried out

Each year over the last three years, all operations of six to thirteen banks and savings banks, and selected business areas of five to thirty banks and savings banks have been examined. In 2000, the examiners of the Bank Supervision Department conducted examinations in twenty-nine banks and savings banks (six full-scope on-site inspections in four banks and in two savings banks), as well as examinations of individual business segments (twenty-three targeted on-site inspections in thirteen banks and two savings banks). In addition, joint activities were conducted by the examiners of the Bank Supervision Department and their counterparts from other parts of the central bank with the aim to screen the criteria for the transitional period of the payment and settlement systems refor.

Regular meetings take place with senior management of banks and savings banks every year, sometimes within the framework of full-scope examinations. These meetings are convened to assess capacity and efficiency of the respective bank, i.e. savings bank, to evaluate the current position and learn about its strategic orientation. Exchange of views and information sharing between banking supervisors and senior management of a bank or a savings bank is essential to a timely identification a problem.

A reduction is envisaged in the number of full-scope examinations to some seven to nine annually, and a rise in the number of targeted examinations. More than thirty targeted examinations of banks and savings banks should be carried out annually. A bank or a savings bank may be examined more than once a year, but each bank is to be examined at least once every year. Which business segment in a particular bank or a saving bank will be examined depends on a host of factors (financial condition and performance, risk profile, risk management practices, governance, etc.).

Focus on targeted examinations

Targeted examinations, i.e. verification of the condition of a designated activity, are the most common form of oversight of the activities with a high degree of inherent risk or those that do not provide comprehensive and consistent information to the Bank of Slovenia. Since credit risk poses a particular challenge to the Slovenian banks and savings banks, the examiners try to verify disclosures a bank or a savings bank has made with regard to the classification of on- and off-balance-sheet items, and may also conduct supervision on a consolidated basis of the respective bank and other connected persons. They analyse financial statements of such connected persons, where that person is the parent undertaking or subsidiary of the bank, they also examine the bank's lending policy towards connected persons, the quality of their asset portfolio, management/governance and the relationship with the bank, as well as operational risk exposures. On the basis of these disclosures, the examiners test if for instance provisions and value adjustments made are commensurate to the potential impact of a particular risk exposure to the bank arising from connected lending or equity holdings/participating interests.

Mandate to the Bank of Slovenia to supervise connected persons and persons who may be engaged in unauthorised banking operations

Targeted examinations focus on the current loan portfolio for corporate and individual customers, investment portfolio, management information, and internal audit function, connected undertakings, reliability and timeliness of financial and management information, information technology, etc.

Ongoing collaboration between banking supervisors of the home and host country, as well as between banking supervisors and other competent authorities within the territory of Slovenia, is one of the founding principles of prudential supervision. The need to supply one another with such information that may facilitate monitoring was materialised in Slovenia last year through the co-operation between the central bank on the one hand and the Securities Market Agency and the Market Inspectorate of the Republic of Slovenia on the other. A team composed of the examiners of the Bank Supervision Department and the examiners of the Securities Market Agency examined two banks (i.e. connected undertakings), while five examinations were conducted on the basis of notifications made by the Market Inspectorate of the Republic of Slovenia (examinations of undertakings suspected of engaging in unauthorised banking activities).

As regards supervision of subsidiaries and branches of Slovenian banks in foreign countries, the first on-site examination of a Slovenian subsidiary incorporated in the U.S.A. was carried out in 2000 by a team of examiners from the Bank of Slovenia, the State of New York Banking Department and the Federal Deposit Insurance

Memoranda of understanding signed with foreign Banking supervisors

Corporation. The Memorandum of Understanding signed with the State of New York Banking Department has provided a legal basis for the on-site examination. At the beginning of 2001, the Memorandum of Understanding was signed with the Federal Ministry of Finance (Bundesministerium für Finanzen), and talks are under way to formalise relationship with Bundesaufsichtsamt from Germany, the Banking Agency of the Federation of Bosnia and Herzegovina and of Republika Srbska, as well as with the National Bank of Macedonia. Furthermore, a communication channel with Banca d'Italia has been functioning for some time already.

In November 2000, the International Monetary Fund (IMF) made an assessment in co-operation with the World Bank of the level of compliance achieved by banking supervisors with the Core Principles for Effective Banking Supervision issued by the standard-setter for banking supervision, the Basel Committee on Banking Supervision in 1997. This assessment and the action plan elaborated by the Bank of Slovenia with the aim to achieve full compliance with the Core Principles, have been drafted on the basis of the self-assessment made by the Bank of Slovenia.

4. OTHER FUNCTIONS

4.1. Management of international reserves

In line with the Bank's core purposes, one of the basic tasks carried out through the Bank of Slovenia is to hold and manage the international reserves of the Republic of Slovenia defined as the aggregate balance of holdings listed below:

- foreign cash and balances on accounts abroad,
- gilt-edged securities of foreign issuers,
- monetary gold,
- Special drawing rights (SDRs) and the IMF reserve position.

International reserves managed by the Bank at year-end totalled US$ 3,196 million …

After a drop in 1999, the international reserves held and managed by the Bank of Slovenia increased during the year under review from 3,168 to 3,196 million US dollars. Part of the foreign exchange reserves (foreign cash, accounts abroad, foreign securities) are liabilities of the Bank of Slovenia to domestic sectors arising from subscribed bills of the Bank of Slovenia denominated in foreign currency and foreign exchange accounts of banks and central government with the Bank of Slovenia. This part of reserves topped 1,733 million US dollars in 2000 rising from 1,699 in 1999. Another portion of the foreign exchange reserves – without counterliabilities - totalled 1,463 million US dollars in 2000. Aggregate claims of the Bank of Slovenia on foreign counterparties include in addition to the official foreign reserves and holdings with the IMF, also some other holdings such as balances on the fiduciary account in Luxembourg.

…including US$1,463 million free of counterclaims in foreign currency.

In 1998, Slovenia's status in the IMF changed to a creditor within the framework of the *Operational Budget* referred to as the *Financial Transactions Plan* (FTP). In 2000, Slovenia participated in the FTP for Mexico in the amount of 2.7 million dollars, while Jordan, Russia and Mexico repaid funds under lending agreements concluded over the past years in the aggregate amount of 22.7 million dollars. Thus the reserve tranche with the IMF decreased in 2000 by 20 million dollars. The reserve tranche of the Republic of Slovenia in March 1998, when Slovenia joined the

Table 19: **International reserves and foreign exchange reserves of the banking system** (year-end in millions of US dollars)

	BANK OF SLOVENIA							BANKS
	International monetary reserves					Including counter value of liabilities in foreign currency * to residents	Other foreign assets	Foreign exchange reserves
	Gold	SDRs	Reserve position in IMF	Foreign exchange reserves	Total			
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	3,168.0	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	1,260.0

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

Operational Budget amounted to 17.4 million dollars, while at the end of 2000 it was 82.3 million dollars, including a 41.6 million dollars increase due to the participation lending operations.

The Governing Board of the Bank of Slovenia sets on a quarterly basis the guidelines for management of the portfolio of foreign exchange reserves of the Bank of Slovenia, determining the currency structure, average maturity, i.e. interest rate sensitivity inherent in foreign exchange deposits, i.e. investments in securities, and short-listed banks (investments in foreign currency assets are allowed only in financial instruments of banks awarded top long-term credit ratings).

The Bank of Slovenia continued in 2000 along the guidelines set out in the strategy endorsed by the Governing Board of the Bank of Slovenia to enlarge the share of investment in securities (predominately in government securities) with the aim to steer better liquidity position and reduce exposure to credit risk.

4.2. Banking services to central government

Cross-border payments

Under the law, the central bank handles cross-border payment transactions, as well as other transactions in foreign currency for the account of the government of the Republic of Slovenia. Thus in 2000, the Bank cleared outgoing payments in the amount of 378.6 million euros, and effected payments in cash totalling 7.8 million euros. Inward flows amounted to 506.4 million euros, whereas foreign cash repayments added up to 2 million euros. The bank sold 40.3 million euros to the users of the budget of the Republic of Slovenia and purchased from them 217.4 million euros including monetised 188.0 million euros. The difference up to the final balance of outgoing payments is made up from disbursements under loan agreements and subsidies from abroad.

Domestic payments

An important element of the payment systems reform has been the migration of accounts used for the purpose of effecting payments within the budgetary framework. These accounts have been integrated under the umbrella of the so-called single treasury account opened with the Bank of Slovenia. The government of the Republic of Slovenia opened its transaction account with the Bank of Slovenia in 1999 with the aim to phase in clearing of designated transactions related to effecting payments for the account of the government. As from the day the single treasury account was opened and throughout 2000, payments and disbursements related to treasury bills have been cleared through this account.

Provision of stamps, securities and cash

The Bank of Slovenia conducts on behalf and for the account of the government of the Republic of Slovenia operations related to the issue, distribution and safekeeping of securities and duty stamps. In 2000, administrative and court stamps were issued in the total value of 5.6 billion tolars (in 1999: 2.4 billion tolars). The work of experts and technical staff on tobacco stamps required the provision of adequate quantities and structure of tobacco stamps, alongside distribution to producers and importers of tobacco products. The total number of stamps issued was 208,220,000 pieces of different tobacco brands (in 1999: 225,445,000 pieces).

Another task entrusted to the Bank of Slovenia is to accept and process redeemed government bonds and coupons when they are due. In 2000, the Bank accepted 57,906 coupons of RS 02 government bonds.

Furthermore, the Bank handled 2,926 incoming and outgoing cash payments in tolars, as well as 14,469 incoming and outgoing payments in foreign currency for travel expenses and other activities of government bodies (in 1999: 3,280 incoming and outgoing payments in tolars and 17,570 incoming and outgoing payments in foreign currency).

4.3. Cash operations

Central bank is under the law responsible for the continuing and smooth provision of banknotes in tolars.

At end-2000, 108.8 million banknotes in the nominal value of 139.6 billion tolars in circulation

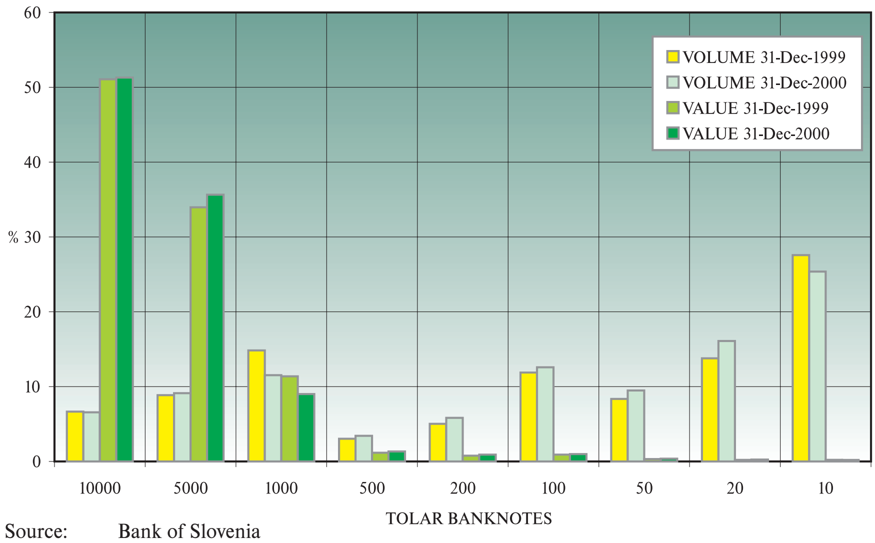
As at 31 December 2000, there were 108.8 million banknotes in circulation in the nominal value of 139.6 billion tolars (including cash balances in the banks). The value of banknotes in circulation decreased by 2 per cent compared to 1999, while the quantity of banknotes in circulation fell by 0.2 per cent. The reduction in cash in circulation indicates shrinking liquidity reserves of individuals and suggests that other payment instruments were used during the period under review. A breakdown of cash in circulation over the last five years is shown in Table 20. At the end of 2000, banknotes accounted for 99.4 per cent of value and 24.5 per cent of quantity of cash in circulation. As regards value, the banknote of 10,000 tolars was the most common banknote (it accounted for 51.3 per cent of the value of all banknotes in circulation as opposed to 1999 when it accounted for 51.1 per cent of the value of all banknotes in circulation). The banknote of 5,000 tolars was the second important

Table 20: **Cash in circulation** (1996 – 2000) in millions of tolars

At year-end	Banknotes in circulation	Coins in circulation	Cash in circulation - total
1996	71,440	414	71,854
1997	85,652	488	86,141
1998	104,667	564	105,232
1999	142,488	641	143,130
2000	139,644	791	140,435

Source: Bank of Slovenia

Figure 14: **Breakdown of banknotes in circulation by volume and denomination** (at the end of 1999 and 2000, in %)



Source: Bank of Slovenia

denomination in cash transactions (it accounted for 35.6 per cent of the value of all banknotes in circulation as opposed to 1999 when it accounted for 34.0 per cent). The denomination of 1,000 tolars is not so important as it used to be; hence the 1,000-tolar banknotes accounted in 2000 for 9.0 per cent of the value of banknotes in circulation compared to 11.4 per cent in 1999. The movements in value and quantity of banknotes in circulation in 1999 and 2000 are shown in Figure 14.

The Bank of Slovenia processed 79 million banknotes including 40.2 million banknotes to be sorted. For the purpose of providing adequate quality of banknotes in circulation, 30.6 million banknotes were removed from circulation and destroyed (in 1999: 17.1 million). The bulk of worn-out banknotes - 9.3 million – were 1,000-tolar pieces. In addition, 3.8 million 5,000-tolar banknotes were destroyed (mainly due to poor to insufficient quality of the first issue put in circulation in 1993), while 3.9 million 10-tolar banknotes were replaced by coins in 2000 and 13.6 million in other denominations.

As regards the supply of cash in tolars, it is organised through contractual depots of banknotes of the Bank of Slovenia and the money distribution network of the Agency for Payments. The Bank of Slovenia determines the ceiling on treasury holdings on a quarterly basis and checks on their operations on a daily basis. Throughout the last year, the set limits were observed and no irregularities were detected in operations involving cash.

In the first half of 2000, the Bank printed: 6 million banknotes of 10,000 tolars, the same quantity of banknotes of 5,000 tolars and 10 million banknotes of 1,000 tolars in response to the rising need for banknotes of the said denominations intended to replace worn-out and damaged banknotes in circulation.

In 2000, the Bank of Slovenia introduced a new 10-tolar coin and released 10 million pieces in circulation, as well as 45 million coins in the nominal value of 5, 2 and 1 tolar. Since 1993, the number of coins in circulation has topped 336 million (in 1999: 300 million), in the value of 791 million tolars (in 1999: 642 million). The quantity of coins in circulation increased in 2000 by approximately 12 per cent.

During the past year, the Bank of Slovenia has sold directly or through intermediaries 1,756 pieces of jubilee coins. The special issues include 564 gold coins and 1,192 silver coins. In 2000, no new jubilee coins were issued.

Box 8: **Cash distribution reform**

There were eight depots responsible for the distribution of banknotes issued by the Bank of Slovenia in 2000 operating within the framework of seven commercial banks-depositories.

Until the network of the Agency for Payments is in place, the depots obtain cash from the Agency branches to keep costs down. The depots of the Bank of Slovenia banknotes are partly supplied with cash derived from operations of banks and savings banks, which use their services.

The direct users of the depots have entered into contracts with the depositors to use the services provided by the respective depot, whereas other banks meet their needs for banknotes by buying from and selling to depositories (retail banknote market operations). The volume of these retail operations increased significantly in 2000 compared to 1999.

As the migration of accounts of legal persons from the Agency for Payments to commercial banks goes on and cash payment transactions are being gradually removed from the Agency for Payments, the banks take over cash incoming and outgoing payments for the account of legal persons. The banks get cash from customers, and cash provided at the distribution points of the central bank (the depots of banknotes of the Bank of Slovenia; for the time being the distribution network of the Agency for Payments) serves to balance cash from operations (surplus or shortage), which is the bottom line of the cash distribution concept.

The Bank of Slovenia examined 4,981 pieces of counterfeited banknotes (in 1999: 6,947 pieces) discovered and confiscated in the territory of the Republic of Slovenia. The Bank's experts collaborated with the Ministry of Home Affairs and Interpol. Counterfeited banknotes of foreign currencies accounted last year for the bulk of all counterfeited banknotes - 3,593 counterfeits. Nevertheless, the number of counterfeits has been falling rather quickly over the past few years (6,079 and 11,960 counterfeited banknotes in 1999 and 1998, respectively).

Plunging number of counterfeited banknotes in foreign currency and …

In spite of the fact that the value of counterfeited Slovenian tolars is rising, counterfeited tolar banknotes still account for a negligible share in total value of cash in circulation (increasing from 0.0010‰ in 1994 to 0.0735‰ in 2000). The total value of confiscated counterfeited tolar banknotes amounted to 10,321,350 tolars. The Ministry of Home Affairs asked the experts of the Bank of Slovenia to examine 791 samples of counterfeited banknotes of 10,000 tolars, 457 samples of 5,000 tolars, 124 samples of 1,000 tolars and 16 samples of other denominations. As opposed to 1999, the number of counterfeited 10,000-tolar banknotes increased by 31.6 per cent, counterfeited 5,000-tolar banknotes surged by 178.7 per cent, and the number of counterfeited 1,000-tolar banknotes rose by 42.5 per cent.

… more counterfeited tolar banknotes whose value remains negligible.

The tasks carried out by the Bank of Slovenia in relation to bills include custody, distribution and redemption of bills. In 2000, 10 bills issued by the Bank of Slovenia were processed at the flotation and 4,882 individual parts of those bills were processed at redemption.

4.4. Payment systems reform

As part of the overhaul of the payment systems in Slovenia, the joint project involving the Bank of Slovenia, Ministry of Finance, Agency for Payments, commercial banks, savings banks, Bank Association of Slovenia, and the Statistical Office of the Republic of Slovenia continued in 2000. Particular attention was paid to further strengthening of the real time gross settlement system (RTGS) and the Giro Clearing system. Besides, efforts focused on identifying and putting together the resources for the migration of accounts of legal persons from the Agency for Payments to banks. The migration of accounts was conceived as the final step of the payment systems reform and it lifted off the ground on 11 September 2000.

September 2000: migration of accounts of legal persons from Agency for Payments to banks starts

To facilitate the changeover, detailed guidelines for conducting payment transactions for the account of legal persons within the territory of the Republic of Slovenia have been drawn up on the basis of the Law on the Agency for Payments (hereinafter referred to as the Criteria). Comprehensive preparations have also included explanatory notes with regard to the changes required within the framework of the migration of accounts of legal persons to the banking environment. For organisational and technical aspects of discharging tasks laid down in the Criteria the document has been prepared, called Substantial Changes at Migration of Accounts, which elaborates on the necessary changes and proposes solutions to overcome problems associated with the migration of accounts of legal persons to the banking environment. Both documents have been prepared by the Bank of Slovenia and reconciled with the officials of the Ministry of Finance, including Tax Administration and the Agency for Payments. These documents have served as a foundation for the experts of the Bank of Slovenia and the Ministry of Finance to prepare guidance notes relating to organisational and technical matters.

Alongside the preparation of the guidance notes for discharging tasks relating to payment transactions, the activities relating to the issue of special authorisations to banks to provide payment services for the account of legal persons within the territory of the Republic of Slovenia were going on. At the end of July, the eligible banks obtained the special authorisation granted by the Bank of Slovenia and the

Ministry of Finance, and 11 September 2000 was set as the date for the commencement of the migration of accounts of legal persons to banks.

In accordance with the decision passed by the Government of the Republic of Slovenia in December 1999, the migration of 50,000 accounts of legal persons from the Agency for Payments to the banking environment started step-by-step in seven phases in line with the endorsed operational plans (lists of legal persons). The banks were asked to present their operational plans relating to the migration of accounts to a special co-ordination team composed of the representatives of the Bank of Slovenia, Ministry of Finance, Agency for Payments, and the Statistical Office of the Republic of Slovenia.

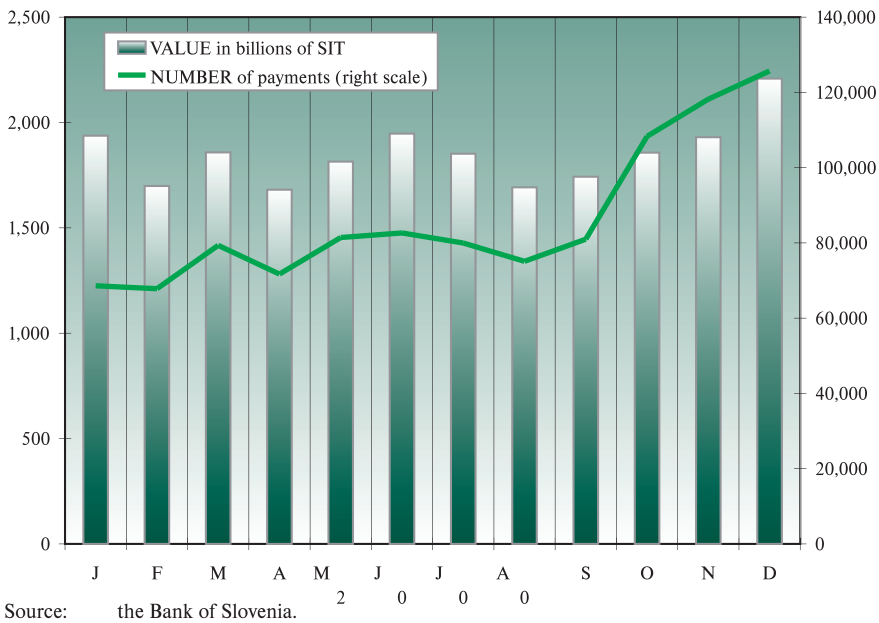
By July 2000, the operational plans for the third and the fourth phase of the migration of accounts to the banks were confirmed. The third phase envisaged the migration of 5,243 and the fourth of 7,017 accounts of legal persons. As a result, after the first four phases, the total number of 20,915 accounts of legal persons would be transferred to commercial banks.

In addition to legal persons covered by the plan for the migration of accounts during the first period, the persons listed below were able to open transaction accounts by the end of 2000 with a commercial bank:

- Newly registered legal persons,
- The legal persons who participated in the pilot training project for banks (by the end of September 2000),
- The legal persons from the organisational unit of the Agency for Payments in Tržič (prior to its closure on 30 November 2000), and
- As from 20 December 2000, the legal persons who were included in the account migration plan in the first period, but who asked for the account transfer at the earliest convenience.

As of the day the migration of accounts started, the accounts of the first five legal persons were transferred to the banking environment, and by the end of September, all banks opened transaction accounts for at least one legal person. Although the blueprint plant envisaged the completion of the migration of accounts for the first period by the end of 2000, the process took more time than expected. By the end of

Figure 15: **Volume of payment transactions cleared through the RTGS** system in 2000



Source: the Bank of Slovenia.

2000, 1,555 out of 4,656 legal persons entitled to opening an account in the first round of migration, actually opened transaction accounts with the banks in 2000. Other legal persons included in the first account migration phase could do so in the second phase, i.e. by the end of March 2001.

Planned completion of accounts migration in June 2002

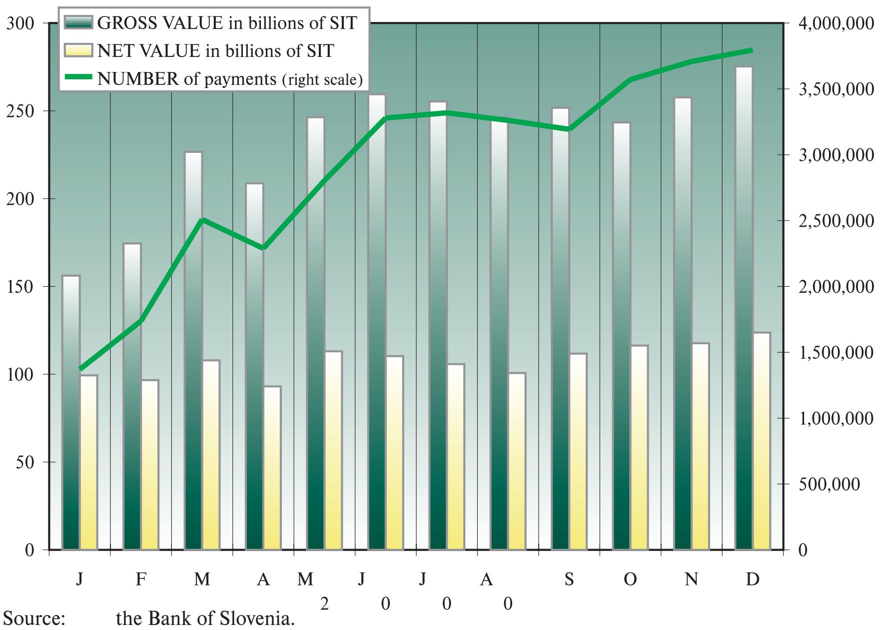
The pace the migration of accounts of legal persons affects the dynamics of the overall process, i.e. two- or three-month steps for the transfer of accounts to the banking environment. If the operational plans were implemented on a quarterly basis, the migration process could be completed by the end of June 2002.

At the end of May, the Expert Committee of the Bank of Slovenia started to check the situation on the ground: the readiness of the banks for the migration (primarily payment transaction functions, cash operations, and information technology) on the one hand and the prepared documentation on compliance with the Criteria for the provision of payments services to legal persons on the other. The assessment was the basis for authorising the respective bank to carry out payment transactions for legal persons within the territory of the Republic of Slovenia. The Committee examined seven banks and their branches by the end of 2000.

Agency for Payments joins RTGS and Giro Clearing payment systems

In 2000, the Agency for Payments fully participated in the operations provided under the Real Time Gross Settlement (RTGS) and the Giro Clearing payment systems also by effecting payments from and to the giro accounts of legal persons kept with the Agency. Thus the consolidation of transactions provided through both systems was concluded on the ground. This has enabled payments between both systems and the giro accounts still held with the Agency for Payments to be transmitted in both directions. By consolidation the importance of the positions the banks have with the Agency for Payments (account 620) has decreased since settlement is conducted between the banking environment and the environment of the Agency for Payments after the full integration of the Agency for Payments in both system with central banking money on settlement accounts with the Bank of Slovenia through systems RTGS and Giro Clearing. The consolidation of the RTGS system was concluded already in 1999, while the Giro Clearing system was fully operational in June 2000. Payment orders were gradually included in the Giro Clearing system starting 1999, but the bulk of work was partly done in the first half of 2000, and the task was completed in the middle of July.

Figure 16: **Volume of payment transactions settled through the Giro Clearing system** in 2000



Source: the Bank of Slovenia.

In 2000, the RTGS system handled 1,039,796 payments during 250 working days in the aggregate value of 22,218.30 billion tolars, i.e. the RTGS system handled on average 4,159 payment transactions daily and the value of each transaction was 21,37 million tolars. During the period under review, the RTGS operated at 99.96 per cent capacity available for settlement.

Within the framework of the Giro Clearing system (net clearing system), during 250 working days, 34,837,077 payment orders were cleared in the aggregate value of 2,801,55 billion tolars. On average, 139,348 payment orders were cleared daily, average gross value per order amounted to 80,419 tolars. Net value of settlement in central bank money through settlement accounts within the framework of the RTGS, amounted to 1,296.40 billion tolars in 2000, i.e. 46.3 per cent of gross value of payment orders.

Modifications to Giro Clearing system

For the purpose of reducing exposure to risk, the limit value of a small value payment order submitted for clearance under the Giro Clearing system was lowered on 2 October 2000 from 3 million to 2 million tolars. On the same day, working hours of the Giro Clearing payment system was changed and an additional (fifth) settlement cut was introduced. Furthermore, charges levied by the Bank of Slovenia on payment orders to be cleared by both systems were also changed. Under the RTGS, the charge was reduced from 300 to 260 tolars, and under the Giro Clearing payment system the charge dropped from 10 to 8 tolars per payment order.

In October last year, intense preparations aimed at integrating the Bank of Slovenia into the Giro Clearing payment system were launched. Through the participation in the system, to effect payment transactions for payment orders of the Bank of Slovenia and its customers would be more cost-effective.

Transaction accounts register in place

At the beginning of 2000, the central transaction account registry set up by the Bank of Slovenia to support the migration of accounts of legal persons from the Agency for Payments to the banking environment was fully operational. The relevant data on settlement transaction accounts banks, savings banks and savings and loan undertakings, as well as of some sole entrepreneurs with banks have been fed to the central registry. After the migration of accounts of legal persons from the Agency for Payments to the banking environment, the banks timely add to the register also transaction accounts of legal persons and sole entrepreneurs who open transaction accounts with the Slovene banks.

Plans to launch integrated small value payment system

In December, the Governing Board of the Bank of Slovenia endorsed the study on the implementation of the integrated small value payments system (ISPMV). The paper elaborates on the objectives of setting up the ISPMV and a proposal for an organisational structure to support the realisation of concrete tasks. As regards the strategic level of policy-setting, decisions will be taken with respect to issues related to the implementation of interbank clearing and settlement, at the operational level the decisions relating to the implementation of clearance and settlement of payments between banks. On the basis of the agreement on the co-operation of banks in the field of the provision of payment services, the Payment Systems Development Committee composed of representatives of banks and the Bank of Slovenia has adopted a plan for future activities.

Efforts to integrate small value payments focus on:

- regulation of usage of payment instruments at the level of the banking system and not at the level of individual banks,
- dissemination and processing of interbank payment messages under the single communication infrastructure provided by the clearing house,
- effecting settlement of netted interbank claims and liabilities in central bank balances,
- transmission of payment messages in electronic and standard formats,

- limitation of membership to credit institutions only and allowing exceptions subject to approval of the credit institution.

In August 2000, the activities aimed at setting up clearing within the banking group of Nova Ljubljanska banka d.d. (NLB) through the RTGS system were launched. Clearing operations within the banking group of NLB will include clearing of payment transactions in tolars for clients within the banking group of NLB. For the purpose of preparing adequate legal basis and technical infrastructure in co-operation with NLB as the clearing agent, the principles applied to the Europay clearing system, where the Bank of Slovenia plays the role of the settlement agent, have been taken into consideration.

In November last year, the Governing Board of the Bank of Slovenia endorsed the study of the new securities trading settlement, i.e. its money-related part. The study addresses the migration of the money-related part of the settlement of accounts held with the Agency for Payments to the banking environment. The banks, stock-broking companies and possibly other institutions (e.g.: management and insurance companies, etc.) will open special accounts with the Bank of Slovenia (at present: accounts 748, 749 and 531) for the purpose of settlement of money-related part of operations involving securities. Only the Central Securities Clearing Corporation will have a special clearing account within the framework of the RTGS system for the purpose of settlement of money-related positions derived from deals on the recognised stock exchange.

Project of migration of money-related part of settlement of securities trading in banking environment

The project of the migration of money-related part of settlement led by the Central Securities Clearing Corporation and the Bank of Slovenia has two equally important objectives. The first objectives is to set up money-related part of settlement of securities trading within the framework of the reformed payment systems, i.e. the migration of the existing mechanism for money-related part of settlement of securities trading between counterparties from the Agency for Payments to the banking environment. The second core segment is to put in place settlement and mechanism of the DVP (delivery-versus-payment) for deals concluded outside the organised securities market (OTC deals).

Compliance with principles for systematically important payment systems

In the second half of 2000, particular attention was paid to the Core Principles for Systemically Important Payment Systems issued by the Bank for International Settlements (BIS) and to the compliance with these principles under the reformed payment systems in Slovenia. That document issued in July 2000 was prepared by the Committee on Payments and Settlement Systems of the central banks of the Group of Ten (G10, made up of the largest creditor countries) within the framework of efforts to boost financial stability by strengthening financial infrastructure with focus on safety and efficiency of payment systems. A valuable tool to be used for this purpose is self-assessment of the level of compliance with the Core Principles. Furthermore, particular attention has been paid to effective compliance and assessment of compliance with the Core Principles also by the Mission of the IMF in November last year, which reviewed the stability of Slovenia's financial system. On the basis of both assessments, an action plan has been drawn up with the aim to foster activities towards full compliance with international principles.

4.5. Statistical system

The statistical system of the Bank of Slovenia serves as support to defining and setting out the monetary policy of the Bank of Slovenia, it informs the domestic and foreign public on financial and macroeconomic movements in the Republic of Slovenia and co-operates with statistics divisions of international institutions of which Slovenia is member or strives to become one.

In line with the National Programme of Statistical Research, the Bank of Slovenia produces on a regular basis comprehensive clusters of statistics relating to credit institutions, balance of payments and international investment. These statistical clusters are primarily based on data and information from direct and indirect reports of banks and companies, as well as on the figures for the exchange of goods prepared the Statistical Office of the Republic of Slovenia on the basis of customs documents. Furthermore, the Bank of Slovenia also gathers, compiles and publishes statistical information related to modern payment instruments, financial markets, etc.

Enhanced collaboration with Eurostat and ECB in statistics

Methodological basis for the said statistics are standards of the International Monetary Fund (IMF), but the standards of the Eurostat and the European Central Bank (ECB) are becoming more and more important due to convergence with the legislative framework of the EU. The Bank of Slovenia disseminates statistics on its web site data in accordance with the Statistical Data Dissemination Standards the IMF for Slovenia, prepared together with the Statistical Office of the Republic of Slovenia and the Ministry of Finance. These standards call for regular and timely publication of methodologically adequate key macroeconomic figures according to a pre-announced calendar. Slovenia was among the first countries to start publishing in spring 2000 also the data on international liquidity in accordance with the broadened standard. Compliance with these standards enhances transparency and gives insight into the state of the country's economy crucial to timely recognition of financial difficulties and the Bank of Slovenia considers disclosure to be of key importance when access to international financial markets is at stake.

Slovenia provides statistical data on international liquidity according to IMF special data dissemination standards

The Bank of Slovenia produces the monthly *Bulletin* with key financial and macroeconomic figures of the Republic of Slovenia. In addition, the Bank published last year four quarterly bulletins the *Financial Markets* and the annual edition of the *Direct Investment*. All these publications along with information on the balance of payments and longer time series of data from the *Bulletin* are also available on the web site of the Bank of Slovenia. Furthermore, key statistical figures are also disseminated according to the calendar of the Bank of Slovenia updates on the web site. Among different domestic and foreign users, the Bank of Slovenia also provides statistical data to the IMF, Eurostat and the OECD.

October meeting in Ljubljana of Executive body of EU Committee for Monetary, Financial and Balance of Payments Statistics

In October 2000, the Bank of Slovenia and the Statistical Office of the Republic of Slovenia jointly hosted in Ljubljana the annual meeting of the Committee on Monetary, Financial and Balance of Payments Statistics (CMFB) with the representatives of statistical offices and statistical departments of the central banks of the candidate countries. The CMFB is the key body for the reconciliation of strategic issues of European macroeconomic statistics. The gathering in Ljubljana was the latest in a series of meetings since 1995, when the representatives of statistical institutions of candidate countries in 2000 started to attend plenary sessions of the CMFB.

4.6. International relations and co-operation

The Bank of Slovenia continued in 2000 with to pursue a constructive stance towards negotiations on succession to the former SFR Yugoslavia in line with the Dayton Accord.

A short-term credit line in the amount of 50 million dollars approved by the Bank for International Settlements (BIS) to the Bank of Slovenia in September 1999, was extended in March and then again in September 2000. Slovenia's share of assets of the former National Bank of the former federation under the succession formula were pledged as collateral to secure the loan. The Republic of Slovenia agreed back in 1996 with the proposal put forward by the BIS relating to the distribution of assets of former SFR Yugoslavia on the basis of the key proposed by the IMF.

The quota of the Republic of Slovenia within the International Monetary Fund (IMF) remained unchanged in 2000 and amounted to SDR 231.7 million, or 0.109 per cent of voting rights of all member countries.

Slovenia participates as the first transition country in IMF lending package

In 1998, Slovenia became the first transition country to join the group of countries whose currencies are used by the IMF when granting loans to its members within the framework of the Operational Budget, which since last year is referred to as the Financial Transaction Plan (FTP). The core purpose of the FTP is to provide assistance to member countries of the IMF, using the currencies regarded as more stable and sound ones serve to support more volatile currencies, i.e. for loans extended to the countries faced with problems relating to the balance of payments. By means of the FTP, with respect to estimated withdrawal and repayment schedule, the amount of funds required for loans in the course of the following quarter is determined. Alongside the selected indicators (member quotas), the IMF uses only the currencies of those member countries it regards as stable. When Slovenia was put on the list of creditors, there were thirty-three countries on that list. In December 2000, the list had thirty-eight countries, but the fact is that Slovenia was put on the list as the first country in transition and was invited to participate in lending operations with the amount of SDR 32.0 million. In the last quarter of 2000, which started with the month of December, Slovenia participated in the FTP with the amount of SDR 3 million. It was back in 1998 when Slovenia was invited for the first time to participate in the case of Indonesia. Last year it was among creditors for the financial package for Mexico. Since 1998, Slovenia has allocated the aggregate amount of SDR 49.0 million and during the same time the repayments under the lending deals amounted to SDR 19 million.

Slovenia joins as the first CEE transition country the developed countries by the World Bank criteria.

Thanks to its relatively high gross domestic product and developed institutions, Slovenia has been upgraded from the group of recipient countries to the group of creditors measured by the World Bank yardstick. Thus Slovenia has become the first transition country to join as full-fledged member the club of forty countries - decision-makers and creditors.

In November 2000, the Mission of the International Monetary Fund (IMF) and the World Bank visited Slovenia within the framework of the implementation of the Financial Sector Assessment Program (FSAP). The purpose of the Mission was to check the functioning and stability of Slovenia's financial system The Board of Executive Directors of the IMF will examine the FSAP Report for Slovenia at the same time with the examination of the regular report pursuant to Article 4 of the Statutes of the IMF in the first half of 2001.

Collaboration with ECB also in the field of central banking operations, legislation and payment systems

The European Central Bank (ECB), which in March 2000 announced its commitment to actively monitor the EU enlargement process and presented a blueprint plan to the European Parliament Committee for Economic and Monetary Issues, has strengthened bilateral and multilateral relations with the central banks of the candidate countries. The Bank of Slovenia co-operates with the ECB in the field of central banking operations, the EMU-related legislation, statistics and payment systems. In November 2000, the legal department of the ECB published a report with assessment of readiness of the central banks of the candidate countries as regards legal issues. The report of the ECB, which is due to be updated on a regular basis in the future, addressed in the first place the issue of autonomy of the central banks of the candidate countries, legislation in the monetary field, as well as legislative framework for the banking sector and financial markets.

Participation of Bank of Slovenia in negotiations for membership of EU

During the year under review, the Bank of Slovenia continued to co-operate actively on the EU-related issues by taking part in assessment of alignment between Slovenia's legislation and the EU legislative framework, as well as through the realisation of additional negotiating positions in the area of free flow of services and free flow of capital. The number of chapters closed for the time being rose at the end of 2000 to fourteen, including the chapters relating to the free flow of services and the economic and monetary union. As regards the area of free flow of capital, three groups of additional negotiating positions were submitted in 2000, including elaborated time schedule for lifting controls on capital flows until the date Slovenia becomes a full-fledged EU Member State.

In June 2000, the second meeting of the Association Council between the Republic of Slovenia and the EU took place. Conceived as a forum or institutional framework for the collaboration between the Republic of Slovenia and the EU, the meeting was also attended by the officials of the Bank of Slovenia. The keynote issue on the agenda was the assessment of the readiness of the Republic of Slovenia for accession. The assessment derived from the Regular Report on the Progress of Slovenia, the Accession Partnership, and the National Programme of the Republic of Slovenia for the Adoption of the *Acquis*, and it was positive. The officials of the Bank of Slovenia also participated in the sub-committee for the internal market, which under its new responsibilities also addressed the issues relating to financial services and establishment. They also attended the meetings of the sub-committee for economic and monetary issues, which also addresses the area of free flow of capital and statistics. At the meeting of the sub-committee for economic and monetary issues held in June, the topics included among other: overall assessment of priority tasks within the framework of economic policy, lifting of capital controls, privatisation, foreign direct investment, as well as transposition of *the acquis communautaire* relating to the EMU.

5. 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 2000 and 1999 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 81 to 96 ("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 2000 and 1999, 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 K. Morscher
Authorised Auditors

Zürich, 27 March 2001

Statement of income and expenditure

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

	Notes	**2000**	1999
Operating income:			
Income from financial assets		**35,010**	29,725
Net foreign exchange gain/loss		**28,642**	38,399
Gain (loss) from unrealized price revaluation		**3,557**	-8,292
Total income from financial assets	4	**67,209**	59,832
Expenses on serviced liabilities	5	**18,580**	16,885
Net investment income		**48,630**	42,947
Other income	6	**1,139**	952
Other expenses	7	**332**	408
Total operating income		**49,437**	43,491
Operating expenses	8	**3,685**	3,298
Provisions		**308**	-
Operating surplus available for appropriation		**45,443**	40,193
Appropriations:			
Transfer to foreign exchange reserves		**28,642**	38,399
Transfer to general reserves – price risks		**3,557**	-
Financial results after the appropriation of net foreign exchange gain/loss and gain (loss) from unrealized price revaluation		**13,244**	1,795
Transfer to general reserves – other risks		9,933	1,555
Total transfer to reserves	13	**42,132**	39,954
Provision for transfer of surplus to the budget of RS		**3,311**	240
Total appropriations		**45,443**	40,193

Balance sheet

at 31 December (in millions of tolars)

	Notes	**2000**	1999
Assets			
Financial assets	9	**764,585**	672,404
Fixed assets	10	**2,777**	2,914
Total assets		**767,363**	675,318
Liabilities and reserves			
Serviced liabilities	11	**492,717**	443,106
Banknotes in circulation	12	**139,644**	142,489
Provision for transfer of surplus to the budget of RS		**3,311**	240
Total liabilities		**635,672**	585,834
Reserves	13	**131,691**	89,484
Total liabilities and reserves		**767,363**	675,318

The notes on pages 84 to 96 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 1998	**5,072**	**42,727**	**500**	**575**	**-**	**48,874**
Operating surplus	-	-	-	-	40,193	40,193
FX gains/losses	-	38,399	-	-	-38,399	-
Operating surplus retained in general reserve	1,555	-	-	-	-1,555	-
Property revaluations	-	-	615	-	-	615
Contributions to welfare fund	-	-	-	41	-	41
Provisions for transfer to RS	-	-	-	-	-240	-240
Total movement	1,555	38,399	615	41	-	40,610
Balance at 31 December 1999	**6,627**	**81,126**	**1,115**	**616**	**-**	**89,484**
Balance at 1 January 2000						
- as previously reported	**6,627**	**81,126**	**1,115**	**616**	**-**	**89,484**
Effect of new securities revaluation method	17	-	-	-	-	17
- as restated	**6,644**	**81,126**	**1,115**	**616**	**-**	**89,501**
Arising in the period						
Operating surplus	-	-	-	-	45,443	45,443
FX gains/losses	-	28,642	-	-	-28,642	-
Operating surplus retained in general reserve	13,490	-	-	-	-13,490	-
Property revaluations	-	-	-	-	-	-
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**

An analysis of the movements in each category within ‘Reserves’ is presented in Note 13.

The notes on pages 84 to 96 form an integral part of the financial statements.

Statement of cash flows

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

	Notes	**2000**	1999
Cash flows from operating activities			
Interest received		**34,233**	22,339
Interest paid		**-17,380**	-18,666
Other		**-2,008**	-1,939
Net cash flow from operating activities	14	**14,845**	1,734
Cash flows from investing activities			
Increase/decrease in foreign deposits		**-39,368**	20,703
Increase/decrease in fixed assets		**-295**	-308
Increase/decrease in loans to domestic banks		**15,184**	-17,998
Net cash flow from investing activities		**-24,479**	2,397
Cash flows from financing activities			
Issue of circulating currency		**-2,695**	37,898
Bank of Slovenia bills, net	15	**818**	-43,579
Other, net		**-2,016**	1,419
Net cash flow from financing activities		**-3,892**	-4,262
Exchange rate effect		**-2,526**	-1,426
Net cash flow from all activities		**-16,052**	-1,557
Opening cash balance		**-75,898**	-74,341
Closing cash balance	16	**-91,949**	-75,898
Increase (decrease) in cash balance		**-16,052**	-1,557

The notes on pages 84 to 96 form an integral part of the financial statements.

These financial statements were approved by the Governing Board on 27 March 2001 and were signed on its behalf by:

Dr. France Arhar
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. These were adopted by the Governing Board at the 90th meeting on 9 May 1995.

3 Specific accounting policies

Financial assets and liabilities

All financial assets and liabilities are recognized 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.

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.

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.

Marketable securities

The Bank invests in marketable securities as a part of its management of international reserves. Marketable securities are carried at market value. The effect of securities price changes appears in Statement of income and expenditure under the item Gain (loss) from unrealized price revaluation. The net amount of unrealized gain (loss) is transfered 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 for purposes of implementing monetary policy and managing loans to banks. The amounts related to foreign exchange swap agreements are not recognised in the balance sheet until the settlement date.

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 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 net.

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 also net gain (loss) from unrealized price revaluation of marketable securities 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

There has been a change in accounting policies since the previous year. In the year 2000 the Bank changed the method of valuation of marketable securities from the lower of amortised cost and market value to the valuation at market value. The reason for the change in accounting policy is more appropriate value of securities portfolio and the intention to adopt the IAS 39 which is effective for periods on or after 1 January 2001. The Bank had not prepared the parallel comparison according to the changed accounting policy for the year ended 1999 because the effect of this change is insignificant (SIT 17 millions).

Implementation of IAS 39: Financial Instruments - Recognition and Measurement

The Bank has not yet implemented IAS 39 which is effective for periods on or after 1 January 2001. The impact of IAS 39 is still being evaluated. According to the adoption of the new revaluation method for securities in 2000, management does not expect the effect of implementation IAS 39 to be material.

4 Income from financial assets

	2000 SIT millions	1999 SIT millions
Income from foreign currency assets		
Interest on deposits	**9,090**	6,674
Investment income on marketable securities, net	**23,397**	20,338
Interest on International Monetary Fund deposits	**827**	550
Net foreign exchange gain/loss	**28,642**	38,399
Gain from unrealized price revaluation	**7,558**	-
Loss from unrealized price revaluation	**4,001**	8,292
Total	**65,513**	57,669
Income from domestic currency assets		
Interest on loans to banks	**1,696**	2,163
Total	**1,696**	2,163
Total income from financial assets	**67,209**	59,832

Investment income on marketable securities consists of the following:

	2000 SIT millions	1999 SIT millions
Interest income	**23,105**	18,642
Gains on sale of securities, net	**292**	1,696
Total investment income on marketable securities, net	**23,397**	20,338

Net foreign exchange gain/loss arises from the following exchange rate changes:

	2000 SIT millions	1999 SIT millions
EUR	**10,329**	6,548
USD	**14,682**	22,668
Other	**3,631**	9,183
Net foreign exchange gain/loss	**28,642**	38,399

5 Expenses on serviced liabilities

	2000 SIT millions	1999 SIT millions
Expenses on foreign currency liabilities		
Interest on current accounts and deposits	**1,389**	809
Interest on Bank of Slovenia bills	**14,786**	9,110
Total	**16,175**	9,918
Expenses on domestic currency liabilities		
Interest on current accounts and deposits	**659**	636
Interest on Republic of Slovenia deposits	**56**	113
Interest on Bank of Slovenia bills	**1,690**	6,217
Total	**2,404**	6,966
Total expenses on serviced liabilities	**18,580**	16,885

6 Other income

	2000 SIT millions	1999 SIT millions
Fees and commissions receivable	**914**	699
Other income	**225**	253
Total other income	**1,139**	952

7 Other expenditure

	2000 SIT millions	1999 SIT millions
Commissions and fees for banking services	**332**	408
Total other expenditure	**332**	408

8 Operating expenses

	2000 SIT millions	1999 SIT millions
Staff costs	**1,958**	1,841
Administration costs	**1,327**	1,183
Printing and minting costs	**273**	159
Other	**128**	114
Total operating expenses	**3,685**	3,298

9 Financial assets

	2000				1999
	Repricing period				
	3 months or less	**3 months to 1 year**	**Over 1 year**	**Total**	Total
	SIT millions				
Foreign currency assets					
Cash and deposits	**233,157**	**3,913**	**-**	**237,070**	181,102
Marketable securities	**244,605**	**35,841**	**194,828**	**475,274**	423,983
Receivables from the Republic of Slovenia	**-**	**646**	**7,534**	**8,180**	7,260
International Monetary Fund	**19,557**	**-**	**-**	**19,557**	21,490
Accrued interest and other	**5,374**	**2,379**	**310**	**8,064**	7,115
Total	**502,693**	**42,779**	**202,673**	**748,145**	640,948
Domestic currency assets					
Receivables from Succession Fund of the RS	**-**	**-**	**8,650**	**8,650**	8,650
Loans to banks	**6,563**	**191**	**111**	**6,865**	22,180
Accrued interest and other	**668**	**41**	**217**	**926**	626
Total	**7,231**	**232**	**8,978**	**16,441**	31,456
Total financial assets	**509,924**	**43,011**	**211,650**	**764,585**	672,404

Average effective interest rates on financial assets.

	2000				1999
	Repricing period				
	3 months or less	**3 months to 1 year**	**Over 1 year**	**Total**	Total
	%				
Foreign currency assets					
Cash and deposits	**5.08**	**5.15**	**-**	**5.09**	4.03
Marketable securities	**4.92**	**5.48**	**5.56**	**5.23**	4.23
Receivables from the Republic of Slovenia	**-**	**-**	**-**	**-**	-
International Monetary Fund	**3.88**	**-**	**-**	**3.88**	3.49
Domestic currency assets					
Receivables from Succession Fund of the RS	**-**	**-**	**-**	**-**	-
Loans to banks	**10.48**	**13.74**	**10.00**	**10.56**	8.13

Deposits with other banks and loans to other banks have a carrying amount equal to the principal less specific provisions (2000: SIT 1,017 million, 1999: SIT 889 million). Interest is paid on maturity.

Market value of marketable securities is SIT 475,274 million. Market value in 1999 was SIT 424,000 million and it exceeded the book value (the lower of amortized cost and market value) for SIT 17 million. Marketable securities pay interest mostly semi-annually.

The deposits with the International Monetary Fund represent the Reserve Tranche Position and Special Drawing Rights (SDR) and pay interest on a quarterly basis.

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.

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. This amount will be repaid after the settlement of claims and liabilities of the Republic of Slovenia and the states of the former SFR Yugoslavia. The amount is not interest bearing and has no fixed repayment term and therefore the fair value of this asset is less than the carrying value. Due to the uncertainty relating to the likely repayment term of this asset, no estimation of the fair value has been provided. However, the Governing Board considers that the carrying value of this asset fairly represents the amount which will be recovered.

The Governing Board considers that the fair value of financial assets, except as mentioned above, is not materially different from the carrying value.

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

Currency concentration and maturity analysis

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 2000:

	SIT %	EUR %	USD %	Other %	Total %
Sovereign issuers	**1.20**	**13.60**	**5.52**	**1.91**	**22.23**
Domestic banks	**0.95**	**-**	**-**	**-**	**0.95**
Foreign banks	**-**	**57.10**	**15.11**	**4.61**	**76.82**
December 31, 2000	**2.15**	**70.69**	**20.64**	**6.52**	**100.00**
December 31, 1999	4.68	60.75	24.94	9.64	100.00

Financial assets at 31 December 2000 will mature within the following periods analysed by currency (in millions of tolars):

	SIT	EUR	USD	Other	Total
Up to 1 month	4,835	217,407	25,829	2,857	250,928
1 to 3 months	2,396	24,158	11,206	4,201	41,961
3 to 12 months	232	76,202	15,098	4,184	95,716
1 year and over	8,978	222,742	105,658	38,602	375,980
December 31, 2000	**16,441**	**540,511**	**157,791**	**49,843**	**764,585**
December 31, 1999	31,456	408,464	167,676	64,809	672,404

Credit Risk Concentration

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 2000 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. Loans to domestic banks are collateralized. The Governing Board believes that there is no significant concentration of credit risk.

10 Fixed assets

	Land and bulidings	**Computers & equipment**	Total
	SIT millions	**SIT millions**	SIT millions
Cost or valuation			
At 1 January 1999	1,947	2,004	3,950
Additions	80	221	301
Investment properties revaluation	615	-	615
Disposals	-	-107	-107
At 1 January 2000	2,641	2,118	4,759
Additions	41	191	232
Disposals	-	-80	-80
At 31 December 2000	**2,682**	**2,229**	**4,912**
Depreciation			
At 1 January 1999	538	1,041	1,578
Disposals	-	-106	-106
Charge for the year	18	354	373
At 1 January 2000	556	1,289	1,846
Disposals	-	-70	-70
Charge for the year	20	339	359
At 31 December 2000	**576**	**1,559**	**2,134**
Net book value			
At 31 December 2000	**2,107**	**671**	**2,777**
At 31 December 1999	2,085	828	2,914

Included in land and buildings at 31 December 2000 and 1999 is an amount of SIT 1,115 million relating to investment properties in Austria.

11 Serviced liabilities

	2000				1999
	Repricing period				
	3 months or less	3 months to 1 year	Over 1 year	Total	Total
	SIT millions				
Foreign currency liabilities					
Current accounts and deposits	**35,997**	**-**	**-**	**35,997**	23,990
SDR allocation	**7,534**	**-**	**-**	**7,534**	6,868
IMF and other international financial organisations	**-**	**-**	**5**	**5**	58
Bank of Slovenia bills	**310,440**	**50,728**	**-**	**361,168**	312,009
Accrued interest and other liabilities	**23**	**-**	**-**	**23**	122
Total	**353,994**	**50,728**	**5**	**404,727**	343,048
Domestic currency liabilities					
Current accounts and deposits	**71,835**	**-**	**-**	**71,835**	65,167
Bank of Slovenia bills	**5,541**	**1,405**	**-**	**6,946**	27,101
Republic of Slovenia deposits	**3,411**	**-**	**-**	**3,411**	2,303
Accrued interest and other liabilities	**1,192**	**383**	**4,222**	**5,797**	5,487
Total	**81,979**	**1,789**	**4,222**	**87,990**	100,058
Total serviced liabilities	**435,973**	**52,517**	**4,227**	**492,717**	443,106

Average effective interest rates on serviced liabilities.

	2000				1999
	Repricing period				
	3 months or less	3 months to 1 year	Over 1 year	Total	Total
	%				
Foreign currency liabilities					
Current accounts and deposits	**5.15**	**-**	**-**	**5.15**	4.40
SDR allocation	**-**	**-**	**-**	**-**	-
IMF and other international financial organisations	**-**	**-**	**-**	**-**	-
Bank of Slovenia bills	**5.01**	**4.95**	**-**	**5.00**	3.76
Domestic currency liabilities					
Current accounts and deposits	**0.96**	**-**	**-**	**0.96**	0.97
Bank of Slovenia bills	**8.94**	**9.71**	**-**	**9.10**	7.21
Republic of Slovenia deposits	**1.00**	**-**	**-**	**1.00**	1.00

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

The SDR allocation liability carried an interest rate of 4.34% at 31 December 2000 (1999: 3.90%). Interest paid by the Bank is recharged directly to the Republic of Slovenia, thereby giving a nil effective interest rate.

Bank of Slovenia bills

Bank of Slovenia bills are comprised of the following at 31 December:

	2000 **SIT millions**	1999 SIT millions
Foreign currency bills	**361,168**	311,286
Tolar bills	**6,945**	17,629
Twin bills	**0**	1,430
Bills with warrants	**1**	8,765
Total Bank of Slovenia bills	**368,114**	339,110

Tolar bills are issued with maturities from two to two hundred and seventy days. Foreign currency bills are issued at a discount in either USD or EUR with maturities from two to twelve months. Twin bills were short-term securities issued in bearer form which are comprised of a Tolar and a foreign currency part. The last issue matured on March 16, 2000. Bills with warrants were short-term securities issued in bearer form in Tolars. Warrants attached to the bills enabled the holder to buy new Tolar bills (without additional warrant) or foreign currency bills at a discount. The last, 14th issue, has no warrants attached and it matured on May 25, 2000. The last foreign currency bill, bought at a discount, matured in november 2000.

Currency concentration and maturity analysis

Financial liabilities at 31 December 2000 will mature within the following periods analysed by currency (in millions of tolars):

	SIT	**EUR**	**USD**	**Other**	**Total**
Up to 1 months	**78,446**	**144,469**	**35,428**	**166**	**258,509**
1 to 3 months	**3,534**	**155,015**	**11,382**	**-**	**169,931**
3 to 12 months	**1,789**	**46,524**	**4,204**	**-**	**52,517**
1 year and over	**4,222**	**-**	**3**	**7,536**	**11,761**
December 31, 2000	**87,990**	**346,008**	**51,017**	**7,702**	**492,717**
December 31, 1999	100,058	284,061	51,976	7,010	443,106

12 Banknotes in circulation

Value of banknotes in circulation by denomination:

		2000 SIT millions	1999 SIT millions
SIT	10	**276**	301
SIT	20	**350**	300
SIT	50	**516**	455
SIT	100	**1,369**	1,295
SIT	200	**1,267**	1,096
SIT	500	**1,862**	1,651
SIT	1,000	**12,542**	16,160
SIT	5,000	**49,629**	48,233
SIT	10,000	**71,426**	72,590
Total		**139,238**	142,082
Tolar coupons		**406**	407
Total		**139,644**	142,489

13 Reserves

	2000 SIT millions	1999 SIT millions
Balance at 1 January	**89,484**	48,874
Marketable securities revaluation	**17**	-
New balance at 1 January	**89,501**	48,874
Transfer to foreign exchange reserve	**28,642**	38,399
Transfer to general reserve – price risk	**3,557**	-
Transfer to general reserve – other risk	**9,933**	1,555
Investment properties revaluation	**-**	615
Contributions to the welfare fund	**58**	41
Balance at 31 December	**131,691**	89,484
Represented by		
Foreign exchange reserve	**109,768**	81,126
General reserve – price risk	**3,574**	-
General reserve – other risk	**16,561**	6,627
Investment properties revaluation	**1,115**	1,115
Welfare fund	**673**	616
Total reserves	**131,691**	89,484

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 has been established to provide recreational and other facilities for the staff of the Bank. The assets representing the fund are included in the Bank's balance sheet and any movement in asset values is taken directly to reserves.

14 Reconciliation of operating cash flows with reported operating surplus

	2000 SIT millions	1999 SIT millions
Reported operating surplus	**45,443**	40,193
Non-cash items		
Net unrealized foreign exchange (gain) loss	**-28,057**	-37,805
Gain (loss) from unrealized price revaluation	**-3,557**	-
Depreciation	**356**	370
Total	**-31,258**	-37,435
Movements in other working capital items		
Changes in interest receivable	**-1,007**	900
Changes in interest payable	**1,199**	-1,781
Changes in other accruals	**467**	-143
Total	**660**	-1,024
Net cash flow from operating activities	**14,845**	1,734

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

	2000 SIT millions	1999 SIT millions
Source		
Foreign currency bills	**22,004**	10,125
Total	**22,004**	10,125
Disbursements		
Tolar bills	**-10,684**	-49,119
Bills with warrants	**-9,034**	-2,618
Twin bills	**-1,468**	-1,967
Total	**-21,186**	-53,704
Total net source	**818**	-43,579

16 Supplemental cash flow information: cash balance

	2000 SIT millions	1999 SIT millions
Foreign currency assets		
Cash	**1,238**	1,618
Total assets	**1,238**	1,618
Foreign currency liabilities		
Demand deposits	**-17,941**	-10,046
Domestic currency liabilities		
Commercial banks demand deposits	**-66,801**	-61,253
Non-bank deposits	**-8,445**	-6,217
Total liabilities	**-93,187**	-77,515
Cash balance	**-91,949**	-75,898

Foreign currency cash assets do not include time deposits of SIT 223,835 million.

Foreign currency demand deposits do not include restricted deposits of SIT 18,056 million.

17 Commitments and off balance sheet instruments

Letters of Credit

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

	2000 SIT millions	1999 SIT millions
Foreign currency letters of credit	**12**	175

Foreign exchange swaps

The Bank entered into certain foreign exchange swap agreements in 2000 and in 1999 which require the Bank to buy EUR for SIT and to sell EUR for SIT. The value of foreign exchange swaps is at follows at 31 December:

	2000 SIT millions	1999 SIT millions
Amounts to be received forward against EUR	**15,461**	3,848

	2000 SIT millions	1999 SIT millions
Amounts to be given forward against EUR	**212**	-

Foreign currency swap agreements have the maturity from seven to sixty days. Because of the short term nature of these transactions, the fair value does not differ materially.

Litigation and other provisions

There are certain legal claims pending or threatened, where the Bank is involved which have not yet been settled. The Governing Board believes that sufficient provision has been made in the accounts for any expected loss from future settlement.

6. APPENDICES

6.1. Statutory basis and tasks of the Bank of Slovenia

Slovenia's central bank, Banka Slovenije (Bank of Slovenia) was established on 25 June 1991 by the Law on the Bank of Slovenia provided for in the Constitutional Law on the Implementation of the Basic Constitutional Charter on Independence of the Republic of Slovenia. As from the introduction of Slovenia's legal tender – the tolar – on 8 October 1991, the Bank of Slovenia discharges all functions relating to the monetary policy.

The Constitution grants the central bank operational independence and makes it accountable to the National Assembly …

In accordance with Article 152 of the Constitution of the Republic of Slovenia, the Bank of Slovenia is independent in exercising the powers and performing tasks and duties conferred on it and is directly accountable to the National Assembly.

Under the Law on the Bank of Slovenia, responsibility for the management of the central bank is vested in the Governing Board and the Governor of the Bank of Slovenia. The Governing Board of the Bank of Slovenia comprises eleven members: the Governor (President of the Governing Board), Deputy Governor, three Vice-Governors and six non-executive members appointed from among persons of recognised professional experience. The Governor and six independent experts are appointed by the National Assembly on a proposal made by the President of the State. The Deputy Governor and the Vice-Governors are appointed by the National Assembly on a proposal made by the Governor. The term of office of all members of the Governing Board is six years and is renewable. The Governing Board acts by a two-third majority.

… and responsible for stability of the Slovenian currency and general liquidity in domestic and international payments.

The main statutory objective of the Bank of Slovenia is to maintain stability of the Slovenian currency and general liquidity in domestic and international payments. To this end the Bank of Slovenia discharges the following functions:

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

The Bank of Slovenia also performs other tasks and carries on 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 the 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 submit reports on its activities to the National Assembly, including its financial plan and annual statement of accounts.

Access of the government to lending by 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.

6.2. 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)

	1996	1997	1998	1999	2000
Operating income:					
Income from financial assets	14,941	19,475	29,188	29,724	35,010
Net foreign exchange gain/loss	8,131	16,797	-4,753	38,399	28,642
Gain (loss) from unrealized price revaluation	-	-	-	-8,292	3,557
Total income from financial assets	**23,072**	**36,273**	**24,435**	**59,832**	**67,209**
Expenses on serviced liabilities	9,310	17,727	24,701	16,885	18,580
Net investment income	**13,762**	**18,546**	**-266**	**42,947**	**48,630**
Other income	511	381	1,299	952	1,139
Other expenses	147	676	286	408	332
Total operating income	**14,125**	**18,251**	**747**	**43,491**	**49,437**
Operating expenses	2,181	2,670	2,923	3,298	3,685
Provisions	579	718	312	-	308
Operating surplus/deficit available for appropriation	**11,366**	**14,862**	**-2,489**	**40,194**	**45,443**
Appropriations:					
Transfer/Release to foreign exchange reserves	8,131	16,797	-4,753	38,399	28,642
Transfer to general reserves – price risks	-	-	-	-	3,557
Financial results after the appropriation of net foreign exchange gain/loss and gain (loss) from unrealized price revaluation	3,235	-1,935	2,264	1,795	13,244
Transfer/Release to general reserves - other risks	2,312	-1,935	1,457	1,555	9,933
Total transfer/release to reserves	10,443	14,862	-3,297	39,954	42,132
Provision for transfer of surplus to the budget of RS	923	-	807	240	3,311
Total appropriations	**11,366**	**14,862**	**-2,489**	**40,194**	**45,443**

Balance Sheet data for five years

As at 31 December (in millions of tolars)

	1996	1997	1998	1999	2000
Assets					
Financial assets	361,496	593,441	614,040	672,404	764,585
Fixed assets	1,657	2,072	2,372	2,914	2,777
Total assets	**363,153**	**595,512**	**616,412**	**675,318**	**767,363**
Liabilities and reserves					
Serviced liabilities	253,578	457,734	462,063	443,106	492,717
Banknotes in circulation	71,441	85,653	104,667	142,489	139,644
Provision for transfer of surplus to the budget of RS	923	-	807	240	3,311
Total liabilities	**325,941**	**543,386**	**567,538**	**585,834**	**635,672**
Reserves	37,212	52,126	48,874	89,484	131,691
Total liabilities and reserves	**363,153**	**595,512**	**616,412**	**675,318**	**767,363**

6.3. Important measures taken in 2000

6.3.1. Monetary and exchange rate policy measures

Lombard loan — **January**

In January, the Bank of Slovenia reduced the percentage of withdrawal of the intervention period Lombard loan from 5.0 % to 2.5 % of securities pledged as collateral; the higher percentage was in effect from 27 December 1999.

Overnight liquidity loan

The Bank of Slovenia made the overnight liquidity facility available on 28 and 31 January on the interbank market at the interest rate of 7.5 %.

Twin bills of the Bank of Slovenia — **February**

On 16 February, the Bank of Slovenia discontinued selling 1st and 12th issue of twin bills with maturity date on 16 March 2000. This was the last series of twin bills.

Temporary purchase of bills denominated in foreign currency with obligatory repurchase

Bidding interest rate for temporary purchase rose from 7.8 % to 8.0 %.

Overenight liquidity loan

On 28 and 29 February, the Bank of Slovenia made overnight liquildity loan available to banks on the overnight interbank market at the exchange rate of 7.7 %.

Sale of foreign exchange for subscription to bills denominated in foreign currency — **March**

By reducing gradually the premium on selling rate of the Bank of Slovenia (from 0.68 % to 0.51 %), the Bank of Slovenia curbed a rise in exchange rate applicable on selling of foreign exchange for the purpose of subscribing to bills denominated in foreign currency.

Bills with warrants

As from 1 March, investors are not entitled to a discount granted on the basis of a warrant when subscribing to bills in the value of 500,000 tolars or bills denominated in foreign currency.

Temporary purchase of bills denominated in foreign currency with obligatory repurchase

Bidding interest rate applicable to temporary purchase of bills rose from 8.0% to 8.5%.

Tolar bills

The Bank of Slovenia rose interest rate on 2-, 12- and 60-day bills (this decision led to a hike in lending granted on 12-day bills pledged as collateral). At the same time, the Bank of Slovenia made available to savings banks 2-day bills and discontinued the issue of 28-day bills.

Overnight liquidity loan

On 30 and 31 March, the Bank of Slovenia made the overnight liquidity facility available to banks on the interbank market at the exchange rate of 7.7 %.

Tolar bills — **April**

As of 3 April, the Bank of Slovenia discontinued the issue of bills with maturity date after 7, 14 in 30 days.

Sale of foreign exchange to subscribe to bills denominated in foreign currency and temporary sale of foreign exchange

The sale foreign exchange for the purpose if subscribing to 120-day bills denominated in foreign currency was abolished; the banks gained access to the temporary purchase of foreign exchange from the Bank of Slovenia for two weeks.

Agreement on participation of banks in interventions in the foreign exchange market

By terminating the previous agreement on the participation of banks in interventions on the foreign exchange markets by agreement, the Bank of Slovenia withdrew the offers for two-month temporary purchase and selling of foreign exchange.The new agreement signed by 22 banks came into force as of the date of its signature by the participating banks. Under the agreement, the Bank of Slovenia sent to two banks signatories of the agreement, two offers for temporary purchase, i.e. sale of foreign exchange with obligatory repurchase, i.e. sale within 7 days, both at the exchange rate of 1.0%.

April

Bills denominated in foreign currency
As from 25 April onward, non-bank legal persons are not entitled to subscribe to bills denominated in foreign currency. Thus after discountinuing twin bills and bills with warrants, the Bank of Slovenia abolished the last instrument intended for non-bank public.

Lombard loan
On 17 April, the Bank of Slovenia increased the percentage of withdrawal of the intervention Lombard loan from 2.5 % to 5.0 % of securities pledged as collateral.

May

Temporary purchase of bills denominated in foreign currency
On 25 May, the interest rate charged for a 28-day temporary purchase of bills increased from 8.5 % to 9.0 %. At the end of May, the Bank of Slovenia made available to banks on a daily basis also 7-day temporary purchase of bills denominated in foreign currency through the same kind of auction and the same bidding interest rate as for 28-day temporary purchase.

Bills in denominations of 500,000 tolars
As of 25 May, the 14th issue of the bills in denominations of 500,000 tolars came to maturity.

Speacial liquidity loan with participation of banks
The Bank of Slovenia and the major Slovenian banks renewed at the end of May the agreement for the fifth time in a row for one year to grant liquidity loans with participation of banks. The banks will be compensated for making a stand-by facility available at the rate of 1.5 % of the stand-by facility.

Overnight liquidity loan
On 30 and 31 May, the Bank of Slovenia made the liquidity facility available to banks on the overnight money market at the exchange rate of 8.2 %.

June

General discount rate and Lombard rate of the Bank of Slovenia
As of 1 June, the Bank of Slovenia rose the discount rate to 9 % (before 8 %) and Lombard interest rate to 10 % (before 9 %). The hike also led to an increase in interest charged on late payments.

Overnight liquidity loan
Between 28 and 30 June, the Bank of Slovenia made liquidity facility available to banks in the overnight money market at the exchange rate of 8.2 %.

July

Intervention in the foreign exchange market by basic rate and maximum spread
Due to fast rise in exchange rate, the Bank of Slovenia decided to intervene in the foreign exchange market by base rate, and by setting the maximum spread between buying and selling exchange rates. The intervention period was in force until 19 September.

Temporary purchase of bills denominated in foreign currency
As of 11 July, the first bidding for temporary purchase of bills denominated in foreign currency for two months took place. At the same time, offers sent to banks for 28-day purchase of bills with obligatory repurchase were discontinued. As a rule, the Bank of Slovenia sends to banks its offer twice a month, in the beginning and in the middle of the month. The base interest rate and the evaluation method for the selection of successful bids remained the same as in the case of 7- (and 28-) day repo bills, *viz.* 9.0 %.

Reccomendation in respect of ceiling deposit interest rates
As of 1 July, the reccomendation made by the Bank of Slovenia in respect of ceiling deposit interest rates is null and void. The Banking Association of Slovenia rose as of 1 August the recommended ceiling interest rates on time deposits with maturity between 91 and 180 days to TOM/D*+2.25% (before: 2.0%), on time deposits with maturity between 181 days and 1 year to TOM/D+3.25 % (before: 2.75 %), and on time deposits with maturity between 1 and 2 years to TOM/D+4% (before:3.5 %).
*TOM stands for base interest rate and D stands for exchange rate.

Treasury bills of the Ministry of Finance pledged as a collateral to secure obligations to the Bank of Slovenia
As of 17 July, for the purpose of securing their obligations to the Bank of Slovenia, banks may use for certain monetary policy instrumens (last resort and overnight liquidity loans, Lombard and short-term facility) also 3-, 6- in 12- month treasury bills issued by the Ministry of Finance entered in the register kept by the Central Securities Clearing Corporation in addition to bills denominated in foreign currency.

Overnight liquidity loan On 31 July, the Bank of Slovenia made available the liquidity facility in the overnight money market granted at the interest rate of 8.2% for the last time in 2000	**July**
Temporary purchase of bills denominated in foreign currency The Bank of Slovenia rose on 1 September the bidding interest rate for foreign currency bills from 9.0 to 9.5 %.	**September**
Intervention in the foreign exchange market by means of base exchange rate and maximum spread The Bank of Slovenia started to intervene once again in the foreign exchange market on 27 October by setting the base exchange rate and the maximum spread. The intervention lasted until 14 November.	**October**
Complying with mandatory reserve requirement by subscribing to securities issued by the Bank of Slovenia As of 27 November, banks comply with the mandatory reserve requirement in relation to assets gathered under the National Housing Savings Scheme by subscribing to 60-day bills denominated in tolars, but only up to the amount of the calculated mandatory reserves from average daily balance of funds gathered under the National Housing Savings Scheme for the entire accounting period.	**November**
Discount and Lombard rates As of 1 December, the Bank of Slovenia increased the discount rate from 9.0% to 10.0% and the Lombard rate from 10.0% to 11.0%. The hike led to a rise in the back (late) interest rate. **Temporary purchase of bills denominated in foreign currency with obligatory repurchase** The Bank of Slovenia increased bidding interest rate for 7-day and 2-month repo bills denominated in foreign currency from 9.5 % to 10.5 %.	**December**

6.3.2 Supervisory measures

Instructions for the Implementation of the Decree on Books of Account and Annual Report of Banks and Savings Banks – Including the Methodology for the Calculation of Ratios	**January**
Instructions for the Calculation of Some Key Deposit and Lending Interest Rates of Banks and Savings Banks for the Non-Bank Sector	**March**
Decree on Amendments to the Decree on Minimum Requirements for Obtaining Authorisation for Provision of Banking and Other Financial Services and Documents Attached to Application Submitted by Bank or Savings Bank **Decree on Amendments to the Decree on Minimum Scope of Documents Submitted by a Foreign Bank with the Application to Establish a Branch** **Decree on Amendments to the Decree on Tariffs for Services Rendered by the Bank of Slovenia**	**June**
Decision (Decree) on Deposit-Guarantee Scheme	**July**
Instructions for Completing Reports on Guaranteed Deposits	**August**
Decree on Adjustment of Amounts of Minimum Own Funds of Banks, Guaranteed Deposits and Minimum Own Funds of Savings Bank **Amendments to the Instructions for Implementation of Decree on Books of Account and Annual Reports and Accounts of Banks and Savings Banks**	**September**
Decree on Amendment to the Decree on Annual Fee and Lump Sum Charges for Prudential Supervision **Decree on Amendments to the Decree on the Calculation of Own Funds, Capital Requirements and Capital Adequacy of Banks and Savings Banks**	**December**

6.4. Governance and organisation chart

6.4.1. Changes in governing board membership in 2000

Professor Dr. Dušan Zbašnik, was re-appointed on 27 July 2000 for another six-year term of office by the National Assembly of the Republic of Slovenia.

6.4.2 Composition of the governing board of the Bank of Slovenia as at 31 December 2000

President of the governing board of the Bank of Slovenia

Dr. France Arhar
(Governor of the Bank of Slovenia)

Members of the governing board of the Bank of Slovenia

Samo Nučič
(Deputy Governor of the Bank of Slovenia)

Darko Bohnec
(Vice Governor of the Bank of Slovenia)

Mag. Janez Košak
(Vice Governor of the Bank of Slovenia)

Andrej Rant
(Vice Governor of the Bank of Slovenia)

Tatjana Fink
(Trimo, Trebnje)

Mag. Bine Kordež
(Merkur, Kranj)

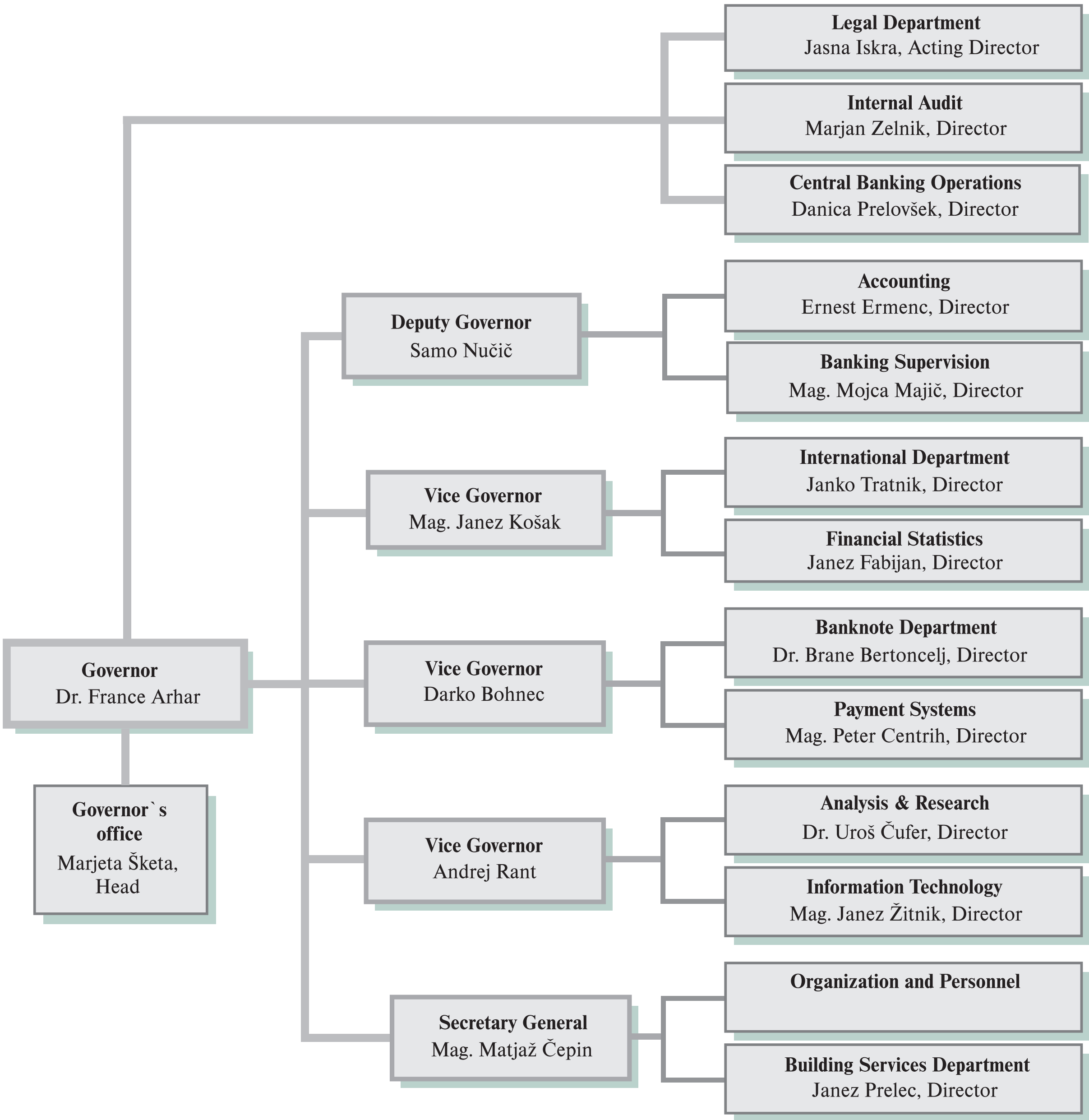
Mag. Vladimir Lavrač
(Institute of Economic Research, Ljubljana)

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

Dr. Ivan Ribnikar
(Faculty of Economics, Ljubljana)

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

6.4.3. Organisation chart of the Bank of Slovenia as at 31 December 2000



6.5. Publications and website

Title and description	Contents
Bulletin · Monthly · Slovenian, English	Macroeconomic statistical data focused on monetary statistics, exchange rates and international economic relations. Review of current trends in figures; notes on methodology; list of authorised banks in Slovenia, data release calendar.
Annual Report · Annual (spring edition) · Slovenian, English	Report of the Bank of Slovenia to the National Assembly of the Republic of Slovenia. Outline of economic developments, monetary policy, operations of banks and the Bank of Slovenia, as well as other activities carried on by the Bank of Slovenia.
Report on Supervision of Banking Operations · Annual (autumn edition) · Slovenian, English	Report prepared by the Bank Supervision Department for the National Assembly of the Republic of Slovenia on operating results posted by banks and savings banks, developments in the legal framework for supervision & surveillance, and oversight of banking operations.
Direct Investment · Annual · Slovenian and English	Statistical survey of direct and portfolio cross-border investments – onward and outward (year-end stock).
Surveys & Analysis · Quarterly · Slovenian	Speeches given by the Governor of the Bank of Slovenia in the National Assembly of the Republic of Slovenia, analytical and methodological surveys of monetary, balance of payments, and related issues.
Financial markets · Quarterly · Slovenian	Statistical survey of non-monetary financial intermediaries, securities market and interest rates.
Monetary Survey · Monthly · Slovenian	Up-to-date analytical and macroeconomics elaboration of monetary and balance of payments movements.
Website · Home page index http://www.bsi.si/... **.../html/kazalo.html** · Home page index (English) http://www.bsi.si/... **.../eng/index.html**	Presentation of the Bank of Slovenia, Slovenian banknotes and coins, laws and secondary legislations related to the central bank's area of work, as well as other useful information. Up-to-date exchange and interest rates, securities issued by the Bank, and key publications.

6.6. Glossary of terms

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

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

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

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

Capital (Own Funds) – The sum of core capital and supplementary capital minus deductions listed under Article 5 of the Decree on Calculation of Own Funds, Capital Requirements and Capital Adequacy of Banks and Savings Banks (Official Gazette of the Republic of Slovenia, Nos. 32/99 and 122/00).

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

Classification of assets – Banks and savings banks classify assets (claims) in five groups on a scale of A (best) to E (worst) based on assessment and evaluation of the ability of the borrower/client 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/clients where the possibility of loss if a borrower/client fails 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 respective Decree.
Group B comprises: claims on borrowers/clients 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/clients 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/clients who are expected to have cash flow insufficient to meet their obligations at maturity; borrowers/clients who are significantly undercapitalised; borrowers/clients who do not have sufficient long-term sources of financing long-term investments; borrowers/clients 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/clients 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/clients where the possibility of loss is high; borrowers/clients are faced with problems of liquidity and insolvency; a motion to commence proceedings against borrowers/clients has been lodged with a competent court, *viz.* compulsory settlement or bankruptcy; borrowers/clients who are in the process of rehabilitation, i.e. compulsory settlement; borrowers/clients in bankruptcy; borrowers/clients 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/clients who are not expected to meet their obligation to repay the debt; claims founded on 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.

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

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

Large exposure – Any exposure of a bank to a single borrower/client or a group of connected borrowers/clients of or in excess of 10% of the bank's capital (own funds).

Mandatory reserve – Statutory amount of assets computed as a percentage in relation to deposits and other obligations of the bank that the bank must maintain on the transactional account or a special mandatory reserve account with the Bank of Slovenia and in cash.

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.

Monetisation – The transformation of assets purchased by the central bank and commercial banks into money. Namely, investments in financial assets are (claims or loans and advances) are financed by newly created or issued money.

Money market – Interbank financial market where first-class (gilt-edged) short-term securities are traded.

(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 – Interest rate composed of indexation part (a compensation for inflation) and real interest rate.

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

Operating expenses – Sum of general administrative expenses (labour costs and other administrative expenses), depreciation and taxes.

Other assets – Equity investments in related (dependent) and unrelated (independent) undertakings, tangible fixed assets, intangible long-term assets, subscribed unpaid capital and holdings of own shares, prepayments and accrued income, and other assets like cheques, claims arising from accrued interest, fees and commissions, etc.

Other liabilities – Accruals and deferred income, general and specific provisions, and other liabilities.

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

Revaluation interest rate– Part of interest rates on loans and deposits in tolars serving as compensation to the creditor and the borrower for inflation.

Secondary liquidity – Amount of bills issued by the Bank of Slovenia denominated in tolars and foreign currency bills, and bonds issued by the government of the Republic of Slovenia (investments in securities of the central bank and the government in domestic and foreign currency (bills issued by the Bank of Slovenia and the Republic of Slovenia, and short-term bonds issued by the Republic of Slovenia).

Sterilisation – In general, 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 bills issued by the Bank of Slovenia denominated in foreign currency by the Bank and selling the bills denominated in tolars by the Bank to neutralise the impact that such purchases of foreign exchange have on the quantity of base money.

Total assets – Amount of all items on the assets or on the liabilities side of the balance sheet of the respective bank or a savings bank.